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

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INTERNAL REVENUE SERVICE NATIONAL OFFICE SERVICE CENTER ADVICE

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SUBJECT: Discretion to Abate Interest on Large Erroneous Refunds

This memorandum responds to a request for Significant Advice dated July 30, 2001. Significant Service Center Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

ISSUE

Whether the Internal Revenue Service ("Service") may abate the assessment of interest on an erroneous refund which exceeds $50,000.

CONCLUSION

The Service has the authority to abate interest assessed on erroneous refunds exceeding $50,000.

DISCUSSION

Section 6602 generally provides that any portion of an internal revenue tax which has been erroneously refunded, and which is recoverable by suit pursuant to section 7405, shall bear interest from the date of the payment of the refund. See also Treas. Reg. section 301.6602-1.

In 1986, Congress enacted section 6404(e) to provide the Commissioner additional flexibility in abating interest when interest had accrued because of the Service's "own errors or delays." H.R. Rep. No. 426, 99th Cong., 2d Sess. 844 (1985); S. Rep. No. 313, 99th Cong., 2d Sess. 208 (1986). Section 6404(e)(2) states that the Secretary shall abate an assessment of interest on any erroneous refund until the date demand for repayment is made, unless the taxpayer (or a related party) has in any way caused the erroneous refund, or the erroneous refund exceeds $50,000. Although the Secretary must abate interest on erroneous refunds that do not exceed $50,000, the statute does not explicitly address whether the Secretary has discretion to abate interest when an erroneous refund exceeds $50,000.

Legislative history can sometimes assist in ascertaining Congressional intent where a statute is ambiguous. Sundstrand v. Commissioner, 17 F.3d 965 (7th Cir. 1994). The legislative history underlying section 6404(e)(2) does not provide an entirely unequivocal answer either. It does, however, appear to give the Secretary more flexibility than might be inferred from the statute itself by stating, "[t]he bill gives the IRS the authority to abate interest but does not mandate that it do so (except that the IRS must do so in cases of certain erroneous refunds of less than $1,000,000[1] ....)." H.R. Rep. No. 426, 99th Cong., 2d Sess. 844 (1985); S. Rep. No. 313, 99th Cong., 2d Sess. 208 (1986) (emphasis added). The legislative history then goes on to state:

> The committee believes that it is inappropriate to charge taxpayers interest on money they temporarily have because the IRS has made an error. Consequently, the IRS may not charge interest on these erroneous refunds until the date it demands repayment of the money. The committee intends that two limitations be placed on this rule. First, it is not to apply in instances in which the taxpayer (or a related party) has in any way caused the overstated refund to occur. Second, it is not to apply to any erroneous refund checks that exceed $1 million.[2]

H.R. Rep. No. 426, 99th Cong., 2d Sess., at 845 (1985); S. Rep. No. 313, 99th Cong., 2d Sess., at 209 (1986) (emphasis added). The Conference Committee Report uses similar language, stating that, "the rule requiring the abatement of interest on erroneous refund checks of $1 million or less is only made applicable to erroneous refund checks of $50,000 or less." Conf. Rep. No. 841, 99th Cong., 2d Sess. II-810, II-811 (1986) (emphasis added). In summary, although the issue is not squarely addressed, neither the statute nor the legislative history explicitly

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[1] The original dollar limitation set forth in both the House Report and Senate Report was $1,000,000. This amount was reduced to $50,000 by the House-Senate Conference Committee. Conf. Rep. No. 841, 99th Cong., 2d Sess. II-810, II-811 (1986).

[2] See footnote 1, supra.

preclude the Secretary from exercising discretion to abate interest for erroneous refunds in excess of $50,000.

In the only case to consider this issue, the government argued, and the district court agreed, that the Secretary was not required under section 6404(e)(2) to abate interest on an erroneous refund which initially exceeded $50,000. United States v. Egypt Planting Co., 92-2 U.S.T.C. (CCH) ¶ 50,603 (N.D. Miss. 1992). In Egypt Planting Co., the taxpayers received an erroneous refund of federal agricultural employment taxes of $65,633.73 and returned $32,159.05 of that amount. The taxpayers argued the Service was required to abate interest on the remaining erroneous refund amount of $33,474.68, since that amount was less than $50,000. The government contended that the mandatory interest abatement rules were inapplicable to erroneous refunds exceeding $50,000. The court found that, although section 6404(e)(2) required abatement of interest on erroneous refunds of $50,000 or less, an erroneous refund that initially exceeded $50,000 must bear interest pursuant to Treas. Reg. § 301.6602-1. The court expressed some reservation about its conclusion. The opinion stated that the combination of unclear abatement provisions along with the lack of regulations "invites speculation and confusion," but ruled "on the side of caution" in holding that no abatement was available.

The statutory language of section 6404(e)(2) is susceptible of two different constructions. Thus, the "limitations" contained in that section might be read as barring any abatement of interest in the case of erroneous refunds that exceed $50,000 or that are in any way caused by the taxpayer (or a related party). On the other hand, the "limitations" could be construed only to limit the type of erroneous refunds subject to the mandatory interest abatement rules of section 6404(e)(2). On balance, we believe that the latter interpretation more closely comports with congressional intent. The legislative history of section 6404(e), as indicated above, evidences a desire to afford the Service authority to abate interest accrued because of Service "errors or delays." It further expresses the intent that the Service exercise this authority to abate interest in instances in which it issues an erroneous refund check. While it did not instruct the Service not to charge interest on the classes of erroneous refunds described in the "limitations," it would be inconsistent with the purposes underlying the statute to read those limitations as precluding the Commissioner from exercising the authority to abate interest in such cases.

The parameters of the Secretary's discretion are not defined in section 6404(e)(2), but we intend shortly to issue formal guidance that will directly address that question. In the interim, the Secretary should consider all the facts and circumstances relevant to determining whether abatement would be consistent with the legislative intent. Taxpayers who fail to return the erroneous refund for a significant period of time after they discover, or reasonably should have discovered, the error are less deserving of relief. In such circumstances, they contributed to the delay and they had the opportunity to profit from the Service's error. The Secretary might also consider whether the taxpayer returned the erroneous refund before the

Service notified the taxpayer of the error, especially if there was a substantial delay between the issuance of the erroneous refund and notification by the Service. The Secretary might want to consider the level of sophistication of the taxpayer which may indicate whether the taxpayer acted reasonably with respect to the error. Even an unsophisticated taxpayer would not merit relief, however, if they contributed in any way to the initial error by the Service, e.g., by filing a frivolous claim for refund.

Please call of CC:PA:APJP:B3 at if you have questions about this matter.

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