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:
CC:ITA:B02
PLR-139660-16

Date:
June 15, 2017

TY:

Legend

Taxable Year =

Taxpayer or Seller1
Seller2 = .
Target Companies =
Parent =
Purchaser =
Facilitator1 =
Facilitator2 =
State =
Sellers' Representative =
Financial Advisor =
Purchaser's CPA =
Sellers' CPA=
Agreement =

Date1 =
Date2 =
Date3 =
Date4 =
Date5 =
Date6 =

Date7 =
Date8 =
Date9 =
Year1 =
Year2 =
$a =
$b =
$c =
$d =
$e =
$f =
$g =
$h =
a% =
b% =
c% =
d%=

Dear :

This responds to the letter of Date1, filed on your behalf by your authorized representative. In the letter, you request an extension to time to a make a safe harbor election under Rev. Proc. 2011-29, 2011-18 I.R.B. 746, to treat 70 percent of Taxpayer's success-based fee as not required to be capitalized under § 263(a) of the Internal Revenue Code for Taxpayer's Taxable Year. The request is made in accordance with §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations.

FACTS AND REPRESENTATIONS:

Taxpayer represents the following:

Taxpayer is a State corporation engaged in the manufacture of cushioned clamping, quick coupling, and support systems. At all relevant times, Taxpayer was a C corporation using the accrual method of accounting on a calendar year basis.

1. The Taxpayer and the Stock Purchase

Taxpayer represents that pursuant to a non-binding letter of intent of Date2, Facilitator1, set forth the terms of a proposed acquisition of all of the stock of Taxpayer and a related corporation, Seller2, from Sellers' Representative, and certain other minority shareholders of the two target companies (Taxpayer and Seller2). The purchase was to be completed by a new entity formed by Facilitator2, an affiliate of Facilitator1.

Facilitator2 established a new entity, Parent, a State2 limited liability company, which in turn established a wholly-owned subsidiary corporation, Purchaser. Pursuant to an Agreement of Date3, Purchaser agreed to acquire substantially all the outstanding shares of common stock of Taxpayer and Seller2. The stock acquisition transactions were completed simultaneously with the execution of the Agreement.

The parties to the transaction agreed upon a base value of Target Companies in the aggregate amount of $a. The parties further agreed that a% of the base value would be allocated to Seller2 stock, and the balance or b% to the stock of Taxpayer. The consideration provided for the stock of Taxpayer was approximately $b.

The parties also agreed that a small portion of the total consideration was to be provided as “rollover equity.” To accomplish this step, shares of stock of Target Companies having an aggregate value of approximately $c were withheld from the purchase transaction with Purchaser. Instead, these shares were transferred to Parent in exchange for each of the Target Companies to have a membership interest in Parent. As a result, Purchaser acquired approximately c% of the outstanding stock of each of the two companies, and Parent acquired approximately d% of such stock.

2. The Transaction Costs

Taxpayer represents that when Sellers’ Representative began its consideration of the disposition of the stock of Taxpayer and Seller2, it selected Financial Advisor to provide financial advisory services in connection with any resulting transaction. Sellers’ Representative caused Taxpayer and Seller2 to engage Financial Advisor for this purpose, and the two companies signed an engagement letter with Financial Advisor on Date7. The minimum success-based fee was established at $d. Taxpayer and Seller2 were each obligated to pay its share of the fees to Financial Advisor upon the completion of a successful transaction. Upon the execution and closing of the Agreement, Taxpayer was obligated to pay Financial Advisor $e, and Seller2 to pay $f.

Taxpayer represents that the proceeds of the purchase and sale transaction were disbursed among several persons. Target Companies liabilities, including the transaction costs and closing costs were paid out of the sale proceeds first, and the selling shareholders received the remainder of the sales proceeds. The total amount of transaction costs paid in this manner was $g for Taxpayer and $h for Seller2.

Taxpayer represents that, because its transaction costs were paid out of the sales proceeds, its transaction costs were not immediately reflected in its books and records.

3. Preparation of Taxpayer’s Returns and Discovery of the Missed Election

Taxpayer represents that prior to the completion of the stock purchase, Taxpayer and Seller 2 were each filing separate federal income tax returns. Taxpayer was using the calendar year as its taxable year. Following the completion of the stock purchase, Purchaser elected to file a consolidated federal income tax return with Taxpayer and Seller2, its eligible subsidiaries, also using the calendar year as its taxable year. Parent was classified as a partnership for federal income tax purposes, and thus was not a member of the Purchaser's affiliated group. Pursuant to applicable consolidated return rules, Taxpayer filed a separate federal income tax return for the Taxable Year. Taxpayer's taxable income for Year1 was included in Parent's consolidated return only for the period of Date4 through Date5.

Under Section 6.01 of the Agreement, Purchaser was responsible for preparing and filing all of Taxpayer's returns for any taxable period ending on or before the closing date, if such returns had an initial due date after the closing date of Date3. Accordingly, Purchaser hired Purchaser's CPA to prepare and file Taxpayer's separate Taxable Year return. Purchaser's CPA had not been Taxpayer's tax advisor prior to Date3. Taxpayer's return for Taxable Year was filed on Date6.

Section 6.01 of the Agreement stated in part that "any Sellers' income tax return will make the safe harbor election provided for in Rev. Proc. 2011-29, and shall be prepared in accordance with such election." Thus, Taxpayer's income tax return was to be prepared in accordance with such election. However, Purchaser's CPA failed to make the safe harbor election for Taxpayer.

In preparing Taxpayer's return for Taxable Year, Purchaser's CPA used practices that it used for other similar clients, by starting with trial balances and identifying expected differences between the book treatment and the tax treatment of certain items of income and expense. Because Taxpayer's books and records did not include its share of the Financial Advisor's fee or any other transaction costs, Purchaser's CPA did not include a deduction for any portion of the fee on Taxpayer's Taxable Year return and did not include the safe harbor election under Rev. Proc. 2011-29, as required by the Section 6.01 of the Agreement.

Subsequent to the closing of the transaction, Taxpayer and Seller2 engaged their own accounting firm, Sellers' CPA, a national accounting and tax advisory firm, to analyze all of the "selling side" transaction costs incurred in connection with this transaction. The purpose of such transaction cost studies was generally to (a) identify all relevant transaction costs, (b) determine the extent to which such costs may be deducted when paid or incurred, (c) determine the extent to which such costs are required to be capitalized, and (d) determine the assets (if any) to which any capitalized transaction costs relate. The final report was delivered by Sellers' CPA on Date8.

In the course of reviewing the transaction costs and preparing its report, Sellers' CPA discovered that many of the transaction costs were not reflected in the books and records of Taxpayer. Accordingly, Sellers' CPA provided Taxpayer with journal entries to reflect the payment of such costs in its books and records. However, these entries were developed and delivered approximately 18 months after Taxpayer filed its return for the Taxable Year.

After Taxpayer's Taxable Year return was filed, Sellers' Representative retained Sellers' CPA to review Taxpayer's return for Taxable Year. Sellers' CPA obtained a copy of Taxpayer's return for the Taxable Year and discovered that Taxpayer had not claimed a deduction on its return for any portion of Financial Advisor's success-based fee and that the Taxpayer had not made an election under Rev. Proc. 2011-29 even though the election had been explicitly contemplated by the Agreement.

After discussions among Sellers' Representative, Purchaser's CPA, and Sellers' CPA, it was determined that a request for a private letter ruling was the only means for Taxpayer to make a late election under Rev. Proc. 2011-29 for Financial Advisor's fee. Accordingly, Taxpayer engaged Sellers' CPA to represent Taxpayer in preparing this ruling request.

Thus, Taxpayer is requesting an extension of time in accordance with §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations to make a late safe harbor election under Rev. Proc. 2011-29, which would permit Taxpayer to treat 70 percent of the success-based fee as an amount that does not facilitate the transaction, i.e., an amount that can be deducted.

LAW:

Section 263(a)(1) of the Internal Revenue Code and § 1.263(a)-2(a) of the Income Tax Regulations generally provide that no deduction shall be allowed for any amount paid out for property having a useful life substantially beyond the taxable year. In the case of an acquisition or reorganization of a business entity, costs that are incurred in the process of acquisition and that produce significant long-term benefits must be capitalized. INDOPCO, Inc. v. Commissioner, 503 U.S. 79, 89-90 (1992); Woodward v. Commissioner, 397 U.S. 572, 575-576 (1970).

Under § 1.263(a)-5, a taxpayer must capitalize an amount paid to facilitate a business acquisition or reorganization transaction described in § 1.263(a)-5(a). An amount is paid to facilitate a transaction described in § 1.263(a)-5(a) if the amount is paid in the process of investigating or otherwise pursuing the transaction. Whether an amount is paid in the process of investigating or otherwise pursuing the transaction is determined based on all of the facts and circumstances. See § 1.263(a)-5(b)(1). Section 1.263(a)-5(f) provides that an amount that is contingent on the successful closing of a transaction

described in § 1.263(a)-5(a) ("success-based fee") is presumed to facilitate the transaction, and thus must be capitalized. A taxpayer may rebut the presumption by maintaining sufficient documentation to establish that a portion of the fee is allocable to activities that do not facilitate the transaction, and thus may be deductible.

A taxpayer's method for determining the portion of a success-based fee that facilitates a transaction and the portion that does not facilitate the transaction is a method of accounting under § 446.

Because the treatment of success-based fees was a continuing subject of controversy between taxpayers and the Service, the Service published Rev. Proc. 2011-29. Rev. Proc. 2011-29 provides a safe harbor method of allocating success-based fees paid in business acquisitions or reorganizations described in § 1.263(a)-5(e)(3). In lieu of maintaining the documentation required by § 1.263(a)-5(f), this safe harbor permits electing taxpayers to treat 70 percent of the success-based fee as an amount that does not facilitate the transaction, i.e., an amount that can be deducted. The remaining portion of the fee must be capitalized as an amount that facilitates the transaction.

Section 4.01 of Rev. Proc. 2011-29 allows a taxpayer to make a safe harbor election with respect to success-based fees. Section 4.01 provides that the Service will not challenge a taxpayer's allocation of success-based fees between activities that facilitate a transaction described in § 1.263(a)-5(e)(3) (costs that must be capitalized) and activities that do not facilitate the transaction (costs that may be deductible) if the taxpayer does three things. First, the taxpayer must treat 70 percent of the amount of the success-based fee as an amount that does not facilitate the transaction and thus may be deducted. Second, the taxpayer must capitalize the remaining amount of the success-based fee as an amount which does facilitate the transaction. Third, the taxpayer must attach a statement to its original federal income tax return for the taxable year the success-based fee is paid or incurred, stating that the taxpayer is electing the safe harbor, identifying the transaction, and stating the success-based fee amounts that are deducted (treated as not facilitating the transaction) and capitalized (treated as facilitating the transaction).

Sections 301.9100-1 through 301.9100-3 of the Procedure and Administration Regulations provide the standards the Commissioner will use to determine whether to grant an extension of time to make an 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(c) provides that the Commissioner has discretion to grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make certain regulatory elections. Section 301.9100-1(b) defines a "regulatory

election" as 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(a) provides that requests for relief under § 301.9100-3 will be granted when the taxpayer provides evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and that granting relief will not prejudice the interests of the government.

Section 301.9100-3(c)(1) provides 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. 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.

Section 301.9100-3(c)(2) provides special rules for accounting method regulatory elections. Section 301.9100-3(c)(2) provides that the interests of the government are deemed prejudiced, except in unusual or compelling circumstances, if the accounting method regulatory election for which relief is requested is subject to the advance consent procedures for method changes, requires a § 481(a) adjustment, would permit a change from an impermissible method of accounting that is an issue under consideration by examination or any other setting, or provides a more favorable method of accounting if the election is made by a certain date or taxable year.

In the present situation, Taxpayer has satisfied the requirements of §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations. The information and representations made by Taxpayer establish that Taxpayer acted reasonably and in good faith. The affidavits presented show that Taxpayer reasonably relied on a qualified tax professional for the proper filing of Taxpayer's federal income tax return for Taxable

Year. The representations also show that the Agreement specifically provided that Taxpayer would make the safe harbor election under Rev. Proc. 2011-29 for the success-based fees it paid to Financial Advisor. However, Purchaser's CPA failed to include the success-based fees expense on Taxpayer's return and failed to make the corresponding election. Sellers' CPA noticed Taxpayer's failure to make the safe harbor election on its return for Taxable Year. Upon discovery of the error, Taxpayer filed for relief before the government discovered the failure to properly make the regulatory election.

The information and representations presented establish that Taxpayer is not seeking to alter a return position for which an accuracy-related penalty had been or could be

imposed under § 6662 at the time relief was requested. Furthermore, Taxpayer is not using hindsight in requesting relief, and no facts have changed since the time of the original filing deadline.

Finally, granting an extension will not prejudice the interests of the government. It is represented that Taxpayer would not have a lower tax liability in the aggregate for all taxable years affected by the safe harbor election under Rev Proc. 2011-29, if given permission to make the election at this time than Taxpayer would have had if the safe harbor election had been properly made by the original deadline for making the election. Taxpayer has represented that the taxable years that would have been affected by the election had it been timely made, are not closed by the period of limitations on assessment. Finally, Taxpayer was not under audit by the IRS before Taxpayer filed for relief. Therefore, the granting of relief will not prejudice the government.

CONCLUSION:

Based upon our analysis of the facts as represented, Taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. Therefore, the requirements of §§ 301.9100-1 and 301.9100-3 have been met. Taxpayer is granted an extension of 60 days from the date of this ruling to file an amended return electing safe harbor treatment for its success-based fees under Rev. Proc. 2011-29.

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. In particular, no opinion is expressed as to whether Taxpayer properly included the correct costs as its success-based fees subject to the retroactive election, or whether Taxpayer's transaction was within the scope of Rev. Proc. 2011-29.

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 representatives. 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.

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

This ruling is based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement 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.

Sincerely,

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BRIDGET E. TOMBUL
Chief, Branch 2
Office of Associate Chief Counsel
(Income Tax & Accounting)

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Enc: copy for § 6110 purposes