Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:ITA:B02
PLR-122529-17

Date: November 24, 2017

ATTN:

TY: Year 1

Legend

Taxpayer	=
Sub 1	=
Sub 2	=
Purchaser	=
Merger Sub	=
Firm	=
Agreement	=
A	=
B	=
C	=
D	=
E	=
F	=
G	=
H	=
I	=
J	=
K	=
L	=
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N =

O =
P =
Year 1 =
Date 1 =
Date 2 =
Date 3 =
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Date 6 =
Date 7 =
Date 8 =
Date 9 =
Date 10 =
Date 11 =
Date 12 =

Dear :

This is in response to your letter of Date 1, requesting permission to make an election to use the safe harbor method of accounting for success-based fees under section 4.01 of Rev. Proc. 2011-29, 2011-1 C.B. 746 for your taxable year ending Date 2. The request is made in accordance with §§ 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations.

FACTS

Taxpayer represents the following:

Taxpayer is the common parent of an affiliated group of corporations that join in filing a consolidated federal income tax return. Taxpayer owns all the stock in Sub 1. Sub 1 owns all the issued and outstanding stock in Sub 2. Sub 2 is engaged in the A.

Pursuant to an Agreement of Date 3, Purchaser effectively acquired all the outstanding stock of Taxpayer. Purchaser had formed Merger Sub solely for the purpose of effectuating the merger, pursuant to which the Merger Sub was merged with and into Taxpayer, with Taxpayer surviving the merger. The transaction was treated as a taxable purchase by Purchaser of Taxpayer's stock. The merger was completed on Date 2, and Taxpayer became a wholly-owned subsidiary of Purchaser on that date.

Sub 2 considered various transactions that could lead to a change in ownership of its stock. It selected B to provide financial advisory and investment banking services in

connection with any resulting transaction. Sub 2 signed an engagement letter with B on Date 4. At that time, Sub 2 thought a specified transaction involving C was feasible. Accordingly, the engagement letter spelled out a reduced fee of $D for a transaction involving C. In the case of any other transaction that was successfully completed, the fee would be the greater of $E. Such fees were only payable upon the completion of a successful transaction. B was also entitled to reasonable out-of-pocket expenses.

The Agreement terminated F months after the date of the engagement. Some progress had been made by Date 5, and Sub 2 and B entered into an extension agreement dated Date 3, wherein Sub 2 agreed to pay B a fee in consideration of the services provided in connection with the transaction involving the Purchaser. B agreed to accept a reduction of $G in the fees payable under the H formula but not below the minimum of $I. Upon the execution and closing of the extended Agreement, Sub 2 became obligated to pay B the sum of $J under the formula, together with reimbursement of $K in out-of-pocket expenses, for a total of $L. B sent Sub 2 an invoice for this amount dated Date 6.

Taxpayer engaged Firm to prepare and file its federal income tax return for the short year Date 7. This return was filed on Date 8. Firm had prepared Taxpayer's consolidated federal income tax returns since Date 9.

Taxpayer's, Sub 1's and Sub 2's taxable income was included in Purchaser's taxable income only for the period from Date 10, the last day of the Purchaser's taxable year during which the acquisition occurred. Purchaser's consolidated federal income tax return for the taxable year ending Date 11, was filed on or before Date 12.

In preparing Taxpayer's final return, Firm would normally discuss its books, records and transactions with officers and employees of Taxpayer. However, M. Therefore, Firm discussed these matters with representatives of Purchaser. Sub 2's books and records did not reflect B's fee or any transaction costs. Firm representatives inquired several times to ascertain whether success-based fees had been paid in connection with the Agreement. They were assured that the fees were paid by N and not by Sub 2. Firm determined the B fee was not deductible by Taxpayer. Therefore, Taxpayer's final consolidated return was prepared and filed without making an election under Rev. Proc. 2011-29 and without deducting any part of the fee.

Approximately O after Taxpayer's final return was filed, Purchaser's CFO was reviewing the computations to determine the final payment to be made to N. He noted that Taxpayer's final return did not include a deduction for any portion of the B fee. He consulted with Firm about this and Firm determined that Sub 2 had consulted with B and was responsible for the fee. Firm and Purchaser also consulted with P, the law firm that represented Purchaser in the acquisition of Taxpayer. P concurred that Sub 2 incurred and paid a success-based fee to B. Taxpayer should have made an election under Rev. Proc. 2011-29 and deducted a portion of the B fee.

Taxpayer represents that, because its books and records did not reflect that it had paid any portion of B's success-based fee, and Firm and Taxpayer had reached a consensus that Taxpayer did not pay or incur any success-based fees, it would not have been necessary to make the election. Taxpayer further represents that the failure to make the election under Rev. Proc. 2011-29 with respect to B's success-based fee was inadvertent. The circumstances resulting in the failure to make the election were not the result of retroactive tax planning or tax avoidance. It was only the discovery, after the return was filed, of the nature and extent of the B engagement and the failure to make the election that Taxpayer determined to request this ruling in order to seek relief to make a late election. Taxpayer filed this request before the failure to make the election was discovered by the Internal Revenue Service.

LAW

Section 263(a)(1) of the Internal Revenue Code and § 1.263(a)-2(a) of the Income Tax Regulations generally 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, 575-76 (1970).

Under § 1.263(a)-5, a taxpayer must capitalize an amount paid to facilitate a business acquisition or reorganization transaction described in § 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. Whether an amount is paid in the process of investigating or otherwise pursuing the transaction is determined based on all the facts and circumstances. *See* § 1.263(a)-5(b)(1).

Section 1.263(a)-5(f) provides that 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.

A taxpayer's method for determining the portion of a success-based fee that facilitates a transaction and the portion that does not facilitate the transaction is a method of accounting under § 446.

Because the treatment of success-based fees was a continuing subject of controversy between taxpayers and the Service, the Service published Rev. Proc. 2011-29. 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). In lieu of maintaining the documentation required by § 1.263(a)-5(f), this safe harbor permits electing taxpayers to treat seventy percent of the success-based fee as an amount that does not facilitate the transaction *i.e.*, an amount that can

be deducted. The remaining portion 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 the 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 deducted) if the taxpayer does three things. First, the taxpayer must treat seventy percent of the amount of the success-based fee as an amount that does not facilitate the transaction and thus may be deducted. Second, the taxpayer must capitalize the remaining amount of the success-based fee as an amount which does facilitate the transaction. Third, 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 (treated as not facilitating the transaction) and capitalized (treated as facilitating the transaction).

Taxpayer requests permission with this ruling request to make the election under Rev. Proc. 2011-29 to treat 70 percent of its success-based fees as not required to be capitalized under section 263(a).

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 extensions of time for regulatory elections (other than automatic changes covered under section 301.9100-2) will be granted when the taxpayer provides evidence (including affidavits described in the regulations) 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 Internal Revenue Service (IRS);

(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, the taxpayer was unaware of the necessity for the election;

(iv) reasonably relied on the written advice of the IRS; 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 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. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the IRS will not ordinarily grant relief.

Section 301.9100-3(c)(1) 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. 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. 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.

Section 301.9100-3(c)(2) provides special rules for accounting method regulatory elections. Section 301.9100-3(c)(2) provides that the interests of the Government are deemed prejudiced, except in unusual or compelling circumstances, if the accounting method regulatory election for which relief is requested is subject to the advance consent procedures for method changes, requires a § 481(a) adjustment, would permit a change from an impermissible method of accounting that is an issue under consideration by examination or in any other setting, 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 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.

RULING

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 statement required by section 4.01(3) of Rev. Proc. 2011-29, stating that it is electing the safe harbor for success-based fees, identifying the transaction, and stating the success-based fee amounts that are deducted and capitalized for its taxable year ending Date 2.

CAVEATS

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. No opinion is expressed as to the federal tax treatment of the transaction under any other provisions of the Internal Revenue Code and the Treasury Regulations that may be applicable or under any other general principles of federal income taxation. This letter ruling is only applicable to matters under our jurisdiction. *See* Rev. Proc. 2017-1, 2017-1 I.R.B. 1, 18, Section 1. No opinion is expressed as to the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the above ruling. 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 any income tax return to which it is relevant. 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.

The rulings contained in this letter are based upon information and representations submitted by the 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.

Enclosed is a copy of this letter ruling showing the deletions proposed to be made in the letter when it is disclosed under § 6110.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives. We are also sending a copy of this letter to the appropriate operating division director.

Sincerely,

_____

Bridget E. Tombul
Branch Chief, Branch 2
Office of the Associate Chief Counsel
(Income Tax & Accounting)

cc: Industry Director, Natural Resources and Construction (LB&I:NRC)

Enc. Copy for § 6110 purposes