

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:ITA:1-PLR-122304-01

Date:

September 28, 2001

Legend

Taxpayer =
Year 1 =
Year 2 =
Year 3 =
Location =
Firm =

Dear :

This ruling responds to a letter dated April 11, 2001, submitted by your authorized representative, requesting an extension of time, under § 301.9100 of the Procedure and Administration Regulations, for Taxpayer to make an election to use the alternative cost method of accounting in conformity with the requirements of Rev. Proc. 92-29, 1992-1 C.B. 748.

FACTS

Taxpayer is a limited liability company that is classified as a partnership for federal income tax purposes and uses an accrual method of accounting. Taxpayer is engaged in real estate development and was formed to develop a parcel of land in Location. The project was projected to last 10-15 years and included various kinds of residential units as well as retail and office space. At the end of Year 1, Taxpayer sold 6 lots to homebuilders for the purpose of erecting model homes. The lots were sold without water and sewer utilities. The number of lots sold in Year 1 for model homes represented a negligible portion of the overall project.

Taxpayer's federal partnership tax return for Year 1 was prepared and filed by employees of Taxpayer's tax matters partner. Because only a small number of lots without utilities were sold in Year 1, Taxpayer did not believe that it was required to make an election under Rev. Proc. 92-29 for Year 1. The election was due on September 15 of Year 2. In January of Year 3, Taxpayer was advised by Firm that an election should have been filed for Year 1. Shortly thereafter, this request for relief was

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filed.

Rev. Proc. 92-29 provides a procedure for a developer of real estate to obtain the Commissioner's consent to use an alternative from the general method under § 461(h) of the Internal Revenue Code for determining when common improvement costs may be included in the basis of properties sold for purposes of determining the gain or loss resulting from the sales. This alternative cost method allows a developer to include in the basis of properties sold their allocable share of the estimated cost of common improvements, without regard to whether the costs have been incurred under § 461(h), subject to certain limitations.

Under section 6.01 of Rev. Proc. 92-29, a developer that is a corporation or partnership must file a request to use the alternative cost method with the appropriate district director for the internal revenue district in which is located the developer's principal place of business or principal office or agency.¹ The request must be filed on or before the due date of the developer's original federal income tax return (determined with regard to extensions of time) for the taxable year in which the first benefitted property is sold. The developer must also attach a copy of the request to its timely filed original federal income tax return for the taxable year.

From the outset of the project, Taxpayer intended to use the alternative cost method. Taxpayer actually used a method similar to the alternative cost method to account for common improvement costs in the bases of properties sold in Year 1. Taxpayer failed to timely file the election under Rev. Proc. 92-29 because it did not initially believe such election was necessary for Year 1.

Taxpayer represents that, but for its failure to timely file an election under Rev. Proc. 92-29, Taxpayer is qualified to use the alternative cost method. Taxpayer is not under examination for Year 1 and has not been notified by the Internal Revenue Service of its failure to comply with the requirements of Rev. Proc. 92-29.

LAW AND ANALYSIS

Sections 301.9100-1 through 301.9100-3 set forth the standards that the Commissioner will use to determine whether to grant an extension of time to make a regulatory election. Section 301.9100-2 provides an automatic extension of time to make certain statutory 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 under § 301.9100-3 will be granted when the taxpayer provides evidence to establish to the satisfaction of the

¹ Under the new structure of the Internal Revenue Service, a developer must now file its request with the director, as defined in section 1 of Rev. Proc. 2001-1, 2001-1 I.R.B. 1.

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Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1) enumerates five circumstances under which a taxpayer is deemed to have acted reasonably and in good faith. A taxpayer is deemed to have acted reasonably and in good faith if the taxpayer requests relief before the failure to make the regulatory election is discovered by the Service, or if the taxpayer failed to make the election because, after exercising reasonable diligence (taking into account the taxpayer's experience and the complexity of the return or issue), the taxpayer was unaware of the necessity for the election.

Section 301.9100-3(b)(3) provides 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 has been or could be imposed under § 6662 at the time the taxpayer requests relief;
- (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 due date for making the election that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief. In such a case, the Service will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

Section 301.9100-3(c)(1) provides, in part, 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). Section 301.9100-3(c)(1) also provides, in part, 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 period of limitations on assessment under § 6501(a) before the taxpayer's receipt of a ruling granting relief under § 301.9100-3.

Section 301.9100-3(c)(2) provides that the interests of the government are deemed to be prejudiced except in unusual and compelling circumstances if the accounting method regulatory election for which relief is requested -

- (i) Is subject to the procedure described in § 1.4461(e)(3)(i);
- (ii) Requires an adjustment under § 481(a) (or would require an adjustment

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under § 481(a) if the taxpayer changed to the method of accounting for which relief is requested in a taxable year subsequent to the taxable year the election should have been made);

- (iii) Would permit a change from an impermissible method of accounting that is an issue under consideration by examination, an appeals office, or a federal court 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
- (iv) 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.

Based on our analysis of the facts, the taxpayer in the present case acted reasonably and in good faith, and granting relief will not prejudice the interests of the government. Therefore, the requirements of § 301.9100 have been met.

Taxpayer failed to timely file an election to use the alternative cost method because of a mistake regarding the proper application of Rev. Proc. 92-29 to its project. Taxpayer always intended to use the alternative cost method under Rev. Proc. 92-29 and in fact used a similar method to compute its basis in the properties sold in Year 1. Taxpayer is not seeking to alter a return position for which an accuracy-related penalty has been or could be imposed under § 6662. Taxpayer did not use hindsight in requesting relief. No facts have changed since the due date for making the election that make the election advantageous to Taxpayer. Finally, Taxpayer acted promptly in filing its request for relief, before the Service discovered the failure to make the regulatory election. Therefore, Taxpayer acted reasonably and in good faith.

Furthermore, granting relief will not result in Taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than Taxpayer would have had if the election had been timely made, nor will any closed taxable years be affected. Additionally, none of the circumstances listed in § 301.9100-3(c)(2), which describes conditions under which the interests of the government are generally deemed to be prejudiced with respect to accounting method regulatory elections, are present in this case. Therefore, the interests of the government will not be prejudiced by granting the requested relief.

Because Taxpayer acted reasonably and in good faith, and because the interests of the government will not be prejudiced if the request for relief is granted, Taxpayer is granted an extension of 45 days from the date of this ruling to file with the director a request to use the alternative cost method under Rev. Proc. 92-29.

The ruling contained in this letter is based upon facts and representations submitted by Taxpayer. Except as specifically addressed herein, no opinion is expressed regarding the tax treatment of the subject transaction under the provisions of any other sections of the Code or regulations that may be applicable thereto.

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Specifically, no opinion is expressed as to whether Taxpayer satisfies any of the other requirements for eligibility to use the alternative cost method of Rev. Proc. 92-29. 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.

In accordance with the power of attorney on file in our office, copies of this letter are being sent to your representatives. A copy of this letter ruling should be attached to the returns, schedules, and forms filed in connection with making the election under Rev. Proc. 92-29 when such forms are filed.

Sincerely,
Kimberly L. Koch
Assistant to Branch Chief, Branch 1
Office of Associate Chief Counsel
(Income Tax & Accounting)