Internal Revenue Service

Number: **202048009**
Release Date: 11/27/2020

Index Number: 475.08-00, 9100.00-00, 9100.10-01

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:FIP:B03
PLR-106280-20

Date:
August 28, 2020

Legend

Taxpayers: =

Husband: =

Wife: =

Business =

Accountant 1 =

Accountant 2 =

Advisor =

Lawyer =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Date 10 =

Date 11 =

Date 12 =

a =

b =

c =

d =

e =

f =

g =

h =

i =

Dear :

This letter responds to a request for a private letter ruling that Taxpayers filed with the Internal Revenue Service (Service). Taxpayers' letter and subsequent submissions requested an extension of time under § 301.9100 of the Procedure and Administration Regulations to make an election to use the mark-to-market method of accounting under § 475(f)(1) of the Internal Revenue Code, effective for the taxable year that ended Date 1. Taxpayers' request was filed with our office on Date 2.

FACTS

Taxpayers are a married couple and are referred to individually herein as Husband and Wife. Husband is the founder, owner, and president of Business, a medical facility where he also works part-time as a physician. Since at least Year 1, Husband has also traded securities and sought short term gains in the stock market. Wife is not directly involved in Husband's trading activities.

During Date 3, Husband communicated with Accountant 1, Taxpayers' federal income tax return preparer and tax advisor, regarding potentially making a § 475(f) election. In a memorandum to file, Accountant 1 noted that he discussed with Husband in detail the requirements for qualifying as a trader eligible to make a § 475(f)(1) election. Based on Husband's claim that he was making multiple trades per day, Accountant 1 noted that it appeared that Husband qualified as a trader.[1]

Taxpayers reported having a short-term capital loss carryover in the amount of a on their Year 3 federal income tax return. Husband's stock trading generated significant additional net losses prior to the Date 4 due date for making the § 475(f)(1) election effective for Year 3. Husband continued to trade and incurred substantial additional trading losses after the election due date. Husband's largest monthly trading losses were incurred in Date 5, after the due date of the election, and approximately b percent of his net trading losses, in the amount of c for Year 3, also arose after the election due date. Further, Husband was unable to generate gains in Year 4 to absorb Taxpayers' capital losses. In early Year 4, Husband received a Form 1099 reporting that Husband's trading activities had generated substantial wash sale losses in the amount of d for Year 3.

On Date 6, e months after the Date 4 election due date, Husband emailed Accountant 1, asking whether it was true that a day trader can deduct more than $3,000 per year in trading losses. Accountant 1 advised Husband that there is some truth to that if Husband qualified as a trader. Accountant 1 did not inform Husband at that time that the deadline to make a § 475(f)(1) election had passed for Year 3, or otherwise inform Husband that making a timely election was required.

[1] In his affidavit, Accountant 1 stated, "I believed at that time [Date 3] that [Husband] appeared to satisfy and meet all the requirements for a valid mark-to-market election."

On Date 7, Husband requested Accountant 1 to do whatever was possible to reduce his federal income tax liability. More specifically, Husband communicated that he would like to deduct all of his stock losses for both Year 1 and Year 2. On Date 8, Accountant 1 emailed Husband information regarding income tax planning considerations associated with potentially making a § 475(f)(1) election. Accountant 1 described additional information that he needed to make the election for Year 2, and provided a description of the requirements for being a trader, including that a taxpayer's trading activities must be frequent, regular, and continuous.[2] Accountant 1 indicated that he was prepared to make the election for Year 2 on Taxpayers' Year 2 federal income tax return if Husband (a) believed he met the requirements for being a trader, (b) was willing to bear the risk of making the election, and (c) provided the additional information needed to make the election.

Taxpayers' Year 2 and original Year 3 federal income tax returns were filed by reporting stock gains and losses on a realization basis. In preparation of Taxpayers' Year 3 tax return, Advisor informed Husband by email on Date 9 that, "Consistent with [Accountant 1]'s earlier analysis, you won't be able to claim trader status for [Year 3]."[3] Following a meeting with Husband and Lawyer, Accountant 2, who was employed at the same accounting firm as Accountant 1 and Advisor, informed Husband by email on Date 10 that a § 475(f)(1) election should have been filed by the unextended due date of the federal income tax return for the year preceding the year for which the election is made. Accountant 2 also alerted Husband of the opportunity to pursue relief under § 301.9100-3 to make a late § 475(f)(1) election for Year 3.[4] Taxpayers filed their first request for relief on Date 11, nearly f months after the due date for making the election and g months after Accountant 2 had alerted Husband of the opportunity to request relief to make a late election. After the first request for relief was withdrawn, a second request was made on Date 12, h months after the Date 4 election due date. After the second request for relief was withdrawn, Taxpayers filed their third and current request on Date 2. The third request was filed i months after the election due date.

LAW AND ANALYSIS

Taxpayers are not entitled to relief under § 301.9100 to make a late § 475(f)(1) election because Taxpayers did not act reasonably and in good faith, and granting relief would prejudice the interests of the Government.

[2] Husband asserts that Accountant 1 made a commitment in the Date 8 email to make a § 475(f)(1) election effective for Year 3 on Taxpayers' behalf.

[3] Advisor further advised in the Date 9 email that Taxpayers might face penalties on audit with respect to Husband's claim of trader status and that the capital losses could be eventually used to offset gain on the sale of Business.

[4] Accountant 2 also advised Husband in the Date 10 email that Husband's prospects for obtaining late relief were lessened because of hindsight.

Relief under § 301.9100 to make a late § 475(f)(1) election is denied

Section 475(f)(1) provides that a taxpayer engaged in a trade or business as a trader in securities may elect to apply the mark-to-market method of accounting to securities held in connection with such trade or business. Section 7805(d) provides that, except to the extent otherwise provided by the Code, any election shall be made at such time and in such manner as the Secretary shall prescribe.

Revenue Procedure 99-17, 1999-1 C.B. 503, sets forth the requirements for making an election under § 475(f). Under section 5.03 of that revenue procedure, a taxpayer must file an election statement not later than the due date (without regard to any extension) of the original federal income tax return for the taxable year immediately preceding the election year and must attach the statement either to that return or, if applicable, to a request for an extension of time to file that return. Section 5.04 of Rev. Proc. 99-17 sets forth the requirements for the statement. The statement must describe the election being made, the first taxable year for which the election is effective, and, in the case of an election under § 475(f), the trade or business for which the election is made. Section 4 of Rev. Proc. 99-17 provides that an election under § 475(f) determines the method of accounting that an electing taxpayer is required to use for federal income tax purposes for securities subject to the election. Once a valid election is made, the taxpayer is required to use a mark-to-market method of accounting under § 475. Section 4 of Rev. Proc. 99-17 also provides that if a taxpayer fails to change the taxpayer's method of accounting to comply with the election, then the taxpayer is on an impermissible method.

Section 6.01 of Rev. Proc. 99-17[5] provides that a change in a taxpayer's method of accounting is a change in method of accounting to which the provisions of §§ 446 and 481 and the regulations promulgated thereunder apply. Section 6.03 of Rev. Proc. 99-17 generally provides that if a taxpayer changes its method of accounting under section 6.01 of Rev. Proc. 99-17, the taxpayer must take into account the net amount of the § 481(a) adjustment over the applicable period.

Section 23.01 of Rev. Proc. 2017-30, 2017-18 I.R.B. 1131, provides procedures for a trader in securities that has made a § 475(f)(1) election to obtain automatic consent of the Commissioner to change the trader's method of accounting for securities to use the mark-to-market method of accounting under § 475.[6] Section 23.01(4) of Rev. Proc. 2017-30 refers to section 5 of Rev. Proc. 99-17 for the requirements to make a § 475(f)(1) election.

[5] Section 6 of Rev. Proc. 99-17 was superseded by Rev. Proc. 99-49, 1999-2 C.B. 725.
[6] Rev. Proc. 2017-30 is the automatic method change revenue procedure that would have applied to Taxpayers' election filing, had it been timely filed.

Revenue Procedure 2015-13, 2015-5 I.R.B. 419, sets forth the general procedures under § 446(e) to obtain the consent of the Commissioner to change a method of accounting for federal income tax purposes, including the procedures to obtain the automatic consent of the Commissioner to change a method of accounting in Rev. Proc. 2017-30. Under section 7.02 of Rev. Proc. 2015-13, unless otherwise provided in a specific change listed in Rev. Proc. 2017-30, a taxpayer making a change in method of accounting must apply § 481(a) and take into account the § 481(a) adjustment in the manner provided in section 7.03 of Rev. Proc. 2015-13. Section 23.01 of Rev. Proc. 2017-30 does not contain an exception to the rule in section 7.02 of Rev. Proc. 2015-13.

Section 301.9100-1(c) provides, in part, that the Commissioner has discretion to grant a reasonable extension of time to make a regulatory election (defined in § 301.9100-1(b) as an election whose due date is prescribed by regulations published in the Federal Register, or by a revenue ruling, revenue procedure, notice, or announcement published in the Internal Revenue Bulletin). Section 301.9100-1(b) defines the term election to include a request to change an accounting method.

Section 301.9100-3 sets forth rules that the Commissioner must use to determine whether it will grant an extension of time for regulatory elections that do not meet the requirements of § 301.9100-2 for an automatic extension. Generally, a taxpayer must provide sufficient evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and that the grant of relief will not prejudice the interests of the Government.

Except as provided in § 301.9100-3(b)(3), § 301.9100-3(b)(1) provides rules for determining when a taxpayer is deemed to have acted reasonably and in good faith. Section 301.9100-3(b)(1)(i) provides that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer requests relief under § 301.9100-3 before the failure to make the regulatory election is discovered by the Service. Section 301.9100-3(b)(3) provides rules as to when a taxpayer is deemed to have not acted reasonably and in good faith. Section 301.9100-3(b)(3)(iii) provides that a taxpayer is deemed to have not acted reasonably and in good faith if specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer. In such a case, the 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) provides 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 that 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)(2) provides special rules for accounting method regulatory elections. Section 301.9100-3(c)(2)(ii) provides that 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 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 the election should have been made).

a) Taxpayers did not act reasonably and in good faith

Section 301.9100-3(b)(3)(iii) provides that a taxpayer is deemed to have not acted reasonably and in good faith if specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer. In such a case, the Service will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

To make a timely § 475(f)(1) election for Year 3, Taxpayers had to make the § 475(f)(1) election by Date 4, the unextended due date of Taxpayers' federal income tax return for Year 2. Taxpayers did not file their first request for relief under § 301.9100-3 until Date 11. Taxpayers' request for a late filing of the § 475(f)(1) election was made with the benefit of nearly f months of hindsight. Husband continued to trade during Year 3 and Year 4. Husband realized his largest monthly trading loss during Date 5, after the due date for filing a § 475(f)(1) election for Year 3. Further, Husband suffered approximately b percent of his trading losses for Year 3 after the election due date. Additionally, Husband received a Form 1099 in early Year 4 reporting wash sale losses in the amount of d from his trading activities in Year 3, and knew the outcome of his trading activities in Year 4 before filing a request for relief under § 301.9100-3 to make a late § 475(f)(1) election. Taxpayers gained a benefit from hindsight because they were able to determine the effect of a § 475(f)(1) election with the benefit of knowledge that Husband's ongoing trading activities (a) produced a significant increase in realized trading losses and wash sale losses,[7] and (b) did not produce meaningful gains to absorb Taxpayers' capital losses. Thus, Taxpayers' specific facts materially changed after the due date for making the § 475(f)(1) election, and those specific fact changes made that election advantageous to Taxpayer. Moreover, Taxpayers did not provide strong proof showing that their decision to seek relief to make a late election did not involve hindsight.[8] Accordingly, under § 301.9100-3(b)(3), Taxpayers are deemed to have not acted reasonably and in good faith.

[7] Under § 475(d), the § 1091 wash sale rules do not apply to securities to which § 475(a) applies.
[8] Husband's assertion that he instructed Accountant 1 to timely make a § 475(f) election is not supported by the facts provided. Rather, it is evident that Husband and Accountant 1 did not even begin to revisit the prospect of making a § 475 election until at least e months after the election due date had passed.

b) Granting Relief Would Prejudice the Interests of the Government

Under § 301.9100-3(c)(2)(ii), 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 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 the election should have been made). Taxpayers have not presented unusual and compelling circumstances. After suffering large trading losses during Date 5, Husband revisited the prospect of making the election with Accountant 1 on Date 6, more than e months after the due date for making the § 475(f)(1) election. Accountant 1 advised Husband of the possibility of deducting his trading losses if Husband qualified as a trader, but Accountant 1 failed to point out the need to have timely made an election (the due date for which had already passed). Those circumstances are neither unusual nor compelling.

Since a § 475(f)(1) election is an accounting method regulatory election that requires a § 481(a) adjustment, the interests of the Government are deemed to be prejudiced because Taxpayers have failed to present unusual and compelling circumstances to justify granting the requested relief.

CONCLUSION

Based on the facts and representations submitted, we conclude that Taxpayers have not satisfied the requirements to justify granting an extension of time under § 301.9100-3 to make an election under § 475(f)(1) to use the mark-to-market method of accounting effective for the taxable year that ended Date 1. Specifically, Taxpayers have failed to demonstrate that they have acted reasonably and in good faith, and that granting relief will not prejudice the interests of the Government. Accordingly, Taxpayers' request for an extension of time to make an election under § 475(f)(1) for Year 3 is denied.

Except as expressly provided herein, no opinion is expressed or implied concerning the federal income tax consequences of the transactions described above. In particular, no opinion is expressed or implied as to whether Husband's securities trading activities constitute those of a trader in securities eligible to make the mark-to-market election under § 475(f)(1).[9]

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

[9] Based on the information supplied by Taxpayers, there is an issue whether Husband's trading activities during Year 3 were sufficiently regular, frequent, and continuous for Husband to have been considered engaged in the trade or business of being a trader in securities for purposes of § 475(f)(1).

In accordance with the terms of a power of attorney on file in this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

Patrick E. White
Senior Counsel, Branch 3
Office of the Associate Chief Counsel
(Financial Institutions and Products)

Enclosures:
Copy of this letter
Copy for section 6110 purposes

cc: