

Part III - Administrative, Procedural, and Miscellaneous

Announcement of rules adopting a reasonable cause standard for section 1503(d) filings

Notice 2006-13

PURPOSE

This notice announces that the Internal Revenue Service (IRS) and Treasury intend to issue regulations under section 1503(d) of the Internal Revenue Code providing that taxpayers who fail to file any agreements, statements, rebuttals, requests or other information required under section 1503(d) in a timely manner may seek relief for such failure under a reasonable cause standard similar to Prop. Treas. Reg. § 1.1503(d)-1(c)(1). Prior to the issuance of those regulations, and except as provided below, taxpayers may rely on the guidance contained in Prop. Treas. Reg. § 1.1503(d)-1(c)(1), as modified by this notice, to cure such late filings. During that time, taxpayers may continue, in lieu of using the reasonable cause procedure contained in this notice, to apply the provisions of Treas. Reg. §§ 301.9100-1 through -3. The IRS and Treasury intend that the reasonable cause procedure set forth in final regulations will be consistent with the reasonable cause standard set forth in Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice, and such final regulations will prospectively supersede relief under Treas. Reg. §§ 301.9100-1 through -3 for purposes of curing all late filings required under section 1503(d).

BACKGROUND

Section 1503(d) provides that a dual consolidated loss of a dual resident corporation is not allowed to reduce the taxable income of any other member of the corporation's affiliated group for any taxable year. The term dual resident corporation includes a domestic corporation that is subject to the income tax of a foreign country on its worldwide income or on a residence basis and a separate unit of a domestic corporation. Sections 1503(d)(2)(A) and (d)(3).

The IRS and Treasury issued temporary regulations under section 1503(d) in 1989 (T.D. 8261, 1989-2 C.B. 220) and final regulations in 1992 (T.D. 8434, 1992-2 C.B. 240). The temporary regulations were initially designated as Treas. Reg. § 1.1503-2T, but were re-designated as Treas. Reg. § 1.1503-2A by the final regulations. The temporary regulations in Treas. Reg. § 1.1503-2A are effective for taxable years beginning after December 31, 1986 and before October 1, 1992. The final regulations in Treas. Reg. § 1.1503-2 are generally effective for taxable years beginning on or after October 1, 1992. In 2002, the IRS and Treasury issued proposed regulations, which were finalized in 2003 (T.D. 9084, 2003-2 C.B. 742) and are effective with respect to transactions constituting triggering events occurring on or after January 1, 2002. These regulations provide that certain events will not trigger the recapture of a dual consolidated loss or payment of the associated interest charge and identify transactions for which a closing agreement is no longer required. In addition, in 2003 the IRS and Treasury issued temporary regulations under section 1503(d) (T.D. 9100, 2004-1 C.B. 297) that modified the final regulations to facilitate electronic filings. These 2003

temporary regulations generally are effective for taxable years beginning after December 31, 2002.

Treasury Reg. §§ 1.1503-2(g)(2) and 1.1503-2T(g)(2) provide an exception to the general limitation on the use of dual consolidated losses if an election is made to be bound by the provisions of Treas. Reg. §§ 1.1503-2(g)(2) and 1.1503-2T(g)(2) by attaching to a timely filed U.S. income tax return for the taxable year in which the dual consolidated loss is incurred an agreement ((g)(2) agreement) which includes a certification that no portion of the dual consolidated loss has been or will be used to offset the income of another person under the laws of a foreign country. In addition to the (g)(2) agreement, taxpayers may be required to attach to their timely filed income tax return other agreements, statements, rebuttals, or information. Similar requirements are contained in Treas. Reg. § 1.1503-2A. Taxpayers who fail to file such agreements, statements, rebuttals, requests or other information in a timely manner must request an extension of time under Treas. Reg. §§ 301.9100-1 through -3.

In order to avoid the recapture of a dual consolidated loss with respect to which a (g)(2) agreement has been filed, taxpayers may, in certain circumstances, enter into a closing agreement with the IRS. Treas. Reg. § 1.1503-2(g)(2)(iv)(B)(3). Under Rev. Proc. 2000-42, 2000-2 C.B. 394, the request to enter into a closing agreement must be submitted by the due date of the return (including extensions) for the year in which the triggering event occurred. Before requesting a closing agreement, a taxpayer is required to have complied with the regulations under section 1503(d), including the

requirement that all the requisite agreements, elections, and certifications have been filed. To the extent the taxpayer has failed to file any agreement, election or certification required under section 1503(d), the taxpayer must request and secure (or at least simultaneously request) relief under § 301.9100-1 through -3.

On May 24, 2005, Treasury and the IRS issued proposed regulations under section 1503(d) regarding dual consolidated losses to address certain fundamental concerns which arise under the current regulations. These proposed regulations would revise the procedures for taxpayers who fail to file any statements, rebuttals, requests, or other information required under section 1503(d) in a timely manner, by replacing the requirement that a taxpayer obtain relief pursuant to Treas. Reg. §§ 301.9100-1 through -3 with a reasonable cause standard. Under Prop. Treas. Reg. § 1.1503(d)-1(c)(1), if a taxpayer that is permitted or required to file an election, agreement, statement, rebuttal, computation, or other information fails to make such filing in a timely manner, the taxpayer shall be considered to have satisfied the timeliness requirement with respect to such filing if the taxpayer is able to demonstrate to the Director of Field Operations having jurisdiction of the taxpayer's tax return for the taxable year, that such failure was due to reasonable cause and not willful neglect. This rule applies only if, once the taxpayer becomes aware of the failure, the taxpayer attaches all documentation that should have been filed previously, as well as a written statement setting forth the reasons for the failure to comply timely, to an amended income tax return that amends the return to which the documents should have been attached. In determining whether the taxpayer has reasonable cause, the Director of Field

Operations shall consider whether the taxpayer acted reasonably and in good faith after considering all the facts and circumstances. The Director of Field Operations shall notify the taxpayer in writing within 120 days of the filing if it is determined that the failure to comply was not due to reasonable cause, or if additional time is needed to make such determination.

DISCUSSION

The IRS and Treasury have determined that it is appropriate to allow taxpayers who fail to file any agreements, statements, rebuttals, requests, or other information required under section 1503(d) in a timely manner, to cure such late filings under procedures similar to those in Prop. Treas. Reg. § 1.1503(d)-1(c)(1) prior to its publication as a final regulation in the Federal Register. The IRS and Treasury believe that these procedures will be beneficial to both taxpayers and the IRS. Therefore, during the elective period of these procedures, taxpayers may choose to seek relief under Treas. Reg. §§ 301.9100-1 through -3 or elect to use the reasonable cause standard contained in Prop. Treas. Reg. § 1.1503(d)-1(c)(1), as modified by this notice.

In order to qualify for the relief provided in this notice, taxpayers must demonstrate to the Area Director, Field Examination, Small Business/Self Employed or the Director, Field Operations, Large and Mid-Size Business (Director) having jurisdiction of the taxpayer's return for the taxable year, that the failure to file in a timely manner was due to reasonable cause and not willful neglect. In addition to the requirements contained in Prop. Treas. Reg. § 1.1503(d)-1(c)(1), taxpayers must

provide a copy of the amended return and all required attachments to the IRS as follows:

- If the taxpayer is under examination for any taxable year when the taxpayer requests relief under Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice, the taxpayer must provide a copy of the amended return and attachments to the IRS personnel conducting the examination.
- If the taxpayer is not under examination for any taxable year when the taxpayer requests relief under Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice, the taxpayer must provide a copy of the amended return and attachments to the Director having jurisdiction of the taxpayer's return.

In determining whether the taxpayer's failure to file any such election, agreement, statement, rebuttal, computation or other information in a timely manner was due to reasonable cause, the Director shall apply the same criteria applicable to reasonable cause determinations under other provisions of the Code, including sections 367(a) and 6038B. Under these provisions, in general, the taxpayer must demonstrate that it exercised ordinary care and prudence in meeting its tax obligations but nonetheless did not comply with the prescribed duty within the prescribed time. Similarly, taxpayers may appeal these determinations in the same manner as reasonable cause determinations made pursuant to other provisions are appealed. A determination that the failure to file in a timely manner was due to reasonable cause is not a determination that the taxpayer is otherwise eligible to file the election, agreement, statement, rebuttal, computation or other information. A determination that such failure to file in a timely

manner was due to reasonable cause is also not a determination that any information provided or position taken by the taxpayer in the election, agreement, statement, rebuttal, computation or other information is correct.

Proposed Treas. Reg. § 1.1503(d)-1(c)(1) provides that the Director shall notify the taxpayer within 120 days if it is determined that the failure to comply with the filing requirements of the section 1503(d) regulations was not due to reasonable cause or if additional time is needed to make such determination. For this purpose, the 120 day period will begin to run on the date the Service notifies the taxpayer in writing that the request has been received and assigned for review. Appropriate procedures will be implemented to ensure that the Service generally issues such notification within ten business days of receipt of a properly submitted request for relief.

Proposed Treas. Reg. § 1.1503(d)-3 eliminates the closing agreement requirement contained in the current regulations and provides an exception in all such cases where a closing agreement would otherwise be available if, among other things, a new domestic use agreement is entered into. This notice does not incorporate these provisions. Thus, in order to avoid the recapture of a dual consolidated loss with respect to which a (g)(2) agreement has been filed, taxpayers must continue to apply the provisions of the current regulations, including the closing agreement requirement. Because requests for closing agreements under Treas. Reg. § 1.1503-2(g)(2) must be submitted to the National Office, taxpayers requiring relief to cure a late request for a closing agreement must continue to seek extensions of time under Treas. Reg. §§ 301.9100-1 through -3 and may not use the reasonable cause procedure contained

in this notice. This restriction applies only to submissions to enter into the closing agreement itself. Taxpayers seeking relief for the failure to file any election, agreement, statement, rebuttal, computation or other information required in connection with the closing agreement, in a timely manner, may cure the late filing pursuant to Prop. Treas. Reg. § 1503(d)-1(c)(1) and this notice. In those cases in which requests are submitted seeking relief under Treas. Reg. §§ 301.9100-1 through -3 for the closing agreement itself and seeking relief under this notice for other late filings in connection with the closing agreement, the National Office will coordinate with the Director to ensure that both requests are handled in a consistent and timely manner.

Until final regulations are published, taxpayers may, in lieu of using the relief provided by this notice, continue to request extensions of time under Treas. Reg. §§ 301.9100-1 through -3. Taxpayers may not, however, apply for relief pursuant to both procedures. For example, if a taxpayer is denied relief for a late filing pursuant to Treas. Reg. §§ 301.9100-1 through -3, such taxpayer may not seek relief under the reasonable cause procedures set forth in Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice. Consideration of any letter ruling request received by the National Office will continue to be coordinated with the Director having jurisdiction of the taxpayer's income tax return.

Taxpayers who have letter ruling requests under Treas. Reg. §§ 301.9100-1 through -3 pending as of March 23, 2006, and that have not yet received a determination on their request, may withdraw their request, consistent with the procedures contained in Rev. Proc. 2006-1, 2006-1 I.R.B. 1 (January 3, 2006) (or any

succeeding document) and use the reasonable cause procedure set forth in Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice. In that event, the IRS will refund the taxpayer's user fee.

EFFECTIVE DATE

This notice is effective on March 23, 2006. Taxpayers may rely on the reasonable cause standard of Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice until final regulations are issued incorporating these provisions. The IRS and Treasury intend that the reasonable cause procedure set forth in final regulations will be consistent with the reasonable cause standard set forth in Prop. Treas. Reg. § 1.1503(d)-1(c)(1) and this notice and that such final regulations will prospectively supersede relief under Treas. Reg. §§ 301.9100-1 through -3 for purposes of curing all late filings required under section 1503(d).

PAPERWORK REDUCTION ACT

The collections of information contained in this notice have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-1946. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collections of information in this notice are described in the Background and Discussion paragraphs above. They are required to notify Service that the taxpayer is asserting reasonable cause and enable it to determine whether the taxpayer is entitled to rely on the reasonable cause standard for a permitted or required filing under the

current section 1503(d) regulations. The collections of information are required in order to obtain the benefit of the reasonable cause standard. The likely respondents are businesses.

The estimated total annual reporting and/or recordkeeping burden is 125 hours. The estimated annual burden hours per respondent and/or recordkeeper is 5 hours. The estimated number of respondents and/or recordkeepers is 25. The estimated frequency of response is occasional.

Books or records relating to a collection of information must be retained as long as their statements may become material in the administration of any internal revenue law. Generally, tax returns and tax information are confidential, as required by 26 U.S.C. § 6103.

DRAFTING INFORMATION

The principal author of this notice is Margaret A. Hogan of the Office of Associate Chief Counsel (International). For further information regarding this notice contact Gerard Traficanti at (202) 622-3619 (not a toll-free call).