**Office of Chief Counsel**
**Internal Revenue Service**
# Memorandum

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date: February 23, 2012

to: Associate Area Counsel (Salt Lake City)
(Small Business/Self-Employed)

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

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subject: The Effect of Certain Entity Changes on the Availability of Interest Netting

This Chief Counsel Advice responds to your request for assistance dated December 5, 2011. This advice may not be used or cited as precedent.

LEGEND

| | |
|---|---|
| Parent | = |
| Country 1 | = |
| Country 2 | = |
| Date 1 | = |
| Date 2 | = |
| Date 3 | = |
| Date 4 | = |
| Date 5 | = |
| Date 6 | = |
| Date 7 | = |
| Entity 1 | = |
| Entity 2 | = |
| Entity 3 | = |
| Entity 4 | = |
| Month | = |

Month/Year =
State 1 =
State 2 =
TY1 =
TY3 =
TY9 =
Year 1 =

ISSUE

Whether Parent, with respect to its underpayments and overpayments of tax, and Entity 1, a former subsidiary of Parent, with respect to its underpayments and overpayments of tax, are the "same taxpayer" for purposes of interest netting under section 6621(d) after the subsidiary was purportedly merged into Parent through a series of transactions.

CONCLUSION

Parent and Entity 1 are not the “same taxpayer” for purposes of interest netting under section 6621(d). Even were we to assume that the surviving corporation after a statutory merger could be considered “the same taxpayer” as the merged entity, the series of transactions described below that Entity 1, Entity 2, Entity 3, Entity 4, and Parent engaged in did not result in a merger of Parent and Entity 1. The transactions did not result in Parent being both liable (as if it were Entity 1) for the tax that Entity 1 underpaid and entitled to a credit or refund of the tax that Entity 1 overpaid.

FACTS

You submitted a follow-up request to prior advice issued by Procedure & Administration that concerned a claim for interest netting filed by Parent on or about Date 1. After the initial advice was issued, Parent, through its representative, filed a subsequent netting claim on or about Date 2. You have asked for our opinion as to whether facts set forth in the new claim establish that Parent and its former subsidiary, Entity 1, are the “same taxpayer” potentially entitled to interest netting. Our advice herein is based on the information provided in the request for assistance, including a copy of the most recent claim, as well as the background to the first claim.

Entity 1, a business entity organized under Country 1 law, was a subsidiary of Parent but did not join in the filing of consolidated federal income tax returns with Parent for the taxable years covered by the claim, which are TY1 and TY3 through TY9.

On Date 3, Entity 1 elected under Treas. Reg. § 301.7701-3(c)(1)(i) and (g)(1)(iii) to be disregarded as an entity separate from Parent. Pursuant to the election, all of Entity 1’s assets and liabilities were deemed distributed to Parent for federal tax purposes in liquidation of Entity 1. The prior advice concluded that Entity 1’s election to be disregarded as an entity separate from Parent did not result in Parent and Entity 1 being the same taxpayer as required under section 6621(d).

Parent then undertook a series of transactions in an apparent effort to accomplish a "merger" of Entity 1 into Parent, to serve as a basis for the current netting claim.[1]

Between Month and Month/Year, Entity 1 merged into Entity 2, a Country 2 entity newly created to effectuate the merger (the "Entity 1 Merger"). A Country 2 entity was chosen because, according to the claim, Country 1 law did not allow Entity 1 to be directly merged into a United States entity. Entity 2 was the surviving entity. Pursuant to the terms of the Entity 1 Merger, established in accordance with Country 2 law, all assets and liabilities of Entity 1 were transferred to and assumed by Entity 2 by virtue of law.

On or about Date 4, Entity 2 merged, pursuant to State 1 law, into Entity 3 (the "Entity 2 Merger"), a wholly-owned subsidiary of Parent, incorporated in State 1 in Year 1. Entity 3 was the surviving entity. It is our understanding that in the Entity 2 Merger, pursuant to State 1 law, all assets and liabilities of Entity 2 were transferred to and assumed by Entity 3.

On Date 5, Entity 4 was incorporated under the laws of State 2. All of the stock of Entity 4 was initially owned by Entity 3. On Date 6, Entity 3 and Entity 4 entered into an agreement (the "Capital Contribution Agreement") under which the parties undertook a series of transactions to produce the same economic effect as if the Entity 2 Merger had not taken place. Pursuant to the Capital Contribution Agreement, Entity 3 contributed to Entity 4 the assets and liabilities related to the business formerly conducted by Entity 1 (the "Entity 1 Operations") in exchange for stock of Entity 4. Entity 3 authorized the Entity 4 stock be issued directly to Parent, which was treated as a distribution of the Entity 4 stock by Entity 3 to Parent.

On Date 7, Parent filed a Certificate of Ownership and Merger with the State 2 Secretary of State, in which Parent certified that, pursuant to State 2 law, Entity 4 merged into Parent effective on Date 7 (the "Entity 4 Merger"). Parent was the surviving entity. It is our understanding that in the Entity 4 Merger, pursuant to State 2 law, all assets and liabilities of Entity 4 were transferred to and assumed by Parent.

[1] The taxpayer has submitted certain documents and other information detailing the series of transactions discussed below. This information has not been verified, and we are not opining on whether the entities complied with the requirements for a "merger" (or any other type of transaction) under the applicable jurisdiction's laws. Where noted, we have included our understanding of how these transactions are treated under the applicable jurisdiction's law.

LAW AND ANALYSIS

Section 6621(d) provides that to the extent "interest is payable under subchapter A [sections 6601-6603] and allowable under subchapter B [sections 6611-6612] on equivalent underpayments and overpayments by the same taxpayer of tax imposed by this title, the net rate of interest under this section on such amounts shall be zero for such period." The purpose of interest netting is simply to relieve a taxpayer from owing more interest than the Service owes the taxpayer on equal amounts of money for equal lengths of time.

Section 6621(d) is effective, generally, for periods of overlap beginning after July 22, 1998 (that is, interest accruing on or after October 1, 1998),[2] but it is also applicable to prior periods of interest if certain timing requirements are met. RRA '98, Pub. L. No. 105-206, § 3301(c)(2), 112 Stat. 685, 741 (1998) (Special Rule), *amended by* Pub. L. No. 105-277, § 4002(d), 112 Stat. 2681, 2681-906 to -07 (1998); Rev. Proc. 99-43, 1999-2 C.B. 579, §§ 3.01, 4.01. Revenue Procedure 99-43 (1999-2 C.B. 579) provides guidance on the application of section 6621(d) to interest accruing before October 1, 1998, while Revenue Procedure 2000-26 (2000-1 C.B. 1257) provides guidance on the section's application to interest accruing on or after that date.[3]

A necessary element to any interest netting under section 6621(d) and the revenue procedures is that the taxpayer to which interest on an overpayment is allowable (for a certain period) must be the "same taxpayer" as the one with an underpayment on which interest is payable (for the same, overlapping period). The statute does not define the term "same taxpayer." It also does not explicitly address situations in which the identity of a taxpayer changes over time or in which one taxpayer succeeds to the tax attributes of another. The Code provides a general definition of a "taxpayer" as "any person subject to any internal revenue tax," and "person" includes a corporation, company, association, or partnership. I.R.C. § 7701(a)(1), (a)(14). This definition reinforces the basic notion that the "same taxpayer" contemplated in section 6621(d) is the entity liable for both the overpaid and underpaid tax, even if it falls short of providing insight into how section 6621(d) applies in instances of mergers, reorganizations, or similar changes.

In certain contexts, a taxpayer that succeeds to the interests of another taxpayer is treated as effectively stepping into the shoes of the other taxpayer. In particular, following a corporate merger, the surviving corporation is, in accordance with state law,

[2] Congress' intent was that netting under "[t]he provision applies to interest for calendar quarters beginning after the date of enactment." S. Rep. No. 174, 105th Cong., 2d Sess. 62 (1998), 1998-3 C.B. 537, 598. Hence the date of October 1, 1998, which was the start of the first calendar quarter after July 22, 1998.

[3] We do not have enough information to determine and express no opinion on either (1) the extent to which periods of interest on underpayments or overpayments of Parent overlap with periods of interest on underpayments or overpayments of Entity 1, or (2) the extent to which the timing requirements in section 4 of Rev. Proc. 99-43 or section 4 of Rev. Proc. 2000-26, as applicable, are met with respect to the periods of interest for which netting is claimed.

primarily liable for the federal taxes of the merged corporation, and the Service can collect the unpaid liability from the surviving corporation as if it incurred the tax. *Southern Pac. Transp. Co. v. Commissioner*, 84 T.C. 367, 374 (1985); *Missile Sys. Corp. v. Commissioner*, T.C. Memo. 1964-212; *cf. Ross Controls, Inc. v. United States*, 73 A.F.T.R. 2d 94-1343 (E.D. Pa. 1994) ("It is well-settled that a successor corporation . . . may be held liable for the tax debt of the predecessor corporation."). The surviving corporation essentially becomes responsible to deal with the tax. *See* Rev. Rul. 59-399, 1959-2 C.B. 488 (ruling that as a result of a merger, "the resultant corporation becomes in effect the same taxable entity as its absorbed constituents" and may validly extend, by written agreement with the Service, both the time for assessment of tax due from the merged corporation and the time for credit or refund of any overpayment); *see also* Treas. Reg. § 301.7701-2(c)(2)(iii)(B) Ex. 1. Likewise, after a merger, the surviving corporation can claim a refund or credit of an overpayment of tax by the merged (non-surviving) corporation. Rev. Rul. 54-17, 1954-1 C.B. 160; *cf. Seaboard Air Line Ry. V. United States*, 256 U.S. 655 (1921) (holding that a successor corporation after a state-law merger could maintain an action against the government to recover money payable to the predecessor, without the Anti-Assignment Act (then 31 U.S.C. § 203) being a bar).

Assuming arguendo that the same general theory extends to the interest netting context, after a merger, the merged entity and the surviving entity could be considered the "same taxpayer." Thus, under that theory, the surviving entity would be entitled to net interest on its underpayments or overpayments of tax with interest on the merged entity's underpayments or overpayments of tax. A further extension of the theory may arguably treat the surviving entity of successive mergers as the "same taxpayer" with respect to each of the merged entities. For example, if Corp 1 merges into Corp 2, which in turn merges into Corp 3, the surviving entity (Corp 3) might claim netting of interest on its underpayments or overpayments of tax with interest on each of the merged entities' (Corp 1 and Corp 2) underpayments or overpayments of tax.

But we are faced with neither of these situations here. Parent was not the surviving entity of a direct merger of Entity 1 into Parent; nor was Parent the surviving entity of successive mergers in which Entity 1 was one of the merged entities. Rather, following the Entity 1 Merger and Entity 2 Merger, Entity 3 contributed the Entity 1 Operations to Entity 4 (which then merged with Parent in the Entity 4 Merger). Unlike a statutory merger, the contribution pursuant to the Capital Contribution Agreement did not result in Entity 4 being primarily liable for Entity 1's underpayments of tax. In the *Southern Pacific Transportation* case (*supra*), the Tax Court distinguished between (1) the transferee liability under section 6901 of a corporation that had received by transfer all of the assets of another corporation and had contractually assumed all of the transferor's liabilities, and (2) the primary liability under state law of the surviving corporation after a merger.[4] 84 T.C. at 372-74 (as a factual matter, both bases of

[4] The court characterized primary liability as "personal liability that may be satisfied from any or all of the obligor's assets," whereas transferee liability "is not a personal liability and only subjects the property or fund, which was received by the transferee from the transferor, to the debts of the transferor." *Id*. at 374.

liability were available in the same case); *see also United States v. Kensington Shipyard & Drydock Corp.*, 187 F.2d 709, 712 (3d Cir. 1951) (transferee liability is secondary liability, not primary).

Nor did the contribution of assets and liabilities entitle Entity 4 to Entity 1's overpayments of tax under state law. *See Keith v. Woodward*, 115 F.2d 897, 899-900 (6th Cir. 1940) (holding that a transfer of one corporation's assets and liabilities to another corporation, without a state-law consolidation or merger of the corporations, did not enable the transferee to claim a refund of the overpaid tax of the transferor, as the transferee corporation "did not become liable for the taxes of the . . . [transferor] corporation by operation of law"). As a consequence, the subsequent Entity 4 Merger does not result in Parent being primarily liable for Entity 1's underpayments of tax or being entitled to Entity 1's overpayments of tax. Therefore, even if a surviving entity of a merger is the "same taxpayer" as the merged entity for purposes of section 6621(d), Parent and Entity 1 are not the "same taxpayer."

Please call (202) 622-4940 if you have any questions.

cc: Acting Chief, Branch 2
(Corporate)