INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM
May 22, 2001

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CASE MIS No.: TAM-104232-01/CC:PA:APJP:B1

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification
Years Involved:

LEGEND: X =
Date 1 =
Date 2 =
Year 1 =
Year 2 =
Year 3=
Year 4 =
Year 5 =
Year 6 =

ISSUE:

Under what circumstances, if any, a taxpayer's designation of a remittance as a payment of tax is to be respected when such remittance is made prior to the issuance of a revenue agent's or examiner's report.

CONCLUSION:

A remittance clearly evincing the taxpayer's intention that it be designated as a payment of tax will be respected when made in response to written notification that the Service plans to propose a liability.

FACTS:

X's return for tax year 1 was audited in year 6. During the course of the audit X cooperated with the Service, requesting in return that the audit be completed promptly. Early in the audit process the Service raised an industry specific issue, which the parties discussed in depth over the course of the next several months. X subsequently retained counsel to advise it with respect to that issue and others likely to arise out of the audit.

With regard to the industry specific issue, the revenue agent advised X's counsel that the Service's position was that X had employed an "unacceptable" methodology. The following week the first of many meetings between X, X's counsel and the Service was held. At that time the Examination Division advised X that it would seek Technical Advice on the issue. With only a few days remaining before the expiration of the statute of limitations, X consented to the Service's request to extend the statute. X did so with the understanding that the timing of the completion of the audit would be such that it would have 6 months within which to take the issue to Appeals, if necessary.

Over the ensuing months the parties worked to try and resolve their disagreements over the issue, including meeting in the National Office for a pre-submission conference with regard to the Technical Advice request.

While X had arranged to pay the year 1 expected deficiency at the end of year 6, (the year it had been anticipated that the audit would close), it became apparent that the audit would not close by year end and that the Service would be asserting a deficiency. In a letter dated two days after the pre-submission conference, the revenue agent advised X of "certain adjustments we intend to propose as a result of our examination of Form 1120 for X for the year 1 tax year... [W]e believe the issues identified in year 1 are recurring issues, and intend to treat these items consistently in year 2 and year 3."

In response, X submitted a check for each of the three taxable years. Accompanying each remittance was a letter stating the amount of the check, "relating to taxes that the IRS agent has told us will result from the current examination of X's" return." After specifically referencing Rev. Proc. 84-58, each letter specified the amount to be applied as TC 640 advance payment of tax and the portion to be designated as TC 680 payment of interest.

By letter dated Date 2, the Service informed X that the monies were being applied to its account as a cash bond.

LAW AND ANALYSIS:

An assessment of tax, the formal recording of a tax liability by the Service, is distinguishable from the posting of a remittance to a taxpayer's account. The formal legal act of assessment can take place with or without the receipt of funds by the Service. For example, pursuant to section 6201(a)(1) the Service may immediately assess taxes shown owing on a return regardless of whether the payment of the tax accompanies the return. A posting can take place with or without an assessment.

Remittances of funds by taxpayers can be characterized as either "payments of tax" or "deposits in the nature of a cash bond" and the distinction between the two is more than semantics; the consequences can, under certain circumstances, be significant.

The provisions of section 6511 present the first set of these practical implications. Section 6511(b)(1) provides that the Service may not allow or make a credit or refund of tax after the expiration of the period of limitations prescribed in section 6511(a) unless a claim for such credit or refund was filed within the statutorily prescribed time. Pursuant to section 6511(a), such claim for credit or refund must be filed within three years of the time the return was filed or two years from the time the tax was paid, whichever is later. Furthermore, the amount payable to the taxpayer is subject to the limitations of section 6511(b)(2)(A) and (B). Pursuant to section 6511(b)(2)(A) if the claim for refund was filed within the three-year period, the amount payable to the taxpayer is limited to the tax paid during the three years immediately preceding the filing of the claim (plus the period of any extension of time for filing the return). The amount of the credit or refund for claims not filed within three years of the filing of the return is limited under section 6511(b)(2)(B) to the portion of the tax paid during the two years immediately preceding the filing of the claim. These limitation periods cannot be waived. United States v. Dalm, 494 U.S. 596, 602 (1990).

However, section 6511 only applies to payments of tax. Rosenman v. United States, 323 U.S. 658, 661-62 (1945). Accordingly, any remittance other than a payment of tax may be returned to the taxpayer even if the taxpayer did not request its return within the time prescribed in section 6511. Id. at 661-62.

The other significant distinction regards interest. While both a payment and a deposit will stop the running of interest on taxes due, a tax payment earns interest if it is eventually returned to the taxpayer whereas, a deposit does not.

Generally, a remittance is not regarded as a payment of tax until the taxpayer intends that the remittance satisfy what the taxpayer regards as an existing tax liability. An assessment however is not a condition precedent to a remittance being characterized as a payment of tax. Where there is a concomitant recognition of a tax obligation by the taxpayer, a remittance is a payment of tax regardless of whether or not the tax has been assessed. Baral v. United States, 528 U.S. 431 (2000).

Recognizing the potential importance of the characterization, Revenue Procedure 84-58 provides procedures for taxpayers to make remittances in order to stop the running of interest with respect to a proposed deficiency. Section 4.03, subparagraph 1 of Rev. Proc. 84-58 advises:

> [A] remittance not specifically designated as a deposit in the nature of a cash bond will be treated as a payment of tax if it is made in response to a proposed liability, for example, as proposed in a revenue agent's or examiner's report, and remittance in full of the proposed liability is made. A partial remittance will not be treated as a partial payment of tax unless the taxpayer specifically designates what portion of the proposed liability the taxpayer intends to satisfy.

Section 4.04, subparagraph 1 of Rev. Proc. 84-58 instructs:

> Any undesignated remittance not described in section 4.03 made before the liability is proposed to the taxpayer in writing (e.g., before the issuance of a revenue agent's or examiner's report), will be treated by the Service as a deposit in the nature of a cash bond. Such a deposit is not subject to a claim for credit or refund and the excess of the deposit over the liability ultimately determined to be due will not bear interest under section 6611 of the Code.

As X's intention was made manifest in the letter accompanying the remittance, section 4.04 is inapplicable. Therefore, the question here is whether X's intention should be honored when it was made in the absence of a revenue agent's or examiner's report. Or more specifically, what constitutes a "proposed liability" for purposes of section 4.03 of the revenue procedure.

The revenue procedure cites a revenue agent's or examiner's report as an illustration of a proposed liability. While illustrative, a revenue agent's or examiner's report are intended as examples, not an exclusive list, of remittances made in response to a proposed liability. For example, Rev. Proc. 84-58 does not mention remittances accompanying Forms 4868, yet such remittances have been held to be payments of tax as a matter of law. See e.g., Gabelman v. Commissioner, 86 F.3d 609 (6th Cir. 1996), aff'g T.C. Memo. 1993-592. Indeed, the Service's position was made clear when it issued a nonacquiescence in response to Risman v. Commissioner, 100 T.C. 91 (1993), AOD CC-1997-006 (May 5, 1997) wherein the court held that such a remittance was a deposit under a facts and circumstances analysis.

Had X's remittance been made pursuant to receipt of a Form 5701, Notice of Proposed Adjustment, there would be little controversy that X's expressed designation should be respected. See Announcement 86-114, 1986-47 I.R.B. 46. While the revenue agent did not utilize Form 5701 when notifying X of the proposed adjustment, the correspondence echoes the language of that form and provides substantially all the same information. Accordingly, we find little basis upon which to accept that a Form 5701 constitutes a "proposed liability" but a letter providing a taxpayer sufficient information to reasonably calculate the deficiency to be asserted for a given tax year does not. Where, as here, a taxpayer receives written notification that the Service proposes to adjust its tax liability and the taxpayer unambiguously designates the remittance as a payment of tax, such designation falls within the purview of section 4.03 of the revenue procedure.

Limiting the ability to designate a remittance as a payment of tax to the examples of a "proposed liability" in the revenue procedure not only defeats the stated purpose of Rev. Proc. 84-58, but is contrary to supplemental published guidance. The Service

recognizing the inherent flexibility of the revenue procedure used Rev. Proc. 84-58 to address unique circumstances created by a change in the law. With the enactment of the Tax Reform Act of 1986, interest on most deficiencies of non-corporate taxpayers would no longer be deductible but was to be treated as nondeductible "personal interest." In order to assist taxpayers who wished to pay actual or contested tax deficiencies in order to deduct the interest paid on their 1986 returns, the Service issued Announcement 86-108, 1986-45 I.R.B.20, interpreting and expanding Rev. Proc. 84-58. The announcement explained that taxpayers with returns under examination might not know before the end of 1986 whether the revenue agent would be proposing deficiencies. Taxpayers were advised to estimate the amount they believed would be proposed and to file an amended return reflecting such amount for in the year in question. Indeed, the fourth category of taxpayers identified as "wishing to make payments of contested or potentially contested deficiencies" included "taxpayers who have not received the final results of a pending examination of their returns by the Service." See also, supplementary Announcement 86-114 providing similar guidance to partnerships and S corporations items.

While recognizing the potential dangers of ambiguous remittances[1], we conclude that when the Service sends written notification to a taxpayer that it plans to propose a liability, either stating the amount or providing sufficient information from which the amount can be reasonably calculated, a remittance clearly evincing the taxpayer's intention to have it treated as a payment of tax is to be respected pursuant to section 4.03 of the Rev. Proc. 84-58.

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

[1]See e.g., New York Life Insurance Co. v. United States, 118 F.3d 1553 (Fed. Cir. 1997).