

# DEPARTMENT OF JUSTICE

## TAX DIVISION

### DIRECTIVE NO. 116

#### Standards to be Applied in Considering Settlement of Civil Tax Cases

The purpose of this directive is to clarify and modify Tax Division policies and procedures for the settlement of civil cases.

#### BACKGROUND

The Tax Division's Settlement Reference Manual (SRM) provides guidelines under which the Division will settle its civil cases. It currently provides that "compromise is justified only by litigation hazards and collectibility concerns." (SRM at 12.) The SRM, heeding the truism that "hard cases make bad law," also provides that "in evaluating the litigation and settlement posture, equities (as well as precedent) must be taken into account." (*Ibid.*)

The Attorney General has broad authority to litigate and settle cases on behalf of the United States. Article II, § 3 of the Constitution imposes on the President the duty to "take care that the Laws be faithfully executed." The Attorney General has determined that, within this Constitutional limitation and within any specific limitations imposed by Congress, the Department's settlement authority may be exercised in any case "to promote the Government's best interest or to prevent flagrant injustice."<sup>1</sup> The Office of Legal Counsel has opined that, in settling cases under this guideline, the Department "is not bound by each and every statutory limitation and procedural requirement that Congress may have specifically imposed upon some other agency head in the administration of that agency's programs."<sup>2</sup> Nevertheless, our policy with respect to the exercise of discretion in settling cases must be consistent with the will of Congress.<sup>3</sup> Based on the Attorney General's authority, which has been delegated to the Assistant Attorney General in tax matters, the Division has on a few occasions entered into settlements even though the settlement was not justified on litigation and/or collection hazards alone, when it was determined that not to do so would be detrimental to the goal of fostering voluntary compliance with our federal tax laws.

Recently, in the IRS Restructuring and Reform Act of 1998, Congress directed the Secretary of the Treasury to issue guidelines for settling cases, and provided further that, in prescribing these guidelines, the Secretary must take into account "that taxpayers entering into a compromise have an adequate means to provide for basic living

---

<sup>1</sup> 38 U.S. Op. Atty. Gen. 98, 102 (Oct. 2, 1934).

<sup>2</sup> 4B Op. O.L.C. 756, 758 (Sept. 4, 1980).

<sup>3</sup> The Office of Legal Counsel has opined that "Congress' will is surely not irrelevant to the Attorney General's discretion." *Ibid.*

expenses.”<sup>4</sup> In addition, the House Conference Report accompanying the Act states that “the IRS will take into account factors such as equity, hardship, and public policy where a compromise of an individual taxpayer’s income tax liability would promote effective tax administration.”<sup>5</sup> Pursuant to the directive set forth in the 1998 Act, on July 21, 1999, the Secretary issued Temporary Regulations providing that in addition to compromising cases where there is doubt as to liability or doubt as to collectibility, the IRS would compromise cases where to do so would “promote effective tax administration.”<sup>6</sup> Cases falling into this latter category are those in which “[c]ollection of the full liability will create economic hardship,”<sup>7</sup> as well as those in which “exceptional circumstances exist such that collection of the full liability will be detrimental to voluntary compliance by taxpayers.”<sup>8</sup>

## **PURPOSE**

The purpose of this directive is two-fold. First, it clarifies that, consistent with current Tax Division settlement policy and the goal of fostering voluntary compliance with the tax laws, the Tax Division will continue (i) to take equities into account to the extent they pose litigation hazards, and (ii) to take economic hardship into account in collectibility settlements. In addition, Tax Division policy is modified to make explicit that even if settlement would not be justified based upon litigating hazards or collectibility concerns, the Division will take into account whether the litigation of a case will be detrimental to the goal of fostering voluntary compliance with our federal tax laws.

## **DIRECTIVE**

By virtue of the authority vested in me by Part O, Subpart N of Title 28 of the Code of Federal Regulations, particularly Section 0.70, the Tax Division’s policies and procedures with respect to the settlement of civil cases are modified and clarified as follows:

1. The Tax Division will continue to settle cases based on litigation hazards and/or collectibility concerns. When settling cases based upon litigation hazards, the Tax Division, recognizing that hard cases indeed often result in bad law, will continue to consider equities to the extent they pose litigation hazards. When settling cases based upon collectibility concerns, the Tax Division will, as it has in the past, take economic hardship into consideration. Consistent with the Settlement Reference Manual, when entering into collectibility settlements, the Tax Division will seek to ensure that the taxpayer is left with sufficient assets to maintain a reasonable standard of living and an

---

<sup>4</sup> I.R.C. § 7122(c)(2)(A).

<sup>5</sup> H.Conf. Rep. No. 105-599 at 289 (1998).

<sup>6</sup> Treas. Reg. § 301.7122-1T(b)(4).

<sup>7</sup> Treas. Reg. § 301.7122-1T(b)(4)(i).

<sup>8</sup> Treas. Reg. § 301.7122-1T(b)(4)(ii).

income stream sufficient to pay reasonable living expenses. This does not necessarily mean that the taxpayer's present standard of living should be preserved, but only that the taxpayer will be able to maintain a reasonable standard of living.

Because this paragraph merely restates Tax Division's current standards for litigation hazard and collectibility settlements, refer to Tax Division Directive No. 105, to determine where settlement authority lies with respect to such settlements.

2. In making its settlement determinations, the Tax Division also will consider whether litigation of the case will be detrimental to the goal of fostering voluntary compliance with our federal tax laws even though settlement is not justified by litigation hazards or collectibility concerns. Thus, it is contemplated that settlement under this standard will be justified only in those cases where, because of the presence of exceptional or unusual circumstances, collection of the full liability would be detrimental to fostering voluntary compliance by taxpayers.

Consistent with the provisions of Section 8(B) of Tax Division Directive No. 105, in any case in which a settlement is not justified based solely on litigation hazards and/or collectibility concerns, but the chief of the litigation section believes that settlement should be considered at a higher level because litigation of the case may be detrimental to the goal of fostering voluntary compliance with our federal tax laws, the recommendation of the litigation section must be referred through the Office of Review to the appropriate Deputy Assistant Attorney General for final action, unless final action must be taken at a higher-level under the Code of Federal Regulations.

3. Nothing in this Directive shall be construed as altering any provision of Subpart Y of Part O of Title 28 of the Code of Federal Regulations requiring the submission of certain cases to the Associate Attorney General or the Solicitor General.

\_\_\_\_\_  
Date

/s/ \_\_\_\_\_ 12/16/99

Loretta C. Argrett  
Assistant Attorney General