

## Internal Revenue Service

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Date:

January 16, 2015

## LEGEND

X =

A =

LLC =

Year 1 =

Year 2 =

\$a =

\$b =

Lender =

Individual =

Firm =

Dear \_\_\_\_\_ :

This letter responds to your letter dated July 15, 2014, requesting an extension of time under § 301.9100-3 of the Procedure and Administration Regulations to make the election described in § 108(c)(3)(C) of the Internal Revenue Code to treat certain indebtedness as qualified real property business indebtedness.

## FACTS

LLC is a limited liability company that is treated as a partnership for federal income tax purposes. LLC has two owners, X and A, and its principal business is owning and managing commercial real property. X, an S corporation whose taxable year is the calendar year, owns an 88.524% interest in LLC. LLC's other owner is A, an individual whose taxable year is the calendar year, who owns an 11.476% interest in LLC.

LLC defaulted on a bank loan, and in Year 1, with the outstanding balance on the defaulted loan of \$a, Lender agreed to discharge \$b. LLC reported \$b as income on its

Year 1 tax return, and it reported each member's distributive share of that income on each of their Schedule K-1s. X and A each reported their distributive share of this income on their tax returns for Year 1.

Individual, a tax preparer with many years of experience, prepared the Year 1 tax returns for X and A. Neither X's Year 1 tax return nor A's Year 1 tax return included the election described in § 108(c)(3)(C).

Prior to Year 1, Individual had experienced health issues that adversely affected Individual's work performance. Although X and A were aware that Individual was experiencing health issues, they did not realize that this illness was preventing him from attending to work responsibilities. Individual did not discuss the § 108(c)(3)(C) election with X or A during the process of preparing the Year 1 tax returns for X and A.

In Year 2, upon becoming aware of the severity of Individual's illness, X hired additional accounting staff, who, with the help of Firm, recreated complete financial records for X and LLC for Year 1. Upon reviewing these financial records, Firm advised X and A that they would have been eligible to exclude \$b from income in Year 1 pursuant to § 108(a)(1)(D) if a timely § 108(c)(3)(C) election had been made.

As of the date of your letter, neither X nor A had been contacted by the Internal Revenue Service regarding either taxpayer's Year 1 tax return or the lack of a § 108(c)(3)(C) election with those returns. X and A represent that granting relief under § 301.9100-3 will not result in a lower tax liability in the aggregate for all years to which the election applies than X and A (and all interested parties) would have had if the § 108(c)(3)(C) election had been timely made (taking into account the time value of money).

## LAW AND ANALYSIS

Section 61(a)(12) provides that, except as otherwise provided, gross income includes income from the discharge of indebtedness (COD income).

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

Section 108(c)(3) provides that qualified real property 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, or if incurred or assumed after that date, is qualified acquisition indebtedness, and (C) with respect to which the taxpayer makes an election to have § 108(c)(3) apply. Section 108(c)(4) provides that qualified

acquisition indebtedness means, with respect to any real property described in § 108(c)(3)(A), indebtedness incurred or assumed to acquire, construct, reconstruct, or substantially improve such property.

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

Section 108(d)(9)(A) provides that the § 108(c)(3)(C) election is made on the taxpayer's return for the taxable year that the discharge occurs or at another time specified in regulations promulgated by the Secretary. Section 108(d)(9)(C) provides that the § 108(c)(3)(C) election is made in the manner prescribed in regulations.

Section 1.108-5(b) of the Income Tax Regulations provides that the § 108(c)(3)(C) election must be made on the timely filed (including extensions) Federal income tax return for the taxable year in which the taxpayer has COD income that is excludible from gross income under § 108(a). The election is made on a completed Form 982, Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment), in accordance with the Form and its instructions.

Section 301.9100-1(c) of the Procedure and Administration Regulations provides that the Commissioner has discretion to grant a reasonable extension of time to make a regulatory election under all subtitles of the Internal Revenue Code except subtitles E, G, H, and I. Section 301.9100-1(d) defines the term "regulatory election" as including an election the due date of which is prescribed by a regulation, revenue ruling, revenue procedure, notice, or announcement.

Section 301.9100-3 provides that requests for extensions of time for regulatory elections (other than automatic extensions covered in § 301.9100-2) will be granted when the taxpayer provides evidence (including affidavits) to establish that the taxpayer acted reasonably and in good faith, and 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) 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 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, however, that a taxpayer is 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 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 fully informed 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)(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 (taking into account the time value of money). Similarly, if the tax consequences of more than one taxpayer are affected by the election, the Government's interests are prejudiced if extending the time for making the election may result in the affected taxpayers, in the aggregate, having a lower tax liability than if the election had been timely made. Furthermore, § 301.9100-3(c)(1)(ii) provides that 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 statute of limitations before the taxpayer's receipt of a ruling granting relief under this section.

Based on the information provided and the representations made, we conclude that X and A acted reasonably and in good faith within the meaning of § 301.9100-3, and that granting an extension of time to make the § 108(c)(3)(C) election will not prejudice the interests of the Government.

Accordingly, X and A are granted an extension of 45 days from the date of this letter to file an amended Federal income tax return for Year 1 to make the election described in §§ 108(c)(3)(C) and 1.108-5(b). The election is to be made on Form 982.

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. Specifically, we express no opinion as to whether the discharged bank loan is qualified real property indebtedness within the meaning of § 108(c)(3)(A) or (B) that is eligible for the election described in § 108(c)(3)(C). In addition, we express no opinion regarding the amount of COD income realized by the discharge, nor whether (or to what extent) any COD income realized is excludible from gross income under § 108(a)(1)(D).

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 Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

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.

Sincerely,

Jeffrey T. Rodrick  
Senior Technician Reviewer, Branch 5  
Office of Associate Chief Counsel  
(Income Tax & Accounting)