REPORT #691

TAX SECTION

New York State Bar Association

REPORT ON
SECTION 6621(c) PROVIDING FOR
INCREASED INTEREST RATE ON
LARGE CORPORATE DEFICIENCIES
AND TEMP. REG. 301.6621-3T

June 7, 1991

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TAX SECTION
New York State Bar Association

June 7, 1991

The Honorable Fred T. Goldberg, Jr.
Commissioner of Internal Revenue
1111 Constitution Avenue, N.W.
Washington, D.C. 20024

Dear Commissioner Goldberg:

I enclose our report on section 6621(c) (which imposes interest at an elevated rate on large corporate tax deficiencies) and the proposed and temporary regulations issued thereunder. The principal authors of the report are Donald C. Alexander and Michael I. Saltzman.

Section 6621(c) was enacted without the benefit of careful deliberation and, in our view, was ill conceived. The report describes a number of flaws in the section. Most importantly, it will disrupt a settlement process that now works rather effectively and will impede access to the Tax Court, our primary forum for the resolution of tax disputes.

We recommend that the section be repealed. If repeal is not feasible, we recommend that the section be modified to minimize its likely adverse effects. Our primary recommendation is that elevated interest be limited to periods following issuance of a statutory notice of deficiency.

In some respects, the temporary and proposed regulations are quite helpful. However, we suggest some changes. Specifically, the regulations should include a de minimis exception, clarify procedures to ensure that taxpayers will timely receive notices, provide liberal crediting procedures as contemplated by the legislative history, and expand relief for abatement of interest attributable to the Service's error or delay.

We would be pleased to discuss the report and its recommendations with your staff at their convenience.

Very truly yours,

James M. Peaslee
Chair

Enclosure

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Tax Report #691

REPORT ON SECTION 6621(c) PROVIDING FOR INCREASED INTEREST RATE ON LARGE CORPORATE DEFICIENCIES AND TEMP. REG. 301.6621-3T

NEW YORK STATE BAR ASSOCIATION TAX SECTION

COMMITTEE ON PRACTICE AND PROCEDURE

June 7, 1991

I. INTRODUCTION[1]

A. THE STATUTE

Section 6621(c),[2] added by the Revenue Reconciliation Act of 1990 (“Act”) , provides that C corporations with a large underpayment of tax must, in the absence of prompt payment, pay interest on the underpayment at a rate 2 percentage points higher than the normal rate for underpayments (the “elevated interest rate”). A large corporate underpayment is defined as any underpayment of tax that exceeds $100,000 by a C corporation for any taxable period. Section 6621(c)(3)(A). The elevated interest rate begins to run on the day after the “applicable date.” In general, the applicable date is the thirtieth day after the earlier of the mailing of (i) the first letter of proposed deficiency which allows the taxpayer to protest to the Office of Appeals (commonly known as the thirty-day letter) (section 6621(c)(2)(A)(i)), or (ii) the statutory notice of deficiency (the ninety-day letter) (section 6621(c)(2)(A)(ii)). For taxes to which the deficiency procedures do not apply (e.g., excise and employment taxes, or correction of mathematical errors), the applicable date is the thirtieth day after the date of mailing of

[1] This report was prepared by the Committee on Practice and Procedure. The principal authors of the report were Donald C. Alexander and Michael I. Saltzman. Helpful comments were received from James M. Peaslee, John A. Corry and Michael L. Schler.

[2] Unless otherwise indicated, all section references are to the Internal Revenue Code of 1986, as amended (the “Code”), or to the regulations promulgated thereunder.

any letter or notice which notifies the taxpayer of an assessment or proposed assessment. Section 6621(c)(2)(B)(i).[3]

If full payment is made within thirty days beginning on the date the letter or notice is sent, such letter or notice is disregarded and does not trigger the elevated interest rate. Section 6621(c)(2)(B)(ii). The taxable period is defined as the taxable year for income taxes and the period to which the underpayment relates for other taxes. Section 6621(c)(3)(B).

Section 6621(c) is effective for determining interest for periods after December 31, 1990, even if the applicable date, as described above, is prior to January 1, 1991. However, under a transitional rule, a notice or letter is disregarded in determining the applicable date if the amount due plus a reasonable estimate of interest is paid by January 31, 1991, even though that date is more than thirty days after the date the notice or letter was sent.

B. OVERVIEW OF REPORT

We believe that section 6621(c) is flawed in a number of respects. First, and most importantly, the section will disrupt a settlement process that now works rather effectively and will impede access to the Tax Court, our primary forum for the resolution of tax disputes.

Second, while it is difficult to identify the point at which an interest rate reaches a level where it can fairly be

[3] An error in the statutory wording would be corrected by the Technical Correction Act of 1991 discussed below.

characterized as a penalty, five points above the short-term Federal rate is significantly higher than the rate at which creditworthy corporations can borrow, and we believe that the section can plausibly be viewed as penalizing corporations that contest tax deficiencies asserted by the Internal Revenue Service ("Service"). However, unlike other civil penalties in the Code, this one is not based on the merits of the taxpayer's position or any other measure of fault. It is ironic that the elevated interest rate provision was enacted only one year after the Omnibus Reconciliation Act of 1989, which overhauled and improved the civil penalty provisions of the Code.

Third, section 6621(c) is unfair in that its effects can more readily be avoided by corporations that can pay asserted deficiencies and seek a refund than by those in a weaker financial state. This issue is important particularly because the elevated interest rate is triggered by a failure to pay in full the deficiencies asserted by examining agents prior to review by the Service's Office of Appeals ("Appeals"), even though deficiencies proposed by examining agents are routinely reduced by Appeals.

Fourth, since the establishment of the Board of Tax Appeals in 1924, the federal tax system has permitted taxpayers to contest disputes through the courts before requiring payment. To the extent the elevated interest rate compels taxpayers to pay taxes before the resolution of disputes, it conflicts with this longstanding policy.

Finally, as currently written and interpreted, the section suffers from technical deficiencies that could cause it to operate in an arbitrary manner. For example, it may apply to one large deficiency as a result of a failure to pay promptly another wholly unrelated deficiency involving a very small amount.

We might be more supportive of the section if we believed that these issues had been given due consideration before the section became law. However, the principal terms of the section became public only upon release of the conference report for the Act, when it was too late to comment. We believe that the provision is another example (along with the repeal of section 1275(a)(4)) of a case where good tax policy was sacrificed imprudently to meet revenue needs.[4]

We recommend that section 6621(c) be repealed.[5] If repeal at this point is not feasible, we propose that the rule imposing the elevated interest rate based on a thirty-day letter be eliminated, so that interest at the elevated rate would begin to accrue only after a deficiency notice was issued. We have

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[4] The repeal of section 1275(a)(4) is described in our Report of Ad Hoc Committee on Provisions of the Revenue Reconciliation Act of 1990 Affecting Debt-for-Debt Exchanges (March 25, 1991).

[5] In examining the revenue effects of repeal, we hope that due regard will be given to the possibility that section 6621(c) will induce taxpayers to pay asserted deficiencies in cases where the expected liability is much less than the amount paid, and then to collect interest on the amount refunded at two percent above the short-term Federal rate. This is an expensive borrowing rate for the government. Also, the taxpayer will benefit by deferring income tax on the interest it receives until the dispute is resolved.

certain other recommendations for statutory changes which are described later in the report. Also, while the regulations that have been issued are helpful in some respects, they could and should go further in remedying some of the anomalies of the section, particularly if it is not changed.

The balance of this report is divided into five parts. Part II describes the history of the section, the temporary regulations, and changes to be implemented in the technical corrections bill. Parts III and IV analyze the effect of the section on Appeals and the Tax Court. Part V discusses certain additional problems arising under the section. Finally, our recommendations are summarized in Part VI.

II. BACKGROUND

A. HISTORY OF STATUTE

For many years the interest rate on Federal tax underpayments and overpayments, both individual and corporate, was six percent. This was changed in 1975 when, at the urging of the then Commissioner of Internal Revenue, Congress increased the rate on underpayments and overpayments to nine percent with a biannual adjustment to 90 percent of prime.[6] The then Commissioner contended that the below-market interest rate charged on tax deficiencies, together with relatively small and ineffective penalties, made the audit lottery a winning proposition for all taxpayers. If a taxpayer lost by reason of

[6] Section 7, Public Law 93-625, 1975-1 C.B. 510, 513.

being audited and corrected, he still won through deferring a tax obligation at below-market cost. After 1975 there were a series of changes resulting in more frequent changes in rates, a change in the rate to one based on the Federal short-term rate, daily compounding, and a one percent differential between interest charged on underpayments and that paid on overpayments.

On September 6, 1990, Congressman Pete Stark of the Ways and Means Committee proposed as a revenue raiser the disallowance of deductions for interest on corporate tax deficiencies, claiming that such disallowance would create equity between corporations and individuals whose interest payments were already disallowed. H.R. 5557, 101st Cong. 2d Sess., 136 Cong. Rec. H7219 (1990). Whether or not this proposal was serious, its revenue consequences were not overlooked in the search for additional taxes that culminated in the budget summit agreement of September 30, 1990. This Tax Section and other groups expressed strong opposition to this proposal. See Letter from Arthur A. Feder, Chair of NYSBA Tax Section, to Chairman Bentsen and Chairman Rostenkowski (October 4, 1990), reprinted in Highlights & Documents Vol. 19, No. 6 (Oct. 9, 1990). In the face of strong opposition, the bill ultimately adopted by the House Ways and Means Committee and accepted by the House of Representatives did not contain any provision disallowing interest for corporate tax deficiencies or increasing the rate of such interest. However, the revenue proposals approved by the Senate Finance Committee on October 13, 1990, did adopt a corporate interest disallowance provision. In conference, perhaps at the suggestion of certain practitioners and their clients,[7] section 6621(c) which increased the interest rate on corporate tax deficiencies but did not

[7] See Letter from Price Waterhouse to Kenneth W. Gideon of the Treasury Department (October 10, 1990), recommending the approach taken in section 6621(c) and listing as supporters numerous corporate clients, reprinted in Highlights and Documents, Vol. 19, pp. 1029-30 (Oct. 30, 1990).

disallow a deduction for such interest, was adopted without hearings, without notice to the public, and on an extremely short time schedule. Section 6621(c) first appeared in the conference agreement on October 25, 1990, and the 1990 Act was passed by Congress on October 27, 1990. Presumably, Congress wanted to exact further revenue from the corporate sector without raising rates or making similar broad-based adjustments. We believe there are better ways to raise revenue, as well as better ways to enact tax legislation. Had there been time to consider and discuss the defects of section 6621(c), it might not have been enacted and, at the least, certain corrections and improvements could have been made.

B. TECHNICAL CORRECTIONS

The proposed Technical Corrections Act of 1991 (H.R. 1555, 102d Cong., 1st Sess. (1991) and S. 750, 102d Cong., 1st Sess. (1991)) would correct the error in current section 6621(c)(2)(B)(i) which states that as to any underpayment of any tax “imposed by this subtitle” to which deficiency procedures do not apply, the letter or notice notifying the taxpayer of the mathematical error or underpayment and the consequent assessment or proposed assessment shall be substituted. Section 6621 is, of course, within Subtitle F -- Procedure and Administration -- of the Code, and a literal reading would render subsection 6621(c)(2)(B)(i) inapplicable to the very taxes to which it is clearly intended to apply.

The Technical Corrections Act would also amend section 6621(c)(2)(A) to provide needed relief in situations where the thirty-day letter or statutory notice of deficiency is withdrawn. A new sentence would be added at the end of subparagraph (A) of section 6621(c)(2) stating: “The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary." This relief is welcome, but it does not appear to be completely clear that letters or notices applicable to non deficiency procedures and described in subparagraph (B) of section 6621(c)(2) are covered. Such seems to be the intent of the provision, given the explanation by the Joint Committee on Taxation staff (JCX-5-91 March 21, 1991, pp. 7-8). It would seem preferable to move the relief provision into subparagraph (B) of section 6621(c)(2) and revise it to read as follows:

> (iii) EXCEPTION WHERE LETTER OR NOTICE WITHDRAWN.--For purposes of subparagraph (A), a letter or notice which is withdrawn by the Secretary shall be disregarded.

C. THE TEMPORARY REGULATIONS

Temporary and proposed regulations were issued on December 19, 1990. Temp. Reg. $ 301.6621-3T, T.D. 8325, 55 Fed. Reg. 52,042 (1990). These regulations were corrected on January 22, 1991. T.D. 8325, 56 Fed. Reg. 2,433 (1991). The Internal Revenue Service (the "Service") issued an announcement providing for a limited extension of a transition rule. Ann. 91-21, 1991-7 I.R.B. 32.

The regulations provide that the elevated interest rate applies if the "threshold underpayment of tax" exceeds $100,000. Temp. Reg. § 301.6621-3T(b). A threshold underpayment of tax is defined as the excess of the tax imposed by the Code (exclusive of interest, penalties, additional amounts and additions to tax) over the amount paid on or before the last date prescribed for payment. This unique definition of an underpayment applies only to section 6621(c).

The concept of the threshold underpayment is very constructive and the Service is to be commended for taking this sound approach. If the general definition of an underpayment of tax had been used, substantial administrative problems would have arisen. For example, to determine whether the section 6621(c) interest rate applied, the amount of an underpayment would depend, in part, upon how much time passed between the last day prescribed for payment and the assessment date. An underpayment might total less than $100,000 as of the thirty-first day following a thirty-day letter but, as a result of the accumulation of interest, the underpayment might be greater than $100,000 at the time of assessment.

Assuming that a large corporate underpayment is present and that a triggering letter or notice is sent, the elevated interest rate will apply for any periods after the applicable date unless the taxpayer pays the full amount shown as due in the letter or notice (including interest, penalties, additional amounts, and additions to tax) on or before the applicable date.

III. EFFECT ON APPEALS CASES

Many deficiencies proposed by examining agents are settled in Appeals, where the deficiencies proposed on audit are often reduced to much smaller numbers.[8] Section 6621(c) will likely discourage taxpayers from protesting cases to Appeals.

The running of interest at the elevated rate will create a substantial incentive to taxpayers to pay in full tax deficiencies asserted in a thirty-day letter, or if no thirty-day letter has been sent, in a ninety-day letter. As discussed in

[8] In 1989, Appeals closed 86,795 cases, approximately 90% on an agreed basis. Internal Revenue Service Annual Report, Tables 15, 16 (1989).

more detail below, full payment of the amount stated in a thirty-day letter will prevent a taxpayer from litigating a dispute in the Tax Court, whereas full payment of the amount claimed in a ninety-day letter will not deprive the Tax Court of jurisdiction. Thus, taxpayers who wish to utilize the Tax Court as a forum may request ninety-day letters in lieu of thirty-day letters, thereby limiting or avoiding Appeals review. Such a strategy would permit the taxpayer to pay in response to the ninety-day letter, thus avoiding the elevated interest rate and still preserving Tax Court jurisdiction over the dispute. Even if a thirty-day letter is issued, the taxpayer may well choose not to file a protest and thus force the issuance of a ninety-day letter.[9] In either circumstance, review by Appeals will be available only under the strict timetable allowed for a docketed Tax Court case. Reg. § 601.106(d)(3)(iii); Rev. Proc. 87-24, 1987-1 C.B. 720.

Moreover, section 6621(c) will complicate many cases before Appeals. Most cases now considered by Appeals involve proposed deficiencies rather than refunds, but Appeals plays the same role in refund claim cases as in those involving deficiencies. Section 6621(c) will likely compel many corporate taxpayers to pay the deficiency proposed in the thirty-day letter in order to escape the elevated interest rate. Therefore, it is reasonable to expect that more settlements considered by Appeals will involve tax refunds. Settlement of large refund claims are more complicated than settlements of deficiencies because they are subject to review by the Joint Committee on Taxation, although the Act raised the threshold requirement for Joint Committee review from a refund of $200,000 to a refund of $1,000,000. See section 6405(a).

[9] To prevent the elevated rate of interest from accruing a taxpayer could post a cash bond in response to the thirty-day letter and convert the bond to a payment after issuance of the ninety-day letter. The inadequacy of the cash bond procedure is discussed below.

IV. EFFECT ON TAX COURT CASES

Taxpayers can litigate tax disputes in the Tax Court, where prepayment is not required, or, after full payment and filing a claim for refund, taxpayers may litigate in the federal district courts or the Claims Court. The vast majority of substantive tax litigation now occurs in the U.S. Tax Court.[10] Section 6621(c) will likely divert many large corporate cases from the Tax Court to either the federal district courts or the Claims Court. This will place a greater burden on those other courts which may have less experience in handling tax disputes.

The Tax Court redetermines deficiencies. If a proposed deficiency has been fully paid, the Tax Court is without jurisdiction. Although section 6213(b)(4) provides an exception to this rule for payments made after issuance of the ninety-day letter, no such exception exists for payments made after a thirty-day letter (unless the payment is a deposit in the nature of a cash bond and a waiver of restrictions on assessment is not executed). Taxpayers that receive a thirty-day letter in situations within the scope of section 6621(c) may thus be forced either to sacrifice the Tax Court as a forum for litigation or to run the risk that the elevated interest rate will apply. Since full payment made after a thirty-day letter will deprive the Tax

[10] Chief Judge Arthur L. Nims, III recently testified that 95% of all substantive tax litigation occurs in the Tax Court, and that the Government's recovery rate in Tax Court cases closed in 1990 was 19.4%. Hearings on the Appropriation Request for the U.S. Tax Court Before the Subcomm. on Treasury, Postal Service and General Government of the Comm, on Appropriations, 102d Cong., 1st Sess. (1991) (Statement of Chief Judge Nims).

Court of jurisdiction but payment made after a ninety-day letter will not, taxpayers seeking to use the Tax Court will be forced to devise strategies both to preserve the Tax Court as a forum and to minimize the risk of the elevated rate of interest.

A. EFFECT ON PARTIAL PAYMENTS

In response to this problem, some taxpayers may pay a portion of the proposed deficiency set forth in the thirty-day letter. Such taxpayers might seek to pay the maximum amount possible to minimize accrual of the elevated rate of interest while leaving part of the proposed deficiency unpaid so that some deficiency remains in the event a ninety-day letter is issued. This strategy is perilous, for the agent's proposed adjustments are changed in some respect in most cases considered by Appeals. If Appeals concurs with some, but not all, of the agent's adjustments, the taxpayer's strategy to preserve a small deficiency could be thwarted, with a loss of Tax Court jurisdiction.

Further, the elevated interest rate would apply notwithstanding partial payment. As seen, the elevated interest rate applies for periods after the applicable date. Any letter or other notice is disregarded and the elevated interest rate is not triggered if the taxpayer makes a timely payment equal to the amount shown in the letter or notice. Temp. Reg. § 301.6621-3T(c)(4). A partial payment of the amount shown in a letter or notice will not be sufficient to prevent the triggering of an applicable date and the application of the elevated underpayment rate to the unpaid amount. For example, assume that a calendar year taxpayer receives a thirty-day letter with respect to its 1990 taxable year on July 1, 1992, and that the amount shown in the letter is $1,000,000. Assume further that the taxpayer timely pays $900,000 on July 31, 1992, and that the deficiency is ultimately sustained. Under the temporary regulations, the underpayment rate is determined without regard to section 6621(c) for the period beginning on March 16, 1991 (the due date of the return), and ending on July 31, 1992 (the applicable date). The underpayment rate is increased pursuant to section 6621(c) for the period beginning August 1, 1992. Furthermore, if the government prevails on a claim for a greater deficiency than the $1,000,000 stated in the letter, the elevated interest rate would apply to that amount as well. Also, the Appeals officer may well construe a partial payment as an indication of how the taxpayer evaluates the case.

B. EFFECT ON DEPOSITS IN THE NATURE OF A CASH BOND

Posting a timely deposit in the nature of a cash bond, in accordance with Rev. Proc. 84-58, 1984-2 C.B. 501, is an inadequate remedy. While posting a cash bond does not impair the taxpayer's right to petition the Tax Court, if the taxpayer ultimately prevails the government is not obligated to pay interest during the time it held the bond. Many taxpayers find it uneconomical to post such a bond, since if they prevail they will have provided the government an interest-free loan for the duration of the dispute.

Further, under the regulations a cash bond is, technically but correctly, held not to be a payment for purposes of determining whether the elevated interest rate is applicable. Temp. Reg. § 301.6621-3T(c)(4)(iii). Since a cash bond stops the running of interest on the amount deposited, this rule is important if the ultimate deficiency is larger than the cash bond. In such a situation the elevated interest rate would apply to the amount not covered by the bond from the applicable date of the notice in response to which the taxpayer posted a bond.

V. PARTICULAR PROBLEMS UNDER THE STATUTE AND THE TEMPORARY REGULATIONS

Section 6621(c) and the temporary regulations also create unnecessary administrative hardships for taxpayers, as the following situations demonstrate.

A. ADVERSE EFFECT OF PRIOR NOTICES

Temp. Reg. § 301.6621-3T(a)(2)(ii) provides the constructive and helpful rule that the applicable date is determined separately for different types of taxes and amounts that relate to different taxable periods. On the other hand, the regulations provide that there is only one applicable date with respect to all taxes of the same type relating to the same taxable period. Consequently, notices as to taxes to which the deficiency procedures apply can trigger an applicable date for taxes to which the deficiency procedures do not apply, and vice versa. Such a result requires taxpayers to pay every notice of assessment, however insignificant, or suffer a potentially severe interest penalty.

This problem is illustrated by Temp. Reg. § 301.6621-3T(d), Example 4(v). A subchapter C corporation timely files its 1989 income tax return and pays the amount on the return, and on May 1, 1990, the Service sends an assessment notice for $1,000 as a result of a math error on the return. The corporation does not pay the $1,000 within either thirty days or the extended transitional period ending on January 31, 1991. Almost two years after the assessment notice, on March 31, 1992, the Service sends the taxpayer a ninety-day letter showing a deficiency of $125,000, which the taxpayer pays within thirty days. Under these circumstances the elevated interest rate of section 6621(c) is imposed from January 1, 1991 (the effective date of the statute), on the entire amount of the deficiency. Had section 6621(c) been effective at the time of the assessment notice, the elevated interest rate would have been imposed for the period beginning on June 1, 1990.

In the example above, a taxpayer that failed to pay timely a minor $1,000 assessment was penalized by being required to pay 2 percent more interest on the $125,000 deficiency (plus interest, additions and penalties). Under the principle of the regulations, the same result would obtain if the mathematical error notice were for $100 and the notice of deficiency were for $10 million. The occurrence of an applicable date months or years before a notice implicating a large underpayment is sent will cause harsh results in many cases.

To remedy the problem, section 6621(c) should be amended to provide that the elevated interest rate will only apply to amounts identified in the notice which triggers the applicable date. Such a modification would eliminate the harsh result of a letter or notice for an insignificant amount triggering an applicable date and the running of the elevated interest rate on a subsequently determined large underpayment. At a minimum the statute should be modified to provide a two - track mechanism under which a notice relating to mathematical or clerical errors shown on a return would not trigger the elevated interest rate on a later deficiency resulting from an audit.

Pending a statutory solution, the regulations should implement a de minimis rule under which insubstantial assessments like that in Example 4(v) would not be taken into account.

Moreover, to the extent an applicable date can be triggered by a letter or notice claiming a small tax liability, the regulations should provide for special procedures to ensure that a taxpayer will timely receive such notices and be alerted to their significance. For example, the regulations should permit taxpayers to designate a specific address to which any notices triggering an applicable date must be mailed. Also, in view of the importance section 6621(c) places upon the date that the thirty-day letter is sent, consideration should be given to requiring that such letters be sent by registered or certified mail, as is the case with statutory notices of deficiency. See section 6212(a). Such provisions would be particularly helpful since the taxpayers most likely to be affected by section 6621(c), large corporations, often have widely scattered business operations and without special notification will find it difficult to respond to a seemingly innocuous letter or notice, such as the mathematical error notice in Example 4(v).

B. EFFECT ON ALTERNATIVE POSITIONS

Section 6621(c) and the regulations do not address the common situation where the Service, to protect itself against whipsaw, claims alternative and inconsistent deficiencies for different taxable years. This often occurs in situations involving timing; if the Service believes a taxable event increasing the taxpayer's income occurred in either one of two years, the Service frequently will propose a deficiency for both years. Of course, only one of the two deficiencies could ultimately be sustained. However, any taxpayer not paying the deficiencies for both years in such a situation is exposed to the risk of the section 6621(c) elevated interest rate. If the taxpayer paid only the deficiency for the earlier of the two years, and later it is determined that the income was properly includible in the later year, the elevated interest rate would apply. While the taxpayer would get an interest credit (at the overpayment rate) for the amount paid for the earlier year, the credit will bear interest at a rate three percentage points lower than that upon the deficiency.

The Conference Report recommends relief for the taxpayer:

> Under present law, the Secretary has the authority to credit the amount of any overpayment against any liability under the Code (sec. 6402). To the extent a portion of tax due is satisfied by a credit of an overpayment, no interest is imposed on that portion of the tax (sec. 6601(f)). The Secretary should implement the most comprehensive crediting procedures under section 6402 that are consistent with sound administrative practice.

H. R. Conf. Rep. No. 101-964, 101st Cong., 2d Sess. 1101 (1990), reprinted in 1991 U.S. Code, Cong. & Admin. News 2017, 2806.

The existing rules permit, but do not require, the Service to credit any overpayment against any outstanding liability for any tax (or for any interest, additional amount, additions to the tax, or assessable penalty) owed by the taxpayer. Reg. § 301.6402-3(a)(6). The enactment of section 6621(c) makes the existing crediting rules deficient. The Service is not required to credit an overpayment against a liability. If the Service should choose to refund the overpayment, the taxpayer will be charged with the elevated interest rate on the large corporate underpayment and will receive a lesser rate (by three percentage points) on the overpayment. Such crediting where needed to minimize the impact of the section 6621(c) elevated interest rate should be mandatory. Also, an overpayment for one year may not be credited against a large corporate underpayment for another year until long after the applicable date, thus triggering elevated interest on any substantial liability determined for such period in the future, even though the taxpayer will not be charged with interest on the amount of the deficiency satisfied by the overpayment. Regulations should be issued under section 6402 establishing liberal crediting procedures so that taxpayers that have overpaid for one taxable period will not suffer the elevated interest rate of section 6621(c) for an underpayment for another taxable period that could be satisfied by crediting the overpayment.

C. EFFECT ON REQUESTS FOR ABATEMENT OF MATHEMATICAL OR CLERICAL ERROR ASSESSMENTS

Temp. Reg. § 301.6621-3T(c)(3) recognizes that taxpayers have the right to file requests for abatement of assessments arising out of mathematical or clerical errors. Requests for abatement may be filed within sixty days after a notice of assessment is sent. Section 6213(b)(2). Assessments for alleged mathematical errors are frequently abated both in response to abatement requests and sometimes in the absence of such a request. Clearly, a math notice found to be sent in error should not trigger the running of the elevated interest rate even though the taxpayer did not file an abatement request. The amendment to section 6621(c)(2)(A) in the Technical Corrections Act of- 1991, in recognition that both thirty-day and ninety-day letters are sometimes withdrawn, provides that such letters are not considered for purposes of the application of the elevated interest rate. As discussed above, this technical correction should be modified to demonstrate that it applies to withdrawn notices of math and clerical error assessments. Moreover, section 6621(c)(2)(B)(ii) should be modified to provide that any letter or notice should be disregarded if the taxpayer pays the amount stated within sixty days, not thirty days, of the date such letter or notice is sent. Such a modification would be consistent with the sixty-day period for filing abatement requests. See section 6213(b)(2).

D. ADVERSE EFFECT OF DELAYS IN THE PROCESS

As pointed out earlier, the penalty imposed by section 6621(c) turns on time rather than fault: the greater the period of time between the applicable date and the date of payment, credit or deposit, the greater the section 6621(c) elevated interest. Therefore a taxpayer seeking to minimize liability for elevated interest wishes to reduce this period to as short a time as feasible. Unfortunately, the Appeals process often works quite slowly. Although by no means all the delays in the process are attributable to the Service, many are caused by the Service. Why should a taxpayer be penalized through elevated interest if negotiations with Appeals are interrupted by the assignment of the Appeals Conferee to a lengthy special detail or to a training course? What if an Appeals Conferee does not even read the taxpayer's protest for months?

Section 6404(e) permits the Service to abate interest attributable to errors and delays by a Service employee in performing a ministerial act, and the existing regulations interpreting this provision take a narrow view of its applicability. See Example (4), Temp. Reg. § 301.6404-2T. These regulations should be made more liberal through the adoption of of a broader view of what may constitute “a ministerial act” and they should be made specifically applicable to elevated interest under section 6621(c).

VI. CONCLUSIONS AND SUGGESTIONS

A. THE STATUTE

1. Because of the severity of the problems caused by section 6621(c) we recommend that it be repealed. If repeal is not feasible, several statutory changes should be made to minimize the likely adverse effect of section 6621(c) upon the present system of resolving federal tax controversies, which works rather well. These are listed below.

2. Utilizing the thirty-day letter date to trigger the running of the elevated interest rate increases the likelihood that an Appeals conference will be bypassed, despite the fact that deficiencies proposed at the District level are very often reduced at the Appeals level. It also creates the possibility that Tax Court review will be precluded or avoided in favor of a refund forum. Under these circumstances, the thirty-day letter stage is neither an appropriate nor a wise stage to trigger the imposition of the elevated rate. To do so is based on the implicit and erroneous assumption that the amounts set forth in the thirty-day letter are truly “underpayments” as determined by the Service rather than post-examination adjustments, subject to review and change in Appeals, before they become the determination of the Service. Accordingly, we recommend the deletion of section 6621(c)(2)(A)(i). If this is done, then the

increased interest rate will be triggered only by the sending of a notice of deficiency. Insofar as the increased interest rate is justifiable at all, it is best justified at this point in the administrative processing of the case. The ninety-day letter represents, at least where an Appeals conference is held, the considered view of the Service, not merely the view of the District.

We wish to emphasize the importance of this proposal, which is not a matter of statutory tinkering. The inclusion of the thirty-day letter trigger date has serious, adverse implications for both the administrative procedures for resolving tax controversies, as well as for the judicial review of tax cases in the Tax Court.

A less desirable solution is to expand the jurisdiction of the Tax Court to include cases where a deficiency proposed in a thirty-day letter is paid by the taxpayer before a ninety-day letter is issued. Another, lesser remedy is to modify section 6611 to require the government to pay interest on cash bonds posted by a taxpayer if the taxpayer prevails, or the proposed deficiency is reduced so that funds are returned.

3. The elevated interest rate should apply only to amounts identified in the notice which triggers the applicable date, or at least a two-track mechanism should be enacted under which math errors and clerical errors appearing on a return would not trigger an applicable date for a later deficiency resulting from an audit. Compare the accuracy-related penalty imposed under section 6662, which applies only with respect to the portion of any underpayment of tax that is attributable to the circumstances resulting in the penalty.

4. The Technical Corrections Act, which grants needed relief in the case of withdrawn letters and notices, should be expanded to modify section 6621(c)(2)(B)(ii) to provide for a sixty-day rather than a thirty-day period in which to pay underpayments claimed in letters or notices attributable to mathematical or clerical errors appearing on a return. Such a modification would be consistent with the sixty-day period for abatement requests now provided for in section 6213(b)(2).

B. THE REGULATIONS

While some of the problems with section 6621(c) are beyond repair through regulations, at a minimum, the temporary regulations should be modified to address the administrative problems described above. More specifically, they should include a de minimis exception for assessment notices under a certain amount (e.g., $10,000). The regulations should also provide a procedure whereby taxpayers can designate a single address for receipt of notices or letters which trigger the elevated interest rate and require that such notices be sent by certified mail. In addition, regulations should be promptly issued under section 6402 to provide comprehensive crediting procedures which require the Service to apply overpayments so as to minimize the impact of section 6621(c). Finally, regulations should be issued modifying and liberalizing the section 6404(e) procedure for the abatement of interest attributable to errors and delays by the Service.