



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR ASSOCIATE AREA COUNSEL
HEAVY MANUFACTURING, CONSTRUCTION, AND
TRANSPORTATION
CC:LM:MCT:DET

FROM: John J. McGreevy
Assistant to the Branch Chief, Branch 1
Administrative Provisions & Judicial Practice

SUBJECT: TL-N-5198-00

This Chief Counsel Advice responds to your memorandum dated June 8, 2001. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Company	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
Date 7	=
Date 8	=
Date 9	=
Year 1	=
Year 2	=
Year 3	=
Year 4	=
Year 5	=
Year 6	=
Year 7	=

Year 8	=	
Year 9	=	
Year 10	=	
Year 11	=	
Year 12	=	
Year 13	=	
Year 14	=	
Year 15	=	
<u>A</u>	=	\$
<u>B</u>	=	\$
<u>C</u>	=	\$
<u>D</u>	=	\$
<u>E</u>	=	\$
<u>F</u>	=	\$
<u>G</u>	=	\$
<u>H</u>	=	\$
<u>I</u>	=	\$
<u>J</u>	=	\$
<u>K</u>	=	\$
<u>L</u>	=	\$
<u>M</u>	=	\$
<u>X</u>	=	\$
<u>Y</u>	=	\$
<u>Z</u>	=	\$

ISSUES

(1) Whether Company is entitled to overpayment interest on abated deficiency interest before Date 8.

(2) Whether Company may apply overpayment interest as a credit in full payment of a subsequent deficiency arising from a carry back recoupment for the same year and type of tax.

CONCLUSIONS

(1) Company is not entitled to overpayment interest on abated deficiency interest before Date 8.

(2) Company may not apply overpayment interest as a credit in full payment of a subsequent deficiency arising from a carry back recoupment for the same year and type of tax.

FACTS

Issue (1):

Company filed a claim requesting a refund in excess of X regarding an interest computation of its Year 4 tax liability. This recomputation resulted from the Year 15 resolution of a claim involving foreign tax credit carry back from the Year 8 taxable year. The primary basis for Company's claim is that the Internal Revenue Service's ("Service") Year 15 recomputation of its Year 4 tax liability improperly applied credits from Year 4 to Year 1, Year 5, and Year 8 to pay off both the tax and accrued, but unposted deficiency interest.

The origin of this claim was Company's timely filing of its Year 4 federal income tax return, Form 1120, in Year 5 with a tax of Z. The Service is certain that the tax in the amount of Z was timely paid.

As a result of a pending Service adjustment to the Year 4 tax liability, Company made an advance payment totaling M on Date 1. This payment was posted to Company's account and put Company's Year 4 tax module in a credit balance position for the first time. In July and August of Year 11, the Service assessed an additional K of tax and H of deficiency interest. This deficiency interest was posted on Date 1, and the tax was posted on Date 2. After this assessment of tax and deficiency interest, Company's Year 4 tax module had a zero balance.

On Date 5, Company again made an advance payment totaling C, which posted to Company's account on that same date. On Date 6, the Service assessed tax of B and deficiency interest of A for a total of C. At this time, Company's Year 4 tax module was again in zero balance.

In Year 15, the Service reached agreement on Company's refund claim for the Year 4 tax period, which involved carry backs and carry forwards encompassing the Year 1 through Year 10. This claim resulted in a total tax abatement of E for Company's Year 4 tax year. The abatement was a combination of a general tax abatement and the allowance of a Year 5 carry back. At the time of the Year 15 adjustment, the Examination, Support, and Processing Division ("ESP") attempted to correct the "previously assessed" deficiency interest. The "previously assessed" deficiency interest then totaled I. ESP recomputed the "corrected" deficiency interest on the Date 2 deficiency, after reducing by this subsequent E abatement of tax. ESP's recomputed "corrected" deficiency interest totaled F. ESP took the difference of the "previously assessed" and "corrected" interest, and abated D of deficiency interest.

These Year 15 postings left Company's Year 4 tax module with a credit balance of G. No interest was paid on this credit. Instead the credit balance was transferred out of the Year 4 tax module to pay off the debit balances (tax and accrued, but unposted interest) on the Years 1,5,6 and 8 tax modules. The Year 4 credit was transferred out to these other modules using the availability dates of the last payments coming into the Year 4 module.

Both the Service and Company agree that only amounts needed to satisfy tax deficiencies for Years 1,5,6 and 8 should have reduced the G credit balance in the Year 4 tax module. Thus, a credit balance should have remained in Company's Year 4 module as of the module credit availability dates of Dates 1 and 5. However, D of this credit balance represented abated deficiency interest.

Issue (2):

Company filed a refund claim for L pertaining to its Year 12 tax liability. This claim arises from a dispute concerning mechanically when unposted allowable interest can be credited against a debit balance for the same taxable year and the same type of tax. Company asserts it may offset a debit "tax" balance with accrued and unposted allowable interest, as of the date the account goes back into debit balance. The Service asserts that no overpayment can exist until all the liability is satisfied, and thus, unposted allowable interest is not available to satisfy the deficiency.

Company's Year 12 tax module started with a debit balance of J on Date 3. Deficiency interest started running on Date 3, as the Company's Year 12 refund was issued on Date 3. On Date 4, the Year 12 module went into credit balance because of an allowed carry back from Year 13. The adjustment and the associated credit-interest on the Year 13 carry back of Y to Year 12 was not processed by the Service until Date 9.

As a result of the recouped carry back from Year 14, Company's Year 12 module went back into debit balance on Date 7. Company's claim asserts that credit interest for Year 12 accruing for the period it had a credit balance, i.e., Date 4 until Date 7, is available to pay off the debit balance created by the recoupment of the Year 14 carry back. Company's proposed offset puts the module back into a credit balance position, and as a result, no additional deficiency interest would accrue.

LAW AND ANALYSIS

Issue (1):

Section 6611(a) of the Internal Revenue Code states that interest shall be allowed and paid on any overpayment at the overpayment rate established under § 6621. Section 301.6611-1(g) of the Regulations on Procedure and Administration provides that interest shall not run on an overpayment until the date of the overpayment. Interest on a subsequently abated deficiency represents an overpayment and the overpayment date on abated deficiency interest is the date the original payment was made. See, Treas. Reg. § 301.6611-1(c), Examples 1 and 2.

Conversely, pursuant to § 6601(a) of the Code, an underpayment of tax begins to accrue interest from the last date prescribed for payment of the tax without regard to any extensions. Generally, interest on unpaid tax is treated in a similar fashion as

unpaid tax, in accordance with § 6601(e)(1) of the Code. However, no interest shall accrue on unassessed interest before December 31, 1982. See, Treas. Reg. § 301.6611-1(h)(2)(v).

Compensation for the use of money is the principle rationale for charging interest with respect to both overpayments and underpayments. See, Manning v. Seeley Tube & Box Co., 338 U.S. 488 (1950); Avon Products, Inc. v. United States, 588 F.2d 342 (2d Cir. 1978); May Department Stores Co. v. United States, 36 Fed. Cl. 680 (1996). Section 6601(f) of the Code provides for the suspension of interest in certain circumstances:

If any portion of a tax is satisfied by credit of an overpayment, then no interest shall be imposed under this section on the portion of the tax so satisfied for any period during which, if the credit had not been made, interest would have been allowable with respect to such overpayment.

Thus, if an underpayment is satisfied with an overpayment, no interest is imposed on the portion of the underpayment that is satisfied by the offsetting application of the overpayment, for any period during which interest would have accrued on the overpayment had the overpayment been refunded to the taxpayer rather than credited against the underpayment. See, Rev. Proc. 60-17, 1960-2 C.B. 942, 949. Similarly, no overpayment interest is paid to the taxpayer with respect to the offset amount and period. Section 6601(f) precludes imposing underpayment interest during the period interest would have been allowable under section 6611 if the credit had not been made. However, if interest is allowable under section 6611, then section 6601(f) does not preclude imposing interest. Moreover, pursuant to § 6402(a) of the Code, the Service has discretion whether to apply overpayments to underpayments or refund them to the taxpayer. See, Northern States Power Co. v. United States, 73 F.3d 764, 767 (8th Cir. 1996), cert. denied, 117 S.Ct. 168 (1996); Pettibone Corp. v. United States, 34 F.3d 534, 536 (7th Cir. 1994).

Therefore, if Company were to be allowed interest on the overpayment resulting from the D of abated deficiency interest during the offset period running from Date 1 to Date 8, the Service would likewise be permitted deficiency interest on the amount of the underpayment during the offset period. To allow Company overpayment interest without the Service receiving underpayment interest during the same period would violate the principle that interest is meant to compensate for use of the money.

Issue (2):

Company may not apply overpayment interest as a credit in full payment of a subsequent deficiency arising from a carry back recoupment for the same year and type of tax. Section 6402 of the Code provides that the Secretary may credit the amount of any overpayment, including interest allowed thereon, against any tax liability on the part of the person who made the overpayment. As such, it is within the sole

discretion of the Secretary to determine whether Company's overpayment interest may be credited to a subsequent deficiency for the same tax year. See, Northern States Power Co. v. United States, supra.

CASE DEVELOPMENT, HAZARDS, AND OTHER CONSIDERATIONS

The question of whether the use of the money principle can be utilized in the manner described in Issue (1) is not entirely free from doubt and is involved in pending litigation (United States v. St. Joe Minerals Corp., Case No. 4:93CV001380 (E.D. Missouri)). That case is expected to go to trial in November. In addition, it should be noted that if interest is payable and allowable for the disputed period of time, then interest netting under section 6621(d) should be considered.

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Please contact Rob Desilets, Jr. at 202-622-4910 if you have any further questions.