



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

OFFICE OF
CHIEF COUNSEL

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WTA-N-103281-99

August 13, 1999

MEMORANDUM FOR N. Gray Joyner, Case Manager
GROUP 1112 OP:IN:D:C:EX:HQ:1112

FROM: W. Edward Williams, Senior Technical Reviewer
Branch 1 (International) CC:INTL:BR.1

SUBJECT: Consent to Extend the Time to Assess Tax
Review of Restricted Language

LEGEND:

Enterprise A	=
Group B	=
Firm C	=
Article D	=
Article E	=
Article F	=
Article G	=
Article H	=
Article I	=
Article J	=
Article K	=
Article L	=
Article M	=
Article N	=
Article O	=
Article P	=
Article Q	=
Article R	=
Business Person R	=
Business S	=
Business T	=
Type U Income	=
Type V Income	=

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Type W Income =

Type X Income =

Type Y Income =

Type Z Income =

Tax AA =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Year 5 =

Year 6 =

Event 7 =

This responds to your memorandum dated January 27, 1999, requesting our review of the language of a draft Form 872 Consent To Extend The Time To Extend Tax, for the years ending Year 1 and Year 2, attached to your memorandum. We have the following comments concerning the currency gains issue.

In your memorandum, you state that your intent is to extend the statute of limitations on all Group B (who have not previously revoked their power of attorney with Firm C) on their income tax reportable under Article D and Article E of the Year 3 and Year 4 Closing Agreements, for tax years ending Year 1 and Year 2. In the Form 872, the types of income covered are described as:

The amount of any Federal Income tax which is determined in Article D or Article F of the Closing Agreement dated Year 5 between the Individual Taxpayers who are Enterprise A and the Commissioner of Internal Revenue, and in Article D or Article E of the Closing Agreement dated Year 6, between the Corporate Taxpayers who are Enterprise A and the Commissioner of Internal Revenue, including Business Person Rs who elect not to report their tax in accordance with the Closing Agreements dated Year 5 and Year 6.

Background

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The Year 3 and Year 4 closing agreements determine the U.S. income tax liabilities imposed on "Enterprise A income (or loss)" for individual Business Person Rs and corporate Business Person Rs, respectively. The term "Enterprise B income (or loss)" is defined identically in the closing agreements "as the Business S profits (and losses) and the investment income derived by a Business Person R from his Business S Business T and investment activities at Enterprise A."

Enterprise A income (or loss) consists of Type U Income and Type V Income. The term Type U Income is also defined identically in the Year 3 and year 4 closing agreements, as including:

- (A) Type W Income;
- (B) Type X Income;
- (C) Type Y Income; and
- (D) Type Z Income.

As to *U.S. individual Business Person Rs*, the Year 3 closing agreement provides for two levels of tax on Enterprise A income (or loss) that is Type U Income. The first level of tax is at the corporate rate under I.R.C. sec. 11 (Article G). This tax is reported on a composite income tax return that Enterprise A files on behalf of all U.S. individual Business Person Rs. The second level of tax (Article H) is the consequence of the requirement that a Business Person R include on his/her individual income tax return the "distributable amount", as defined in Article I, whether or not this amount is actually distributed. The "distributable amount" is Type U Income plus Type V Income less (i) the section 162 deductions allowed in determining the corporate level taxable income; (ii) the amount of the first level corporate tax paid; and (iii) the amount of foreign tax deemed paid or accrued under Article J; and increased, if the taxpayer elects to claim a credit for the deemed paid or accrued foreign tax, by the amount of any creditable foreign tax. While the reporting of this income is deferred until the year following the close of a Enterprise A syndicate (generally, the fourth year), Article K requires Enterprise A to pay an annual advance tax on behalf of the Business Person Rs which they may claim as a credit on their fourth year tax liability.

Pursuant to the Year 3 closing agreement, non-U.S. individual Business Person R agree that they are engaged in a U.S. trade or business through a permanent establishment and that their Type U Income is U.S. source income attributable to the permanent establishment. Under Article L, the Type U Income of a non-U.S. individual Business Person R is subject to the U.S. tax imposed by section 11 of the Code. Under Article M, a non-U.S. Business Person R is also subject to U.S. tax under section 871 of the Code on any U.S. source investment

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income that is Enterprise A income and is not Type U Income. Enterprise A includes on its annual composite Form 1120, the taxes imposed under Article L and Article M.

As to "*eligible corporate Business Person Rs*", pursuant to the Year 4 closing agreement, non-U.S. corporate Business Person Rs concede that they are engaged in a U.S. trade or business through a permanent establishment and that their Type U Income is from U.S. sources and connected to the permanent establishment (Article M). This income, Type U Income, is subject to U.S. tax under I.R.C. sec. 11, with the exception that the small-company exceptions in sections 501(c)(15) and 831(b) do not apply (Article L). Further, non-U.S. corporate Business Person Rs are subject to U.S. tax on U.S. source investment income, that is Enterprise A income but not Type U Income, pursuant to section 881 and any tax treaty under which the corporate Business Person R is entitled to benefits (Article O).

As to *U.S. corporate Business Person Rs*, each is subject to tax under section 11 on taxable Type U Income (Article M). Each U.S. corporate Business Person R is also subject to section 11 tax on its Type V Income distributable amount in the year subsequent to the year in which a Event 7 ("Distribution Year") (Article N). Article O requires Enterprise A to pay an annual advance tax on behalf of U.S. corporate Business Person Rs which they may claim as a credit against the tax imposed under Article N.

In summary, the following liabilities of U.S. and non-U.S. individual Business Person Rs are reported annually by Enterprise A on a composite Form 1120:

Year 3 Closing Agreement

Article G - The first level corporate rate tax on U.S. individual Business Person R;

Article L - The corporate rate tax imposed on the Type U Income of non-U.S. individual Business Person Rs;

Article P - The tax imposed under I.R.C. sec. 871 on the U.S. source Enterprise A investment income of non-U.S. Business Person Rs.

Year 4 Closing Agreement

Article L - The corporate rate tax on Type U Income of non-U.S. corporate Business Person Rs.

Article O- The sec. 881 tax imposed on Enterprise A U.S. source investment income of non-U.S. Business Person Rs.

Discussion

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It is the liabilities reported on the composite return filed by Enterprise A on behalf of Business Person Rs, as well as the tax imposed by Article E of the Year 4 closing agreement on a U.S. corporate Business Person R's Type U Income that are covered by the proposed Consent.

Where a rule of taxation is provided in the Year 3 or Year 4 closing agreements, this rule is applied by the Commissioner. Where a rule is not provided, the Code and applicable income tax conventions apply. Further, the Enterprise A closing agreements do not determine liability for tax on income that is not Enterprise A income (or loss). Article P of the year 3 closing agreement includes the following:

2. In any case where this Closing Agreement does not provide a rule of taxation, Business Person Rs shall be taxable under the general provisions of the Code and any applicable income tax convention.

Similarly, Article Q of the Year 4 closing agreement includes the following:

2. Eligible corporate Business Person Rs shall be taxable as corporations on Business S and investment income derived from their Business T business carried on at Enterprise A. (The non-Enterprise A income (or loss), if any, of an Eligible Corporate Business Person R shall be taxable under the general provisions of the Code and any applicable income tax convention and not under the terms of this Closing Agreement.)

We are aware that the question of whether Enterprise A has currency gains or losses on any transactions is pending in another Branch in this office. It is our view that if it is determined that there are currency gains or losses, such gains or losses will be taxable pursuant to the closing agreements if the income is "Enterprise A income" as this term is defined in the closing agreements. If, on the other hand, such gains or losses are determined not to be "Enterprise A income," they will be subject to the rules of taxation under the Code.

The Consent will be signed by a person designated in limited powers of attorney given by each Business Person R to Firm C, and the powers given by individual Business Person Rs authorize the attorney to represent an Business Person R only as to the following tax matters:

Federal income taxes due pursuant to Articles Article D and Article E of the Closing Agreement Between Enterprise A and the I.R.S., dated Year 5 ..., and all Tax AA due by Enterprise A.

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Accordingly, if currency gains or income is not "Enterprise A income" and subject to tax under the closing agreements, the Consent will not extend the period to assess any tax deficiency attributable to such income. It is our view that it would be necessary to obtain additional Consents from each of the Business Person Rs to protect the statute as to these matters.

Finally, the entire consent is not correct grammatically, as each phrase that is added ends with a period rather than a comma or semicolon, and paragraph (1) uses the term "tax" twice, once before addition *2 and once after. Part of this problem stems from attempting to insert the taxpayers affected and the tax liabilities covered into the printed form. We recommend that instead of attempting to insert this information into the printed form, the Consent be typed out using the language from the form. The consent will be equally binding whether using a printed form or whether typing the entire consent using the language from the form.

If you have any further questions, please call (202) 622-3880.

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