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December 21, 2000

MEMORANDUM FOR ASSOCIATE AREA COUNSEL – ST. LOUIS
(SMALL BUSINESS / SELF-EMPLOYED)

FROM: Joseph W. Clark
Senior Technical Reviewer, Branch 2
(Collection, Bankruptcy & Summonses)

SUBJECT: Automatic Stay Violation: Notice of Final Determination of Denial of "Innocent Spouse" Relief

This constitutes our response to your September 15, 2000, request for advice on whether a notice of final determination denying innocent spouse relief to a taxpayer in bankruptcy constitutes a potential violation of the automatic stay. We believe that the issuance of this type of determination generally does not violate the stay.

ISSUE: Whether the issuance of a notice of final determination denying relief from joint and several liability on a joint income tax return, pursuant to I.R.C. § 6015, constitutes a potential violation of the stay on various actions imposed upon the filing of a bankruptcy petition, pursuant to B.C. § 362.

CONCLUSION: No. Since the issuance of a notice of final determination denying innocent spouse relief generally does not fall within any of the categories of activities proscribed by B.C. § 362(a), it generally does not constitute a stay violation.

STATUTORY BACKGROUND: The Internal Revenue Service Restructuring and Reform Act of 1998 eased the requirements for obtaining relief from joint and several liability on a tax return jointly filed by a husband and wife. The new provisions are set forth in the current version of I.R.C. § 6015.

Section 6015(b) provides that, with respect to a jointly-filed return, an individual may be partially or fully relieved of liability for an understatement of tax, if: 1) the understatement is attributable to erroneous items of the individual's spouse; 2) the spouse seeking relief establishes that in signing the return he or she did not know, and had no reason to know, that the understatement existed; 3) taking into account all the facts and circumstances, it would be inequitable to hold the

spouse seeking relief liable for the deficiency in tax attributable to such understatement; and 4) relief is sought within two years of the date the Service has commenced collection activities with respect to the spouse seeking the relief. Alternative avenues of relief available to spouses filing jointly are afforded by Section 6015(c) and Section 6015(f). These provisions, respectively, limit liability for taxpayers no longer married, legally separated, or no longer living together (Section 6015(c)) and allow for potential relief on an equitable basis where subsections (b) and (c) do not afford relief (Section 6015(f)).

Once an individual or entity files a bankruptcy petition, the Bankruptcy Code imposes a stay, "applicable to all entities," against various actions. B.C. § 362(a). These actions are enumerated in subsections (1) through (8) of Section 362(a), and include, inter alia:

> (1) the commencement or continuation ... of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title.
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> (4) any act to create, perfect, or enforce any lien against property of the estate;
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> (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;
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> (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;
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> (8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

B.C. § 362(a).

Section 362 also renders the stay inapplicable to certain specific activities. These include, inter alia, conducting audits, issuing Notices of Deficiency, and making assessments, if such activities are undertaken by "governmental units." B.C. § 362(b)(9).

LAW AND ANALYSIS: Your request for advice presents the novel issue of whether a notice of final determination denying innocent spouse relief to an individual in bankruptcy violates the automatic stay. 1/ For purposes of this memorandum, we assume that the determination is of an administrative nature, issued by the Service.

In general, the issuance of this type of administrative determination does not constitute a stay violation. Spouses who file joint tax returns are jointly and severally liable for any deficiency of tax for the period encompassed by that return, pursuant to I.R.C. § 6013(d)(3). Thus, in the innocent spouse context, a determination adverse to the individual seeking relief, while denying the relief sought, fails to have the effect of imposing any additional liability upon him or her, since the individual is already liable for the full amount of the deficiency. Thus, the determination issued by the Service arguably does not violate the automatic stay because it does not constitute action taken "against the debtor" or his or her property as is generally required under section 362(a).

Moreover, the issuance of a determination denying innocent spouse relief would not, for other reasons, violate any of the individual subsections of B.C. § 362(a). The issuance of the determination would not violate the automatic stay under section 362(a)(1) as it would not constitute a proceeding "against the debtor that was or could have been commenced before the commencement of" the bankruptcy case, or "to recover a claim against the debtor that arose before the commencement of the case." Even if we were to agree that an administrative proceeding determining innocent spouse relief constituted a proceeding "against the debtor," the ultimate denial of relief would not violate the stay because the proceeding which culminated in the determination would have been initiated by the debtor, rather than by someone else. The majority view in this regard is that where a given proceeding is initiated by the debtor himself or herself, the ultimate outcome of the proceeding -- regardless of whether it is favorable or unfavorable to the debtor -- does not violate the automatic stay. See, e.g., Roberts v. Commissioner, 175 F.3d 889 (11th Cir. 1999); Freeman v. Commissioner, 799 F.2d 1091 (5th Cir. 1986) (cases involving appeals of Tax Court cases -- since the Tax Court case was determined to have been initiated by the debtor, the appeal of the Tax Court decision was not stayed). 2/ See also

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1/ We are aware of no case law addressing this issue.

2/ Under the minority view on this issue, an appeal of a Tax Court decision is stayed on the rationale that an investigation into an individual's tax liability is inherently an action taken "against" that individual, and thus a "continuation" of that proceeding, including an appeal of a Tax Court decision ruling on the individual's liability, is prohibited by section 362(a)(1). See Delpit v. Commissioner, 18 F.3d 768 (9th Cir. 1994). We think it is possible, although

Parker v. Bain, 68 F.3d 1131 (9th Cir. 1995); Maritime Electric Co., Inc. v. United Jersey Bank, 959 F.2d 1194 (3d Cir. 1991); Jefferson Ward Stores, Inc. v. The Doody Co., 48 B.R. 276, 278 (E.D. Pa. 1985)(nontax cases in which denials of actions requested by debtors were found not to violate the stay).

Issuance of a determination denying innocent spouse liability also would not violate subsections (a)(3) or (a)(4) of Section 362, since the determination would not address or attempt to affect property of the bankruptcy estate. Nor would the determination even indirectly affect estate property since, as has previously been noted, both the spouse seeking relief and the other spouse are already jointly and severally liable for the tax at issue. By denying innocent spouse relief, the Service essentially reaffirms that liability and maintains the status quo, resulting in no impact on either the estate's assets or its liabilities.

Similarly, the determination denying innocent spouse relief would not violate the stay under subsections (a)(5) and (a)(6). The determination would have no impact on any lien against the debtor-spouse's property, rendering subsection (a)(5) inapplicable. It also would not be tantamount, in itself, to "an act to collect, assess, or recover" a claim against the individual seeking innocent spouse relief, as it would be only embody a decision, not purport to lead to imminent collection action. One possible exception to the conclusion that these subsections do not stay issuance of a determination denying innocent spouse relief might exist if the determination were issued as part of a Letter 3193, Notice of Determination Concerning Collection Actions Under Section 6320 and/or 6330, otherwise known as a Collection Due Process (CDP) determination. Innocent spouse liability may be determined as part of a CDP proceeding undertaken pursuant to I.R.C. §§ 6320 or 6330. The position of this office is that the Service should not institute any aspect of a CDP proceeding during bankruptcy, as doing so could be characterized as an act to collect a liability on the debtor's part and, thus, as a stay violation under section 362(a)(6). 3/ Accordingly, where the notice of final

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unlikely, that courts adopting this rationale might view the issuance of a determination of innocent spouse liability as a "continuation" of an investigation into a couple's tax liability and, analogous to the Delpit situation, as an action accordingly prohibited by the stay under section 362(a)(1). Because this appears to be an attenuated extension of what is already a minority view, however, we recommend assuming that innocent spouse determinations may be issued in bankruptcy even in districts where Delpit would apply.

3/ We have been told that, in many instances, the innocent spouse determination is reported on a form separate from the CDP determination and may even be sent to the taxpayer at a different time from the time the CDP determination is sent. In that event, issuance of the innocent spouse determination, in itself, clearly would not be a violation of section 362(a)(6). Of note, however, is that this division has issued Chief Counsel Advice reflecting the

determination denying innocent spouse relief is inseparable from a CDP determination, the notice should not be issued during bankruptcy.

The legislative history relevant to the Bankruptcy Code reflects that the automatic stay was never intended to prohibit the type of action at issue here. The House Report accompanying the Bankruptcy Reform Act of 1978, through which the Bankruptcy Code was added to the United States Code, states, in pertinent part:

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan or simply to be relived of the financial pressures that drove him into bankruptcy.

H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 340 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News 5963, 6296-97.

The type of action at issue here, issuance of a determination on innocent spouse relief, constitutes one which was precipitated by a taxpayer, and which – even if the determination is adverse and the spouse seeking relief is in bankruptcy -- has no impact on the debtor-spouse's creditors, property, or rights in bankruptcy. In this respect, it is analogous to issuance of a Notice of Deficiency, which is specifically rendered not subject to the automatic stay pursuant to B.C. § 362(b)(9)(B). A notice of final determination denying innocent spouse relief is not the type of action which was contemplated by Congress when the automatic stay provisions were included in the Bankruptcy Code. For this reason and for the other reasons discussed herein, the issuance of a determination denying innocent spouse relief would not generally constitute a violation of the automatic stay.

Our response on this matter has been coordinated with both the Office of Assistant Chief Counsel (Administrative Provisions & Judicial Practice), and Branch 1 (Collection, Bankruptcy & Summonses) in the Procedure and Administration function of the National Office. If you have further questions,

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position that issuance of a CDP Notice, in which the taxpayer is notified of the Service's proposed action (for example, the Service's intention to levy on the taxpayer's property), and the taxpayer's right to be heard on the proposed action, is violative of the automatic stay under section 362(a)(6). See General Litigation Bulletin 476 (May 2000) at 10. Therefore, we believe that the final CDP determination may also violate the stay, as would the determination as to innocent spouse relief if it is issued within the CDP determination.

please call 202/622-3620.

cc: Assistant Chief Counsel (Administrative Provisions & Judicial Practice)
Attention: Bridget Finkenaur

Chief, Branch 1 (Collection, Bankruptcy and Summonses)