

Office of Chief Counsel
Internal Revenue Service
Memorandum

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to: Jan B. Geier
Special Counsel to SB Division
(Small Business/Self-Employed)

Josephine Bonaffini
Supervisory Attorney (Estate Tax)
(Small Business/Self-Employed)

Mary L. Edelstein
Appeals Officer
(Office of Appeals)

from: Blaise G. Dusenberry
Special Counsel, Administrative Provisions & Judicial Practice
(Procedure & Administration)

subject: Section 6166; reasonable cause exception for an untimely filed estate tax return and an untimely installment payment

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent. ISSUES

1. Whether, like a failure to file penalty under section 6651, there is a reasonable cause exception for denial of a section 6166 election because it was made in connection with an untimely filed estate tax return.
2. Whether reasonable cause may be considered by Appeals when there has been a late installment payment under section 6166.

CONCLUSIONS

1. There is no reasonable cause exception for denial of a section 6166 election if it was made in connection with an untimely filed estate tax return, however, it may be possible for the taxpayer to seek relief under section 301.9100.
2. There is no reasonable cause exception for avoiding the imposition of late payment penalties when an estate makes an untimely section 6166 installment payment, and has not timely requested an extension of time pursuant to section 6161 to pay such installment or the section 6161 extension has expired.

FACTS

An estate has elected on its untimely filed United States Estate (and Generation Skipping Transfer) Tax Return (Form 706) to pay a portion of the estate tax in installments under section 6166. The estate had reasonable cause for not filing a timely Form 706.

The estate has been granted a section 6166 election to pay the estate tax in annual installments. The next installment payment is due and payable on Date 1. The estate does not make the required payment on Date 1, but rather, makes the payment on Date 2, which falls after Date 1. At no time has the estate requested an extension of time under section 6161 to pay the tax on Date 2. It appears the estate has reasonable cause for not making the prescribed installment payment on Date 1.

LAW AND ANALYSIS

As a general rule, the estate tax return (Form 706) and payment of the estate tax liability of a decedent is due within nine months of the decedent's death. I.R.C. §§ 6075(a); 6151(a). Section 6166(a) of the Internal Revenue Code, as an exception to the above rule, provides that if the value of an interest in a closely held business included in determining the value of the gross estate of a decedent exceeds 35 percent of the adjusted gross estate, the executor of the estate may elect to pay part or all of the tax imposed by section 2001 (estate tax) in two or more (but not exceeding ten) equal installments. The first installment of tax must be paid on or before the date selected by the executor which is not more than 5 years after the date prescribed by section 6151(a) for payment of the tax. An executor electing to defer estate taxes under section 6166 must make annual payments of interest during the deferral period. In particular, interest must be paid annually during the five-year period before the first installment of tax is due. I.R.C. § 6166(f). When an estate fails to make payments of principal or interest the Service may terminate the deferred payment election and force an acceleration of payment of the estate tax by issuing notice and demand. I.R.C. § 6166(g)(3).

Issue 1:

Section 6166(d) provides that the election to defer payment of an estate tax liability "shall be made not later than the time prescribed by section 6075(a) for filing the return

of tax imposed by section 2001 (including extensions thereof)." In this case, the section 6166 election was made with the tax return, but the tax return was not timely filed. As a result, the section 6166 election was not timely made. Therefore, the section 6166 election was not valid. See Estate of Hinz v. Commissioner, T.C. Memo 2000-6; Bank of the West v. Commissioner, 93 T.C. 462, 473 (1989) (stating that an untimely section 6166 election was not valid); Estate of La Meres v. Commissioner, 98 T.C. 294, 324 (1992).

Section 6651 provides for an addition to tax for failure to file a return by the extended due date of the return and a separate addition to tax for failure to pay the tax when due (taking into account extensions of time to pay) "unless it is shown that such failure is due to reasonable cause and not due to willful neglect." Generally, if a taxpayer fails to pay the tax due shown on the return, the Service can impose the failure to timely file penalty under section 6651. Under section 6651, a taxpayer's failure to pay the tax shown on the return is due to reasonable cause if the taxpayer exercised ordinary business care and prudence and was nevertheless unable to pay the tax within the prescribed time. See Treas. Reg. § 301.6651-1(c)(1).

While section 6651 specifically provides a reasonable cause exception to those taxpayer's who fail to pay the tax shown on the return when due, we note that there is no similar reasonable cause exception listed under section 6166. Accordingly, we do not believe there is a reasonable cause exception for a denial of a section 6166 election made in connection with an untimely filed estate tax return.

Issue 2:

Section 6166(a)(3) provides that if an election is made under 6166, the first installment shall be paid on or before the date selected by the executor which is not more than five years after the date prescribed by section 6151(a) for payment of the tax, and each succeeding installment shall be paid on or before the date which is one year after the date prescribed for payment of the preceding installment. An executor may elect to pay estate tax in 10 equal installments, starting at the end of a five-year period during which only interest is payable, if a closely held business constitutes more than 35 percent of the adjusted gross estate. I.R.C. § 6166(a)(1).

Section 6166(f)(1) provides that if the time for payment of any amount of tax has been extended under section 6166, interest payable under section 6601 on any unpaid portion of such amount attributable to the first five years the date prescribed by section 6151(a) for payment of the tax shall be paid annually. Section 6166(f)(2) provides that interest payable under section 6601 on any unpaid portion of such amount attributable to any period after the five-year period shall be paid annually at the same time as, and as a part of, each installment payment of tax.

Sections 6161(a) and (b) provide that the Secretary may extend, for reasonable cause, the time for payment of the amount of federal estate tax determined by the taxpayer on

the return or the amount determined by the Commissioner as a deficiency. Generally, an extension of time to pay under section 6161(a)(1) may be authorized for an installment payment due under a section 6166 election for a period of time not exceeding one year from the date the tax is due. Under section 6161(a)(2), the Service may extend the time for payment of estate tax under section 6166 for a reasonable period that does not exceed 10 years from the date the tax is due upon a showing of reasonable cause.

Certain activities trigger the acceleration of the estate tax payments. In this regard section 6166(g) identifies the activities which terminate the deferred payment election and force an acceleration of payment of the estate tax. In particular, section 6166(g)(3) provides that if an election is made under 6166, the first installment shall be paid on or before the date selected by the executor which is not more than five years after the date prescribed by section 6151(a) for payment of the tax, and each succeeding installment shall be paid on or before the date which is one year after the date prescribed for payment of the preceding installment. In addition, that section also provides that if any installment is not paid on or before the date fixed for its payment (including any extension of time for the payment of such installment), the unpaid portion of the tax payable in installments shall be paid upon notice and demand.

As a general rule, when an estate fails to pay a section 6166 installment, a letter is issued to inform the estate to pay the installment or lose the installment privilege. Rev. Proc. 2005-33, 2005-24 I.R.B. 131. In addition the letter will advise the taxpayer of the taxpayer's right to appeal the determination by requesting a conference with the Office of Appeals. The taxpayer must request, in writing, an Appeals conference within 30 calendar days after the mailing date of the preliminary determination letter, or by such later date for responding to the preliminary determination letter as is agreed to between the taxpayer and the Service. Id.

Although an estate defaults on a payment, acceleration of the remaining installment payments does not actually occur until the Service serves notice and demand for payment on the estate. See Lake Shore National Bank v. Coyle, Jr., 419 F.2d 958 (7th Cir. 1969). Note, however, that if an estate fails to make a timely payment, but pays within six months of the due date, the estate loses the benefit of the two percent interest rate for that payment and must include in its late payment a penalty equal to five percent of the payment originally due, multiplied by the number of months (including fractions thereof) from the original due date to the date of actual payment. I.R.C. § 6166(g)(3)(B)(ii), (iii).

In the present situation, the taxpayer did not timely pay the amount due on Date 1, nor did the taxpayer pay the amount within six months of the due date. In addition, the taxpayer did not seek an extension of time to pay the amount due under section 6161. As noted previously, section 6166 does not provide a reasonable cause exception under any circumstance. Thus, Appeals may not consider whether the taxpayer has reasonable cause for the late installment payment. Accordingly, we believe that the

Service is entitled to issue notice and demand to terminate the taxpayer's installment privileges. I.R.C. § 6166(g)(3)(B)(i).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

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