Michael v. Comm'r, 133 T. C. 237 (U. S. Tax Court 2009)

In Michael v. Comm'r, the U. S. Tax Court ruled on the IRS's authority to enforce tax penalties through levy when a settlement agreement exists. The court found that while the IRS abused its discretion by sustaining a levy for 1989 due to an overpayment under the settlement terms, it did not abuse its discretion for 1990 and 1991. This decision underscores the IRS's ability to use statutory collection methods even after a settlement, emphasizing the necessity of clear settlement terms and the IRS's discretion in collection actions.

Parties

Anthony G. Michael, the petitioner, challenged the Commissioner of Internal Revenue, the respondent, over the imposition of tax preparer penalties under section 6694 of the Internal Revenue Code for the taxable years 1989, 1990, and 1991. Michael was the plaintiff in a prior refund suit against the Commissioner in the U. S. District Court for the Eastern District of Michigan, where the Commissioner was also the defendant and had filed a counterclaim for the unpaid penalties.

Facts

In June 1995, the IRS assessed return preparer penalties totaling $35,000 against Anthony G. Michael under section 6694(b) of the Internal Revenue Code for recklessly or intentionally disregarding rules and regulations with respect to 35 returns for the taxable years 1989, 1990, and 1991. Michael paid 15% of the assessed penalties, amounting to $5,250, to file a refund claim, which the IRS credited $1,000 toward 1989 and $4,250 toward 1990, leaving 1991 uncredited. After the IRS denied Michael's refund claim, he filed a refund suit in the U. S. District Court for the Eastern District of Michigan. In August 1997, the parties reached a settlement agreement, reducing Michael's liability to $15,500, minus the $5,250 already paid. Michael did not fulfill the payment terms of the settlement, leading the IRS to issue a notice of intent to levy in April 2005 based on the original assessments. Michael requested a collection due process (CDP) hearing, during which the settlement officer determined that Michael was entitled to a reduction in accordance with the settlement terms. On August 22, 2007, the IRS issued a notice of determination upholding the levy for the taxable years 1989, 1990, and 1991, prompting Michael to challenge the IRS's authority to levy based on the settlement agreement.

Procedural History

Following the IRS's assessment of penalties in June 1995, Michael paid part of the penalties and filed a refund claim, which was denied. He then filed a refund suit in the U. S. District Court for the Eastern District of Michigan. The parties reached a settlement in August 1997, and the District Court dismissed the case with prejudice, retaining jurisdiction for 60 days to enforce the settlement. Michael did not pay the settled amount, leading the IRS to issue a notice of intent to levy in April 2005. Michael requested and received a CDP hearing, where the settlement officer determined that Michael was entitled to a reduction in the assessed penalties in accordance with the settlement agreement. On August 22, 2007, the IRS issued a notice of determination upholding the levy for the taxable years 1989, 1990, and 1991. Michael filed a petition with the U. S. Tax Court, challenging the IRS's determination. The Commissioner filed a motion for summary judgment, which the Tax Court granted in part and denied in part, finding that the IRS abused its discretion in sustaining the levy for 1989 but not for 1990 and 1991.

Issue(s)

Whether the IRS abused its discretion in sustaining a levy to collect tax preparer penalties under section 6694 for the taxable years 1989, 1990, and 1991, given the existence of a settlement agreement reducing Michael's liability?

Rule(s) of Law

The IRS is authorized to collect unpaid tax liabilities by levy under section 6331 of the Internal Revenue Code. Section 6330 grants taxpayers the right to a CDP hearing before an impartial officer, where they may raise issues regarding the collection action. The Tax Court reviews the IRS's determination for abuse of discretion if the underlying liability is not properly at issue. Section 6404 authorizes the IRS to abate the unpaid portion of an assessment if it is excessive. The settlement agreement between the parties is not invalidated by the original assessment, and the IRS may still pursue statutory collection remedies.

Holding

The Tax Court held that the IRS abused its discretion in sustaining the levy for 1989 because Michael had overpaid his tax liability for that year based on the settlement agreement. However, the IRS did not abuse its discretion in sustaining the levy for the taxable years 1990 and 1991, and the IRS was entitled to summary judgment for those years as a matter of law.

Reasoning

The Tax Court's reasoning focused on several key points. First, the court found that it had jurisdiction to review the IRS's determination to sustain the levy, as the statutory collection remedies are separate from the Government's right to counterclaim in a refund action. The court rejected Michael's argument that the settlement agreement invalidated the original assessments, holding that an assessment is not void because the liability is reduced by settlement. The court also rejected Michael's argument that the IRS failed to issue a notice and demand for payment based on the settlement agreement, as there is no requirement for a second notice and demand. The court found that the IRS satisfied the assessment and notice and demand requirements based on the original assessments. The court also held that the IRS's failure to provide the entire administrative file did not create a genuine issue of material fact for trial. The court's analysis of the settlement agreement terms led to the conclusion that Michael overpaid his tax liability for 1989, resulting in an abuse of discretion by the IRS in sustaining the levy for that year. For 1990 and 1991, the court found no abuse of discretion, as the IRS's determination was based on the settlement agreement terms and was not arbitrary or capricious.

Disposition

The Tax Court denied the Commissioner's motion for summary judgment for the taxable year 1989 and granted summary judgment in Michael's favor for that year. The court granted the Commissioner's motion for summary judgment for the taxable years 1990 and 1991.

Significance/Impact

Michael v. Comm'r clarifies the IRS's authority to enforce tax penalties through levy even after a settlement agreement has been reached. The decision emphasizes the importance of clear settlement terms and the IRS's discretion in collection actions. The case highlights the need for taxpayers to fulfill their obligations under settlement agreements to avoid statutory collection remedies. The decision also underscores the Tax Court's role in reviewing the IRS's determinations for abuse of discretion, particularly when the underlying tax liability is not at issue. The case's doctrinal significance lies in its affirmation of the IRS's ability to adjust assessments and pursue collection based on settlement terms, while also protecting taxpayers from overpayment and abuse of discretion by the IRS.

