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From:
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To:
Cc:
Subject: application of mitigation to refund claim, POSTS-134863-15

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You requested our views regarding the application of the mitigation provisions, sections 1311-1314, to a refund claim being considered by the IRS Examination function. An estate has submitted amended Forms 1041 that are untimely unless the mitigation provisions can be properly invoked. As further explained below, we do not believe the mitigation provisions are properly invoked; therefore, we recommend the claims be denied as untimely.

Facts:
The value of an asset reported on a Form 706 for estate tax purposes was challenged and litigated by the IRS. The same valuation listed on the Form 706 was used on subsequent years' Forms 1041, income tax returns, for purposes of reporting gain on transactions involving the asset. The litigation involving the value on the Form 706 was resolved based on a settlement on the issue of that asset's value. The litigation then concluded with a stipulated decision document signed by the parties and entered by the Tax Court.

Analysis:
In order for the mitigation provisions to apply, the first requirement is that there be a determination, as defined by IRC section 1313(a). The decision of the Tax Court in the estate tax (Form 706) case is what the estate is relying on as the determination. While this may appear to meet the definition of section 1313(a)(1), it is our position that it does not.

For the mitigation provisions to apply, a determination must involve a substantive decision on the merits which establishes that the inconsistent position in the closed year is erroneous. See, e.g., Fruit of the Loom, 72 F.3d 1338 (7th Cir. 1996), affg. T.C. Memo. 1994-492. Simply because the taxpayers have met the requirements in form regarding what constitutes a determination does not mean that they have met the substantive requirements. For example, even though under Treas. Reg. Section 1.1313(a)-1 a decision by the Tax Court or other court is a determination for mitigation purposes, that decision may not have the proper substance to demonstrate that there was an inconsistent position and that the circumstances of adjustment were described in section 1312. See, e.g., Fong v. Commissioner, T.C. Memo 1998-181. Additionally, "general administrative settlement agreements are not regarded as constituting determinations under section 1313(a)." See, e.g., Fruit of the Loom, supra; Rasmussen v. United States, 811 F.2d 949 (5th Cir. 1987). A settlement agreement does not indicate that the parties agreed on the particular value of the asset; instead, it indicates the parties reached a result both sides felt warranted conclusion of the litigation due to an acceptable result. Based on our review of the hearing transcript and documents filed in the case, we do not believe there is a "determination" as defined by section 1313(a).

For purposes of a complete analysis, we will assume the Tax Court decision is a determination under section 1313(a)(1). If that were the case, then the question would be whether a circumstance of adjustment in section 1312 applies. Paragraph 7 of section 1312 requires a determination that determines basis in property, which is what the estate is arguing the Tax Court decision does (it does reflect an agreement regarding the value, or basis), the same taxpayer (estate), and that there was an erroneous inclusion in gross income on the Form 1041 due to the incorrect valuation. However, because the Tax Court decision is a stipulated decision, neither of these circumstances is actually shown in the decision. The determination does not establish the basis, nor does it include in income the amount related to the basis. As explained in the cases cited regarding the definition of a determination, the estate will not be able to show a circumstance of adjustment applies.

We note that the requirements of section 1311(b) are satisfied here. That provision requires in a case such as this one, where the adjustment would be in the taxpayer's favor and the circumstance of adjustment is paragraph 7 of section 1312, that the determination (Tax Court decision) adopt the position of the IRS. That is the case here, where the issue was raised in the deficiency notice and defended against by the estate. As the regulations explain, the estate would fail this element only if the IRS did not propose the adjustment and the estate had instead raised the issue itself in order to pay the tax to later ask for a refund of the related income tax.

Because the value of the asset was determined through settlement negotiations that did not result in agreement on the merits, but instead resulted in a general agreement on the appropriateness of settlement in order to resolve the case, the mitigation provisions do not apply and the refund claim should be denied as untimely.