Office of Chief Counsel
Internal Revenue Service
Memorandum

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date: June 05, 2007

to: Associate Area Counsel (San Diego)
(Large & Mid-Size Business)
Attn: Robert Cudlip

from: Susan T. Mosley
Senior Technician Reviewer, Branch 7
(Procedure & Administration)

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subject:

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

LEGEND

Year A=
Year B=
Year C=
Date 1=
Date 2=

LAW AND ANALYSIS

This memo responds to your request for assistance in determining whether estoppel applies in this case. The basic facts here are that the taxpayer executed Forms 870-AD for its Year A through Year C taxable years on Date 1. The agreements made no specific reservation of any issues. On Date 2, the taxpayer filed amended tax returns on which they claimed certain research credits and R&D deductions under sections 41 and 174 respectively, as well as deductions for certain lease interest expenses for each of the Year A, Year B and Year C tax years. These claimed

deductions result in refunds for each tax year. In opposing the taxpayer's refund claim, you wish to know: 1) whether a Form 870-AD can bar a subsequent claim for refund, and 2) whether equitable estoppel bars the taxpayer's refund claim. In addition, through subsequent correspondence, you have questioned whether quasi-estoppel, also known as the duty of consistency, may apply in this case to prevent the refund claims.

1) A Form 870-AD does not bar a subsequent claim for refund in the Ninth Circuit.

A Form 870-AD is not a closing agreement and cannot bind the taxpayers with finality. While some federal courts have found that a Form 870-AD still may prevent a taxpayer from later filing a claim for refund, in this case the taxpayer is domiciled in the Ninth Circuit, where a Form 870-AD alone is not a bar to a subsequent claim for refund. In the case cited by the taxpayer in its responses to the several IDRs, Whitney v. United States, 826 F.2d 896 (9th Cir. 1987), the court was clear in stating that, "standing alone [the Form 870-AD] should not estop the executing taxpayer from seeking a refund." Where a taxpayer takes action contrary to the agreed terms of a previously executed Form 870-AD, the Service's only recourse is to assert that, due to additional factors, the taxpayer should be estopped from doing so.

2) Equitable Estoppel does not apply in this case.

What is less clear is the applicability of equitable estoppel against a taxpayer that has executed only a Form 870-AD. The court in Whitney declined to address that issue since it required a fact-intensive analysis and instead remanded the case. Based on the facts we have reviewed in this case, equitable estoppel does not apply.

Equitable estoppel prevents any party from profiting from an action that induced reliance in another party. The elements of estoppel are as follows: (1) there must be false representation or wrongful misleading silence; (2) the error must originate in a statement of fact, not in an opinion or a statement of law; (3) the one claiming the benefits of estoppel must not know the true facts; and (4) that same person must be adversely affected by the acts or statements of the one against whom an estoppel is claimed. Whitney, 826 F.2d at 898, fn. 5 (citing Lignos v. United States, 439 F.2d 1365, 1368 (2d Cir.1971)); Uinta Livestock Corp. v. United States, 355 F.2d 761, 766 (10th Cir.1966). These are also the accepted elements of equitable estoppel used by the Tax Court. Estate of Emerson v. Commissioner, 67 T.C. 612, 617-18 (1977).

There are certain circuits that have held that a Form 870-AD can equitably estop a taxpayer from claiming a refund. Aronsohn v. Commissioner, 988 F.2d 454, 456-57 (3d Cir. 1993); Elbo Coals, Inc. v. United States, 763 F.2d 818, 820 (6th Cir.1985); Stair v. United States, 516 F.2d 560, 564-65 (2d Cir.1975); General Split Corp. v. United States, 500 F.2d 998, 1003-04 (7th Cir.1974); Cain v. United States, 255 F.2d 193, 199 (8th Cir.1958); Daugette v. Patterson, 250 F.2d 753, 756 (5th Cir.1957), In these cases, the courts have generally found that there was some form of misrepresentation by the taxpayer in claiming a refund based on an issue that was resolved in the Form 870-AD.

As applied to this case, according to the facts provided by the taxpayer in its responses to the IDRs, the misrepresentation element of the widely-accepted equitable estoppel analysis is lacking. Where a Form 870-AD is not in and of itself binding, as Whitney clearly states, failure to abide by its prohibition against refund claims is not misrepresentation. See Whitney, 826 F.2d at 898 (where the Ninth Circuit, in looking at the bare facts before it, stated in dicta that "the government can point to no false representations (since Form 870-AD alone will not suffice) by the [taxpayers] which would justify application of the doctrine of equitable estoppel."). In this case, there are similar facts, since there are only the Forms 870-AD to rely upon and the information relating to the credits and deductions now giving rise to the refund claim was not discovered by the taxpayer until after the Forms 870-AD were executed. The basis of the refund claims did not form part of the issues settled by the Form 870-AD, which distinguishes this case from those cases where courts have found basis for equitable estoppel.

3) The duty of consistency does not apply in this case.

The duty of consistency, or quasi-estoppel, is a form of equitable estoppel that has been narrowly tailored to apply to taxpayers' actions in cases arising under federal tax laws. See United States v. Matheson, 532 F.2d 809 (2d Cir. 1976); Beltzer v. United States, 495 F.2d 211 (8th Cir. 1974); Lefever v. Commissioner, 103 T.C. 525 (1994), aff'd 100 F.3d 778 (10th Cir. 1996); Unvert v. Commissioner, 72 T.C. 807 (1979), aff'd 656 F.2d 483 (9th Cir. 1981); Hollen v. Commissioner, T.C. Memo. 2000-99, aff'd, 25 Fed.Appx. 484 (8th Cir. 2002); Hughes and Luce, L.L.P. v. Commissioner, T.C. Memo. 1994-559, aff'd, 70 F.3d 16 (5th Cir. Nov 15, 1995); see generally 15 Mertens, The Law of Federal Income Taxation 60:05 (2000) (the author provides a general discussion of the duty of consistency, as compared with other equitable doctrines); Steve R. Johnson, The Taxpayer's Duty of Consistency, 46 Tax L. Rev. 537 (1991) (the article examines the use of the duty of consistency by the Service and the associated jurisprudence).

The duty of consistency has been developed by the courts into a doctrine with more simplified applicability than equitable estoppel. Where a taxpayer takes a defined position on an issue in one tax year or makes a representation to the Service, the duty of consistency prohibits the taxpayer from taking a different position on that same issue regarding a later tax year or the same tax year at a later time, particularly where the Service would be prevented from recalculating or reassessing tax liability stemming from the earlier year due to statutes of limitation. There are only three commonly cited elements to the duty of consistency: (1) taxpayer's representation or reporting of an item for Federal income tax purposes in one year, (2) Service's acquiescence to or reliance on that representation or report for that year, and (3) taxpayer's attempts to change that representation or report in a subsequent year, after the expiration of the period of limitations with respect to the tax year at issue, where such change is to the detriment of the Service. Janis v. Commissioner, 461 F.3d 1080, 1085 (9th Cir. 2006). Noticeably, the duty of consistency does not require that there be a false representation

or misleading silence.[1] Instead, as in the cases you have cited in correspondence, the Ninth Circuit has long applied a loose standard, based primarily on "the principle that no one shall be permitted to found any claim upon his own inequity or take advantage of his own wrong." Estate of Ashman v. Commissioner, 231 F.3d 541, 543 (9th Cir. 2000) (quoting R.H. Stearns Co. v. United States, 291 U.S. 54, 62 (1934).

In looking at both the formal elements of the duty of consistency and the underlying principle as expressed by both the Supreme Court and the Ninth Circuit, that doctrine does not apply in this case. The nature of the representations made and the manner in which the taxpayer has acted do not conform to the required elements of the duty of consistency or the manner in which it is meant to be used.

Specifically, we are concerned that the "representation or report" to the Service, such as is required to apply the duty of consistency, is not sufficient here. The taxpayer executed Forms 870-AD that contained no claims for credits or deductions for research expenses or for deductions from interest payments. At the time of the execution, these claims were not under consideration by either party. To date, the Service has not claimed that the taxpayer was aware that there was a reasonable possibility that such claims would be viable for the tax years at issue. The absence of a claim for deduction or a credit is not equivalent to a representation that such claim does not exist. At most, it is a representation that there is not sufficient information to support such a claim at the time the representation is made. We understand that it was only after the execution of the agreements that the taxpayer obtained enough information to determine that such claims were potentially applicable for those tax years. This is in keeping with the underlying premise of amended returns in general-- that there are instances in which taxpayers discover information that supports a tax position different from one stated on an initial return. As the availability of forms for filing amended returns seems to indicate, the Service allows original positions to be adjusted to conform to newly discovered facts. Since the relevant courts are clear that a Form 870-AD is no impediment to filing a refund claim, there is no other procedural or policy basis to support a bar on the filing of an amended return.

Furthermore, the facts in this case are not aligned with the facts of prior cases in which the duty of consistency was imposed upon a taxpayer, in that they do not give the appearance that the taxpayer is taking advantage of the Service by changing a fundamental representation. In prior cases, such as Janis, Estate of Ashman, and others already cited, the taxpayers all made representations relating to a tax characteristic, such as characterization of a person as "owner" of an asset rather than lessor, or the undervaluation of stock held by an estate. In these instances, the representation made, then subsequently changed, is directly related to the tax

[1] In LeFever v. Commissioner, 100 F.3d 778 (10th Cir. 1996), the court mentioned that there was a divergence amongst the courts nationwide in their approach to the elements of the duty of consistency-with certain courts retaining the element of false representation or misleading silence, akin to equitable estoppel, and the others using the simplified elements discussed above. The Ninth Circuit has clearly taken the latter position. Janis, 461 F.3d at 1085.

consequences for the taxpayer. Essentially, these representations relate to what a taxpayer *is*, or what an asset *is*, for tax purposes

In contrast, in this case, the representation alleged to have been made by the taxpayer is that no further claims would be made that could lead to a refund. A refund claim, in this instance, is only indirectly related to the tax consequences for the taxpayer, because, although the statute of limitations on assessment has run, the Service may still evaluate the merits of the refund claims for the tax years at issue. This representation is related, thus, to what the taxpayer will *do* regarding its taxes, not what it or a tax item *is*, as far as tax treatment is concerned.

As such, the silence of the Forms 870-AD on the issues of claims for refund based on certain deductions and credits that were not under consideration at the time of execution is not a representation that can bind the taxpayer under the duty of consistency.

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Please call (202) 622-7950 if you have any further questions.