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Department of the Treasury
Washington, DC 20224

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November 16, 2018

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Dear :

This letter responds to your correspondence, dated , requesting an extension of time under §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations to make the safe harbor election for success-based fees provided in Section 4 of Rev. Proc. 2011-29, 2011-18 I.R.B. 746. Section 4 requires a taxpayer, on its original federal income tax return for the year of the election, to: (1) allocate 70 percent of its success-based fees to activities that do not facilitate the transaction at issue and 30 percent to activities that do facilitate that transaction and (2) attach a statement setting forth, among other items, that the taxpayer is making the election.

FACTS

Taxpayer is a limited liability company formed under the laws of A on Date 1. Taxpayer employs an accrual method of accounting and has a taxable year ending on Date 2. Since Date 3, Taxpayer has been treated as a partnership, for federal tax purposes and has filed its federal income tax returns on Form 1065. Throughout its short taxable year ending on Date 5, Taxpayer owned L percent of B, C, D, and E, all single member limited liability companies.

Also, throughout the short taxable year ending on Date 5, holding company B, C, D. and E were in the business of designing, manufacturing, and selling Products. During this time, B, C, D, and E were disregarded entities for federal income tax purposes, and Taxpayer reported their activities directly on its federal income tax return.

On Date 4, C engaged F to assist in the sale of Taxpayer or its assets. In exchange for F's services, F was entitled to a success-based fee, calculated as a flat fee plus a percentage of the value for which Taxpayer was sold over a threshold amount. The success-based fee was payable only upon the successful sale of Taxpayer (whether through a sale of Taxpayer or its assets).

G emerged as a potential purchaser of Taxpayer. At that time G held no interest in Taxpayer. On Date 5, G acquired a controlling interest in Taxpayer through the direct and indirect acquisition of H percent of Taxpayer's equity interests (the "Transaction") pursuant to an agreement and plan of merger entered into by and among G, Taxpayer, and certain other parties. G acquired a direct J percent membership interest in Taxpayer by purchasing membership interests from existing members. G accomplished this by merging its subsidiary, K, a disregarded entity, into Taxpayer with existing members of Taxpayer receiving cash consideration in exchange for their interests. As part of the Transaction, G acquired L percent of the stock of M. M owned N percent of

Taxpayer immediately before and after the Transaction. Thus, G obtained H percent of Taxpayer's overall capital and profits interests pursuant to the Transaction.

The transfer of all funds was settled at closing, including the O owed to F. The funds and expenses were paid by Taxpayer and ultimately reduced the sale proceeds paid to P and to the selling members. Because J percent of Taxpayer's capital and profits interest was transferred to G in the Transaction on Date 5, Taxpayer represents its existence terminated pursuant to § 708(b)(1)(B) of the Internal Revenue Code. As a result, Taxpayer's taxable year ended on Date 5.

Pursuant to the merger agreement, the sellers' member representative (Sellers' Representative) would file all tax returns required of Taxpayer for periods on or before Date 5. Sellers' Representative engaged Q to prepare Taxpayer's tax return for the short taxable year ending on Date 5. The Sellers' Representative provided Taxpayer's books and records to Q. However, the Sellers' Representative failed to include in the books and records, or in any other documentation, provided to Q, the success-based fee paid to F. On Date 6, Q timely filed Taxpayer's federal income tax return for its taxable year ending on Date 5 by the extended due date, but the return did not reflect the O success-based fee.

M and the direct sellers received their final Schedules K-1 from Taxpayer on or around Date 7. R, as M's tax preparer, reviewed M's final Schedule K-1 on Date 8 and noted that the income reported was significantly higher than anticipated. M then contacted Taxpayer's controller who ultimately determined on Date 9 that no portion of the O success-based fee had been taken into account on Taxpayer's tax return.

LAW

Section 263(a)(1) and § 1.263(a)-2(a) of the Income Tax Regulations 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 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, 112 S. Ct. 1039, 117 L. Ed. 2d 226 (1992); Woodward v. Commissioner, 397 U.S. 572, 575-576, 90 S. Ct. 1302, 25 L. Ed. 2d 577 (1970).

Under § 1.263(a)-5(a), a taxpayer must capitalize an amount paid to facilitate the business acquisition or reorganization transactions described in § 1.263(a)-5(a). In general, 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 paid that is contingent on the successful closing of a transaction described in § 1.263(a)-(5)(a) (i.e., a success-based fee) is presumed to facilitate the transaction. A taxpayer may rebut this presumption by maintaining sufficient documentation to establish that a portion of the fee is allocable to activities that do not facilitate the transaction.

Section 4.01 of Rev. Proc. 2011-29 provides a safe harbor election for taxpayers that pay or incur success-based fees for services performed in the process of investigating or otherwise pursuing a covered transaction described in § 1.263(a)-5(e)(3). In lieu of maintaining the documentation required by § 1.263(a)-5(f), a taxpayer may elect to allocate a success-based fee between activities that facilitate the transaction and activities that do not facilitate the transaction by treating 70 percent of the amount of the success-based fee as an amount that does not facilitate the transaction and by capitalizing the remaining 30 percent as an amount that does facilitate the transaction. In addition, 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 and capitalized.

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.

Sections 301.9100-1 through 301.9100-3 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 301.9100-3(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(b)(1) provides that a taxpayer is 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) 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 (taking into account the taxpayer's experience and the complexity of the return at issue), 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, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

Section 301.9100-3(b)(3) provides that a taxpayer will not be deemed 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, 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.

Section 301.9100-3(c)(1) provides that an extension of time to make a regulatory election will be granted only when the interests of the government are not prejudiced by the granting of relief. The interests of the government are prejudiced if granting relief would result in a 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)(i).

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 under § 6501(a) before the taxpayer's receipt of a ruling granting relief under § 301.9100-3.

Section 301.9100-3(c)(2) provides special rules for accounting method regulatory elections. The interests of the government are deemed to be prejudiced except in unusual and compelling circumstances if the accounting method regulatory election for which relief is requested:

(i) is subject to the procedure set forth in § 1.446-1(e)(3)(i) of this chapter (requiring advance written consent of the Commissioner);
(ii) requires an adjustment under § 481(a) (or would require an adjustment under § 481(a) if the taxpayer changed to the method of accounting for which relief is requested in a taxable year

subsequent to the taxable year in which the election should have been made);

(iii) would permit a change from an impermissible method of accounting that is an issue under consideration by examination, an appeals office, or a federal court and the change would provide a more favorable method or more favorable terms and conditions than if the change were made as part of an examination; or

(iv) provides a more favorable method of accounting or more favorable terms and conditions if the election is made by a certain date or taxable year.

ANALYSIS

Taxpayer's election is a regulatory election, as defined in § 301.9100-1(b), because the due date of the election is prescribed in § 1.263(a)-5(f). The Commissioner has the authority under §§ 301.9100-1 and 301.9100-3 to grant an extension of time to file a late regulatory election.

The information provided and representations made by Taxpayer establish that Taxpayer acted reasonably and in good faith. Taxpayer requests relief before the failure to make the regulatory election is discovered by the Service, and taxpayer reasonably relied on Q to prepare its short year return. Moreover, Taxpayer is not seeking to alter a return position for which an accuracy related penalty has been or could be imposed under § 6662 at the time relief is requested. Taxpayer did not affirmatively choose not to make the election after having been informed in all material respects of the required election and related tax consequences. Taxpayer is not using hindsight in requesting relief.

Further, based on the information provided and representations made by Taxpayer, granting an extension will not prejudice the interests of the government. The Taxpayer will not have a lower tax liability in the aggregate for all taxable years to which the election applies than Taxpayer would have had if the election had been timely made. In addition, the taxable year in which the regulatory election should have been made and any taxable years that would have been affected by the election had it been timely made will not be closed by the period of limitations on assessment under § 6501(a) before Taxpayer's receipt of the ruling granting an extension of time to make a late election.

CONCLUSION

Based solely on the information provided and representations made, we conclude that Taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. Accordingly, 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 for its taxable year ending on Date 5, reflecting 70 percent of the O success-based fee as an amount that does not facilitate the transaction and capitalizing the remaining 30 percent of the success-based fee as an amount that does facilitate the transaction. Taxpayer must also attach the mandatory statement to its return, as required by section 4.01 of Revenue Procedure 2011-29. The mandatory statement must state that Taxpayer is electing the safe harbor for success-based fees, identify the transaction, and state the success-based fee amounts that are deducted and capitalized.

The ruling contained in this letter is based upon information and representations submitted by 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 this ruling, 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. 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) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to Taxpayer’s federal tax returns for the tax years affected. 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.

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

Sincerely,

Sean M. Dwyer
Senior Technician Reviewer, Branch 1
(Income Tax & Accounting)

Enclosure:
Copy of letter