**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:B03
PLR-130367-12

In Re:

Date:
December 19, 2012

Legend:

Taxpayers =
Related Party =
Tax Return Preparer =
Year 1 =
Year 2 =
Year 3 =

Dear :

This responds to your letter dated June 6, 2012, requesting an extension of time under §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations for you to make a late election to treat qualified dividends and net capital gain as investment income pursuant to §§ 163(d)(1) and 163(d)(4)(B) of the Internal Revenue Code (the Code) for Year 1, Year 2, and Year 3.

FACTS

Taxpayers are individual taxpayers filing a joint return. Taxpayers hold all the interests in Related Party which is taxed as a corporation. Taxpayers and Related Party timely filed federal income tax returns for Year 1, Year 2, and Year 3. Tax Return Preparer, a CPA, prepared the tax returns for both Taxpayers and Related party for these taxable years. On its tax returns, Related Party claimed deductions for the payments made to Taxpayers. Taxpayers reported the payments received from Related Party as income and they also took a deduction for interest.

Related Party's tax return for Year 1, Year 2, and Year 3 were examined, as well as Taxpayers' individual income tax returns for Year 1, Year 2, and Year 3. As a result of

the examination and Appeals process, it was determined that Taxpayers have dividend income and investment interest that was previously reported as rental income and mortgage interest. Because of this, Taxpayers request a ruling that they be allowed to make the election under § 163(d)(4)(B) that they would have made had the amounts been considered dividends when the returns were originally filed for Year 1, Year 2, and Year 3. Taxpayers have made a representation that Related Party is taxed as a domestic corporation and that constructive dividends paid out of earnings and profits of Related Party are qualified dividend income to Taxpayers as defined in § 1(h)(11)(B) of the Code.

Further, Taxpayers did not originally make the election to treat net capital gain as investment income in Year 2 because there was no investment expense. Now that there are investment interest expenses for that year, Taxpayers wish to elect to include net capital gain in investment income for Year 2.

Taxpayers have signed Forms 872-A to extend the period of limitations on assessment under § 6501(a) for Year 1 and Year 2 for an indefinite period of time. The statute of limitations has not run for Year 3 and thus, Year 3 is still open to tax assessment.

LAW

Section 163(d)(1) of the Code provides that, in the case of a taxpayer other than a corporation, the amount allowed as a deduction for investment interest for any taxable year shall not exceed the net investment income of the taxpayer for the taxable year.

Section 163(d)(4)(A) of the Code provides that the term “net investment income” means the excess of investment income over investment expenses.

Section 163(d)(4)(B) of the Code provides, in pertinent part, that investment income means the sum of --

(i) gross income from property held for investment (other than any gain taken into account under clause (ii)(I)),

(ii) the excess (if any) of --

> (I) the net gain attributable to the disposition of property held for investment, over
>
> (II) the net capital gain determined by only taking into account gains and losses from dispositions of property held for investment, plus

(iii) so much of the net capital gain referred to in clause (ii)(II) (or, if lesser, the net gain referred to in clause (ii)(I)) as the taxpayer elects to take into account under this clause.

Such term shall include qualified dividend income (as defined in § 1(h)(11)(B)) only to the extent the taxpayer elects to treat such income as investment income for purposes of this subsection.

Section 1.163(d)-1(b) of the Income Tax Regulations provides that the election for net capital gain and qualified dividend income must be made on or before the due date (including extensions) of the income tax return for the taxable year in which the net capital gain is recognized or the qualified dividend income is received.

Sections 301.9100-1 through 301.9100-3 of the Procedure and Administration Regulations provide the standards the Commissioner uses to determine whether to grant an extension of time to make a regulatory election. For this purpose, § 301.9100-1(b) defines the term "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 301.9100-1(c) provides that the Commissioner may grant a reasonable extension of time to make a regulatory election, or a statutory election (but no more than six months except in the case of a taxpayer who is abroad), under all subtitles of the Internal Revenue Code except subtitles E, G, H, and I.

Section 301.9100-3(a) provides that requests for extensions of time for regulatory elections (other than automatic changes covered under § 301.9100-2) 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 will be 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) inadvertently failed to make the election because of intervening events beyond the taxpayer's control;

(iii) failed to make the election because, after exercising due diligence, 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, 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 considered to have acted reasonably and in good faith if the taxpayer --

(i) seeks to alter a return position for which an accuracy-related penalty could be imposed under § 6662 at the time the taxpayer requests relief and the new position requires 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. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

Section 301.9100-3(c)(1) provides that the Commissioner will grant a reasonable extension of time only when the interests of the Government will not be prejudiced by the granting of relief. Under paragraph (c)(1)(i), 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 paragraph (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 years that would have been 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 this section.

ANALYSIS

Taxpayers' election is a regulatory election, as defined under § 301.9100-1(b), because the due date of the election is prescribed in the Income Tax Regulations under § 1.163(d)-1(b). In the present situation, the requirements of §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations have been satisfied. The information and representations made by Taxpayers establish that Taxpayers acted reasonably and in good faith. Taxpayers reasonably relied on Tax Return Preparer, a qualified tax professional, for the filing of their tax returns and Tax Return Preparer failed to make the election. Neither Taxpayers nor Tax Return Preparer knew of the need to make an election under § 163(d)(4)(B) at the time Taxpayers' original tax returns were filed because they did not become aware of it until the Service's examination of Taxpayers' federal income tax returns.

Further, based on the facts of the case provided, granting an extension will not prejudice the interests of the Government. Taxpayer will not have a lower tax liability in the aggregate for all taxable years affected by the election if given permission to make the election at this time than Taxpayer would have had if the election had been timely

made. In addition, the taxable years 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.

RULING

Because they acted reasonably and in good faith and granting relief will not prejudice the interests of the Government, Taxpayers have met the requirements for an extension under § 301.9100-3 for making the § 163(d)(4)(B) election for Year 1, Year 2, and Year 3. Accordingly, Taxpayer is granted an extension of time for making the election until 60 days from the date of this ruling. The election should be made by filing Forms 4952, "Investment Interest Expense Deduction," with amended returns for Year 1, Year 2, and Year 3, and by including a copy of this ruling letter.

The rulings contained in this letter are based upon information and representations submitted by Taxpayers 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. 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 Taxpayers' authorized representative.

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.

Sincerely,

Christopher F. Kane
Branch Chief, Branch 3
(Income Tax & Accounting)

Enclosure (1)