First Chicago Corp. v. Commissioner, 80 T. C. 648 (1983)

The statute of limitations for assessing a deficiency related to a carryback adjustment is extended only when the deficiency results from an error in the carryback itself, not for subsequent adjustments to other years.

Summary

First Chicago Corp. sought a refund for 1971 using capital loss and investment credit carrybacks from 1974. The IRS later determined a deficiency in the 1972 minimum tax due to a reduced tax carryover from 1971. The court held that the general three-year statute of limitations barred the deficiency assessment for 1972 because the extended period under sections 6501(h) and (j) applies only to deficiencies directly resulting from errors in the carryback itself, not to subsequent adjustments to other years.

Facts

First Chicago Corp. filed a 1974 tax return showing a net capital loss and an unused investment credit. Using the quick refund procedure under section 6411, it applied these carrybacks to 1971, resulting in a refund. The IRS later determined a deficiency in First Chicago's 1972 minimum tax, arguing that the tax carryover from 1971 to 1972 should be reduced due to the 1971 refund. The notice of deficiency was issued more than three years after the 1972 return was filed.

Procedural History

First Chicago filed its 1972 and 1974 returns on time. It applied for a tentative refund for 1971 based on carrybacks from 1974, which was granted. The IRS issued a notice of deficiency for 1972 on June 2, 1978, more than three years after the 1972 return was filed. First Chicago challenged the notice as barred by the statute of limitations. The Tax Court granted summary judgment to First Chicago, holding that sections 6501(h) and (j) did not extend the limitations period for the 1972 deficiency.

Issue(s)

1. Whether sections 6501(h) and (j) extend the statute of limitations for assessing a deficiency in the 1972 minimum tax, where the deficiency results from a reduction in the tax carryover from 1971 to 1972 due to a carryback adjustment from 1974 to 1971?

Holding

1. No, because sections 6501(h) and (j) extend the statute of limitations only for deficiencies directly attributable to errors in the carryback itself, not for subsequent adjustments to other years resulting from the carryback.

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Court’s Reasoning

The court analyzed the legislative history of sections 6501(h) and (j), which were enacted to allow the IRS to recover refunds improperly allowed due to errors in the carryback process. The court emphasized that these sections apply only when a carryback is erroneously applied, resulting in an improper refund. In this case, the carryback to 1971 was correctly computed and applied, and the deficiency for 1972 was not due to an error in the carryback but rather a subsequent adjustment to the tax carryover. The court cited previous cases like *Leuthesser* and *Bouchey*, which held that the extended period applies only to deficiencies directly resulting from errors in the carryback itself. The court rejected the IRS’s argument that the deficiency could be traced to the carryback, as the deficiency was for a different year and tax.

Practical Implications

This decision clarifies that the extended statute of limitations under sections 6501(h) and (j) is narrowly applied to deficiencies directly resulting from errors in the carryback itself. It does not extend to subsequent adjustments to other years or taxes affected by the carryback. Taxpayers can rely on the general three-year statute of limitations for deficiencies unrelated to the carryback error. The IRS must be diligent in auditing carryback claims within the standard limitations period to prevent unintended consequences like those in this case. This ruling may encourage taxpayers to be more proactive in notifying the IRS of potential adjustments to subsequent years when claiming carrybacks, as such adjustments may not be subject to extended limitations periods.

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