Internal Revenue Service

Department of the Treasury
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Person To Contact:
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Telephone Number:

Refer Reply To:
CC:ITA:B03
PLR-121378-20

Date:
March 22, 2021

In Re:

Legend

Date 1 =
Taxable Year =
State =
Target =
Parent =
Merger Sub =
Corporation =
Managing Member =
Advisor =
$a =
Accounting Firm 1 =
Accounting Firm 2 =
Accounting Firm 3 =
Accounting Firm 4 =
Date 2 =

Dear :

This letter responds to a letter ruling request dated September 25, 2020, requesting an extension of time to make a late safe harbor election under Rev. Proc. 2011-29, 2011-18 I.R.B. 746. Taxpayer failed to attach the required election statement to its originally filed federal income tax return for Taxable Year in order to make the safe harbor election to allocate success-based fees between facilitative and non-facilitative amounts. Therefore, Taxpayer requests an extension of time under §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations to attach the required election statement to its Taxable Year return.

FACTS

Taxpayer, a State corporation, which, directly and through its subsidiaries, designs, sources, and sells branded kitchenware, tableware, and other products used in the home. Taxpayer uses an overall accrual method of accounting and has a calendar year end.

Taxpayer was interested in acquiring Target, a limited liability company formed under the laws of State. Target operated as a holding company for its subsidiaries that primarily designed, marketed, and distributed consumer and food service precision measurement products, wine accessories, kitchen tools, select outdoor, and other related products. Target is classified as an association taxable as a corporation for federal income tax purposes and was the common parent of an affiliated group of corporations filing a consolidated federal income tax return. The membership interests of Target were held by Parent, a limited liability company formed under the laws of State.

The acquisition of the Target by the Taxpayer was completed pursuant to an Agreement and Plan of Merger ("Agreement") by and among the Taxpayer, Merger Sub, Corporation, Parent, and Managing Member of the Target. Under the Agreement, two successive mergers were completed. In the first merger, Merger Sub merged with and into the Target, with the Target surviving. In the second merger, the Target merged with and into Corporation, with the Corporation surviving. Corporation is disregarded an entity separate from its owner for federal income tax purposes. As a result, Taxpayer is deemed to have acquired all of the assets of the Target pursuant to a statutory merger under Treas. Reg. § 1.368-2(b)(1)(ii). Consistent with Rev. Rul. 2001-46, the transaction was properly treated as a reorganization under IRC § 368(a)(1)(A), pursuant to which the Target was deemed to have merged directly into the Taxpayer.

Taxpayer incurred a success-based fee in connection with its acquisition of the Target. This fee was paid to Advisor for services performed in the process of investigating or otherwise pursuing the acquisition completed pursuant to the Agreement. Taxpayer successfully acquired the Target on Date 1. Pursuant to Taxpayer's agreements with Advisor, Taxpayer paid success-based fees of $a after successful closing of the acquisition. The fee was contingent upon the successful closing of the acquisition as described in Treas. Reg. § 1.263(a)-5(f).

Under the terms of the acquisition, Taxpayer was responsible for filing all income tax returns for Target and its subsidiaries for all periods ending on or prior to the closing date, if such returns were required to be filed after the closing date. Taxpayer engaged Accounting Firm 1 to analyze the proper federal income tax treatment of the transaction costs incurred by the Taxpayer and the Target. Accounting Firm 1 provided a summary of the costs that could be deducted, costs that were required to be capitalized and amortized, or were required to be capitalized without amortization. Accounting Firm 1

identified success-based fees in its analysis of the relevant transaction costs for both entities and prepared the safe harbor election statements in accordance with Rev. Proc. 2011-29.

Taxpayer's federal income tax returns had previously been prepared by Accounting Firm 2. Target's tax return preparation had been historically handled by Accounting Firm 3. Accounting Firm 1 provided a copy of its analysis and the election statements to Accounting Firm 2 and Accounting Firm 3. Eventually, Taxpayer decided to change its tax return preparation firm to Accounting Firm 4 for preparation of Tax Year. Accounting Firm 4 requested all tax return files from Accounting Firm 2, but the safe harbor elections drafted by Accounting Firm 1 were not included in the information Accounting Firm 2 provided. Accordingly, it became evident that Taxpayer's federal income tax return was timely filed on Date 2, but the return failed to include the safe harbor election statement. Although the election statement was not attached to the return, Taxpayer capitalized the transaction costs in accordance with § 263 of the Internal Revenue Code and §§ 1.263(a)-2 and 1.263(a)-5 of the Income Tax Regulations, and in a manner consistent with the safe harbor election outlined in Rev. Proc. 2011-29.

Taxpayer discovered the election statement pursuant to Rev. Proc. 2011-29 had inadvertently been omitted from its return for Taxable Year. Taxpayer obtained advice from Accounting Firm 4 for advice regarding the omitted election. Taxpayer files this request for relief under Treas. Reg. §§ 301.9100-1 and 301.9100-3.

Taxpayer represents that the transactions completed in the acquisition of Target constituted a "covered transaction" within the meaning of Treas. Reg. § 1.263(a)-5(f). It further represents that Advisor's fees paid in connection with the transaction constitute amounts contingent on the successful closing of a covered transaction within the meaning of Treas. Reg. § 1.263(a)-5(f). The Taxpayer is not seeking to alter a return position for which an accuracy related penalty has been or could be imposed under IRC § 6662 as of the date of the request. The Taxpayer relied on Accounting Firm 4 to make the required election under Rev. Proc. 2011-29 and has not used hindsight in requesting relief to make the late election. Thus, Taxpayer promptly requested an extension of time to allow Taxpayer to attach to the required statement regarding the election to use the safe harbor method for allocating success-based fees to its federal income tax return for Taxable Year.

LAW

Section 263(a)(1) of the Internal Revenue Code 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 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 § 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. Section 1.263(a)-5(b)(1). Whether an amount is paid in the process of investigating or otherwise pursuing the transaction is determined based on all the facts and circumstances. Section 1.263(a)-5(b)(1).

Under § 1.263(a)-5(f) 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.

Rev. Proc. 2011-29 provides a safe harbor method of accounting for allocating success-based fees paid in business acquisitions or reorganizations described in § 1.263(a)-5(e)(3) (covered transactions), including a taxable acquisition by the taxpayer of assets that constitute a trade or business. 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, meaning that amount that can be deducted. The remaining portion (30 percent) of the fee must be capitalized as an amount that facilitates the transaction.

Section 4.01 of Rev. Proc. 2011-29 allows the 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: (1) treats 70 percent of the amount of the success-based fee as an amount that does not facilitate the transaction and thus may be deducted; (2) capitalizes the remaining amount of the success-based fee as an amount which does facilitate the transaction and thus must be capitalized; and (3) attaches 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 pursuant to the safe harbor election.

Sections 301.9100-1 through 301.9100-3 provide the standards that 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 §§ 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(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 or 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)(2) provides that 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:

(i) Competent to render advice on the regulatory election; or
(ii) Aware of all relevant facts.

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

ANALYSIS

The Commissioner has the authority to grant an extension of time to file a later regulatory election under §§ 301.9100-1 and 301.9100-3. Taxpayer's election is a regulatory election under §301.9100-1(b) because it is prescribed under Rev. Proc. 2011-29.

Taxpayer represents that its acquisition of Target was a covered transaction under §1.263(a)-5(e)(3) and that fees $a paid to Advisor were success-based fees as defined in §1.263(a)-5(f). The payment of the fees was contingent upon the successful closing of the transaction.

Taxpayer represents that Accounting Firm 4, although identifying the safe harbor provision of Rev. Proc. 2011-29 and preparing the federal income tax return for Taxable Year as though the safe harbor had been elected, failed to provide to the taxpayer the requisite statement that is needed as an attachment for returns that elect the safe harbor provisions of Rev. Proc. 2011-29. attach the required statement to Taxpayer's federal income tax return for Taxable Year because it was not included in the materials received from Accounting Firm 2. Taxpayer further represents that its own failure to detect the omitted election statement was inadvertent. Based on these representations, Taxpayer reasonably relied on a qualified tax professional and, under § 301.9100-3(b)(1)(v), is deemed to have acted reasonably and in good faith.

Taxpayer represents that granting relief would not result in a lower tax liability in the aggregate for all taxable years affected by the election than Taxpayer would have had if the election had been timely made (taking into account the time value of money). Furthermore, Taxpayer represents that 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. Based on these representations, granting an extension of time to file the election will not prejudice the interests of the government under § 301.9100-3(c)(1).

CONCLUSION

Based upon our analysis of the facts and representations provided, 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 the election statement required by Section 4.01(3) of Rev. Proc. 2011-29, stating that it is electing the safe harbor for success-based fees for Taxable Year, identifying the covered transaction, and stating the success-based fee amounts that are deducted and capitalized, in accordance with Taxpayer's representations.

The ruling contained in this letter is based on 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 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. In particular, no opinion is expressed as to Taxpayer's classification of its fees as success-based fees or whether Taxpayer's acquisition of Target is within the scope of Rev. Proc. 2011-29.

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

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.

In accordance with the provisions of the power of attorney currently on file with this office, copies of this letter are being sent to your authorized representative. We are also sending a copy of this letter to the appropriate operating division director.

Sincerely,

BRINTON T. WARREN
Chief, Branch 3
Office of Associate Chief Counsel
(Income Tax and Accounting)

Enclosure: Copy for § 6110 purposes