

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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TY:

Legend

Taxpayer =  
Year 1 =  
Trustee =  
Year 2 =

Dear :

This is in response to your letter dated . In your letter, you requested an extension of time on behalf of the taxpayer to make a late election to take net capital gain from the disposition of stock held for investment into account as investment income under §§ 163(d)(1) and 163(d)(4)(B) of the Internal Revenue Code for Year 1. You also requested revocation under § 1.163(d)-(1)(c) of the Income Tax Regulations of the election previously made to treat qualified dividend income as investment income under § 163(d)(1) for Year 1. The request is based on §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations.

FACTS

Taxpayer is a trust that makes long term investments of trust assets in various investment alternatives for the benefit of its beneficiaries. Taxpayer timely filed Form 1041, U.S. Income Tax Return for Estates and Trusts for Year 1. Trustee prepared the return manually, without the aid of software. It is represented that Trustee is not a tax professional nor in the business of preparing tax returns. Taxpayer's return included Form 4952, Investment Interest Expense Deduction and Schedule D, Capital Gains and Losses. In previous years, Taxpayer had minimal investment interest expense easily absorbed by investment income and had not encountered this particular issue regarding the election to treat capital gains as investment income. Trustee completed Form 4952 making an election to include all capital gain as ordinary income and deducted the

investment interest expense of the trust. In completing Schedule D, Trustee inadvertently left line 21 blank, resulting in all of the capital gain being taxed at the lower capital gain rate. The effect of electing to treat all of the taxpayer's net capital gain as investment income should have resulted in the capital gain being taxed at ordinary income tax rates. Only a small portion of the capital gain was needed to offset Taxpayer's investment interest expense. In Year 2, the Service notified Taxpayer of a change to the calculation of tax on the tax return. Taxpayer paid the balance due.

#### APPLICABLE LAW

Section 163(d)(1) of the Code provides that in the case of a taxpayer other than a corporation, the amount allowed as a deduction for investment interest for any taxable year shall not exceed the net investment income of the taxpayer for the taxable year.

Section 163(d)(4)(B) of the Code provides, in part, that investment income means the sum of –

(i) gross income from property held for investment (other than any gain taken into account under clause (ii)(I)) ,

(ii) the excess (if any) of –

(I) the net gain attributable to the disposition of property held for investment, over

(II) the net capital gain determined solely by taking into account gains and losses from dispositions of property held for investment, plus

(III) so much of the net capital gain referred to in clause (ii) (II) (or, if lesser, the net gain referred to in clause (ii)(I) as the taxpayer elects to take into account under this clause.

Section 1.163(d)-1(b) of the Regulations provides that the election under § 163(d)(4)(B)(iii) must be made on or before the due date (including extensions) of the income tax return for the taxable year in which the net capital gain is recognized. The net capital gain taken into account as investment income under this election is not eligible to be taxed at capital gain rates.

Section 1.163(d)-1(c) of the Regulations provides that the election under § 163(d)(4)(B) is revocable with the consent of the Commissioner.

Sections 301.9100-1 through 301.9100-3 of the Procedure and Administration Regulations provide the standards the Commissioner uses to determine whether to grant an extension of time to make a regulatory election. Section 301.9100-2 provides

automatic extensions of time for making certain elections. Section 301.9100-3 provides extensions of time for making elections that do not meet the requirements of § 301.9100-2.

Section 301.9100-1(b) of the Regulations defines the term “regulatory election” as an election whose due date is prescribed by a regulation published in the Federal Register, or a revenue ruling, procedure, notice or announcement published in the Internal Revenue Bulletin.

Section 301.9100-1(c) of the Regulations provides that the Commissioner may grant a reasonable extension of time to make a regulatory election, or a statutory election (but no more than six months except in the case of a taxpayer who is abroad) under all subtitles of the Internal Revenue Code except subtitles E, G, H and I.

Section 301.9100-3 provides extensions of time to make a regulatory election under Code sections other than those for which § 301.9100-2 expressly permits automatic extensions. Requests for extensions of time for regulatory elections will be granted when the taxpayer provides evidence (including affidavits described in the regulations) 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 will be deemed to have acted reasonably and in good faith if the taxpayer –

- (i) requests relief before the failure to make the regulatory election is discovered by the Service;
- (ii) inadvertently failed to make the election because of intervening events beyond the taxpayer’s control;
- (iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;
- (iv) reasonably relied on the written advice of the Service; or
- (v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make, the election.

Under § 301.9100-3(b)(3), a taxpayer will not be considered to have acted reasonably and 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 § 1.6664-02(c)(3)) and the new position requires 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 original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant 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 these criteria, the interests of the government are not prejudiced in this case. The taxpayer has represented that granting relief would not result in 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). Furthermore, the taxable year in which the regulatory election should have been made and any taxable years that would have been affected had it been timely made, are not closed by the period of assessment.

#### CONCLUSION

Taxpayer's election is a regulatory election, as defined under § 301.9100-1(b), because the due date of the election is prescribed in the regulations under § 1.163(d)-1(b). In the present situation, the requirements of §§ 301.9100-1 and 301.9100-3 of the regulations have been satisfied. The information and representations made by the taxpayer establish that the taxpayer acted reasonably and in good faith with this request. Furthermore, granting an extension will not prejudice the interests of the Government. It is represented that the taxpayer will not have a lower tax liability in the aggregate for all taxable years affected by the election if given permission to make the election in the appropriate amount at this time than taxpayer would have if the election were made in the appropriate amount by the original deadline for making the election. Accordingly, taxpayer is granted an extension of time for making the election until 60 days following the date of this ruling. The election should be made by filing a revised Form 4952 and Schedule D, and by including a copy of this ruling with an amended return for Year 1. Additionally, taxpayer is granted consent to revoke the first election made on the Year 1 return.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal income tax consequences of any aspect of any transaction or item discussed or referenced in this ruling.

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.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. 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.

Sincerely,

Christopher F. Kane  
Branch Chief, Branch 3  
(Income Tax & Accounting)

Enclosure (1)