



OFFICE OF
CHIEF COUNSEL

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

CC-2002-01

Feb 11, 2002

January 9, 2002

Attachment 1

CC:ITA:B05

ORPirfo

ACTION ON DECISION

SUBJECT: Internet Corporation & Subs. v. Commissioner
Docket No. 8246-97
Opinion filed: Oct. 2, 2001 (117 T.C. No. 13)
Decision: Not yet entered

Issue:

Whether deductions for state income tax deficiencies and interest thereon as well as interest on federal income tax deficiencies, all attributable to tax liabilities arising at least three years before the beginning of the taxable year, and taken into account in computing a net operating loss, qualify for a ten-year carryback as specified liability losses under former I.R.C. § 172(f)(1)(B).

Discussion:

The Tax Court has ruled against the Commissioner in the subject case on the litigated issue set forth above. In addition, the Service recently lost Host Marriott Corp. v. United States, 113 F.Supp. 2d 790 (D. Md. 2000), aff'd in unpublished opinion, 88 AFTR2d 2001-5074 (4th Cir. 2001), a case similar to Internet. In light of these two losses and notwithstanding the prior Service-favorable opinions in Sealy Corp. v. Commissioner, 107 T.C. 177 (1996), aff'd, 171 F.3d 655 (9th Cir. 1999), the Service will no longer assert the position that liabilities for state income tax deficiencies and any interest accruing on those deficiencies or on federal tax deficiencies do not arise under federal or state law and thus do not qualify as specified liability losses under former section 172(f)(1)(B).

The Tax Court also concluded in Internet that the deduction for interest accruing within three years of the beginning of the taxable year qualifies as a specified liability loss because the act giving rise to the entire interest liability is the failure to pay the correct amount of tax by the return due date. The Service disagrees with the Tax Court's

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rationale for allowing this portion of the interest to qualify as a specified liability loss. Despite that disagreement, the Service acquiesces in the result and will not challenge the treatment as a specified liability loss the portion of any net operating loss attributable to interest on federal or state tax liabilities that arose at least three years before the beginning of the taxable year.

Recommendation:

Acquiescence in result only.

Reviewers:

ORESTE RUSS PIRFO
Trial Attorney (Tax)

Approved:

RICHARD W. SKILLMAN
Acting Chief Counsel

By: _____
JAMES L. ATKINSON
Deputy Associate Chief Counsel
Income Tax & Accounting