

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:B04

PLR-128072-19

Date:

November 04, 2021

Taxpayers	=
Entity 1	=
Entity 2	=
Entity 3	=
Business Activities	=
Property	=
Loan	=
Bank	=
Advisor	=
Document	=
State	=
State Tax Entity	=
Date 1	=
Date 2	=

Date 3	=
Date 4	=
Date 5	=
Year 1	=
Year 2	=
Year 3	=
Percentage 1	=
Percentage 2	=
Percentage 3	=
Amount 1	=
Amount 2	=
Amount 3	=
Amount 4	=
Amount 5	=
Amount 6	=

Dear _____ :

This letter responds to your request for a private letter ruling granting an extension of time under section 301.9100-3 of the Procedure and Administration Regulations to make an election under section 108(c)(3)(C) of the Internal Revenue Code to exclude from income the discharge of qualified real property business indebtedness for tax year Year 1. Your authorized representatives have provided additional information and participated in an adverse conference, as provided in Revenue Procedure 2021-1. As set forth below, we have denied your request.

FACTS

Based on the representations of Taxpayers and the information provided by your authorized representative, the facts are as follows.

Taxpayers together own a Percentage 1 interest in Entity 1, a partnership for federal tax purposes. Entity 1 owns a Percentage 2 interest in Entity 2, a limited liability company formed in State, and a Percentage 3 interest in Entity 3, a limited liability company for federal tax purposes. Entity 2, formed in Year 2, is in the business of Business Activities and was the sole owner of real property located at Property.

Pursuant to a Loan dated Date 1, the Property was encumbered by a loan payable to Bank. On Date 2, the total outstanding loan balance was Amount 1.

On Date 2, Entity 2 sold the Property to Entity 3 for Amount 2. Entity 2 paid Amount 3 to Bank on the outstanding loan balance, and Bank discharged the remaining loan balance, amounting to Amount 4. For tax year Year 1, Entity 2 reported a loss of Amount 5 under section 1231 of the Internal Revenue Code and cancellation of debt (COD) income of Amount 6.

Taxpayers engaged Advisor, a qualified tax professional, to prepare their tax returns for tax year Year 1. Taxpayers and Advisor state that (1) Advisor did not advise Taxpayers on the availability of the section 108(c)(3)(C) election, (2) the failure to make the election was due to inadvertence and not tax planning, and (3) that Taxpayers would have made the election if its availability had been known. For tax year Year 1, Entity 2 reported no taxable income as its 1231 loss exceeded income. Advisor provided contemporaneous Year 1 return documents, including a Document, showing computations related to the 1231 loss and COD income resulting in Entity 2's 1231 loss being only partially offset by the COD income. Advisor, during discussions with us, stated that at the time he prepared Entity 2's and Taxpayers' returns there was no benefit to making the § 108(c)(3)(C) election because of the large 1231 loss. As such, the COD income was reported and recognized in Year 1 and Advisor did not advise to elect to exclude the COD income and reduce tax attributes.

The State Tax Entity examined Entity 2's state tax return for tax year Year 1 and disallowed the section 1231 loss pursuant to I.R.C. section 707(b)(1)(B)¹. The State Tax Entity determined that the sale of the Property by Entity 2 to Entity 3 constituted a sale or exchange of property, directly or indirectly, between two partnerships in which the same persons own, directly or indirectly, more than 50% of the capital interest or profits interests. The state tax matter is currently under appeal pending the resolution of this private letter ruling request. The Service did not examine Taxpayers' Year 1 Federal income tax return, and the claimed 1231 loss, prior to the expiration of the statute of limitations and has no ability to now do so.

¹ State's tax law conforms to federal tax law with modification.

On Date 3, more than six years after a timely election was required to be made, Taxpayers submitted this request for an extension of time under §§ 301.9100-1 and 301.9100-3 to make an election under section 108(c)(3)(C) for tax year Year 1. The representations and facts provided establish that allowing the late election would require amended returns for closed tax years Year 1-Year 3 (and possibly beyond) that would affect each years' computations and amount of tax due; however, Taxpayers concede that the statute of limitation is closed for those years so that Taxpayers may not request a refund and the Service may not examine the returns and/or assess additional tax.

On Date 4, we informed your representative that we were tentatively adverse. We subsequently held an adverse conference of right and follow-up telephonic conferences. In addition, your representative provided additional information and documents. On Date 5, we informed your authorized representative that we had made a final adverse determination.

LAW

Section 108(a)(1)(D) provides that gross income does not include the amount which (but for § 108(a)) would be includible in gross income by reason of the discharge of indebtedness of the taxpayer if in the case of a taxpayer other than a C Corporation, the indebtedness discharged is qualified real property indebtedness.

Section 108(c)(1) provides that the amount excluded from income under § 108(a)(1)(D) shall be applied to reduce basis of the depreciable real property of the taxpayer.

Section 108(c)(3) provides that the term "qualified real property business indebtedness" means indebtedness that:

- (A) was incurred or assumed by the taxpayer in connection with real property used in a trade or business and is secured by such real property;
- (B) was incurred or assumed before January 1, 1993; and
- (C) with respect to which such taxpayer makes an election to have § 108(c)(3) apply.

Section 108(d)(6) provides that in the case of a partnership, § 108(a) and (c) apply at the partner level.

Section 108(d)(9)(A) provides that an election under § 108(c)(3)(C) shall be made on the taxpayer's return for the taxable year in which the discharge occurs or at such other times as may be permitted in regulations prescribed by the Secretary.

Section 108(d)(9)(C) provides that an election referred to in § 108(d)(9)(A) shall be made in such manner as the Secretary may by regulations prescribe.

Section 1.108-5 of the Income Tax Regulations, which is effective December 27, 1993, provides that the election to treat indebtedness as qualified real property business indebtedness under § 108(c)(3) is to be made on Form 982 and attached to a timely-filed return for the taxable year in which the taxpayer has discharge of indebtedness income that is excludable under section 108(a).

Section 301.9100-1(c) provides that the Commissioner has the discretion to grant a reasonable extension of time to make a regulatory election. Section 301.9100-1(b) defines the term “regulatory election” as including any election the due date for which is prescribed by a regulation. Because the due date of the section 108(c)(3)(C) election is prescribed in § 1.108-5, that election is a regulatory election.

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

Section 301.9100-3(a) provides that requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides evidence, including affidavits described in § 301.9100-3(e), to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of the relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(3)(iii) provides that a taxpayer is considered to have not acted reasonably and in good faith if the taxpayer uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to the taxpayer, the Service will not ordinarily grant relief.

Section 301.9100-3(c)(1) provides that the Service 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 the 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. Under § 301.9100-3(c)(1)(ii), the interests of the Government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made, or any taxable year affected by the election had it been timely made, are closed by the period of limitations on assessment under § 6501(a) before the taxpayer’s receipt of a ruling granting relief under § 301.9100-3. However, the IRS may condition a grant of relief on the taxpayer providing the IRS with a statement from an independent auditor (other than an auditor providing an affidavit pursuant to paragraph (e)(3) of this section) certifying that the interests of the Government are not prejudiced by means of subsection (c)(1)(i).

Section 5.03(2) of Revenue Procedure 2021-1 (and its predecessors) provides that the Service ordinarily will not issue a § 301.9100 ruling if the period of limitation on assessment under § 6501(a) for the taxable year in which an election should have been made, or for any taxable years that would have been affected by the election had it been timely made, will expire before receipt of a § 301.9100 letter ruling. However, the Service may issue the letter ruling if the taxpayer consents to extend the period of limitation on assessment under § 6501(c)(4) for the taxable year in which the election should have been made and for any taxable years that would have been affected by the election had it been timely made.

DISCUSSION

Based on the facts provided and representations made, we deny Taxpayers' request for relief under § 301.9100-3. We find that Taxpayers did not act reasonably and in good faith because the request is based on hindsight and we find the interests of the Government would be prejudiced by granting the requested relief because the statute of limitations is closed for Year 1 and subsequent years affected by the late election.

In addition, we find that the requested six-year extension is not a reasonable extension of time because the Taxpayers should have discovered the missed election before the statute of limitations expired and/or the state tax authority disallowed the 1231 loss. Lastly, we find that granting relief would not be in the interest of sound tax administration because the expired statute of limitations prevents the Service from examining Entity 2's and Taxpayers' Year 1 return, as well as subsequent affected returns. Each of the reasons described herein independently support our denial.

Under § 301.9100-3(b)(3), a taxpayer is considered to have not acted reasonably and in good faith if the taxpayer uses hindsight in requesting relief. The representations and statements provided establish that at the time the Year 1 return was prepared, Advisor was aware of the § 108 election, the election provided no benefit to Taxpayers, and Taxpayers have no explanation as to why they would have made the election if informed of its availability. We find Taxpayers' statement that they would have made the election to be self-serving and unsupported by the facts. The sole reason provided for seeking relief to make the election is to affect the outcome of a subsequent state tax proceeding. The state tax proceeding is a change of facts after the original deadline that makes the election advantageous to the Taxpayers and, as such, establishes that Taxpayers request is due to hindsight.

Under § 301.9100-3(c)(1)(ii), the interests of the Government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made, or any taxable year affected by the election had it been timely made, are closed by the period of limitations on assessment under § 6501(a). Tax year Year 1, for which Taxpayers are seeking to make the late section 108(c)(3)(C), is closed. Subsequent tax years, years in which Taxpayers did not reduce basis of depreciable real property as required by section 108(c)(1) but rather took depreciation deductions, are closed as well.

The Service may condition a grant of relief on the taxpayer providing a statement from an independent auditor certifying that the taxpayer will not have a lower tax liability should the late election be allowed. Taxpayers offered to provide a certification after we notified them that we were tentatively adverse; however, an independent audit and certification is insufficient as it assumes the propriety of the § 1231 loss, the eligibility for the § 108 election, and that other positions and computations on the returns are proper, which the Service is not permitted to examine. For this reason, and other legal and administrative considerations, § 5.03(2) of Revenue Procedure 2021-1 provides that the Service ordinarily will not issue a § 301.9100 ruling if the period of limitation on assessment under § 6501(a) has expired for the taxable year in which an election should have been made, or for any taxable years that would have been affected by the election had it been timely made.

CONCLUSION

Based on the facts and representations provided, and for the reasons discussed, Taxpayers are not granted an extension of time under § 301.9100-3 to make a late § 108(c)(3)(C) election because Taxpayers did not act reasonably and in good faith, the interests of the Government would be prejudiced, the amount of time requested is not reasonable, and granting the extension would not be in the best interests of tax administration.

This letter is being issued electronically in accordance with Rev. Proc. 2020-29, 2020-21 I.R.B. 859. A paper copy will not be mailed to the taxpayer. Pursuant to the Form 2848, Power of Attorney and Declaration of Representation, on file, we are sending a copy of this letter to your authorized representatives.

Sincerely,

Ronald J. Goldstein
Senior Technician Reviewer, Branch 4
(Income Tax & Accounting)

cc: