

# **Legal Reference Guide for Revenue Officers**

**Internal Revenue Manual 57(16)**

**February 9, 1990**

(4) For a more complete discussion of the effect of bankruptcy, see the section on bankruptcy in Chapters 900 and (10)00.

### 333.5 (1-14-87) Invalid Seizure

57(16)0

Since the Code limits the period in which taxes may be collected, a levy upon property after the expiration of the statute of limitations is invalid. *United States v. Havner*, 101 Fed. 2d 161 (8th Cir. 1939). In addition, mere notice of intent to levy does not result in actual or constructive possession through seizure. There can be no levy in the absence of service of levy or notice of levy upon the taxpayer or third party. *United States v. O'Dell*, 160 F. 2d 304 (6th Cir. 1947). A levy upon property of a taxpayer before giving notice and demand or before neglect or refusal to pay the tax within 10 days after notice and demand (except in jeopardy cases) is invalid. *Mrizek v. Long*, 187 F. Supp. 830 (N.D. Ill. 1959). A levy made on property of one person to satisfy tax liability of another is invalid. *Maule Industries v. Tomlinson*, 244 F. 2d 897 (5th Cir. 1957). Also, property of a third party in the hands of a taxpayer may not be levied upon to satisfy the taxpayer's liabilities. *Stuart v. Chinese Chamber of Commerce of Phoenix*, 168 F. 2d 709, (9th Cir. 1958). A levy made prior to a final decision of the Tax Court is invalid, unless made pursuant to a jeopardy assessment, as previously discussed. *Dierks v. United States*, 215 F. Supp. 338 (S.D.N.Y. 1963). Finally a levy is not complete in the absence of seizure of the property in question so as to obtain possession (actual or constructive) of such property. *Henkin v. United States*, 229 F. 2d 895 (2d Cir. 1956).

### 333.6 (1-14-87) Erroneous Release of Lien

57(16)0

(1) On occasion, a certificate of release of lien, discharge of property from a lien, or non-attachment of lien may be issued erroneously. IRC 6325(f)(1) provides that in the case of a certificate of release of lien, the certificate shall be conclusive that the tax lien referred to in the certificate is extinguished. In the case of a certificate of discharge, it is provided that such certificate shall be conclusive that the property covered by the certificate is discharged from the tax lien. However, such provisions do not affect the basic tax liability and merely because it is conclusive that the lien upon certain property is extinguished, it is not conclusive that the

tax liability has been satisfied. *Commissioner of Internal Revenue v. Angier Corporation*, 50 F. 2d 887 (1st Cir. 1931), cert. denied, 284 U.S. 673 (1931). The conclusiveness of the extinguishment of the tax lien as to property covered by the issuance of a certificate of release or discharge applies to a third party acquiring an interest in the property formerly subject to such lien. *Brittle v. United States*, 209 F. Supp. 409 (S.D. Cal. 1962). Therefore, levy may be made upon property which was subject to the issuance of an erroneous certificate of release of lien or discharge of property from a lien, provided third parties have not acquired the property in question. As previously discussed in Chapter 200, IRC 6325(f)(2) provides that a certificate of release or non-attachment of lien issued erroneously or improvidently, or pursuant to a collateral agreement entered into in connection with an offer in compromise which has been breached, and the period of limitations on collection after assessment has not expired, such certificate may be revoked and the tax lien reinstated. NOTE: This provision does not apply to the issuance of a certificate of discharge. As of the effective date of reinstatement, a reinstated lien has the same force and effect as a general tax lien which arises upon assessment of a tax liability. Thus, the reinstated lien shall not be valid against any holder of a lien or interest described in IRC 6323(a) until notice thereof has been filed in accordance with the provisions of IRC 6323(f) subsequent to the time the reinstated lien became effective. However, the reinstated lien is subject to the same limitations as the extinguished lien and, absent any extension on collection, the reinstated lien will become unenforceable by reason of lapse of time six years after the date the tax liability was assessed.

(2) To summarize, the right to levy upon property which was subject to the issuance of an erroneous certificate of release of lien or discharge of property from a lien is subject to the intervening rights of third parties in the property in question. However, the effect of IRC 6325(f)(2) is to reinstate the Government's lien priority as of the effective date of reinstatement of the tax lien in the case where it has been extinguished by the issuance of a certificate of release or non-attachment erroneously or improvidently. The reinstated lien shall prime all subsequently arising interests except that it shall not be valid as against any holder of a lien

or interest as described in IRC 6323(a) until notice thereof is duly filed after the time the reinstated lien became effective. Where there is a question as to the extent of the intervening rights, the advice of District Counsel should be sought prior to levy.

**334 (11-15-85) 57(16)0**  
**Notice of Levy**

**334.1 (11-15-85) 57(16)0**  
**General**

The Code does not set forth the manner in which levy is to be made. IRC 6331(b) merely defines the term to include "the power of distraint and seizure by any means." *Treas. Regs. 301.6331-1(a)(1)* states, "levy may be made by serving a notice of levy on any person in possession of, or obligated with respect to property or rights to property subject to levy . . . ."

**334.2 (2-9-80) 57(16)0**  
**Final Demand**

When a notice of levy is served upon a third party and there is no response or a refusal to comply, it is followed by service of a Final Demand (Form 668-C). IRC 6332(a) states that except as otherwise provided in subsection (b), (which contains a special rule for life insurance and endowment contracts) and subsection (c), (which contains a special rule for banks requiring a 21-day delay before payment for the levy is sent, with interest) a person in possession of property or rights to property upon which levy has been made shall, upon demand, surrender such property. IRC 6332(a) permits two defenses for noncompliance; the property or rights to property are not property of the taxpayer and the property is subject to prior judicial attachment or execution. The demand is contained in the Notice of Levy (Form 668-A) and the Notice of Levy on Wages, Salary, and Other Income (Form 668-W). A Notice of Final Demand (Form 668-C) although in general use, is not required to be served under the Code. In the event the Final Demand is not complied with, a suit for failure to honor levy under IRC 6332(d) would be appropriate.

**334.3 (1-14-87) 57(16)0**  
**Seizure**

(1) To effect a levy upon tangible property there must be a seizure of the property levied

upon; that is, the taxpayer's property must be reduced to possession and control (actual or constructive). *United States v. O'Dell* 160 F. 2d 304 (6th Cir. 1947); *Freeman v. Mayer*, 152 F. Supp. 383 (D.N.J. 1957). *aff'd*; 253 F. 2d 295 (3rd Cir. 1958). Seizure would be analogous to levy of execution by a judgment-creditor where the officer must not only have the property in view, but also within his/her power and must exercise such dominion over it as to make him/her a trespasser, except for the protection of legal process. The size, bulk or quantity of property may prevent its removal upon seizure, but sufficient steps must be taken to evidence constructive possession. Property capable of removal, such as an automobile should be removed.

(2) As previously indicated, force should not be used in seizing property of a taxpayer. The same reasoning applies where property has been levied upon and seized and, at some later date, it is sought to remove the levied property to another location or to sell such property. Local or other law enforcement authorities may be contacted to assist the revenue officer in performing his/her duties. Also, resort can be had to the courts to restrain the taxpayer or third party from interfering with such removal or sale.

**334.4 (1-14-87) 57(16)0**  
**Tangibles—Intangibles**

Levying upon and seizing tangible personal property presents few legal as opposed to practical difficulties. Such property is generally capable of being reviewed and physically seized and, if conditions warrant, of being removed for safe keeping pending sale. (Real property is, of course, not susceptible of removal. Thus, posting of a notice of levy along with notification to the owner, tenant or occupant amounts to dominion.) Problems arise with respect to intangibles; e.g., accounts receivable, debts, promissory notes, and stocks, as a few examples. The best approach to a levy and seizure of intangibles is to do everything possible to constructively reduce the intangible to possession. Seizure of everything in taxpayer's place of business, padlocking premises and posting notices of distraint for taxes did not constitute a levy upon certain accounts receivable owing the taxpayer, since no steps were taken "to establish possessory dominion" over any sums owed the taxpayer. *Freeman v. Mayer, supra*. (Service of notice of levy upon the taxpayer's debtors would have been sufficient in this case.) Where

a document represents a right to property (promissory note, stock certificate, negotiable certificate of time deposit) an actual seizure of the document must be made. Service of notice of levy upon the maker of the note, the corporation or the bank is ineffective to reduce the property right to possession. (Money on deposit in a bank represented by a nonnegotiable certificate of deposit in the hands of a delinquent taxpayer is subject to the levy. *Rev. Rul. 73-12, 1973-1 C.B. 601.*)

334.5 (11-15-85)

57(16)0

### Suits Against Third Party

Where a taxpayer has instituted suit against a third party for damages in tort or contract, the right of the taxpayer to satisfaction of any judgment obtained may be levied upon. Service of notice of levy upon the defendant in most cases will amount to constructive seizure of the taxpayer's property rights. However, it is advisable to serve a notice of levy, at both the commencement and conclusion of the litigation, upon the defendant's attorney and the taxpayer-plaintiff's attorney and upon any insurance company, whether named a party defendant or not, or other party who may be contractually obligated to satisfy, in whole or in part, any judgment obtained in the court proceedings.

334.6 (2-9-90)

57(16)0

### Offset

(1) A problem frequently encountered when serving a notice of levy upon a third-party debtor of the taxpayer is the claim of the party served to the right of offset; that is, the third party claims a right to set off against the debt owed the taxpayer a portion of or an amount equal to the indebtedness of the taxpayer to the third party. This asserted right of offset most commonly occurs with banks and, to a lesser degree, the taxpayer's employer, but it is not limited to these. With regard to a bank, the right of offset is effective only if exercised prior to service of the levy. *United States v. Citizens and Southern National Bank*, 538 F.2d 1101 (5th Cir. 1976); *United States v. Sterling Nat'l Bank and Trust Co. of N.Y.*, 494 F. 2d 919 (2nd Cir. 1974); *United States v. First Nat'l Bank of Arizona*, 458 F. 2d 513 (9th Cir. 1972); *Bank of America National Trust and Savings Ass'n v. United States*, 345 F. 2d 624 (9th Cir. 1965), *cert. denied*, 382 U.S. 927 (1965), *rehearing denied*, 382 U.S. 1000 (1966); *Bank of Nevada v. United States*,

251 F. 2d 820 (9th Cir. 1958), *cert. denied*, 356 U.S. 938 (1958). The bank is not entitled to any set-off against the taxpayer's bank account for deposited checks later returned for insufficient funds after being served with a notice of levy, provided the taxpayer and the bank have an agreement that the taxpayer can draw on uncollected funds. *United States v. First Nat'l Bank of Commerce in New Orleans*, 493 F.2d 1228 (5th Cir. 1974). Where the bank's loan to the taxpayer was made before the tax lien arose, set-off cannot be made until the right to do so exists—such as would accrue upon default in payment of a note. Therefore, a notice of levy served before default has preference, since the bank could not have exercised its right of offset.

(2) When the party levied upon is not a bank, however, it may not be necessary that the offset be exercised prior to the service of the notice of levy. The rationale for the distinction is that it can generally be established that the taxpayer enjoys an unqualified right of withdrawal from the funds on deposit with the bank, but a non-bank obligor may claim that even if the taxpayer had demanded payment, it would have claimed its right of offset. For example, commissions earned which are applied by the employer as a credit against an employee's overdrawn account, and expense money advanced under an arrangement in which it must be accounted for by the employee, may be offset by the employer after the service of a notice of levy. *Rev. Rul. 73-365, 1973-2 C.B. 407.*

(3) In the case of *United States v. Graham*; 96 F. Supp. 318 (S.D. Calif. 318), *affirmed sub nom. State of California v. United States*, 195 F. 2d 530 (9th Cir. 1952), *cert. denied*, 344 U.S. 831 (1952), (although a suit to foreclose federal tax liens), the State of California was denied the right to set off against its debt to the taxpayer, taxes owed by the taxpayer to the state, where federal taxes were assessed well in advance of any right of set-off in the State of California.

(4) An insurer was denied the right to set off or deduct from the renewal commissions due to a former employee the expenses and attorney's fees incurred in garnishment proceedings brought by a judgment-creditor of the taxpayer, where the notice of levy was served after the garnishment proceedings, but the federal taxes were already assessed. *Beeghly v. Wilson*, 152 F. Supp. 726 (N.D. Iowa 1957).

(5) In the case of *In re DeKalb Ave. Reconstruction*, 12 N.Y. 2d 1051 (N.Y.C.A. 1963) the court noted that, except as to mortgagees, pledgees, purchasers and judgment-creditors (security interests), the federal tax lien that arises on the date the assessment is made is not dependent upon filing a Notice of Federal Tax Lien. Thus the City of New York could not set off sales taxes due against a condemnation award when federal tax liens arose and attached to property of the taxpayer before the lien for city taxes became perfected, giving rise to the city's right of set-off.

(6) In *Trinity Universal Insurance Co. v. United States*, 382 F. 2d 317 (5th Cir. 1967), cert. denied, 390 U.S. 906 (1968), the court held that when a surety completed performance under its performance bond on a federal contract, it is in effect subrogated to the rights of the United States and therefore had a right to apply the contract retainages to minimize damages flowing from the contractor-taxpayer's breach of contract. Therefore, the United States cannot set off tax claims due from the contractor. *Security Insurance Co. of Hartford v. United States*, 428 F. 2d 838 (Ct. Cl. 1970); *Aetna Casualty and Surety Co. v. United States*, 435 F. 2d 1082 (5th Cir. 1970) (performance and payment bonds); *United States Fidelity & Guaranty Co., 477 F. 2d 567* (9th Cir. 1973) (United States completed performance while surety paid laborers and materialmen). If the surety makes payments only under the payment bond, the United States is entitled to set off tax liabilities of the contractor against retainages under a federal construction contract.

### 334.7 (2-9-90) Third Party

57(16)0

Except as otherwise provided in the case of levies on banks accounts and the cash loan value of life insurance and endowment contracts, when a person is in possession of property or rights to property subject to levy upon which a levy has been made, the person shall, upon demand, surrender the property or rights to property of the taxpayer, except that which is subject to attachment or execution under any judicial process. IRC 6332(a). Although Chapter 400 discusses actions on behalf of the United States to enforce a levy, the following describe the position of a third party upon whom notice of levy is served.

## 334.6

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## 334.8 (2-9-90) Defenses

57(16)0

(1) A person upon whom a levy has been served may refuse to surrender property upon demand if: the person is not in possession of nor obligated with respect to property or rights to property of the taxpayer, or the property or rights to property are subject to prior attachment or execution under any judicial process.

(2) Property is subject to an attachment or execution under any judicial process when, prior to or at the time of service of notice of levy on a third party, the party has already been served with papers from a court notifying him/her that another party has laid claim to whatever property he/she has in his/her possession belonging to the taxpayer. The property is then subject to the jurisdiction and final disposition of the court.

(3) When a taxpayer obtains money through the commission of a crime and state law provides that such money is not the taxpayer's property, the money need not be surrendered by a police property custodian in response to a notice of levy. *United States v. Ortiz*, 140 F. Supp. 355 (S.D.N.Y. 1956). If the money is property of the taxpayer, even though it was obtained through the commission of criminal offenses, the custodian must surrender the money upon levy, except when the sum is in custodia legis. *Simpson v. Thomas*, 271 F. 2d 450 (4th Cir. 1959).

(4) Particularly when dealing with entities as opposed to individuals, be sure that the party having actual possession of the taxpayer's property is served with a notice of levy. A notice of levy addressed to the Chairman, Board of Supervisors of a particular county was held not binding on the county, as to an indebtedness owed to the taxpayer, because the levy was not addressed to either the county or the county supervisors, individually or collectively. Nor was the levy effective as to the chairman because, under state law, only the county treasurer had possession and control of county money. *United States v. Brechtel*, 90 F. 2d 516 (8th Cir. 1937).

(5) Certain property is not subject to levy. However, this does not require a party upon whom a notice of levy is served to determine whether the property in his/her possession belongs to someone other than the taxpayer, nor to determine whether such property is subject to levy. *Determan v. Jenkins*, 111 F. Supp. 604 N.D. Ga. 1953).

(6) A person in possession of a taxpayer's property may not refuse to surrender it in response to a notice of levy on the ground that the statute of limitations on collection of the tax has expired, *United States v. American Exchange Irving Trust Co.*, 43 F. 2d 829, (S.D.N.Y. 1930), that the assessment was untimely, that no notice and demand was made on the taxpayer, nor that a levy was being made before the expiration of 10 days. *Commonwealth Bank v. United States*, 115 F. 2d 327 (6th Cir. 1940). Fear of multiple liability is not justification for refusing to honor a notice of levy, *United States v. Third Nat. Bank & Trust Co.*, 111 F. Supp. 152 (M.D.Pa. 1953), nor is the certain expectancy of a contractual obligation arising from the taxpayer's default grounds for refusing to honor a levy. *United States v. DeCicco*, 170 F. Supp. 394 (S.D.N.Y. 1959). Of course, if a notice of levy is invalid because it is defective and thus, no levy is made, property of rights to property of a taxpayer need not be surrendered. *United States v. O'Dell*, 160 F. 2d 304 (6th Cir. 1947).

**334.9 (2-9-90)**  
**Saved Harmless**

57(16)0

IRC 6332(e) makes it clear that when a person levied upon honors a levy and surrenders to the Government property or rights to property with respect to which the levy is made, he/she is discharged from any obligation or liability to the taxpayer and any other person with respect to the property surrendered. Similarly, when a person becomes personally liable under IRC 6332(d)(1), for failing or refusing to surrender property or rights to property subject to levy, and subsequently pays this liability, he/she, too, is discharged from any obligation or liability to the delinquent taxpayer and any other person with respect to such property or rights to property arising from such payment. IRC 6332(e) further provides that when an insurance company honors a levy with respect to a life insurance or endowment policy, the company is to be discharged to the extent of any obligation or liability, not only with respect to the insured, but also with respect to any beneficiary under the policy. The aforementioned section does not relieve from liability any person who mistakenly surrenders to the United States property or rights to property belonging to a third party. The owners of mistakenly surrendered property may secure the administrative relief provided for in IRC 6343(b) or may bring suit to recover their property under IRC 7426.

**335 (11-15-85)**  
**Interference with Levy**

57(16)0

**335.1 (1-14-87)**  
**General**

57(16)0

In attempting to levy upon property of the taxpayer, a revenue officer may experience difficulty in locating property or rights to property of the taxpayer, as well as interference by the taxpayer or a third party. Such interference may take the form of overt acts committed directly against the revenue officer or attempts to place property beyond the reach of levy through removal or secreting of such property, or the institution of judicial proceedings to restrain the collection of a tax, or attempts to rescue or recover the property after its seizure.

**335.2 (1-14-87)**  
**Officer**

57(16)0

(1) It is a criminal offense to forcibly assault, resist, oppose, impede, intimidate or interfere with any officer of the Internal Revenue Service in the performance of his/her official duties. 18 U.S.C. 111, 114. Commission of the act itself is a crime even though the doer of the act had no knowledge that the person assaulted, resisted, etc. was an officer of the Service. *Bennett v. United States*, 285 F. 2d 567 (5th Cir. 1960), *certiorari denied*, 366 U.S. 911 (1961).

(2) Under IRC 7212, it is a criminal offense, punishable by fine or imprisonment, or both, to endeavor to intimidate or impede, by force or threats of force, any officer or employee of the United States acting in an official capacity. It is also an offense to endeavor to obstruct or impede the due administration of the Internal Revenue Code. "Threats of force", which includes any threatening letter or communication, means threats of bodily harm to a revenue officer or to a member of his family.

(3) Furthermore, any person who "removes, deposits, or conceals" any property subject to levy or who is concerned in such, with intent to defeat the collection of any tax, is guilty of a felony. IRC 7206(4). Thus, where an employer purposely pays a taxpayer in advance to preclude the Government from levying upon the accrued salary of the employee, consideration could be given to a possible violation of this provision of the Code. However, under IRC 7206(4), the burden is upon the Government to prove intent, a necessary element of the of-

fense, and a most difficult burden to sustain. Compare 334.6:(2).

**335.3 (1-14-87)**  
**Rescue**

57(16)0

(1) Once property has been levied upon and seized, attempts may be made by the owner or other party to regain possession of such property. Any person forcibly rescuing, or causing such rescue of seized property, or attempting or endeavoring to do so, shall, under IRC 7212(b) be fined not more than \$500.00, or not more than double the value of the property rescued, whichever is greater, or be imprisoned not more than 2 years. Also, a fine or imprisonment or both is imposed under 18 U.S.C. 2233 against one who "forcibly rescues, dispossess, or attempts to rescue or dispossess any property" taken, detained or seized by any officer under the authority of any revenue law of the United States. The offense of rescuing property consists of the forcible retaking of property out of the hands of an officer who has it in legal custody. It is not necessary that actual violence be committed against the person of the officer (conduct and language may be sufficient). An attempted rescue is an unsuccessful forcible effort to rescue property. *United States v. Ford*, 33 F. 861 (W.D.N.C. 1887). Leaving property in possession of an individual after levy does not justify him/her in taking and disposing of it. Also, rescuing a portion of seized property on the ground that it did not belong to the taxpayer, but to the party making the rescue is an inadequate defense. *T.D. 3747, C.B. IV-2, 220*.

(2) A revenue officer should never employ force to effect a seizure. However, if attacked by the taxpayer or another, and if retreat is impossible, he/she may legally employ sufficient force to protect his/her person. The statutes referred to above have been enacted by the Congress to afford protection to the revenue officer and assist him/her in the performance of his/her duties without resorting to the very conduct condemned by these laws.

**335.4 (1-14-87)**  
**Injunction**

57(16)0

(1) Another means of interfering with levy and seizure of property or rights to property of the taxpayer, though by no means violent, is a court action to enjoin or restrain the collection of a tax. IRC 7421 prohibits a suit to restrain the

collection of any tax except where levy is sought to be made:

(a) during the period a taxpayer may petition the Tax Court;

(b) prior to the Tax Court's decision becoming final, if a Tax Court petition is filed;

(c) prior to the final resolution of a refund suit brought under IRC 6671(b) (100% penalty) (but only if a bond is filed), 6694(c) (tax return preparer penalties), or 6703(c) (abusive shelter promoter penalties, aiding and abetting understatement penalties and frivolous return penalties); or,

(d) where a party has brought a wrongful levy action (IRC 7426(b)) or a suit to review a jeopardy assessment (IRC 7429(b)).

(2) However, this prohibition has been construed not to apply where suit is brought against a purchaser in possession to set aside the Government's sale of seized property if conditions precedent to a levy sale have not been substantially complied with. *Margiotta v. District Director of Internal Revenue*, 214 F. 2d 518 (2nd Cir. 1959). Further, where there are special and extraordinary circumstances combined with the illegality of the tax (failure to give notice of the tax and demand for payment thereof), the collection of which is sought to be restrained, the courts, in the exercise of their equitable powers, will restrain collection of such tax by levy, notwithstanding IRC 7421. *Mrizek v. Long*, 187 F. Supp. 830 (N.D. Ill. 1959). The illegality, however, must be clearly apparent and convincingly established. *Bob Jones University v. Simon*, 416 U.S. 725 (1974); *Commissioner v. "Americans United," Inc.*, 416 U.S. 752 (1974); *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1 (1962). Under certain circumstances, however, the Government may be required to furnish information as to how the liabilities were arrived at. *Commissioner v. Shapiro*, 424 U.S. 614 (1976).

**335.5 (11-15-85)**  
**Replevin**

57(16)0

Generally defined, this is an action to recover possession of goods or chattels wrongfully taken or detained, and such action lies in favor of one entitled to possession. The primary concern of the moving party is to obtain possession of personal property itself rather than sue for damages in tort for trespass or conversion under state law. Where a replevin action is commenced, the seized property is returned to the one entitled to possession (usually upon post-