Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
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PLR-146700-07
Date: February 5, 2008

LEGEND:

Taxpayer	=
Year 1	=
Year 2	=
Date X	=
Member A	=
Member B	=
Accounting Firm A	=
Accounting Firm B	=

Dear :

This responds to your letter dated October 12, 2007, submitted by your authorized representatives, requesting an extension of time under §§ 301.9100-1 and -3 of the Procedure and Administration Regulations (the Regulations), for Taxpayer to make an election under § 198 of the Internal Revenue Code (the Code) to deduct qualified environmental remediation expenditures (QER expenditures) for Year 2.

FACTS

Taxpayer is a limited liability company treated as a partnership for federal income tax purposes. Taxpayer uses a calendar taxable year and an overall accrual method of accounting. Taxpayer is engaged in the business of developing commercial real estate. During Year 1, Taxpayer discovered ground contamination on a property it previously purchased. In cooperation with the governing state agency and upon the agency's approval, Taxpayer began remediation of the ground contamination during Year 1 and completed remediation of the ground contamination and demolition of the existing structures on the property during Year 2. Taxpayer elected to deduct the costs of the QER expenditures incurred during Year 1 on Taxpayer's income tax return for Year 1. Taxpayer has represented that it incurred QER expenditures during Year 2 but the § 198 election was not made due to a ministerial error.

Since Taxpayer's inception, outside accountants always have prepared Taxpayer's income tax returns. For several years, extensions of time for filing Form 1065 (U.S. Return of Partnership Income) have not required taxpayer signatures, and it has become routine practice for CPAs to file extensions without any instruction from Taxpayer. For all periods prior to Year 2, Member A, a member of Taxpayer, was responsible for the books and records of Taxpayer as well as the preparation and filing of the federal and state tax returns of Taxpayer. For the income tax returns for Year 1 and the year prior to Year 1, Member A hired Accounting Firm A to prepare Taxpayer's tax returns. For each of those years, Accounting Firm A filed the appropriate federal and state forms on behalf of Taxpayer to extend the time for filing Taxpayer's income tax returns.

During Year 2, Member B, another member of Taxpayer, took over maintenance of the books and records of Taxpayer. The controller of Member A informed Accounting Firm A that Accounting Firm A would not be preparing Taxpayer's returns or extensions for Year 2, but did not communicate this information to the controller of Member B. After Date X, when the deadline for filing an extension for Taxpayer's Year 2 return had passed, the controller of Member B learned that an extension had not been filed. Until then, the controller of Member B believed that Accounting Firm A was engaged to file the necessary extensions on behalf of Taxpayer for Year 2. As a result, the time for making an election under § 198 of the Code to deduct QER expenditures for Year 2 had expired. Afterwards, the controller of Member B retained Accounting Firm B to prepare Taxpayer's income tax returns for Year 2. Accounting Firm B recommended to the controller of Member B that Taxpayer should request relief under §§ 301.9100-1 and -3 of the Regulations to make a late § 198 election.

STATEMENT OF LAW

Section 198 of the Code provides, in part, that a taxpayer may elect to treat any QER expenditure which is paid or incurred by the taxpayer as an expense which is not chargeable to capital account. Any expenditure which is so treated shall be allowed as a deduction for the taxable year in which it is paid or incurred.

Under § 198(b), a "qualified environmental remediation expenditure" means any expenditure which is otherwise chargeable to capital account and which is paid in connection with the abatement or control of hazardous substances at a qualified contaminated site.

Rev. Proc. 98-47, 1998-2 C.B. 319, provides the procedures for taxpayers to make the election under § 198 to deduct any QER expenditure. Under section 3.01 of Rev. Proc. 98-47, the election must be made on or before the due date (including extensions) for filing the income tax return for the taxable year in which the QER expenditures are paid or incurred. In addition, persons other than individuals are required to make the election by including the total amount of § 198 expenses on the line for "Other Deductions" on their appropriate federal tax return. On a schedule attached to the return that separately identifies each expense included in "Other Deductions," the taxpayer must write "Section 198 Election" on the line on which the § 198 expense amounts separately appear. See section 3.02(2) of Rev. Proc. 98-47.

Section 3.03 of Rev. Proc. 98-47 provides that, if for any taxable year, the taxpayer pays or incurs more than one QER expenditure, the taxpayer may make a § 198 election for any one or more of such expenditures for that year. Thus, the taxpayer may make a § 198 election with respect to a QER expenditure even though the taxpayer chooses to capitalize other such expenditures (whether or not they are of the same type or paid or incurred with respect to the same qualified contaminated site). Further, a § 198 election for one year has no effect for other years. Thus, a taxpayer must make a § 198 election for each year in which the taxpayer intends to deduct QER expenditures.

Section 301.9100-3 of the Regulations generally provides extensions of time for making regulatory elections. For this purpose, § 301.9100-1(b) defines the term "regulatory election" to mean an election whose due date is prescribed by a regulation published in the Federal Register, or a revenue ruling, revenue procedure, notice or announcement published in the Internal Revenue Bulletin.

Section 301.9100-3 provides that requests for extensions of time for regulatory elections will be granted when the taxpayer provides evidence (including affidavits described in § 301.9100-3(e)) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1) states that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer --

(i) requests relief under this section before the failure to make the regulatory election is discovered by the Internal Revenue Service;

(ii) failed to make the election because of intervening events beyond the taxpayer's control;

(iii) failed to make the election because, after exercising reasonable diligence, the taxpayer was unaware of the necessity for the election;

(iv) reasonably relied on the written advice of the Internal Revenue Service; or

(v) reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

A taxpayer will not be considered to have reasonably relied on a qualified tax professional if the taxpayer knew or should have known that the professional was not competent to render advice on the regulatory election or aware of all relevant facts. Section 301.9100-3(b)(2).

Under § 301.9100-3(b)(3), a taxpayer is deemed to have not acted reasonably or in good faith if the taxpayer --

(i) seeks to alter a return position for which an accuracy-related penalty has been or could be imposed under § 6662 at the time the taxpayer requests relief (taking into account any qualified amended return filed within the meaning of § 1.6664-2(c)(3) of the Income Tax Regulations) and the new position requires or permits a regulatory election for which relief is requested;

(ii) was informed in all material respects of the required election and related tax consequences, but chose not to file the election; or

(iii) uses hindsight in requesting relief. If specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer, the Internal Revenue Service will not ordinarily grant relief. In such a case, the Internal Revenue Service will grant relief only when the taxpayer provides strong proof that the taxpayer’s decision to seek relief did not involve hindsight.

Section 301.9100-3(c)(1) provides, in part, that the Commissioner will grant a reasonable extension of time to make a regulatory election only when the interests of the Government will not be prejudiced by the granting of relief.

Section 301.9100-3(c)(1)(i) provides, in part, that the interests of the Government are prejudiced if granting relief would result in the taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money).

Section 301.9100-3(c)(1)(ii) provides, in part, that the interests of the Government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made or any taxable years that would have been affected by the election had it been timely made are closed by the period of limitations on assessment under § 6501(a) before the taxpayer's receipt of a ruling granting relief under § 301.9100-3.

ANALYSIS

Based on the facts of the present case, Taxpayer acted reasonably and in good faith. The affidavits made by the controllers of Member A and Member B demonstrate that Taxpayer reasonably relied on those two qualified tax professionals. The time for making an election under § 198 to deduct QER expenditures for Year 2 had simply expired because the transfer of Taxpayer's accounting and tax responsibility from one tax professional to another was poorly executed during Year 2. Given the fact that the § 198 election was made on Taxpayer's income tax return for Year 1, Taxpayer had no reason in Year 2 to know that the tax professionals were not competent to render advice on the regulatory election or aware of all relevant facts. Additionally, the three specified circumstances provided in § 301.9100-3(b)(3) where a taxpayer is deemed to have not acted reasonably or in good faith are not applicable in this case. Taxpayer is not requesting relief using hindsight or with an intent to avoid accuracy-related penalties. In fact, it was the intent of Taxpayer to have eligible QER expenditures in Year 2 and any later years be the subject of an election under § 198, but the § 198 election for Year 2 was simply not made due to inadvertence.

Further, based on the facts provided, the interests of the Government will not be prejudiced by granting relief in this case. Granting relief will not result in Taxpayer having a lower tax liability for Year 2 than Taxpayer would have had if the election had been timely made. Taxpayer is requesting relief contemporaneously with filing its original income tax return for Year 2 which, but for the absence of an extension, would be timely. Thus, the tax liability here will be identical to that of a timely made election. In addition, the taxable year for which Taxpayer is requesting relief is not a closed year, nor will any closed taxable years be affected by the making of the election for Year 2.

RULING

Because Taxpayer acted reasonably and in good faith and the interests of the Government will not be prejudiced if the request for relief is granted, Taxpayer has met the requirements for an extension under § 301.9100-3 for making the § 198 election for its Year 2 taxable year. Accordingly, Taxpayer is granted an extension of 60 days from the date of this ruling letter to make the § 198 election by filing an amended federal income tax return for its Year 2 taxable year. Taxpayer must comply with all the requirements of Rev. Proc. 98-47 for the manner of making such an election upon its amended return. A copy of this letter ruling must be attached to its amended return to which it is relevant.

CAVEATS

This ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by penalty of perjury statements executed by appropriate parties. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed as to whether the expenditures discussed in this ruling constitute QER expenditures under § 198. This ruling simply extends the period of time in which the taxpayer may make an election under § 198.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative who is first listed.

Enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under § 6110 of the Code.

Sincerely,

Christopher F. Kane
Branch Chief, Branch 3
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosure (1)