Office of Chief Counsel
Internal Revenue Service
memorandum

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to: Mark Scott
Director, Tax Exempt Bonds SE:T:GE:TEB
Attn: Cliff Gannett, Manager, Outreach, Planning and Review

from: Carol P. Nachman
Special Counsel, Administrative Provisions & Judicial Practice
(Procedure & Administration)

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subject: Request for recovery of rebate overpayment

This memorandum responds to your request for assistance concerning the period of limitations for processing claims for recovery of rebates paid pursuant to IRC § 148(f).

ISSUES

(1-a). Whether the filing of an administrative claim for refund pursuant to IRC § 148(f) suspends the six-year period under 28 U.S.C. §§ 2401 and 2501 for bringing a civil suit in a district court or the Court of Federal Claims, respectively.

(1-b). Whether the Service must process a claim and pay any refund pursuant to IRC § 148(f) within the six-year period.

(2). Whether a bond issuer must file a claim for an amount related to an interim payment within a six-year period from the date of that interim payment.

CONCLUSIONS

(1-a). No. The filing of an administrative claim for refund pursuant to IRC § 148(f) does not suspend the six-year period for bringing a civil suit.

(1-b). No. In general, the extent of the Service's authority to act while claimants' periods for filing nontax civil suits and tax refund suits are open should be the same. Published guidance regarding tax refund claims indicates that if the Service has processed a claim within the two-year period for filing a tax refund suit and has decided to allow the claim, the Service may then issue a refund after the two-year period. Thus, we believe the same would apply when the period is for six years. There are grounds,

however, for arguing that the Service could take a more restrictive approach regarding the extent of its authority for nontax civil suits. We advise, however, that you not take a more restrictive approach before there is published guidance on the applicability of the six-year period under IRC § 148(f). We are especially concerned that our denial of a claim on procedural grounds, where the issuer may argue that it was not aware the administrative submission did not protect its rights, may appear to be a harsh result that could be reversed in litigation, leaving us with a precedent that restricts our processing options.

(2). In general, no. A bond issuer must file a claim for an amount related to an interim payment within a six-year period from the date of the final payment. If an interim payment, however, turns out to be the last rebate payment made for the issue, the six-year period would run from the date of the discharge of the last bond in the issue.

BACKGROUND

IRC § 103 excludes from gross income interest on any State or local bond. This exclusion, however, does not apply to an "arbitrage bond" as defined by IRC § 148. In general, IRC § 148(a) defines an arbitrage bond as "any bond issued as part of an issue any portion of the proceeds of which are reasonably expected (at the time of issuance of the bond) to be used directly or indirectly (1) to acquire higher yielding investments, or (2) to replace funds which were used directly or indirectly to acquire higher yielding investments." IRC § 148(a)(1), (2). A bond which is part of an issue is treated as an arbitrage bond unless the issuer rebates (turns over) to the Service any arbitrage profits earned from investing the proceeds of the tax-exempt issue in higher yielding investments. IRC § 148(f).

The computation to determine if an arbitrage rebate is due is made at the end of every fifth year during the term of the issue (a "Required Computation") and when the last bond in the issue is discharged (the "Final Computation"). The computations are based on future values. A rebate amount must be paid no later than 60 days after each Required Computation date, as well as the Final Computation date. IRC § 148(f). A rebate payment is paid when it is filed with the Service at the place designated by the Commissioner. Treas. Reg. § 1.148-3(g). A rebate payment must be accompanied by Form 8038-T, *Arbitrage Rebate*. The failure to pay a rebate amount when required can result in the bonds being classified as arbitrage bonds, and the interest paid on bonds may lose the IRC § 103 exemption. The Service does not make any assessment as described in IRC § 6201 or undertake any collection activity under IRC § 6301 against the issuer for failure to pay the rebate, but the Service would assess the bondholders for the interest income, after following the deficiency procedures in IRC §§ 6211-6215.

Treas. Reg. § 1.148-3(i)(1) provides that an issuer may recover an overpayment for an issue of tax-exempt bonds by establishing to the satisfaction of the Commissioner that the overpayment occurred. An overpayment is the excess of the amount paid to the United States for an issue under IRC § 148 over the sum of the rebate amount for the issue as of the most recent computation date and all amounts that are otherwise

required to be paid under IRC § 148 as of the date the recovery is requested. The regulation does not prescribe a time by which a request for recovery must be filed with the Service. A refund is requested on Form 8038-R, *Request for Recovery of Overpayments Under Arbitrage Rebate Provisions*.

In regard to Issue (2), you have informed us that Treas. Reg. § 1.148(f) provides that the first interim rebate payment must be made for a computation date that is not later than 5 years after the issue date and additional interim payments must be made at five year intervals thereafter. Also, Treas. Reg. § 1.148-3(g) provides that each rebate payment must be paid no later than 60 days after the computation date to which the payment relates. Treas. Reg. § 1.148-3(i)(2)(i) provides that an overpayment may be recovered only to the extent that a recovery on the date that it is first requested would not result in an additional rebate amount if that date were treated as a computation date. You also note that an interim payment may become the last rebate payment where no final rebate payment is required upon the final date of discharge.

LAW AND ANALYSIS

(1-a). Whether the filing of an administrative claim for refund pursuant to IRC § 148(f) suspends the six-year period under 28 U.S.C. §§ 2401 and 2501 for bringing a civil suit in a district court or the Court of Federal Claims, respectively.

The Service has not prescribed a rule under IRC § 148 mandating the submission of a claim for administrative consideration in order to recover an overpayment of a rebate. That is, neither the regulations nor form instructions prescribe a time by which a request for refund must be filed with the Service. The only action that governs the timeliness of pursuing a claim is the filing of a suit in court. The optional submission of an administrative claim thus does not suspend the period of limitations for filing suit. Compare Rev. Rul. 57-242, 1957-1 C.B. 452, regarding (nontax) claims for overpayment interest (discussed further below). Therefore, the submission of an administrative claim on Form 8038-R has no effect on the six-year period of limitations for filing a civil suit under 28 U.S.C. §§ 2401 and 2501.

(1-b). Whether the Service must process a claim and pay any refund pursuant to IRC § 148(f) within the six-year period.

The common and earliest application of the six-year period in the tax law involves claim for overpayment interest under IRC § 6611. See Rev. Rul. 56-506, 1956-2 C.B. 959. In regard to such a claim, Rev. Rul. 57-242 cautions that even though an adjustment of overpayment interest may be allowed and paid upon request at any time within the six years, the only manner in which a taxpayer can fully protect its rights is by filing suit before the expiration of the six-year period. Rev. Rul. 57-242 has not generated controversy regarding the endpoint by which the Service may act on a claim. We suspect such an issue does not arise because the right to interest follows from the settlement of the substantive tax controversy. Indeed, the Service will generally provide

the interest without the taxpayer making a claim, and the revenue ruling contemplates an apparently straightforward adjustment of that amount.

Rev. Rul. 57-242 indicates that the Service must issue any refund before the expiration of the six-year period even if the Service were working a claim that had been submitted with a year left in the period and had determined that the claim was correct at the end of the period. Nevertheless, we would not apply the revenue ruling to the rebate refund procedure because (1) published guidance for an analogous situation involving the two-year period for filing a civil suit for a tax refund under IRC § 6532(a) is more generous to the claimant (see Rev. Rul. 59-212, 1959-1 C.B. 692, and Rev. Rul. 69-508, 1969-2 C.B. 262, discussed below), and (2) the apparently stricter requirement in Rev. Rul. 57-242 may have to do with its being a more general interpretation compared to the tax refund revenue rulings. Those rulings actually focus on the timeliness of the submission of additional information for a claim that could not be completely processed before the expiration of the period for filing suit.

The procedures for administrative tax claims for credit or refund are generally not helpful for nontax claims because the former are mandatory, and the two-year period of limitations for filing suit under IRC § 6532(a) does not begin to run until the Service issues a letter of claim disallowance. Once the notice of claim disallowance is issued (as is the case in Rev. Rul. 59-212 and Rev. Rul. 69-508), however, the administrative procedures are similar because the Service may reconsider a disallowance, but only within the claimant's period for filing suit.[1]

In Rev. Rul. 59-212 an employer filed a timely claim for an overpayment of the employer and employee's shares of employment tax. The Service disallowed the claim because information necessary to support it was missing. The revenue ruling provides that the information may be provided any time within the applicable statutory period of limitation. Specifically, the District Director had to receive the information in sufficient time for his office "*to reconsider the claim and authorize the refund prior to the expiration of the two-year period provided by*" the IRC of 1939's predecessor of IRC § 6532(a). Italics added. Similarly, in Rev. Rul. 69-508 a taxpayer filed a claim for an overpayment of communications excise tax. The timely claim was disallowed because information necessary to support the claim was missing. The revenue ruling provides that the claim may be reopened and reconsidered to the extent the information is submitted to the

[1] In regard to tax refund suits, IRC § 6514(a)(2) makes any credit or refund of tax (based on a timely filed but disallowed claim) erroneous if the credit or refund was made after the two-year period of limitation for bringing suit, unless within such period suit was begun by the taxpayer. While the six-year statute does not contain an outright prohibition comparable to IRC § 6514(a)(2), the Service is in a similar situation regarding the processing of nontax claims. In each situation the claimant's filing of a claim right before the expiration of the period does not trigger any rights for the claimant. The Service is not in the position of a court taking jurisdiction over an action, rather, its processing only serves the purpose of possibly eliminating the need for judicial action. As indicated by the caution in Rev. Rul. 57-242, the only action that provides the claimant with rights is the filing of a suit in court.

District Director in sufficient time for his office "*to reconsider and take action on the claim prior to the expiration of the two-year limitation period prescribed by section 6532(a)(1) of the Code within which suit may be brought on disallowed claims.*" Italics added. These revenue rulings do not define, as steps in the processing, the terms "authorize" and "take action," so they are not addressing a specific point in time in the processing of the relevant claims. Nevertheless, they make it clear that a tax refund does not have to be issued before the expiration of the two-year statutory period if the refund is approved by that time. We see no reason why the Service does not have similar authority for claims subject to the six-year period.

If the Service receives a claim with more than adequate time to process it within the six-year period, and did, in fact, decide to allow it before then, but inadvertently allowed a lengthy period of time to pass before preparing the refund check, we would exercise caution and allow the refund to be issued. While Rev. Rul. 59-212 and Rev. Rul. 69-508 assume the Service will issue the refund check shortly after approving the refund, we see no reason why the Service's approval authority would be retroactively removed due to an inadvertent delay in completing the processing.

The caution in Rev. Rul. 57-242 that a taxpayer can protect his rights only by filing suit within the appropriate period suggests that the Service may take a more restrictive approach than that in Rev. Rul. 59-212 and Rev. Rul. 69-508. We advise not considering such an approach without publishing guidance regarding the recovery of rebates and the six-year period. Otherwise, we see a litigating hazard should the Service deny a claim that may have substantive merit. The denial would produce a harsh result for the issuer, who may argue it thought the administrative submission protected its rights.

(2). Whether a bond issuer must file a claim for an amount related to an interim payment within a six-year period from the date of that interim payment.

In general, a civil action commenced against the United States shall be barred unless the complaint is filed within six years after the right of action first accrues. 28 U.S.C. §§ 2401(a); 2501. The starting date for the six-year period is based on the common law rule for when the period for the cause of action begins (i.e., when all the events which fix the government's alleged liability have occurred and the taxpayer was or should have been aware of their existence). General Instruments Corp. v. United States, 33 Fed. Cl. 4, 7-8 (1995). See also Norwest Bank Minn. Nat'l Ass'n v. Federal Deposit Insurance Corporation, 312 F.3d 447, 452 (D.C. Cir. 2002), rehearing and rehearing en banc denied, 2003 U.S. App. LEXIS 2528 (D.C. Cir. Feb. 11, 2003) (For claims that are similar to one 'for restitution of money paid through mistake.' . . . . In such cases, courts generally regard the statutory period to begin to run when the payment is made.")

Where an issuer made its Final Computation under IRC § 148(f) and timely paid the rebate with the Form 8038-T, we have opined that at the time of payment, all the events which fixed the government's alleged liability had occurred and an issuer should have been aware of their existence. These events are: (1) the discharge of the last bond in

the issue; (2) the requirement to do the Final Computation under IRC § 148(f); and (3) the requirement to pay the arbitrage rebate within 60 days after the Final Computation date. You inform us that the regulations referenced in the Background, above, clearly fix both an obligation on the part of both the Issuer (to make interim rebate payments) and the government (to refund overpayments prior to the date of discharge under certain circumstances). As the issuer should have been aware of the government's obligation regarding refunds of interim payments as of the filing of the Form 8038-T, you ask whether a six-year period should begin upon a timely interim payment.

As we understand it, as long as the bonds are outstanding, the Service may assert that they are not exempt and thus may assess a deficiency for the open years of the bondholders. One ground for the Service's assertion may be an insufficient interim payment made, for example, ten years earlier. As the Service's examination upon the retirement of the bonds would cover the whole issue period, we believe, conversely, the issuer should be able to claim a refund for the whole issue period after the final payment. The general rule of General Instruments Corp. does not preclude this result as it does not address the concept of interim payments. Accordingly, a six-year period does not start on a payment of an interim payment, at the earliest, until the bonds are discharged. Thus, even if the amount of an interim payment was incorrectly computed, but otherwise unchanged by subsequent events except for the discovery of the error, the issuer may, nevertheless, obtain a refund within six years of the timely final payment or, if there is no final payment, within six years of the date of discharge.

Please call John Moran at (202) 622-7107 if you have any questions.

cc: Tim Jones