

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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to: Kelli D. Winegardner, Program Manager
(Office of Servicewide Interest)
Attention: Clay Coleman

from: Pamela Wilson Fuller
Senior Technician Reviewer, Branch 2
(Procedure & Administration)

subject: Request for Counsel Advice – IRC 6621(d) – Prior Net Rate Interest Netting
Adjustments

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

ISSUES

(1) Whether an underpayment applied against an equivalent overlapping overpayment to obtain a net interest rate of zero pursuant to Internal Revenue Code section 6621(d) is available for netting against another equivalent overlapping overpayment if the Service determines the first overpayment was erroneous, (2) Whether the same is true for an overpayment netted against an erroneous underpayment, and (3) Whether the cause of the error affects these answers.

CONCLUSIONS

(1) An underpayment that was previously netted against an equivalent overlapping overpayment is not available to net against another equivalent overpayment if the taxpayer has retained the benefit of the original interest netting (the interest differential amount paid or credited to the taxpayer). If, however, the taxpayer did not retain the benefit of the original netting, then the underpayment is available for netting against another overpayment. (2) The same analysis applies to an overpayment netted against an erroneous underpayment. (3) We are unaware of any circumstance where the cause of the error would change our answers.

FACTS

The following fact pattern illustrates the issue. In year 1 Taxpayer had an overpayment of \$500X which accrued allowable interest. In year 2, Taxpayer had a \$500X underpayment which accrued payable interest. In year 3 Taxpayer had an additional overpayment of \$500X which accrued allowable interest. For all years, the underpayment rate was 4%, the overpayment rate was 3%.

At the beginning of year 4, Taxpayer requested interest netting of the \$500X year 1 overpayment against the \$500X year 2 underpayment. The Service allowed the interest netting request and paid Taxpayer the 1% interest differential.

The Service later determined that Taxpayer did not have an overpayment for year 1. Taxpayer subsequently requested interest netting of the \$500X year 2 underpayment against the \$500X year 3 overpayment. In scenario 1 Taxpayer has repaid the interest differential amount it received as a result of the original interest netting request. In scenario 2, Taxpayer has not repaid the interest differential amount it received.

LAW AND ANALYSIS

Where interest is payable under subchapter A and allowable under subchapter B of chapter 67 for the same taxpayer on equivalent underpayments and overpayments for any period, the net rate of interest for that period shall be zero. See I.R.C. § 6621(d). The Service applies the net rate of zero where applicable by decreasing the underpayment rate to match the overpayment rate if the period of limitations for refunding underpayment interest is open. See Rev. Proc. 2000-26, 2000-24 I.R.B. 1257 sec. 4.03(1). If only the period of limitations for paying additional overpayment interest is open, the Service instead increases the overpayment rate to match the underpayment rate. See *id.* sec. 4.03(2).

The Internal Revenue Code does not clearly address the circumstances under which a single equivalent underpayment (or overpayment) is available for interest netting.¹ Nor is there any case law which answers this question. See I.R.C. § 6621.

Where the meaning of the [statutory] language is ambiguous, legislative history may add clarity, see *Milner v. Dep't of Navy*, 131 S. Ct. 1259, 1267 (2011); *Blum v. Stenson*, 465 U.S. 886, 896 (1984). “[I]nterpretations of a statute which would produce absurd results are to be avoided if alternative interpretations consistent with the legislative purpose are available,” *Griffin v. Oceanic Contractors, Inc.*, 458 U.S. 564, 575 (1982). The legislative history of section 6621(d) indicates Congress’s intent that “[e]ach overpayment and underpayment is considered only once in determining whether equivalent amounts of overpayment and underpayment exist.” See S. Rep. No. 105-174, at 62 (1998); H.R. Rep. No 105-599, at 257 (1998). Consistent with the

¹ The Service typically refers to the availability analysis as whether the underpayment (or overpayment) has been “used.” See *generally* IRM 20.2.14.

legislative history, Revenue Procedure 2000-26 states that “each overpayment or underpayment is considered only once in determining whether equivalent amounts of overpayment and underpayment overlap for a particular period. However, like the legislative history, the revenue procedure does not indicate under what circumstances a single equivalent underpayment (or overpayment) is available for interest netting.”

Additionally, “Congress has previously concluded that comprehensive interest netting is desirable to the maximum extent feasible.” See Department of the Treasury, Office of Tax Policy, *Report to the Congress on Netting of Interest on Tax Overpayments and Underpayments* (“Treasury Report”) 2 (1997), available at <http://treasury.gov/resource-center/tax-policy/Documents/t0neting.pdf>.

Here, the statute is not clear on when a payment remains available for netting, thus we must interpret section 6621(d) consistently with the legislative intent to apply interest netting wherever feasible, consider each overpayment and underpayment only once, and avoid producing absurd results.

When the Service allows an underpayment to be net against an equivalent overlapping overpayment and pays (or credits) the interest differential amount to the taxpayer, that underpayment has been “considered.” If the Service determines that the originally netted overlapping overpayment was erroneous, the underpayment has still been “considered” because the taxpayer has still retained the benefit of interest netting. If, however, the taxpayer repays to the Service the interest differential amount it received as a result of the netting, then the underpayment has no longer been “considered” because the taxpayer did not retain the benefit of netting. As stated above, Congress intended the Service to apply interest netting wherever feasible. Our interpretation that the underpayment becomes available to net against another overlapping overpayment in this circumstance is consistent with this legislative intent.

If the taxpayer does not return the interest differential amount it received, then the taxpayer has retained the benefit of the original interest netting request. Consequently, the underpayment will not be available to net against another overlapping overpayment. If the taxpayer were allowed to retain the benefit of netting the same underpayment against more than one equivalent overpayment, the effect would not be the net interest rate of zero on equivalent amounts required by statute, but a reduction in underpayment interest or increase in overpayment interest in contravention of the established rates and Congress’s intent.

As applied to the hypothetical facts in scenario 1, after the Service disallows the year 1 overpayment, Taxpayer returned the 1% interest netting differential to the IRS. The year 2 underpayment has not been considered, because Taxpayer has not retained the benefit of interest netting. The year 2 underpayment may be netted against the year 3 overpayment.

In scenario 2, where the same facts apply except Taxpayer does not return the 1% differential, the year 2 underpayment has been considered because Taxpayer has

retained the benefit of netting from its first request. The year 2 underpayment is not available for netting. We note that if the net rate of zero was initially achieved by lowering the underpayment rate per Revenue Procedure 2000-26 section 4.03(1), then as a practical matter the underpayment interest rate is already equal to the overpayment rate for the overlapping overpayment period. In such a case, the net rate of zero is already achieved, thus there is no differential to net. However, there could be a different result if the net rate of zero was initially achieved by raising the year 1 overpayment rate per Revenue Procedure 2000-26 section 4.03(2). For example, Taxpayer might request that the year 3 overpayment rate be raised to match the higher year 2 underpayment rate. Accordingly, be aware there may be a risk of excess benefit in this situation.

These principles all apply regardless of whether the payment determined to be erroneous is an underpayment or an overpayment. We are unaware of any circumstance where the cause of the error would change our advice.

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Please call (202) 317-6845 if you have any further questions.