OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR DISTRICT COUNSEL,

Attn:

FROM: DEBORAH A. BUTLER
               ASSISTANT CHIEF COUNSEL CC:DOM:FS

SUBJECT: LOANS VERSUS CONSTRUCTIVE DIVIDENDS

This Field Service Advice supplements and clarifies the Field Service Advice issued to you on October 27, 1999 (the "prior FSA")(200011003), which responded to your memorandum dated August 30, 1999. The prior FSA is hereby incorporated by reference. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND

Corp 1   =
Corp 2   =
X   =

DISCUSSION

Concern exists that taxpayers may at some point seek to disavow their current loan characterization with respect to closed years. If the purported loan patterns are substantially the same in the Closed Years as in the open years, the Service could have asserted and the Service most likely would have prevailed in asserting that the distributions in the Closed Years were constructive dividends. However, X, Corp 1 and Corp 2 treated the distributions during the Closed Years as loans and X represented to the revenue agent that he intended to repay the purported loans. The revenue agent relied on X's representations, and the Closed Years are closed.

The Service is now entitled to rely on the taxpayers' characterization of the closed year distributions as loans and to hold taxpayers to their form under one or more legal doctrines. We recommend that the Service monitor the taxpayers' treatment of these distributions and that the Service seek further advice from the Office of Chief Counsel upon discovery of any such inconsistent action.

If you have any further questions, please call (202) 622-7530.

DEBORAH A. BUTLER
ASSISTANT CHIEF COUNSEL
(FIELD SERVICE)

By: _____
ARTURO ESTRADA
Acting Branch Chief
Corporate Branch