

**Internal Revenue Service**

Department of the Treasury

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Washington, DC 20224

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Date:  
December 5, 2001

**LEGEND**

- Taxpayer =
- Year 1 =
- Year 2 =
- Month 1 =
- Month 2 =
- Date 1 =
- Broker =
- Dollar 1 =
- Date 2 =
- Date 3 =
- Accountant A =
- Date 4 =
- Date 5 =
- Doctor =
- Accountant B =
- Date 6 =
- Date 7 =

Dear:

This is in reply to a letter dated October 27, 2000, and subsequent correspondence, submitted on your behalf by authorized representatives, requesting an extension of time under section 301.9100 of the Procedure and Administration Regulations to make an election under section 475(f) of the Internal Revenue Code to use the mark-to-market method of accounting for the Year 2 tax year.

**FACTS**

Taxpayer is an individual who uses the calendar year as his taxable year and uses the cash method of accounting. Taxpayer represents that he is engaged in the trade or business of trading securities.

In the fall of Year 1, Taxpayer decided to wind down his law practice after a legal career of many years and begin a new career as a securities trader. During Year 1, Taxpayer's law practice was his full-time occupation. He spent Month 1 of Year 1 and Month 2 of Year 2 on settlement-related work for a class action settlement. The bulk of

this work was completed by late Month 2 of Year 2, at which point Taxpayer turned his entire attention to securities trading. Taxpayer continued to trade regularly until Date 1 when Broker forced the liquidation of his entire account. Between the first of Month 2 of Year 2 and Date 1, Taxpayer had net trading losses of almost Dollar 1. Taxpayer did not buy or sell any securities between Date 1 and Date 2.

Accountant A prepared Taxpayer's Form 4868, Application for Automatic Extension of Time To File U.S. Individual Income Tax Return, and brought it to Taxpayer for signature on Date 3. At that time, Accountant A was not aware that the section 475(f) election was available to Taxpayer. Accountant A was aware that Taxpayer had sustained losses by the due date of Taxpayer's Year 1 tax return. The Form 4868 was filed on Date 4. Subsequently, on Date 5, Taxpayer learned of the availability of the section 475(f) election from Doctor, his friend and internist.

After his conversation with Doctor, Taxpayer immediately contacted Accountant B. Accountant B confirmed the availability of the section 475(f) election but informed Taxpayer that the election should have been filed by Date 4. Accountant B also informed Taxpayer that based on Accountant B's knowledge of the facts and review of the relevant regulations, relief should be available under section 301.9100-3. On Date 6, Accountant B further advised Taxpayer that he should not resume his trading activities until his application for section 301.9100 relief and his section 475(f) election were submitted to the Internal Revenue Service.

On Date 2, Taxpayer filed an original Form 3115 and a faxed copy of a section 475(f) election to the Service. He also attached a presubmission letter regarding a proposed request for a private letter ruling granting relief under section 301.9100-3. Taxpayer resumed his trading activities on Date 7.

## **LAW AND ANALYSIS**

Section 475(f) provides that a taxpayer engaged in a trade or business as a trader in securities may elect to apply the mark-to-market accounting method to securities held in connection with such trade or business. See section 475(f)(1). Section 7805(d) provides that, except to the extent otherwise provided by the Code, any election shall be made at such time and in such manner as the Secretary shall prescribe.

On February 16, 1999, the Internal Revenue Service published Rev. Proc. 99-17, 1999-1 C.B. 503, section 6 *superseded by* Rev. Proc. 99-49, 1999-2 C.B. 725. Rev. Proc. 99-17 provides the exclusive procedure for traders in securities to make an election to use the mark-to-market method of accounting under section 475(f). Section 5.03(1) of Rev. Proc. 99-17 provides, in relevant part, that taxpayers (other than a taxpayer for which no federal income tax return was required to be filed for the taxable year immediately preceding the election year) make an election under section 475(f) for a tax year beginning on or after January 1, 1999, by filing a statement no later than the due date (without regard to extensions) of the original federal income tax return for the

taxable year immediately preceding the election year. The statement must be attached to either that return or to a request for an extension of time to file that return. Section 5.03 of Rev. Proc. 99-17. The statement must describe the election being made, the first taxable year for which the election is effective, and the trade or business for which the election is made. Section 5.04 of Rev. Proc. 99-17.

Section 4 of Rev. Proc. 99-17 states that the election under section 475(f) determines the method of accounting an electing trader is required to use for federal income tax purposes for securities subject to the election. A method of accounting for securities subject to the election is impermissible unless the method is in accordance with section 475 and the regulations thereunder. If an electing trader's method of accounting for its taxable year immediately preceding the election year is inconsistent with section 475, the taxpayer is required to change its method of accounting to comply with its election. Thus, a taxpayer that makes a section 475(f) election but fails to change its method of accounting to comply with that election is using an impermissible method.

Section 6.03 of Rev. Proc. 99-17 provides that a taxpayer that changes its method of accounting pursuant to Rev. Proc. 99-17 must take into account the net amount of the section 481(a) adjustment. The section 481(a) adjustment generally is taken into account ratably over four taxable years beginning with the year of change. Section 6.03 of Rev. Proc. 99-17 and section 5 of Rev. Proc. 99-49.

Section 301.9100-1(c) of the regulations provides, in part, that the Commissioner has discretion to grant a reasonable extension of time to make a regulatory election (defined in section 301.9100-1(b) as an election whose due date is prescribed by regulations published in the Federal Register, or by a revenue ruling, revenue procedure, notice, or announcement published in the Internal Revenue Bulletin), or a statutory election (but no more than 6 months except in the case of a taxpayer who is abroad), under all subtitles of the Internal Revenue Code except subtitles E, G, H, and I.

Sections 301.9100-3(a) through (c)(1)(i) set forth rules that the Internal Revenue Service generally will use to determine whether, under the facts and circumstances of each situation, the Commissioner will grant an extension of time for regulatory elections that do not meet the requirements of section 301.9100-2. Section 301.9100-3(b) provides that subject to paragraphs (b)(3)(i) through (iii) of section 301.9100-3, when a taxpayer applies for relief under this section before the failure to make the regulatory election is discovered by the Service, the taxpayer will be deemed to have acted reasonably and in good faith; and section 301.9100-3(c) provides 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 years to which the regulatory election applies 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(b)(3) provides, in part, that a taxpayer is deemed to have not acted reasonably and in good faith if the taxpayer uses hindsight in requesting relief. If specific facts have changed since the due date for making the election that make the election advantageous to the 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)(2) provides special rules for accounting method regulatory elections. This section provides, in relevant part, that the interests of the Government are deemed to be prejudiced by granting an extension of time, except in unusual and compelling circumstances, if the accounting method regulatory election is subject to the procedure described in section 1.446-1(e)(3)(i) (requiring the advance written consent of the Commissioner) or if the accounting method regulatory election for which relief is requested requires an adjustment under section 481(a) (or would require an adjustment under section 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).

As noted above, section 4 of Rev. Proc. 99-17 states that the election under section 475(f) determines the method of accounting an electing trader is required to use for federal income tax purposes for securities subject to the election. If an electing trader's method of accounting for its taxable year immediately preceding the election year is inconsistent with section 475, the taxpayer is required to change its method of accounting to comply with its election. A taxpayer that makes a section 475(f) election but fails to change its method of accounting to comply with that election is using an impermissible method. Because the election is integrally related to the change in accounting method to mark-to-market, it is an accounting method regulatory election subject to section 301.9100-3(c)(2).

Rev. Proc. 99-49 provides procedures by which a taxpayer may obtain automatic consent to change to the mark-to-market accounting method. However, the automatic change applies to a taxpayer only if the taxpayer has made a valid election under section 475(f) and is required to change its method of accounting to comply with the election. Section 10A.02(2)(a)(i) of the Appendix to Rev. Proc. 99-49.

Taxpayer requests an extension of time to make an accounting method regulatory election that is subject to the provisions of section 301.9100-3(c)(2). Because Taxpayer failed to make a timely section 475(f) election pursuant to Rev. Proc. 99-17, the accounting method regulatory election is subject to section 301.9100-3(c)(2)(i). Further, because the accounting method regulatory election requires a section 481(a) adjustment, it is also subject to section 301.9100-3(c)(2)(ii). Therefore, under section 301.9100-3(c)(2), absent unusual and compelling circumstances, a grant of relief is deemed to prejudice the interests of the Government.

Based on the facts and representations submitted, we conclude that Taxpayer has not satisfied the requirements for our granting a reasonable extension of time to

make an election under section 475(f) to use the mark-to-market method of accounting. Taxpayer has failed to demonstrate unusual and compelling circumstances regarding his failure to make a timely election sufficient to overcome the presumption of prejudice to the Government's interests.

## **CONCLUSION**

Taxpayer's request for an extension of time to make the section 475(f) election for Year 2 is denied. Because Taxpayer's request for relief is denied pursuant to section 301.9100-3(c)(2) for lack of unusual and compelling circumstances, it is unnecessary for us to consider Taxpayer's assertion that he acted reasonably and in good faith under section 301.9100-3(b), without using hindsight in requesting relief. Taxpayer may not change his method of accounting without making a timely section 475(f) election; therefore, Taxpayer may not report income using the mark-to-market method of accounting on his Year 2 tax return.

No opinion is expressed as to the tax treatment of the transaction under the provisions of any other sections of the Code and regulations, which may be applicable thereto, or the tax treatment of any conditions existing at the time of or effects resulting from the transaction, which are not specifically set forth by the above ruling.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code 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 Taxpayer's authorized representative.

Sincerely yours,  
ALVIN J. KRAFT  
Chief, Branch 1  
Office of Associate Chief Counsel  
(Financial Institutions & Products)

Enclosures:

Copy of this letter  
Section 6110 Copy