

Internal Revenue Service

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LEGEND

Taxpayers =
State 1 =
State 2 =
Year 1 =
Year 2 =
Year 3 =
Year 4 =

Dear :

This ruling is in reply to your request for extensions of time under section 301.9100-1(c) of the Procedure and Administration Regulations and Rev. Proc. 2006-1, 2006-1 I.R.B. 1 (Jan. 3, 2006), to elect to capitalize certain property taxes paid on unimproved, unproductive real property in lieu of claiming those expenditures as deductions on your federal income tax returns for the taxable years in question. Your request is made in accordance with section 301.9100-3.

FACTS

The Taxpayers are married individuals who filed joint federal income tax returns for taxable Year 1 through Year 2. The Taxpayers represent that throughout the taxable years in question they owned and held for investment purposes certain parcels of unimproved real property in State 1 and State 2. The Taxpayers paid property taxes on their investment properties each year and they did not elect under section 266 of the Internal Revenue Code to capitalize these taxes to the appropriate property. Accordingly, the taxes paid each year by the Taxpayers would ordinarily be deductible by them on that year's federal income tax return. However, for taxable Year 1 through Year 2, the Taxpayers were subject to the alternative minimum tax. Because property taxes are a tax preference item for purposes of the alternative minimum tax, the Taxpayers were not able to obtain the tax benefit they would have if they had been able

to deduct the property taxes on their federal income tax returns for taxable Year 1 through Year 2.

The Taxpayers' tax adviser was generally knowledgeable 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 unproductive and unimproved real property. At a professional conference early in Year 3, he learned about the interplay between section 266 and the alternative minimum tax. Once he understood that taxpayers subject to the alternative minimum tax could obtain tax benefits by capitalizing property taxes, the tax adviser promptly informed the Taxpayers, and the Taxpayers made a section 266 election with their timely filed Year 4 federal income tax return. The Taxpayers' tax adviser also informed them in Year 3 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 section 266 elections for taxable Year 1 through Year 2. Soon thereafter, the Taxpayers filed this request for a private letter ruling. The Taxpayers sold the property in question in Year 4. The tax adviser represents also that the Taxpayers relied on him to provide tax advice.

LAW AND ANALYSIS

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(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 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).

Section 301.9100-3(c)(1)(ii) provides in part that the interests of the Government ordinarily are 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.

The Taxpayers have shown that they acted reasonably and in good faith. Further, 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).

RULING

Consent is hereby granted to the Taxpayers, for taxable Year 1 through Year 2, to comply with the requirements of section 266 for making annual elections to capitalize property taxes on unimproved real properties that had been held for investment. Accordingly, the Taxpayers are granted an extension of time until 30 days from the date of this private letter ruling to make the election to capitalize taxes under section 266 for taxable Year 1 through Year 2 regarding the property in question. The elections shall be made in accordance with the regulations under section 266 and shall be filed with the Director's office having jurisdiction over the Taxpayers' federal income tax returns. Please attach a copy of this private letter ruling to the amended returns, schedules, and forms filed in connection with making the elections 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

This private letter ruling is directed only to the 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 each of the Taxpayers' authorized representatives.

Sincerely,

Jeffery G. Mitchell
Branch Chief, Branch 6
(Income Tax & Accounting)