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INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR:

FROM: Elizabeth G. Beck
Senior Technical Reviewer, CC:INTL:BR6

SUBJECT:

This Field Service Advice responds to your memorandum dated April 21, 2000. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

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LEGEND:

A	=
B	=
C	=
Accounting Firm	=
FSC1	=
NewCorp	=
State	=
Possession	=
USCorp	=
Year 1	=
Year 2	=
Year 3	=
Year 4	=
Year 5	=

ISSUE:

Under the facts presented, whether FSC1 or its related supplier, USCorp, timely filed a redetermination pursuant to Temp. Treas. Reg. § 1.925(a)-1T(e)(4) with respect to commissions payable by USCorp to FSC1 for Year 1.

CONCLUSIONS:

No. Neither FSC1 nor USCorp timely filed a redetermination with respect to commissions payable by USCorp to FSC1 for Year 1 because, under the facts presented, the requirements of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) were not met. Temp. Treas. Reg. § 1.925(a)-1T(e)(4) requires first, that both the FSC's and related supplier's statutes of limitation for refund under section 6511 must be open, and second, that any redetermination shall affect both the FSC and the related supplier. Here, FSC1's period of limitation for assessment had expired before USCorp and FSC1 filed their respective redeterminations for Year 1. Therefore, any redetermination could not affect FSC1. In addition, the requirement that the statutes of limitation for making claims for refund be open for the FSC and the related supplier was not met. The voluntary payment by FSC1, which was made after its period of limitation on refund on FSC1's original return had expired, had no effect on FSC1's refund period of limitation for purposes of Temp. Treas. Reg. § 1.925(a)-1T(e)(4). Therefore, USCorp made its redetermination after the expiration of FSC1's period of limitation for refund had expired.

FACTS:

USCorp, now known as NewCorp, is a U.S. corporation headquartered in State. USCorp is a Coordinated Examination Program taxpayer and is examined each year. FSC1, a corporation incorporated in Possession, is a wholly-owned subsidiary of USCorp. FSC1 properly elected treatment as a foreign sales corporation ("FSC") pursuant to sections 922(a) and 927(f)(1), and receives a commission on certain items exported by USCorp. Both USCorp and FSC1 file U.S. income tax returns on a calendar year basis. This memorandum addresses U.S. income tax returns filed by USCorp and FSC1 for Year 1.

USCorp

USCorp filed its original Year 1 income tax return (Form 1120, "U.S. Corporation Income Tax Return") on July 27 of the following year, Year 2. USCorp and the Service timely executed Forms 872 ("Consent to Extend the Time To Assess Tax") for Year 1, extending USCorp's period of limitation for assessment for Year 1 to December 31, Year 5.

During Year 3 while under examination for Year 1 and two subsequent taxable years, USCorp retained Accounting Firm to recompute its commissions payable to FSC1. Several times between June and August of Year 4, USCorp orally stated to the Exam Team that it intended to file refund claims based upon increased commissions payable to FSC1 for the taxable years under audit and that the increased commissions would cause FSC1 to have additional taxable income. There is no evidence to suggest that USCorp informed the Exam Team of the amount of USCorp's anticipated refund for any taxable year under audit or the amount of the redetermined FSC commissions when these statements were made. Several years later on February 23, Year 5, USCorp filed an amended return (Form 1120X) claiming a refund in the amount of $A for Year 1 based upon increased commission expenses payable to FSC1 due to a change from grouping of transactions to a transaction-by-transaction basis.

FSC1

Subject to a six-month filing extension through September 15, Year 2, FSC1 timely mailed its Year 1 income tax return (Form 1120-FSC, "U.S. Income Tax Return of a Foreign Sales Corporation") on September 8, Year 2, to the Philadelphia Service Center. The Service Center received FSC1's Year 1 income tax return three days later on September 11, Year 2. FSC1's Year 1 income tax return was not examined by the Service. FSC1 and the Service did not execute Forms 872 to extend FSC1's period of limitation to assess tax beyond the initial three-year assessment period under section 6501(a). FSC1 failed to attempt to preserve its period of limitation for assessment for Year 1.

On September 14, Year 4, a date more than three years after the Service received FSC1's original return for Year 1, FSC1 remitted an electronic payment to the Service in the amount of $B for Year 1. On September 15, Year 4, USCorp mailed, on behalf of FSC1, FSC1's amended Form 1120-FSC for Year 1 to the Service.[1] The amended Form 1120-FSC, which was signed and dated September 10, Year 4, reflected additional tax due in the amount of $B, based upon increased commission income in the amount of $C to FSC1. This amended return was received by the Service on September 17, Year 4. On October 12, Year 4, the Service processed FSC1's $B electronic payment. The increased commission payments to FSC1 were also reflected in USCorp's amended return filed several years later on February 23, Year 5, as referenced above.

LAW AND ANALYSIS:

Overview of the Law

Section 6501(a) states the general rule on the period of limitation for assessment of tax, and requires the Service to assess tax due within three years after the return was filed. Section 6501(c) provides several exceptions to the general rule. In particular, section 6501(c)(4) states that the Service and taxpayers may enter into agreements to extend the period of limitation for assessment of tax, provided the agreement is executed before the expiration of the period for assessment under section 6501(a), or as previously extended under section 6501(c)(4).

Section 6511(a) states the general rule on the period of limitation for filing a refund claim, and requires a taxpayer to file a claim for a refund of an overpayment of tax the later of three years from the time the return was filed or two years from the time the tax was paid. Section 6511(c) provides several exceptions to the general rule. In particular, section 6511(c)(1) provides that if the Service and a taxpayer have entered into an agreement to extend the period of limitation for assessment of tax pursuant to section 6501(c)(4), the period for filing a claim for refund shall not expire before six months after the expiration of the extended period for assessment.

Section 7502(a) and Treas. Reg. § 301.7502-1(a) state the general rule that a return, claim, statement, or other document is deemed to be filed on the date of the postmark stamp that the document is mailed rather than the date that it is received by the Service after its due date ("mailbox rule"), provided the postmark date falls within the prescribed period or, on or before the prescribed due date of the return, claim, statement or document. Therefore, if a return or claim is postmarked timely, the return, claim or document is considered timely filed even if received after the

[1] It is unclear whether USCorp had any authority to represent FSC1, a separate taxpayer, before the Service with respect to FSC1's income tax liabilities.

last date prescribed to file the document or claim. Treas. Reg. § 301.7502-1(a). Hence, section 7502 applies only where a document is delivered to the Service after the last date prescribed for filing. First Charter Financial Corp. v. United States, 669 F.2d 1342 (9th Cir. 1982); Treas. Reg. § 301.7502-1(e)(2). A return (or refund claim) that is filed prior to the due date, as extended, is deemed filed on the date of receipt by the Service. Id. Section 7502 applies only to "documents" as defined in Treas. Reg. § 1.7502-1(b), including a claim or statement. Treas. Reg. §§ 1.7502-1(a), (b). Therefore, it does not apply to the payment of any tax. Treas. Reg. § 1.7502-1(a).

Treas. Reg. § 301.6402-3(a)(5) provides that a properly executed original or amended income tax return, e.g., Form 1120X, shall constitute a claim for refund or credit within the meaning of sections 6402 and 6511 for the amount of the overpayment disclosed by such return or amended return. For purposes of section 6511, a claim for refund or credit is considered filed on the date on which such return or amended return is considered filed, except if the requirements of Treas. Reg. § 301.7502-1, relating to timely mailing treated as timely filing, are met. If the requirements of Treas. Reg. § 301.7502-1 are met, the claim is considered filed on the date of the postmark stamped on the cover in which the return or amended return was mailed. Treas. Reg. § 301.6403-3(a)(5) further provides that an amended return shall constitute a claim for refund or credit if it contains a statement setting forth the amount determined as an overpayment and advising whether such amount shall be refunded to the taxpayer or shall be applied as a credit.

Section 6401(a) defines the term "overpayment" to include the part of a payment of any internal revenue tax that is assessed or collected after the expiration of the period for assessment. Section 6401(c) provides that no amount paid shall be considered to be an overpayment "solely by reason of the fact that there was no tax liability in respect of which such amount was paid." In the case of an overpayment of tax, section 6402(a) provides that the Service may credit the amount of the overpayment against any tax liability of the party that made the overpayment, and refund any balance to the party.

The rules governing redeterminations of FSC commissions for taxable years beginning before January 1, 1998, are contained in Temp. Treas. Reg. § 1.925(a)-1T(e)(4) (1987), and pertain to transactions of a FSC and its related supplier. See T.D. 8126, 1987-1 C.B. 184. A "related supplier" is defined as a related party that directly supplies to a FSC property or services which are disposed by the FSC in a transaction that produces foreign trading gross receipts, or, as in this case, a related party which uses the FSC as a commission agent to dispose of any property or services that produce foreign trading gross receipts. Temp. Treas. Reg. § 1.927(d)-2T(a). "Related party" means a person that is owned or controlled directly or indirectly by the same interests as the FSC pursuant to section 482 and Treas. Reg. § 1.482-1(a). Temp. Treas. Reg. § 1.927(d)-2T(b).

Temp. Treas. Reg. § 1.925(a)-1T(e)(4) (1987), applicable for Year 1, states:

> (4) *Subsequent determination of transfer price, rental income or commission*. The FSC and its related supplier would ordinarily determine under section 925 and this section the transfer price or rental payment payable by the FSC or the commission payable to the FSC for a transaction before the FSC files its return for the taxable year of the transaction. After the FSC has filed its return, a redetermination of those amounts by the Commissioner may only be made if specifically permitted by a Code provision or regulations under the Code. Such a redetermination would include a redetermination by reason of an adjustment under section 482 and the regulations under that section or section 861 and § 1.861-8 which affects the amounts which entered into the determination. In addition, a redetermination may be made by the FSC and related supplier if their taxable years are still open under the statute of limitations for making claims for refund under section 6511 if they determine that a different transfer pricing method or grouping of transactions may be more beneficial. Also, the FSC and related supplier may redetermine the amount of foreign trading gross receipts and the amount of the costs and expenses that are used to determine the FSC's and related supplier's profits under the transfer pricing methods. Any redetermination shall affect both the FSC and the related supplier. The FSC and the related supplier may not redetermine that the FSC was operating as a commission FSC rather than a buy-sell FSC, and vice versa.

Temp. Treas. Reg. § 1.925(a)-1T(e)(4) (1987) (emphasis added).[2]

The above-cited language sets forth two requirements for a redetermination of FSC commission. First, the regulation requires that both the FSC's and related supplier's statutes of limitation for refund must be open under section 6511. The United States Tax Court held in Union Carbide Corp v. Commissioner that a related supplier could not claim a refund for overpayment of taxes based on recomputations of commission expenses payable to its FSC under Temp. Treas. Reg. § 1.925(a)-1T(e)(4), where the statutes of limitation for refund were not open for both the related supplier and its FSC. Union Carbide Corp. v. Commissioner, 110 T.C. 375 (1998). The court rejected the related supplier's argument that the language of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) requires that only the party in the position of overpayment, often the related supplier, must file its claim for refund within the time period allowed under section 6511. Second, the regulation requires

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[2] Temp. Treas. Reg. § 1.925(a)-1T(e)(4), as amended in 1998 by T.D. 8764, 1998-1 C.B. 844, excludes grouping of transactions as a basis for redetermination of transfer price, rental income or commission.

that the redetermination of FSC commission "shall affect" both the related supplier and the FSC. A redetermination "shall affect" both the related supplier and the FSC where the Service assesses and collects additional tax due from the taxpayer that is placed in a deficiency position (typically the FSC) as a result of the redetermination of FSC commission, and refunds the overpayment of tax to the related taxpayer (typically the related supplier) placed in an overpayment position.

Analysis

In this case, there are three possible situations in which a redetermination may have been made under Temp. Treas. Reg. § 1.925(a)-1T(e)(4). A redetermination may have been made, first, when FSC1 remitted its electronic payment on September 14, Year 4, or when its amended Form 1120-FSC was filed; second, when USCorp orally advised Examination of its intent to file a refund claim involving a redetermination of FSC commissions; or third, when USCorp filed its amended return (Form 1120X) on February 23, Year 5, claiming a refund due to overpayment of commissions to FSC1. To determine whether FSC1 or USCorp made a timely redetermination, inquiry focuses first on what constitutes a "redetermination" under Temp. Treas. Reg. § 1.925(a)-1T(e)(4).

Temp. Treas. Reg. § 1.925(a)-1T(e)(4) (1987) states clearly that the Commissioner may redetermine the transfer price, rental payment or commission payable to the FSC. Additionally, Temp. Treas. Reg. § 1.925(a)-1T(e)(4) (1987) allows a FSC and its related supplier to redetermine the amount of foreign trading gross receipts and the amount of costs and expenses used to compute their profits under the transfer pricing methods, where the FSC and related supplier determine that a different transfer pricing method or grouping of transactions is more beneficial.

In the instant case, the recomputation of FSC1's commission was based upon a change from grouping of export transactions to a transaction-by-transaction basis (including attendant changes in the allocation of costs and expenses). As such, the recomputation constitutes a redetermination and must meet the requirements of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) in a manner consistent with the general rules regarding amended returns and refund claims.

Below, we review the three possible situations in this case to discern whether a redetermination was timely under the requirements of Temp. Treas. Reg. § 1.925(a)-1T(e)(4).[3]

Situation 1 FSC1's Voluntary Payment of Additional Tax

[3] For additional discussion, see FSA 200006006 (Feb. 11, 2000), FSA 199924016 (June 18, 1999) and FSA 199919021 (Feb. 10, 1999).

Pursuant to section 6501(a), the Service has three years from the date of filing of a return to assess tax related to that return, unless an exception applies. In the instant case, FSC1 filed its Form 1120-FSC for Year 1 on September 11, Year 2, the date that the return was received by the Service since it was received before its extended due date. See First Charter Financial Corp. v. United States, 669 F.2d 1342 (9th Cir. 1982); Treas. Reg. § 301.7502-1(e)(2). FSC1 did not execute an agreement to extend its period of limitation for assessment of tax for Year 1. The facts do not indicate that any other exception under section 6501 would apply here. Therefore, the Service had three years from September 11, Year 2, to assess any income tax due from FSC1 for Year 1.

When FSC1 made its electronic payment of additional tax on September 14, Year 4, the section 6501 three-year period of limitation for assessment had expired. Additionally, the three-year period of limitation for assessment had expired before FSC1's amended return was filed on September 17, Year 4, the date the amended return was received by the Service. Where, as here, a payment of additional tax is made after expiration of the period for assessment, the Service may accept voluntary payments of additional tax, but cannot assess the additional amount tendered. I.R.C. § 6501; I.R.M. § 403(26). Where a taxpayer voluntarily makes a payment of additional tax after the expiration of its period of limitation for assessment, the taxpayer is entitled to a refund of its payment. Diamond Gardner Corp. v. Commissioner, 38 T.C. 875, 881 (1962); Rev. Rul. 74-580, 1974-2 C.B. 400. In such cases, the Service must refund the amount of the voluntary payment, provided the taxpayer files a timely claim for refund in accordance with the terms of section 6511(a). Rev. Rul. 74-580, 1974-2 C.B. 400.

In this case, FSC1's voluntary payment of additional tax is simply that, a payment, not a redetermination of transfer price, rental payment or FSC commission based on a change in transfer pricing method, grouping of transactions or related costs and expenses. Although FSC1's amended return for Year 1 may have been the proper manner by which to make a redetermination, FSC1's amended return, and thus its redetermination, was not timely because the “shall affect” requirement of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) was not met. The Service could not assess additional tax against FSC1 since its period of limitation for assessment had expired.

In addition, the voluntary payment by FSC1, which was made after the period of limitation on assessment had expired, had no effect on FSC1's refund period of limitation for the purposes of Temp. Treas. Reg. § 1.925(a)-1T(e)(4). The relevant refund period for this purpose pertains to the original tax return, that is, the Form 1120-FSC filed by FSC1 in Year 2. As noted above, the refund period of limitation had expired on September 11, Year 4, which was prior to the voluntary payment.

In sum, because FSC1's three-year period of limitation for assessment, which began to run on September 11, Year 2, had expired before the filing of its amended

return on September 17, Year 4, any assessment of additional tax based on the amended return is barred by section 6501(a). Therefore, FSC1's redetermination is untimely because it failed the "shall affects" requirement of Temp. Treas. Reg. § 1.925(a)-1T(e)(4). Moreover, the voluntary payment of additional tax had no effect on the refund period of limitation applicable to FSC1 under Temp. Treas. Reg. § 1.925(a)-1T(e)(4). Therefore, the regulation's requirement that the statutes of limitation for making claims for refund be open for the FSC and its related supplier was not met.

Situation 2 USCorp's Oral Notification of Intent to File a Refund Claim

USCorp argues that its redetermination was timely, as it was made between June and August of Year 3, prior to the expiration of FSC1's three-year period of limitation for assessment, when USCorp orally notified the Exam Team of its intent to file a redetermination. Therefore, the focus of inquiry is whether USCorp's oral statements of future intent to file a redetermination, made prior to the expiration of FSC1's period of limitations for assessment, constitute a timely filing of an informal refund claim.[4]

Informal claims for refund are recognized as valid claims for refund, although they are not made in the form of an amended return.[5] New England Elec. Sys. v. United States, 32 Fed. Cl. 636, 641 (Fed. Cl. 1995) citing United States v. Kales, 314 U.S. 186 (1941); Furst v. United States, 678 F.2d 147 (Ct. Cl. 1982); American Radiator & Standard Sanitary Corp. v. United States, 318 F.2d 915 (Ct. Cl. 1963). An informal claim for refund serves the same purpose as a formal claim for refund, that is, to put the Commissioner on notice that the taxpayer asserts a right with respect to an overpayment of tax. Furst, 678 F.2d at 151 quoting Newton v. United States, 163 F. Supp. 614, 618 (Ct. Cl. 1958).

An informal claim must contain the following three components. First, an informal claim must provide the Service with notice that the taxpayer asserts a right to a refund. New England Elec. Sys., 32 Fed. Cl. at 641. Second, the claim must

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[4] As noted above, FSC1 did not file a refund claim. Rather, FSC1 made a voluntary payment of additional tax, as evidenced by its electronic payment and amended Form 1120-FSC showing additional tax owed.

[5] The formal requirements of a return differ from the elements of an informal refund claim. A return qualifies as a sufficient return under the Code where it is filed on the proper form (I.R.C. § 6011, Treas. Reg. § 1.6011-1(a)), contains sufficient information to permit the Service to calculate tax (see Germantown Trust v. Commissioner, 309 U.S. 304 (1940); United States v. Mundt, 666 F.2d 1029 (6th Cir. 1981)), and is signed under penalties of perjury by the person making the return (I.R.C. §§ 6061, 6062, 6065(a)).

describe the legal and factual basis for the refund. Id. Third, the informal claim must have some written component. Id. citing American Radiator, 318 F.2d 920. Courts have required the written component in recognition of turn over in government personnel working on a case. Furst, 678 F.2d at 151 citing Wrightsman Petroleum Co. v, United States, 35 F. Supp. 86, 96 (Ct. Cl. 1940), cert. denied, 313 U.S. 578 (1941).

Stating that an informal claim arises through conduct consisting of both written and oral elements, the New England Electric court noted that,

> An informal claim, however, requires a court to go beyond the written component and examine the facts and circumstances which are presented in every case . . . . As such, no set rules can be elucidated as to what constitutes an adequate informal claim; rather, each case must be determined based on its own unique set of facts. Of primary importance, however, is the existence of some written component. While courts have varied on the degree of detail required for a writing to adequately constitute an informal claim, all courts agree that some written component is required.

New England Elec. Sys., 32 Fed. Cl. at 641-642 (emphasis added).

The court explained further that while undocumented oral claims alone cannot establish the elements of an informal claim, oral statements of a taxpayer documented in writing by IRS personnel may satisfy the written component of an informal claim. New England Elec. Sys., 32 Fed. Cl. at 643 citing Sicanoff Vegetable Oil Corp. v. United States, 181 F. Supp. 265, 269 (Ct. Cl. 1960) (oral claims alone are insufficient); Disabled American Veterans v. United States, 650 F.2d 1178, 1179-80 (Ct. Cl. 1981) (oral claims alone are insufficient); Newton v. United States, 163 F. Supp. 614, 619 (Ct. Cl. 1958) (IRS memorandum considered a component of informal claim); Pinckes v. United States, 7 Cl. Ct. 570, 571 (1985) (undocumented oral statements are insufficient); Faria Corp. v. United States, 77-1 U.S.T.C. ¶ 16,251 at 87,317 (Tr. Div. Ct. Cl. 1977) (written component of informal claim need not be a writing created by taxpayer, but may be an internal IRS memorandum recording what taxpayer intended to do).

While an informal claim as a whole must specifically request a refund of a sum certain, must indicate the taxable years for which the refund is requested and must contain a description of the legal basis for the claim, “the written component [of the informal claim] alone does not necessarily have to be the source [of the required information].” New England Elec. Sys., 32 Fed. Cl. at 644 citing Furst v. United States, 678 F.2d at 151; American Radiator, 318 F.2d 915, 920; Faria Corp., 77-1 U.S.T.C. at 87,325; United States v. Commercial Nat’l Bank of Peoria, 874 F.2d, 1665, 1171 (7th Cir. 1989). The degree of specificity required of a taxpayer’s written component of an informal claim is reduced when a revenue agent obtains

detailed information on audit. New England Elec. Sys., 32 Fed. Cl. at 644 citing National Newark & Essex Bank v. United States, 410 F.2d 789, 795 (Ct. Cl. 1969) (explaining that while Service's knowledge may lessen the degree of specificity required, the burden does not shift from taxpayer to Service). The written component of an informal claim must, at a minimum, be a sufficient assertion by a taxpayer that the tax has been overpaid. New England Elec. Sys., 32 Fed. Cl. at 644 citing Newport Indus. v. United States, 60 F. Supp 229, 232 (Ct. Cl. 1945).

In the instant case, USCorp has not met the requirements for an informal claim for refund. First, although USCorp's oral statements of intent to file refund claims may have given the Exam Team notice that it would assert a right to refund(s), there is no evidence indicating that the Exam Team was given a legal or factual basis for the FSC commission redetermination, until FSC1 filed its amended return on September 15, Year 4, a date after the expiration of FSC1's period of limitation for assessment. Second, there is no evidence of a written component, either by USCorp or a Service employee, until USCorp filed its amended return on February 23, Year 5, claiming overpayment of FSC commissions. As a result, the purported informal claim did not contain the necessary components to constitute an informal claim for refund.

Assuming arguendo that USCorp can establish that there was an informal refund claim filed in Year 4, we believe the "shall affects" requirement of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) still has not been met. The Service cannot assess additional tax against FSC1 because its period of limitation for assessment had expired. We believe that FSC1 had an affirmative duty under the "shall affects" language of the regulation to timely extend its statute of limitation for assessment, in order for it or its related supplier to gain the benefits under the regulation.

In sum, USCorp failed to meet the requirements for an informal refund claim where no legal or factual basis was provided for the purported informal claim and there was no written component. Thus, one must determine whether, under the third situation presented, USCorp's amended return meets the redetermination requirements of Temp. Treas. Reg. § 1.925(a)-1T(e)(4).

Situation 3 USCorp's Amended Return Fails to Satisfy Redetermination Requirements under Temp. Treas. Reg. § 1.925(a)-1T(e)(4)

USCorp filed its amended return (Form 1120X) on February 23, Year 5, claiming a refund on the basis of additional FSC commission deductions for Year 1. At that time, FSC1's period of limitation for assessment for Year 1 had lapsed. Accordingly, USCorp's amended return failed to satisfy the "shall affects" requirement of Temp. Treas. Reg. § 1.925(a)-1T(e)(4) since the Service could not assess FSC1 the additional tax arising from the increased commission income payable by USCorp. Furthermore, FSC1's voluntary payment of additional tax and filing of its amended return after the expiration of its period of limitation on

assessment did not affect its periods of limitation for refund or assessment. Accordingly, the Temp. Treas. Reg. § 1.925(a)-1T(e)(4) requirement that the statutes of limitation for making claims for refund for both the FSC and its related supplier was not met.

Please call (202) 874-1490 if you have any further questions.

By: _____

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