



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

MEMORANDUM FOR JAMES C. LANNING
ASSISTANT REGIONAL COUNSEL (LARGE CASE) ,
MIDSTATES REGION, CHICAGO, ILLINOIS
CC:MSR:POD:CHI:LC

FROM: Deborah A. Butler
Assistant Chief Counsel (Field Service) CC:DOM:FS

SUBJECT: Crediting pre-merger overpayments of consolidated group

This Field Service Advice responds to your memorandum dated January 6, 2000. 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

GROUP A	A1	
and subsidiaries		TIN:
	A2	subsidiary of A1
	A3	other subsidiaries of A1 that were members of GROUP A during YEAR 2 through YEAR 4

GROUP B

and subsidiaries

B1

TIN:

B2

subsidiary of B1

B3

other subsidiaries of B1 that were members of GROUP B prior to DATE A

Representative(s):

YEAR 1

YEAR 2

YEAR 3

YEAR 4

YEAR 5

YEAR 6

YEAR 7

YEAR 8

YEAR 9

DATE A

DATE B

ISSUES

1. Whether tax overpayments for the pre-acquisition years of a consolidated group (GROUP A) may be credited against outstanding tax liabilities for post-acquisition years of the consolidated group (GROUP B) into which the corporate members of the GROUP A were merged, if GROUP A's corporate parent and some GROUP A subsidiaries were liquidated or otherwise ceased to exist after the merger.
 - A. Who is liable for the payment of GROUP B's liabilities for the post-acquisition years?
 - B. Who is entitled to claim and receive a refund of the overpayment of GROUP A's overpayment for the pre-acquisition years?
2. Whether, for purposes of computing interest on equivalent overpayments and underpayments of tax under section 6621(d), the above-referenced overpayments and underpayments are "of the same taxpayer."

CONCLUSIONS

On the facts presented, tax overpayments made by members of GROUP A may be credited, upon a request made on behalf of all former members of GROUP A, against outstanding tax liabilities of GROUP B under section 6402(a). If such credits are made, interest on the overpayments and on the underpayments of tax satisfied by the credits may be computed under section 6611(b)(1) and section 6601(f), respectively. Since a request for interest netting is not appropriate on the facts presented, we are not opining whether corresponding and equivalent overpayments and underpayments by the members of two consolidated groups, one of which was merged into the other, are liabilities of “the same taxpayer” for purposes of interest netting under section 6621(d).

FACTS

GROUP A is an affiliated group of corporations that, pursuant to the authority in section 1502, filed consolidated income tax returns for YEAR 1 through YEAR 5. A1 is the parent of GROUP A and used its TIN to file the GROUP A returns. The subsidiaries of A1 whose income was included on the consolidated returns filed by A1 for GROUP A are designated as A2 and A3.

GROUP B is an affiliated group of corporations that, pursuant to the authority in section 1502, filed consolidated income tax returns for YEAR 1 through YEAR 9. B1 is the parent of GROUP B. The subsidiaries of B1 whose income was included on the consolidated returns filed by B1 for GROUP B for years prior to YEAR 6 are designated as B2 and B3.

In a single transaction on DATE A during YEAR 6, B1 acquired (either directly or indirectly through B2 and B3) 100% of the stock of A1. As a result, A1 and its subsidiaries A2 and A3 all became subsidiaries of B1 and members of GROUP B for the tax years following the acquisition. A1 filed a final short year income tax return for GROUP A with the year ending DATE A. B1 filed an income tax return for GROUP B, including the new members from GROUP A, for YEAR 6.

On December 31, YEAR 6, A1 was liquidated pursuant to sections 332 and 334(b)(2). On DATE B during YEAR 7, A2 was merged into B2. Through YEAR 9 and the present, some of the former members of GROUP A continue to exist as a subsidiary of B1 or its subsidiaries, and as a member of GROUP B. Other subsidiaries in GROUP A that were acquired by GROUP B have been sold or spun-off, and therefore ceased to be members of GROUP B. B1 filed consolidated income tax returns for GROUP B for YEAR 7 through YEAR 9.

With respect to tax liabilities either collected by or due from GROUP A, A1 was the primary contact between the members GROUP A and the Service until it was

dissolved at the end of YEAR 6. After A1 was dissolved, B1 began acting on behalf of GROUP A in contacts with the Service.

The Service has recently agreed to adjust the income tax liabilities of GROUP A and GROUP B for YEAR 1 through YEAR 9. GROUP B is liable for income tax deficiencies for YEAR 8 and YEAR 9. Although GROUP B has overpaid its net tax liability for YEAR 1 through YEAR 7 and these overpayments may be credited against the outstanding liabilities of GROUP B for YEAR 8 and YEAR 9, the crediting of these overpayments is not sufficient to satisfy GROUP B's unpaid tax balances for YEAR 8 and YEAR 9.

GROUP A has tax overpayments for YEAR 2, YEAR 3, and YEAR 4, but has a small tax deficiency for the short year ending DATE A. For YEAR 1 through YEAR 5 and the short year ending DATE A, GROUP A has a net overpayment of tax. The tax abatements that created the overpayments for GROUP A's YEAR 2, YEAR 3, and YEAR 4 are attributable to "items" carried back or forward from other tax years that ended before DATE A. All of these carryback and carryforward adjustments are attributable to A2.

For interest computation purposes, B1, acting on behalf of GROUP B, has asked the Service to apply the net overpayments of GROUP A's tax liability for YEAR 1 through YEAR 5 against the outstanding tax liability of GROUP B for YEAR 8 and YEAR 9.

LAW AND ANALYSIS

1. Credits under section 6402

We first address the request as one for the crediting of interest under section 6402(a). In enacting section 6621(d), Congress has indicated that in situations in which interest is both payable and allowable by the same taxpayer for the same period, the Secretary will take all reasonable steps to offset the liabilities, rather than process them separately using the net interest rate of zero under section 6621(d). See H.R. Conf. Rep. No. 599, 105th Cong. 2d Sess. 257 (1998). Accordingly, the authorization for crediting overpayments under section 6402(a) is the relevant statutory authorization with respect to these facts.

Section 6402(a) authorizes the Service, in lieu of refunding an overpayment of tax to a taxpayer, to credit an overpayment against any existing liabilities "on the part of the person who made the overpayment." Thus, whenever an overpayment of tax is determined and another tax liability of the person who made the overpayment remains unpaid, the Service has the option of refunding the overpayment or of crediting the outstanding overpayment against the outstanding underpayment pursuant to section 6402(a). Northern States Power Co. v. United States, 73 F.3d

764, 767 (8th Cir. 1996); Pettibone Corp. v. United States, 34 F.3d 536, 538 (7th Cir. 1994). See also Treas. Reg. § 301.6402-1.

When overpayments are credited against outstanding liabilities, interest is accrued on either the overpayment or the underpayment satisfied by the credit only until the date on which the two amounts simultaneously exist. When an overpayment is credited against another tax liability of the same taxpayer, section 6611(b)(1) provides that interest is to be allowed and paid on the overpayment “from the date of the overpayment to the due date of the amount against which the credit is taken.” For underpayments satisfied by a credited overpayment, section 6601(f) parallels section 6611(b)(1) by providing that “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.”

In contrast, interest continues to accrue independently during an overlapping period on both the overpayments and underpayments if a section 6402(a) credit is not made. Section 6611(b)(2) allows interest on refunds from the date the overpayment arises until a date preceding the date of a refund check by no more than 30 days. With respect to underpayment of tax, section 6601(a) provides that interest on an underpayment of tax that is not paid on or before the last date prescribed for payment accrues from the prescribed payment date until the date on which the tax is paid.

If a taxpayer has an underpayment of tax from one year and an overpayment of tax from a different year that are outstanding at the same time, the taxpayer usually benefits by having the interest on simultaneously existing underpayments and overpayments computed, whenever possible, using the section 6402(a) credit process. Because the overpayment interest rates imposed under section 6621(a)(1) between January 1, 1987 and December 31, 1998 were lower than the underpayment interest rates imposed under section 6621(a)(2) during that period,¹ taxpayers benefit by having interest computed on simultaneously existing overpayments and underpayments for the shortest period possible.

The relevant criteria for using the credit is that section 6402(a) only authorizes the Service to credit an overpayment against any existing liabilities “on the part of the person who made the overpayment.” Thus, it is necessary to determine, first, which

¹ Section 3302(a) of the IRS Restructuring and Reform Act of 1998 (RRA), Pub.L. No. 105-206, 112 Stat. 741, increased the overpayment interest rate under section 6621(a) to equal the underpayment rate for non-corporate taxpayers for the second and succeeding calendar quarters beginning after the July 22, 1998 effective date of the Act.

person or persons are liable for the payment of an outstanding liability and, second, whether such person or persons “made [an] overpayment” of tax than can be credited in payment of the liability.

A. GROUP B’s tax liabilities

Under section 7701(a)(1), a person is to “be construed to mean and include an individual, a trust, estate, partnership, association, company or corporation.” A consolidated group is not a person, but each corporate member of the group is a separate person. Generally, a member of a consolidated group is severally liable for the income tax liability of the group. See Treas. Reg. § 1.1502-6(a). When a tax is severally owed by two or more taxpayers, the Service has the authority to collect the full amount of the unpaid tax from any of the liable taxpayers. See U.S. Life Title Insurance Company of Dallas v. United States, 784 F.2d 1238, 1243 (5th Cir. 1986)(applying several liability of responsible persons under section 6672).

In this case, GROUP B includes at least one subsidiary, A3, that was a member of GROUP A during YEAR 2 through YEAR 4 and a member of GROUP B during YEAR 8 and YEAR 9. As a member of GROUP B during YEAR 8 and YEAR 9, A3 is severally liable for the underpayment of GROUP B’s tax for those years. The Service would be authorized to collect the unpaid tax from A3 or any other member of GROUP B included in filing the group’s consolidated returns for YEAR 8 and YEAR 9.²

B. GROUP A’s overpayments

The issue of determining who made the tax payments that gave rise to GROUP A’s tax overpayments for YEAR 2 through YEAR 4 is more difficult. A3, as a member of GROUP A during YEAR 2 through YEAR 4, can be viewed, along with the other GROUP A members during those years (and their successors) as having made the overpayments that are to be credited or refunded under section 6402(a).

Because the payments were collectively made by the consolidated group, however, they cannot be readily allocated among members of the group. The Service does not keep records of which member of a consolidated group actually made any payments of a consolidated group’s tax liabilities, but records the payments as being made on an account for each taxable period of the group using the TIN of the group’s parent. Thus, payments of GROUP A’s tax liabilities for YEAR 2 through

² Treas. Reg. § 1.1502-77(a) adds the procedural requirement that “any levy, any notice of a lien, or any other proceeding to collect the amount of any [consolidated group] assessment, after the assessment has been made, will name the corporation from which such collection is to be made.”

YEAR 4 would have been recorded as payments by the group on a single account under A1's TIN.

Nothing in the statute or regulations governing consolidated returns requires the Service to make such allocations. Section 1501 gives groups of corporations the privilege of filing consolidated returns and section 1502 gives the Service the authority to prescribe regulations that it deems necessary for returning, determining, computing, assessing, collecting, and adjusting a consolidated group's tax liability. As part of these regulations, in Treas. Reg. § 1.1502-77(a), the common parent of a consolidated group is designated as "the sole agent for each subsidiary in the group, duly authorized to act in its own name in all matters relating to the tax liability for the consolidated return year."

The usual practice of making payments, as we understand it, is for the common parent of a consolidated group to make a collective payment or payments on behalf of the group, and then to allocate the liability among the group, using accounting adjustments or transferring payments among the group members. Sometimes group members make their own cash deposits, but the Service does not track the source of the deposits.

Under routine circumstances, the Service has no need to allocate the source of payments among the members of a consolidated group. If the Service determines that an overpayment of the taxes paid by the consolidated group is to be refunded to the group, the Service would mail a single payment to the parent of the group. Likewise any credits under section 6402(a) would be made to the consolidated group's income tax accounts maintained in the name of the common parent. As provided in Treas. Reg. § 1.1502-77(a):

The common parent will file claims for the refund of or credit, and any refund will be made directly to and in the name of the common parent and will discharge any liability of the Government in respect thereof to any such subsidiary. . . .³

Treas. Reg. § 1.1502-77(a) also discusses the effect of consolidated group members ceasing to be members of the group in later years:

³ Treas. Reg. §§ 1.1502-78, 1.1502-79, 1.1502-79A provides separate instructions for claiming the carryback of net operating losses, net capital losses and other tax items that may affect more than one tax year and the allocation of these items among the members of a consolidated group. Since the adjustments to A2's loss "items" in this case all originate in and are carried to years for which A2 was a member of GROUP A, we need not consider those provisions.

The provisions of this paragraph shall apply whether or not a consolidated return is made for any subsequent year, and whether or not one or more subsidiaries have become or ceased to be members of the group at any time. . . .

The Service has also acted to provide a remedy if the common parent designated by the regulation to act as the agent for the group dissolves (as in this case). Treas. Reg. § 1.1502-77(d) provides:

If the common parent corporation contemplates dissolution, or is about to be dissolved, or if for any other reason its existence is about to terminate, it shall forthwith notify the district director with whom the consolidated return is filed of such fact and designate, subject to the approval of such district director, another member to act as agent in its place to the same extent and subject to the same conditions and limitations as are applicable to the common parent. If the notice thus required is not given by the common parent, or the designation is not approved by the district director, the remaining members may, subject to the approval of the district director, designate another member to act as such agent, and notice of such designation shall be given to the district director. Until a notice in writing designating a new agent has been approved by such district director, . . . if such district director has reason to believe that the existence of the common parent has terminated, he may, if he deems it advisable, deal directly with any member in respect of its liability.

Thus, whereas the regulations provide that the parent of a consolidated group is the person authorized to file a claim for refund or credit, we believe that the member of the consolidated group designated to replace a dissolved parent under Treas. Reg. § 1.1502-77(d) is the appropriate person to claim to credit of any overpayment.

In this case, however, it appears that no member of GROUP A has been designated to act on behalf of the group in claiming a credit or a refund. With some members of GROUP A (such as A1) having been dissolved, some members of GROUP A (such as A2) having been merged into other corporations in GROUP B, some members of GROUP A continuing to exist as members of GROUP B, and other members of GROUP A having been sold or spun-off to shareholders, the Service cannot readily determine which former members of GROUP A are entitled to claim the refund or credit of the overpayments for YEAR 2 through YEAR 4 or to share in the allocation of such refund or credit.

We understand, however, that Congress intends that the Service not take a restrictive view in crediting amounts under section 6402(a). Therefore, in order to honor the Congressional intent by allowing common members of GROUP A and

GROUP B to have GROUP A's overpayments credited against GROUP B'S outstanding liabilities, we would allow GROUP A's overpayment credited against the outstanding liability of GROUP B under section 6402(a) if a properly designated representative of GROUP A made a claim for such credit. To protect the Service against potential duplicate claims by members of GROUP A (and their successors), we recommend that the Service secure a closing agreement executed on behalf of B1 and a corporation properly designated to represent GROUP A under Treas. Reg. § 1.1502-77(d) before processing the credit.

Since A1 ceased to exist without designating a new agent to act for GROUP A, the members of GROUP A that continue to exist must designate one of the remaining members to act for GROUP A. Accordingly, each member of (and each successor to any member that has been merged or otherwise succeeded) must designate one remaining corporate member of GROUP A to act as agent for GROUP A for the YEAR 2 through YEAR 5. Each written designation should indicate the name and TIN of the consolidated group (GROUP A), the consolidated years for which the designated agent is authorized to act as agent, and the name, current address, and TIN for the corporation being designated to serve as agent. Each written designation request must be signed by an officer of the corporation making the request. Requests made by successors of former members of GROUP A must identify the member of GROUP A on whose behalf the request is being made and the relationship between the corporation making the request and the member of GROUP A.

Once a representative for GROUP A is properly designated, an officer of the designated representative of GROUP A should sign a claim by the designated representative on behalf of GROUP A to have the GROUP A overpayments credited to the GROUP B liabilities. The claim should be explicit.

The GROUP A representative and B1 should then execute a closing agreement that explains the basis for the credit and specifying that the overpayments otherwise refundable to GROUP A for YEAR 2 through YEAR 4, or its former members is being credited under section 6402(a) in payment of the outstanding tax liabilities of GROUP B for YEAR 8 and YEAR 9 because a specified corporation (or corporations) were members of GROUP A during YEAR 2 through YEAR 4 and were severally liable for the payment of GROUP B taxes as members of GROUP B for YEAR 8 and YEAR 9.

Crediting the refund subject to these conditions should serve to discharge the Service's liability to each member of GROUP A for crediting or refunding the overpayments for YEAR 2 through YEAR 4 pursuant to Treas. Reg. 1.1502-77. The Service should not make the credit if any one or more of the former members of GROUP A, or their successors, refuse to designate a single former member of

GROUP A to act as the designated representative of the group or claims the right to the refunds of the GROUP A overpayments.

2. Determination of “same taxpayer” under section 6621(d)

As effective for periods beginning after July 22, 1998, section 6621(d) provides for a net interest rate of zero to the extent of overlapping tax underpayments and overpayments by the “same taxpayer.” The statute, as enacted by section 3301 of the RRA, and amended by section 4402(d) of the Tax and Trade Relief Extension Act of 1998 (TTREA), Pub. L. No. 105-277, 112 Stat. 2681, provides:

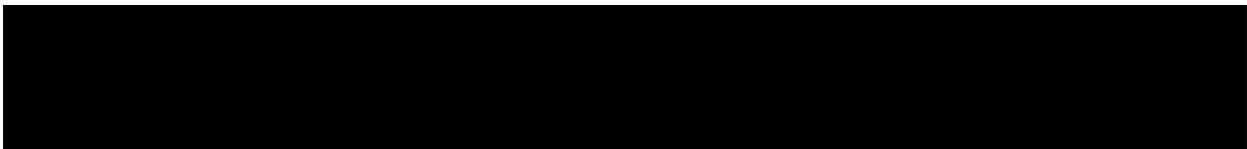
To the extent that, for any period, interest is payable under subchapter A and allowable under subchapter B on equivalent underpayments and overpayments by the same taxpayer of tax imposed by this title, the net rate of interest under this section on such amounts shall be zero for such period.

In limited circumstances, the statute will also apply to periods beginning before the effective date if the applicable statute of limitations has not expired with regard to either the tax underpayment or overpayment, and the taxpayer reasonably identifies and establishes the overlapping period for which the zero rate applies and files a timely request. See Rev. Proc. 99-43 (issued November 22, 1999), 1999-47 I.R.B. 579, for guidance on making a timely request.

As noted above, to the extent that the Service can credit overpayments against outstanding underpayments of the person who made the overpayment, section 6621(d) is inapplicable. The Service may credit the overpayments against outstanding liabilities under section 6402.

You have not advised us of any previously made refunds and payments that might bring section 6621(d) into play. Without specific facts to address, we have not determined whether underpayments and overpayments by consolidated groups that share some, but not all, common members, are the “same taxpayer.” We do note, however, that the legislative history of section 6621(d) indicates that the zero interest rate applies in those circumstances where the Service would normally offset if the underpayments and overpayments were currently outstanding. H.R. Conf. Rep. No. 599, 105th Cong., 2d Sess. 257 (1998).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS





Please call if you have any further questions.

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By: _____
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