

Notice

CC-2004-035 (Reissue)

September 16, 2004

Subject: Inclusion of Interest in Overpayment Decision Documents
Cancel Date: Upon incorporation into CCDM

Purpose

This Notice advises Counsel attorneys that assessed and unassessed underpayment interest should be taken into account when preparing overpayment decision documents and stipulations in light of Estate of Smith v. Commissioner, 123 T.C. No. 2 (July 13, 2004).

Background

When preparing decision documents, the Service has followed a long-standing practice of not reducing the amount of an overpayment by the amount of any unpaid underpayment interest. The Service adopted this practice because the Tax Court lacks jurisdiction over the determination of interest except in certain limited circumstances.

In Estate of Smith, the Tax Court entered a decision for an overpayment of estate tax of \$238,847.24, based on the parties' agreed Rule 155 computations. The court sustained the Service's determination of deficiency, but in an amount less than that determined by the Commissioner. Advance payments of the deficiency and interest were made after the petition was filed, but the payments did not satisfy the assessed liability in full. Subsequent to the determination of the deficiency by the court, extensive additional proceedings occurred, and a number of years passed before the parties were able to prepare a Rule 155 computation. When the parties finally completed the Rule 155 computation, there was outstanding underpayment interest on the deficiency determined by the court, although the taxpayer had overpaid the amount of tax. The agreed Rule 155 computation showed the amount of unpaid underpayment interest but did not include it in the computation of the amount of the overpayment to be shown on the decision document submitted to the court. In accordance with Service practice, the decision document did not reduce the overpayment by the amount of the underpayment interest. The court adopted the decision document as submitted when entering its decision. The Service later offset a portion of the overpayment by the underpayment

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interest. After the decision became final, petitioner filed a motion under T.C. Rule 260 to enforce the court's overpayment determination.

In a reviewed opinion, the court granted the petitioner's motion and held that an overpayment is the amount by which payments exceed the tax and interest for the period of overpayment because, for purposes of determining an overpayment, the term "tax" includes underpayment interest. The court further held that the Service should not have reduced the amount of the refund by the amount of the underpayment interest because the Service should have taken the underpayment interest into account in computing the amount of the overpayment to be shown on the decision document. Thus, pursuant to the holding, the decision for an overpayment of \$238,847.24 precluded accounting for any remaining unpaid underpayment interest to which respondent could apply the overpayment.

New Procedure

A. Future Decisions

Counsel attorneys should take into account both assessed and unassessed underpayment interest when computing the amount of overpayment to set forth in decision documents and stipulations. The computation should include entries, as necessary, for the underpayment interest paid, the total assessed underpayment interest liability, and the unassessed underpayment interest liability:

- The amount of underpayment interest paid will include any amount paid by the taxpayer with respect to the underpayment interest on the taxpayer's account. This amount does not need to be listed as a separate payment where the tax and interest are paid by the taxpayer on the same date.
- The amount of assessed underpayment interest liability will include the total amount of the assessed interest liability on the taxpayer's account.
- The amount of unassessed interest liability will be computed by calculating the amount of underpayment interest due on the underpayment, including interest accruing on that interest.

Attached as Exhibit A is a sample computation and decision document addressing the issues raised by Estate of Smith. The decision document should reflect the overpayment amount as adjusted for underpayment interest.

Where the inclusion of unpaid deficiency interest in the computation results in a net amount owed to the Service, the decision document should simply reflect that there is no overpayment, without providing the amount of the underpayment.

Exhibit A: Computation and Decision Document

COMPUTATION STATEMENT

Tax Liability		100,000	
Tax Assessed:			
Assessed per return filed on April 15, 2000	75,000		
Net Tax Assessed		<u>75,000</u>	
Deficiency to be assessed		<u>25,000</u>	
Tax liability		100,000	
Tax Payments and Credits			
April 15, 2000	63,000		
June 15, 2001	77,000		
		<u>140,000</u>	
Overpayment before calculation of underpayment interest		40,000	40,000
Interest liability		30,000	
Underpayment interest Assessed:			
Assessed July 17, 2001	1,000		
Net interest assessed		<u>1,000</u>	
Underpayment interest to be assessed		<u>29,000</u>	
Underpayment interest liability		30,000	
Overpayment after calculation of underpayment interest			<u>10,000</u>

DECISION

Pursuant to the stipulation of the parties filed in the above-entitled case, and incorporating herein the facts stipulated by the parties as the findings of the Court, it is

ORDERED AND DECIDED: That there is a deficiency in income tax of \$25,000 which has been paid and an overpayment in income tax for the taxable year 1999 in the amount of \$10,000, which amount was paid on June 15, 2001; and for which amount a claim for refund could have been filed, under the provisions of I.R.C. § 6511, on [date], the date of the mailing of the notice of deficiency.

Judge.

Entered:

* * * * *

It is hereby stipulated that the Court may enter the foregoing decision in the above-entitled case in accordance with the stipulation of the parties submitted herewith.