

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

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Refer Reply To:

CC:ITA:3 PLR-121725-01

Date:
June 20, 2001

Taxpayers =

Tax Professionals =

Year 1 =

Year 2 =

Dear

This is in response to your letter dated April 12, 2001. In your letter you requested permission to revoke an election under section 1.163(d)-1(c) of the Income Tax Regulations to treat capital gains as investment income under sections 163(d)(1) and 163(d)(4)(B)(iii) of the Internal Revenue Code for Year 1 (the "Election").

FACTS

Taxpayers timely filed a joint Form 1040, Individual Income Tax Return, for Year 1. The return was prepared and reviewed by Tax Professionals. Taxpayers' return included Form 4952, Investment Interest Expense Deduction, on which they elected to treat all net capital gains attributable to property held for investment as investment income.

During the course of researching and preparing the Taxpayers' Individual Income Tax Return for Year 2, Tax Professionals believe that Taxpayers should have filed as a securities trader for Year 1. Generally, in situations where taxpayers are treated as securities traders for federal income tax purposes, such taxpayers would be entitled to a deduction for net investment expense without having to make an election to treat net

capital gains as investment income under section 1.163(d)-1. The effect of electing to treat net capital gains as investment income is to tax the net capital gains at ordinary income tax rates. If the Election had not been made, the net capital gains allocated to Form 4952 would have been taxed at a lower rate than the applicable ordinary income tax rate. Taxpayers intend to amend their Year 1 federal income tax return to reflect a securities trader status. As a result, Taxpayers seek permission to revoke the Election.

APPLICABLE 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)(B) of the Code provides, in 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 solely by taking into account gains and losses from disposition 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.

Section 1.163(d)-1(b) of the Regulations provides that the election under section 163(d)(4)(B)(iii) 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.

Section 1.163(d)-1(c) of the Regulations provides that the election under section 163(d)(4)(B)(iii) is revocable with the consent of the Commissioner.

Taxpayers are requesting permission to revoke the Election, which was based on tax advice rendered by Tax Professionals. This situation is analogous to those situations concerning taxpayers who have not made a particular election provided in the regulations because of inadequate or incorrect advice from knowledgeable tax professionals and are subsequently seeking extensions of time under section 9100 of the regulations. Rev. Rul. 83-74, 1983-1 112.

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. 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 section 301.9100-2.

Section 301.9100-1(b) of the Regulations defines the term “regulatory election” as an election where the 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) of the Regulations provides, in part, that the Commissioner may grant a reasonable extension of time to make a regulatory election.

Section 301.9100-3(a) of the Regulations 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 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) of the Regulations 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) of the regulations 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 section 6662 at the time the taxpayer requests relief and the new position requires a regulatory election for which relief is requested;

- (ii) was fully informed 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) of the Regulations 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.

CONCLUSION

Taxpayers timely filed the Election, on Form 4952, based on the advice of Tax Professionals. Taxpayers exhibited due diligence by timely selecting Tax Professionals to prepare their federal income tax return and relied on the Tax Professionals to make the Election. After being advised by Tax Professionals that Taxpayers should seek to revoke the Election, Taxpayers promptly filed with the Internal Revenue Service a request to revoke the Election. The Election was made by Taxpayers as a result of inadvertence. These actions, coupled with Taxpayer's prompt request for revocation, indicate that Taxpayers did not take any action inconsistent with their intent to file a proper federal income tax return for Year 1. Furthermore, granting the revocation would neither prejudice the interests of the Government, nor cause undue administrative burden, nor would revocation be inconsistent with the objectives of the underlying statute and the regulatory election.

RULING

Taxpayers are granted permission to revoke the Election made on their Year 1 federal income tax return.

This ruling is based upon information and representations submitted by the Taxpayers and accompanied by a penalty of perjury statement. While this office has not verified any of the material submitted in support of the ruling request, it is subject to verification on examination.

No opinion is expressed about the tax treatment of the Election under other provisions of the Code or regulations, or the tax treatment of any conditions existing at the time of, or effects resulting from, the Election that is not specifically covered by the above ruling. In particular, no opinion is expressed concerning whether Taxpayer qualifies as a securities trader for federal income tax purposes.

Under the power of attorney on file in this office, a copy of this letter is being sent to your authorized representative.

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

Sincerely yours,
Assistant Chief Counsel
(Income Tax & Accounting)
By: Robert M. Casey
Branch Chief, CC:ITA:3