Internal Revenue Service

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Date:
November 10, 2015

LEGEND

Year 1 =

Year 2 =

Taxpayers =

Lot A =

Lot B =

County =

State =

Month =

Year 3 =

Dear :

This letter responds to a request for an extension of time under sections 301.9100-1 and 301.9100-3 of the Procedure and Administration Regulations to elect to capitalize property taxes pursuant to section 266 of the Internal Revenue Code for the Year 1 calendar year.

FACTS

Taxpayers are married individuals who timely filed a joint federal income tax return for the Year 1 calendar year on or around April 15, Year 2. Taxpayers represent that they owned and held for investment purposes two parcels of unimproved and unproductive real property (Lot A and Lot B) during Year 1, which are located in County, State. Taxpayers paid property taxes on these investment properties in Year 1 and did not elect under section 266 to capitalize these taxes to the properties. Instead, the property taxes were reported as itemized deductions by Taxpayers on their Year 1 federal income tax return. In Year 1, Taxpayers were subject to the alternative minimum tax ("AMT"). Because the deduction for property taxes is not allowed in computing AMT, Taxpayers obtained a limited tax benefit from reporting the property taxes as itemized deductions for Year 1.

Taxpayers' tax return preparer (Preparer) was not aware of and therefore did not advise Taxpayers of the opportunity to make an election under section 266 and sections 1.266-1(b)(1) and (c)(3) of the Income Tax Regulations to capitalize taxes on unimproved and unproductive real property. In Month of Year 2, Taxpayers sold Lot B for a capital gain. In Year 3, when Preparer was completing preparation of Taxpayers' Year 2 federal income tax return, Taxpayers' accountant alerted Preparer to the opportunity of Taxpayers making the election to capitalize property taxes under section 266. Preparer then advised Taxpayers of the opportunity to make this election, which Taxpayers did on their Year 2 return. Preparer then also informed Taxpayers of the possibility of filing a request for a private letter ruling granting extensions of time under sections 301.9100-1 and 301.9100-3 to file a section 266 election for Year 1.

Preparer represents that Taxpayers relied on him to provide tax advice. Preparer states that "Until [Year 3], I did not appreciate that the election under section 266 to capitalize certain expenses paid or incurred with respect to nonproductive real property extended to property taxes."

LAW AND ANALYSIS

Section 56(b)(1)(A)(ii) provides that in determining the amount of the alternative minimum taxable income, no deduction shall be allowed for any taxes described in section 164(a)(1).

Section 164(a)(1) provides that a deduction for state and local, and foreign real property taxes are allowed as a deduction for the taxable year within which paid or accrued.

Section 266 provides that no deduction shall be allowed for amounts paid or accrued for such taxes and carrying charges as, under regulations prescribed by the Secretary, are chargeable to capital account with respect to property, if the taxpayer elects, in accordance with such regulations, to treat such taxes or charges as so chargeable.

Section 1.266-1(b)(1) provides in part that the taxpayer may elect, as provided in paragraph (c) of this section, to treat the items enumerated in this subparagraph which are otherwise expressly deductible under the provisions of subtitle A of the Code as chargeable to capital account either as a component of original cost or other basis, for the purposes of section 1012, or as an adjustment to basis, for the purposes of section 1016(a)(1). The items thus chargeable to capital account are –

> (i) In the case of unimproved and unproductive real property: Annual taxes, interest on a mortgage, and other carrying charges.

Section 1.266-1(b)(2) provides that an item not otherwise deductible may not be capitalized under 266.

Section 1.266-1(c)(2)(i) provides that an election with respect to an item described in paragraph (b)(1)(i) is effective only for the year for which it is made.

Section 1.266-1(c)(3) provides in part that if the taxpayer elects to capitalize an item or items under this section, such election shall be exercised by filing with the original return for the year for which the election is made a statement indicating the item or items (whether with respect to the same project or to different projects) which the taxpayer elects to treat as chargeable to capital account.

Under section 301.9100-1(c), the Commissioner has discretion to grant a reasonable extension of time to make a regulatory election under all subtitles of the Code except subtitles E, G, H, and I, provided that the taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the Government. 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. An “election” includes an application for relief in respect of tax as well as a request to adopt, change, or retain an accounting method.

Section 301.9100-3 provides extensions of time to make regulatory elections under Code sections other than those for which section 301.9100-2 expressly permits automatic extensions.

Section 301.9100-3(a) provides in part that the Commissioner will grant a request for an extension of time when a taxpayer provides the evidence, including affidavits described in paragraph (e), establishing to the Commissioner's satisfaction that the taxpayer acted reasonably and in good faith, and that the grant of relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1) provides in part that except as provided in paragraphs (b)(3)(i) through (b)(3)(iii), a taxpayer is deemed to have acted reasonably and in good faith if

(A) 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 or (B) the taxpayer reasonably relied on a qualified tax professional and the tax professional failed to make, or to advise the taxpayer to make, the election.

Section 301.9100-3(b)(3) provides in part 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 section 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. The Internal Revenue Service will ordinarily not grant relief because of the use of hindsight if specific facts have changed since the due date for making the election that make the election advantageous to the taxpayer. 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)(i) provides in part that the interests of the Government are prejudiced if granting relief would result in the 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).

Taxpayers have shown that they acted reasonably and in good faith. No specific facts have changed since the due date for making the section 266 election for Year 1 that make the election advantageous to Taxpayers, despite the fact that Lot B was sold after the due date for making the election. Because property taxes are not deductible for purposes of computing alternative minimum taxable income, the property taxes are not added to Taxpayers' Lot B alternative minimum tax basis if a section 266 election is made. *See* section 56(b)(1)(A)(ii) & section 1.266-1(b)(2). Accordingly, the amount of Taxpayers' capital gain that they must recognize in computing alternative minimum taxable income arising from the sale of Lot B is not affected by Taxpayers' election to capitalize property taxes in lieu of claiming those taxes as deductions for Year 1. Furthermore, the Taxpayers have shown that the interests of the Government are not prejudiced by granting the requested relief for an extension of time under section 301.9100-1(c) for Year 1.

RULING

Based solely on the facts and representations submitted, consent is hereby granted to Taxpayers for Year 1 to comply with the requirements of section 266 for making an annual election to capitalize property taxes on unimproved and unproductive real property. Accordingly, Taxpayers are granted an extension of time until 90 days from the date of this private letter ruling to make the election to capitalize taxes under section

266 for Year 1 for Lot A and Lot B. The election shall be made in accordance with the regulations under section 266 and shall be filed with the appropriate office of the Service having jurisdiction over the Taxpayers' federal income tax return for Year 1. Please attach a copy of this private letter ruling to the amended return, schedules, and forms filed in connection with making the election under section 266 when such documents are filed.

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 private letter ruling. The ruling contained in this letter ruling is based upon facts and representations submitted by Taxpayers with accompanying penalty of perjury statements executed by appropriate parties. While this office has not verified any of the material submitted in support of this request for an extension of time to make the section 266 election, all material is subject to verification on examination.

This private letter ruling is directed only to Taxpayers. 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 private letter ruling is being sent to Taxpayers' authorized representative.

Sincerely,

Cheryl L. Oseekey
Senior Counsel, Branch 6
Office of Associate Chief Counsel
(Income Tax & Accounting