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Tax Regs in Plain English

# IRS Restructuring and Reform Act of 1998

## 3102 - Civil Damages for Collection Action

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### Section 3102

**A. Provision covered:** Section 3102 Civil Damages for Collection Action (I.R.C. §§ 7433, 7430, 7426)

**B. Background:** Under prior law, taxpayers could recover damages up to \$1,000,000 under section 7433 for reckless or intentional disregard of the Code and regulations. Third parties and debtors in bankruptcy could not recover damages under section 7433. Also, under prior law, there was no exhaustion of administrative remedies requirement, although the courts could reduce the damages award if administrative remedies were not exhausted. Congress believed that expansion of the circumstances in which damages could be obtained from the Service was appropriate.

**C. Change(s):** The provision allows taxpayers to recover up to \$100,000 in damages as the result of the negligent disregard of the Code or regulations by Service personnel. This provision also amends section 7426, regarding actions for wrongful levy, and allows third parties to recover damages up to \$1,000,000 for reckless or intentional disregard of the Code or regulations, or up to \$100,000 for negligent disregard of the Code or regulations. The provision requires that all administrative remedies be exhausted before a suit for damages can be filed.

The provision also allows taxpayers to petition the bankruptcy court for damages up to \$1,000,000 for willful violations of sections 362 (automatic stay) and 524 (discharge

injunction) of the Bankruptcy Code. The provision provides that notwithstanding section 105 of the Bankruptcy Code, section 7433 is the exclusive remedy for damages for willful violations of section 524, whereas section 7433 is not the exclusive remedy for damages for willful violations of section 362. A debtor in bankruptcy may still recover damages for willful violations of section 362 under section 362(h). However, if damages are awarded under section 362(h), administrative and litigation costs may only be awarded as provided by section 7430. Administrative costs for automatic stay violations recoverable under section 7430 are administrative costs incurred on or after the date of filing the bankruptcy petition. This means that for purposes of section 7430(4)(B)(i), "the position of the United States in the proceeding" is judged from the date a bankruptcy petition is filed. "The position of the United States in the proceeding" is not judged from the date an adversary proceeding is commenced. Likewise, while damages for violation of section 524 are recoverable under section 7433 with reference to section 7430, "the position of the United States in the proceeding" is also judged from the date a bankruptcy petition is filed notwithstanding the limitation in section 7430(c)(2) that administrative costs only include costs incurred on or after the date of receipt of the notice of decision by Appeals, or the date of the notice of deficiency. A debtor must exhaust all administrative remedies before petitioning the bankruptcy court for damages under section 7433 for willful violations of the the automatic stay and discharge injunction.

When a taxpayer sues in the bankruptcy court for violations of section 362 and 524, the standard is "willful" not negligent or reckless.

#### **D. Impact**

The Service can expect to see administrative claims and suits by taxpayers and third parties claiming damages under the new negligence standard. The Service can also expect to see administrative claims and suits by debtors for damages under section 7433 for violations of the automatic stay and discharge injunction.

#### **E. Necessary Actions**

1. Actions/Procedures The Internal Revenue Manual and the CCDM will be revised.
2. Things we CAN do: The Service can continue to process administrative claims of taxpayers for damages up to \$1,000,000 caused by the reckless or intentional disregard of the Code and regulations. The Service can also pay administrative claims up to \$100,000 for negligence, and up to \$1,000,000 for willful violations of the Bankruptcy Code provisions.

**F. Other Special Comments:** The administrative remedies for wrongful levy are prescribed in section 6343, which only allows the Service to

1. return the specific property levied upon,
2. return an amount of money equal to the amount of money levied upon, or
3. return an amount of money equal to the amount of money received by the Service from a sale of the property levied upon. Congress has added a new remedy for third parties that allows them to sue for direct economic damages under section 7426. In addition, section 7426, as amended, provides that the rules in section

7433 regarding exhaustion of administrative remedies applies. When a third party files an administrative claim for damages other than those covered by section 6343, the Service may already have the authority to pay such damages under section 7433, where administrative procedures already exist.

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