

Office of Chief Counsel
Internal Revenue Service
Memorandum

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to: Associate Area Counsel (Dallas, Group 2)
(Large & Mid-Size Business)
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from: Jason A. Spitzer
Senior Technician Reviewer
(Procedure & Administration, Branch 6)

subject: Closing Agreement

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

LEGEND

Taxpayer =
Predecessor =
Property =

ISSUES

Whether the closing agreement, signed by Predecessor, is valid for Taxpayer under section 7121.

CONCLUSIONS

While Taxpayer may reap the benefits of the closing agreement as the purchaser, from Predecessor, of the main asset covered by the closing agreement, the agreement itself is *ultra vires*, as a matter of delegated authority to execute the agreement.

FACTS

In _____, the owners of the Property and Appeals reached an agreement regarding the treatment by the owners of certain _____ costs of the Property. Specifically, the parties created a Form 906 Closing Agreement on Determination Covering Specific Matters that set forth a defined amount to be deducted by each of the owners of the Property for the tax years _____ through _____. The aggregate deduction was _____ and was allocated among the owners based on their proportional ownership of the Property.

The closing agreement was executed by the multiple owners of the Property and their corporate parents, including Predecessor, beginning on _____ through _____. On _____, the agreement was signed by _____, using the title “Chief, Appeals Office.” That title seems to indicate that _____ was the Chief of a local Appeals office, in this case, _____.¹

In the years since the execution of the closing agreement, Taxpayer purchased Predecessor’s ownership interest in the Property. Taxpayer now seeks to take advantage of the tax treatment of the Property costs, as set forth in the closing agreement.

LAW AND ANALYSIS

1. Taxpayer’s Rights Under the Agreement

The closing agreement, in determination clauses 1, 2, 4, 5 and 8, refers to “successors in interest” to the owners of the Property and applies the terms of the agreement to such entities, provided they have expressly assumed the obligations of an owner. Pursuant to our own analysis and an informal review by CC:CORP, the Property is treated by its owners as an asset. Thus, Taxpayer’s acquisition of Predecessor’s ownership interest in the Property appears to entitle Taxpayer to the tax treatment set forth in the closing agreement. If there is any indication that Taxpayer somehow did not assume all ownership obligations that accompany the Property, this conclusion will require reconsideration.

2. The Validity of the Agreement

The closing agreement between the owners of the Property and Appeals was expressly executed under section 7121. Under section 7121, the Secretary of the Treasury, and by delegation, the Commissioner of the Internal Revenue Service, may enter into written agreements with persons concerning their tax liabilities. I.R.C. § 7121; Treasury Order 150-07. Closing agreements are final and conclusive. I.R.C. § 7121(b). Closing

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agreements are not strictly subject to the common law of contracts, because they are legislatively authorized agreements that require no consideration for formation. Part of this legislative authorization is the requirement that the representative of the Commissioner who executes the agreement has been delegated the authority to do so.

The Chief of the Appeals Office, at the time he signed the Agreement on behalf of the Service, only had the delegated authority to make an agreement with a taxpayer regarding “a taxable period or periods ended prior to the date of the agreement and related specific items affecting other taxable periods.” Delegation Order No. 97 (Rev. 23), ¶ 4, 1984-2 C.B. 468.² Such language is still in effect today. See Delegation Order No. 97 (Rev. 34). It is a standard principle that the government cannot be bound by the *ultra vires* acts of its representatives. Heckler v. Community Health Serv., Inc., 467 U.S. 51, 63 n.17 (1984) (“anyone entering into an agreement with the Government takes the risk of having accurately ascertained that he who purports to act for the Government stays within the bounds of his authority. . . . And this is so even [where] the agent himself may have been unaware of the limitations upon his authority.”); Utah Power and Light Co. v. United States, 243 U.S. 389, 409 (1917) (“[T]he United States is neither bound nor estopped by acts of its officers or agents in entering into an arrangement or agreement to do or cause to be done what the law does not sanction or permit.”); Dori v. Commissioner, 507 F.2d 406, 407 (2d Cir. 1974), affg. T.C. Memo. 1973-145; Stiskin v. Commissioner, T.C. Memo. 1996-306; Webb v. Commissioner, T.C. Memo. 1994-549.

In the closing agreement at issue, the period purported to be covered was to That is, years that had ended prior to the date of execution and years that would end subsequent to that date. Under the terms of Delegation Order 97, the Chief of the Appeals Office had only the authority to bind the government regarding the first years covered by the agreement.

The Taxpayer may attempt to argue that the Chief of the Appeals Office did have authority to execute an agreement for future years because the treatment of Property deductions was a “related specific item affecting other taxable periods.” This argument will fail because it is contrary to the manner in which the Service has operated in accordance with the “related specific items affecting other taxable periods” language of Delegation Order No. 97. Both the Service and the courts view each tax year as a separate source of liability and new cause of action. See Commissioner v. Sunnen, 333 U.S. 591, 598 (1948). While Sunnen concerned the application of res judicata to tax issues, the principle enunciated by the Supreme Court is a useful analogy. It means that, where a type of transaction is separately recurring in several taxable years, the

² D.O. No. 97 (Rev. 23) became effective May 4, 1984. We do not have the text of the Delegation Order in effect at the time the closing agreement in question was executed. We do, however, believe that the language of paragraph 4 of the Delegation Order was identical to that in Revision 23, as the same paragraph, with the exception of a few different position titles, is contained in Revision 28 (found at 1989 WL 225332), effective March 2, 1989.

transactions in each taxable year are independently evaluated pursuant to information pertaining to that taxable year.

Instead, the phrase “related specific items affecting other taxable periods” is used by the Service to accommodate those cases where the nature of the transaction resolved in a closing agreement for one year necessitates a binding effect on that taxpayer’s liability in another year. The regulation for section 7121 states that “[c]losing agreements with respect to taxable periods ending subsequent to the date of the agreement may relate to one or more separate items affecting the tax liability of the taxpayer.” Treas. Reg. §301.7121-1(b)(3). In the regulations, there is the following illustration of this concept:

A owns 500 shares of stock in the XYZ Corporation which he purchased prior to March 1, 1913. A is considering selling 200 shares of such stock but is uncertain as to the basis of the stock for the purpose of computing gain. Either prior or subsequent to the sale, a closing agreement may be entered into determining the market value of such stock as of March 1, 1913, which represents the basis for determining gain if it exceeds the adjusted basis otherwise determined as of such date. Not only may the closing agreement determine the basis for computing gain on the sale of the 200 shares of stock, but such an agreement may also determine the basis (unless or until the law is changed to require the use of some other factor to determine basis) of the remaining 300 shares of stock upon which gain will be computed in a subsequent sale.

Treas. Reg. §301.7121-1(b)(4). This regulation was last amended on October 24, 1960, and was therefore in effect at the time of the execution of the Agreement. The significant feature of this example is that it is the determination of the tax consequences of a *past* basis-determining transaction, the acquisition of the shares, (which could represent multiple transactions, although that is irrelevant) that has effect in future years. Essentially, the binding determination made by the Service and the taxpayer, due to the nature of the past transaction, must be applied to future years to ensure accurate determination of the taxpayer’s tax liability in those years. In fact, in the example above, the tax liability of those future years would be impossible to determine accurately without reference back to the determination made in the year covered by the closing agreement.

This is markedly different from the transactions at issue in the closing agreement here. By the terms of the closing agreement, the owners of the Property are entitled to deductions for _____ costs because the _____ activities were ongoing during the time frame of the agreement. Determination clause 2 of the agreement states that the deductions were allowed through “the first to occur of _____ or the month in which _____ of the [Property] facilities is completed.” Thus, the deduction taken in each year represented separate and new activity or transactions.

While the treatment of a transaction in one year may provide a good indication of the proper treatment of a transaction of the same type in a future year, the treatment in the earlier year cannot affect the later year in such a way to bind the Service with the finality of a closing agreement. The Service is free, using the analogy to Sunnen, to examine the later transaction independently of the prior transaction. Accordingly, the recurring

transactions in which the Taxpayer (and Predecessor) was engaged in during and subsequent to the years covered by the Agreement do not fit the meaning of “related specific items affecting other taxable periods.”

As the Taxpayer’s transactions are not in the nature of related specific items, and the Chief of the Appeals office clearly lacked the authority to expressly bind the Service for future years, the Agreement was binding on the Service only for tax years ended prior to . Taxpayer acquired its ownership of the Property in ; thus, the agreement is entirely invalid as to Taxpayer.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

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Please call if you have any further questions.