



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

August 13, 2002

Number: **200238042**
Release Date: 9/20/2002
CC:PA:CBS:BR3
SCAF-121954-02WLI3.wpd
UILC: 6502.00-00

MEMORANDUM FOR JOSEPH M. ABELE, ASSOCIATE AREA COUNSEL, SBSE
ATTN: DBREEN AND JBAYER CC:SB:2:PHI:1

/S/

FROM: Robert A. Miller
Senior Technician Reviewer, Branch 3
(Collection, Bankruptcy and Summonses)

SUBJECT: Erroneous Refund Procedures

This responds to your memorandum dated May 17, 2002. Your memorandum requested Significant Service Center Advice. However, upon coordination, this matter was reclassified as Chief Counsel Advice.

ISSUE

Following a timely assessment of tax in respect of a return, what is the period of limitations for making a reversal of a withheld income tax credit which is overstated on the return?

CONCLUSION

The period of limitations for making a reversal of an overstatement of a payment credit reported on a return following a timely assessment of tax in respect of the return is the I.R.C. § 6502 collection period.

FACTS

The factual scenario which you pose is as follows. A taxpayer filed a return for taxable year 1994 in May 1995. The return reported a tax of \$1,500 and a credit for

withheld income tax of \$7,800, and claimed a refund of \$6,300. The IRS assessed the tax of \$1,500 and issued a refund of \$6,300 in June 1995.

In November 1998, the IRS reversed \$6,100 of the credit for withheld income tax as an overstatement, only \$1,700 of the claimed \$7,800 had actually been paid as withholding. At this point in time, the tax account reflected a debit for the tax assessment of \$1,500, a positive credit of \$7,800 for the posted withholding, a negative credit for the paid refund of \$6,300, and a negative credit for the credit reversal of \$6,100. The effect of the two negative credits (\$6,300 amount paid out and \$6,100 credit reversal) reduced to zero the positive credit (\$7,800), leaving the assessed tax (\$1,500) collectible. 1/

LAW AND ANALYSIS

You ask whether the IRS acted timely in reversing the overstatement of credit for withheld income tax, as timely reversal of the credit would allow collection of the assessed tax under the facts of the described scenario.

Under the facts provided, the reported tax was timely assessed. The reversal of the overstatement of credit was made about three years and six months after the return was filed. The reversal was made after expiration of the three year assessment limitations period of I.R.C. § 6501(a) and after expiration of the two year erroneous refund suit period of IRC 6532(b), but within the five year erroneous refund suit period of section 6532(b) and within the ten year collection period of section 6502(a). 2/

The administrative reversal of a payment credit because the alleged payment does not exist is neither an assessment nor the filing of a legal action. The reversal is an

1/ The assessment was not satisfied by the overstated credit since the overstated amount was not received by the IRS.

2/ You indicate that the five year erroneous refund suit period of section 6532(b) is not applicable by referring to the absence of fraud in the factual scenario. However, a nonfraudulent but negligent overstatement of the dollar amount of withheld income tax is a misrepresentation of material fact subject to the five year period of section 6532(b). See, Merlin v US, 243 F.2d 821 (5th Cir. 1957). The government is litigating the question of whether a taxpayer's assertion of a litigable position on a return subjects the government to a higher standard of proof than negligence. In Estate of Powell v United States, 2002 TNT 77-7 (4th Cir. 2002), the Fourth Circuit held that the government need not show more than gross negligence, and the court rejected the holding in United States v Northern Trust Co., 93 F. Supp. 2d 903 (N.D. IL 2000), that the government must show intentional misrepresentation.

adjustment of a payment (a collected amount). Reversal of a payment credit is an action which can occur during the assessment period prior to assessment, or during the collection period after assessment. **3/**

Because the reversal was timely made within the section 6502 collection period following assessment, and since the period for filing an erroneous refund action expired before the section 6502 collection period expired, we need not address whether reversal could also be made within the section 6532(b) period. **4/**

Please call if you have any further questions.

3/ Prior to assessment, the assessment period is the period for collection without assessment; I.R.C. § 6501(a). After assessment, the collection period is the ten year period of section 6502(a), which runs from the assessment of the tax. United States v. Langrehr, 2001 U.S. Dist. LEXIS 2374, at p. 5 (D. NE 2001) (the IRS has discretion to administratively reverse an erroneous credit prior to expiration of the collection period); Billion v. United States, 921 F.2d 182, 183 (8th Cir. 1990) (the IRS can administratively reverse an erroneous credit during the collection period); C&R Investments, Inc. v. United States, 444 F.2d 765, 769-770 (10th Cir. 1971) (the tax was unpaid to the extent of the erroneous credit, and the director has administrative power to correct an error); Commissioner v. Newport Industries, Inc., 121 F.2d 655, 657-658 (7th Cir. 1941) (the IRS has administrative discretion to undo what has been done to eliminate error, within the periods of limitation for assessment and collection; however, an erroneous credit can also be recovered by an erroneous refund suit).

4/ A period of limitations may apply to both filing of legal actions and to other matters. For example, an assessment period under section 6501 includes the period for administrative or judicial action without assessment; the collection period under section 6502 includes the period for administrative or judicial action after assessment; the erroneous refund recovery period of section 6532(b) includes the period for settlement or voluntary payment of the government's claim without filing a judicial action. See, also, footnote 1, supra; and Commissioner v. Newport Industries, Inc., footnote 4, supra.