



OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR DISTRICT COUNSEL,

FROM: Assistant Chief Counsel (Field Service)

SUBJECT: Reconsideration of Field Service Advice Previously Issued
Concerning the Computation of Deficiency Interest on the
Taxpayer's Tax Deficiency
Tax Period:

This Field Service Advice responds to your request for further explanation of the conclusion reached in the Field Service Advice issued on November 10, 1998, that interest on the deficiency for Year 1 begins to accrue on the unextended due date of the Year 2 return. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND:

X =

Year 1 =

Year 2 =

Year 3 =

u = \$

v = \$

w = \$

x = \$

ISSUE:

The field attorney has requested further explanation of the Service's position stated in the Field Service Advice dated November 10, 1998, as to when underpayment interest begins to accrue on X's deficiency in tax for Year 1.

CONCLUSION:

It is our understanding that X has not provided any different or additional facts in connection with this issue addressed in the Field Service Advice dated November 10, 1998. Based on the facts provided, the Service's position remains the same as that stated in the initial Field Service Advice provided which concluded that underpayment interest on X's deficiency in tax of \$u for the Year 1 began to accrue on March 15, Year 3, the original due date, without extensions, of X's income tax return for Year 2.

FACTS¹:

We have included in this Field Service Advice the same facts that we were provided in preparing the Field Service Advice dated November 10, 1998. It is our understanding that the taxpayer has not supplemented or otherwise changed the facts since the initial Field Service Advice was provided. On September 15, Year 2, X timely filed, with extension, its Form 1120 (U.S. Corporation Income Tax Return) for Year 1. On its Form 1120 for Year 1, X reported an overpayment of \$v, which X elected to have credited against its liability for estimated tax for Year 2. X did not, however, designate against which installment of estimated tax the overpayment for Year 1 was to be applied. Thus, pursuant to Rev.Rul. 84-58, 1984-1 C.B. 254, the Service credited the overpayment against X's estimated tax for Year 2 as of March 15, Year 2, the due date for X's first installment of estimated tax for Year 2. X's tax liability for Year 2 was less than the amount of the overpayment applied from Year 1, and none of the Year 1 overpayment was needed to avoid the addition to tax imposed under I.R.C. § 6655 for failure to pay any estimated tax due for Year 2. \$w of the overpayment was used to pay X's tax liability for Year 2, which arose in the fourth quarter of Year 2 when there was a sale of an asset which resulted in investment tax credit recapture. X elected to have the balance of the overpayment of \$x credited against its estimated tax for Year 3. According to the facts provided, X has never used the balance of the overpayment from Year 1 against the estimated tax for any subsequent year in

¹The facts recited herein are taken from your Request for Field Service Advice. Inasmuch as we have not verified these facts, we express no opinion on their accuracy.

order to avoid the imposition of the addition to tax imposed under I.R.C. § 6655 for failure to pay estimated tax.

As a result of the audit of X's Year 1, the Service determined that there was a deficiency of \$u for that year which has yet to be assessed pending the resolution of this interest issue. X contends that interest should never begin to accrue on the subsequently determined deficiency for Year 1 since no portion of the Year 1 overpayment was ever used to avoid the imposition of the addition to tax under I.R.C. § 6655 for failure to pay estimated tax.

LAW AND ANALYSIS:

The Service is not changing its position and conclusions reached in the Field Service Advice dated November 10, 1998. Accordingly, the analysis stated in that Field Service Advice is the same and is incorporated by reference herein. Additionally, as noted in the Field Service Advice dated November 10, 1998, in all cases, the overpayment is a payment of the succeeding year's income tax liability no later than the due date (without regard to extensions) of the succeeding year's income tax return. Consequently, to the extent the overpayment is not needed to satisfy specific installments of estimated tax for the succeeding year's estimated tax, interest on the first year's deficiency begins to run from the original unextended due date of the succeeding year's income tax return.

It is the Service's position that the date the overpayment becomes a payment on account of the succeeding year's estimated tax determines the date the prior year's tax became unpaid for purposes of I.R.C. § 6601(a). Prior to that date, the government has had the use of the funds with respect to the prior year's tax, and no interest is payable on the overpayment that is the subject of the taxpayer's election. See I.R.C. § 6402(b); Treas. Reg. § 301.6402-3(a)(5) and § 301.6611-1(h)(2)(vii). Interest should be charged from the point the prior year's tax is both due and unpaid. May Department Stores Co. v. United States, 36 Fed. Cl. 680 (1996), acq. AOD CC-1997-008 (Aug. 4, 1997); Avon Products, Inc. v. United States, 588 F.2d 342 (2d Cir. 1978); Rev. Rul. 88-98, 1988-2 C.B. 356.

Where the overpayment is not needed to satisfy any installment of estimated tax in the succeeding year, the overpayment would be treated as a payment of the succeeding year's income tax. Section 6513(d) provides that if any overpayment of income tax is, in accordance with I.R.C. § 6402(b), claimed as a credit against estimated tax for the succeeding tax year, such amount shall be considered as a payment of income tax for the succeeding taxable year (whether or not claimed as a credit in the return of estimated tax for such succeeding taxable year) and no claim for credit or refund of such overpayment shall be allowed for the taxable year in which the overpayment arises. See also I.R.C. § 6513(a) which provides that a

payment of income tax made before the date prescribed for payment of the tax is considered paid on that date. The date prescribed for payment of tax is the time fixed for filing the return (determined without regard to any extension of time for filing the return). I.R.C. § 6151. Further, it is on this date that the overpayment is treated as a payment for purposes of computing interest on any overpayment of income taxes with respect to the succeeding year under I.R.C. § 6611(a) and (d). Thus, we conclude that the statute requires that an overpayment which the taxpayer elects to credit against estimated tax for the succeeding year must be treated as a payment against the next year's tax liability with an effective date no later than the due date of the next year's return.

In the instant case, no part of the Year 1 return overpayment was needed to avoid the addition to tax for failure to pay estimated income taxes in Year 2. Therefore, interest on the subsequently determined deficiency for Year 1 begins to run from the date on which the return overpayment is applied to the succeeding year's tax liability which is the unextended due date of the succeeding year's income tax return - March 15, Year 3. It is on this date that the Year 1 deficiency became both due and unpaid.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

X has taken that position that the Year 1 overpayment was not used to pay estimated taxes for Year 2, and therefore, the Government had full use of the Year 1 overpayment during all of Year 2. X makes the statement in its request for reconsideration that there was no tax liability for Year 2, when, in fact, there was a tax liability for Year 2. As noted herein, even though the Year 1 overpayment is not used to pay the estimated taxes for Year 2, the overpayment is still considered as payment of the Year 2 tax liability and thus deemed paid as of the due date (without extensions) of the Year 2 tax return. X's position is based on an analysis that the Government had full use of the Year 1 overpayment during all of Year 2, and under a use of funds analysis, interest should not begin to run until there is an actual application of the overpayment to pay estimated taxes. [REDACTED]

[REDACTED]

Based on the foregoing, we still recommend that the Service calculate the interest due for the underpayment of the assessed tax deficiency for X's Year 1 from March 15, Year 3. If you have any questions please call .

DEBORAH A. BUTLER
Assistant Chief Counsel
(Field Service)

By: _____
SARA M. COE
Chief, Procedural Branch
Field Service Division

cc: Regional Counsel (Southeast)
Southeast Assistant Regional Counsel (TL)