LATE ELECTIONS AND SECTION 9100 – DON’T CALL YOUR MALPRACTICE CARRIERS YET

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CHAPTER 4
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BACKGROUND, EDUCATION AND PRACTICE

Since 1997, Dan has practiced law in Dallas representing small and emerging closely-held businesses in business, federal and state tax planning and federal tax controversies. He also represents business owners and professionals in estate and asset preservation planning. He serves as an Adjunct Professor of Law at SMU’s Dedman School of Law teaching “Counseling the Small Business Owner,” a hands-on business and tax planning and drafting course for upper level J.D. and graduate law students.

Dan began the practice of law in Dallas in 1979. In 1988 he was appointed Special Assistant to the Assistant (now Associate) Chief Counsel (Passthroughs and Special Industries) of the Internal Revenue Service in Washington, D.C. Dan then served as Assistant General Counsel of the Central Intelligence Agency before entering private practice in Washington in 1991. From 1993 through 1997 Dan served as Director of IRS Practice at Coopers & Lybrand’s National Tax Office in Washington, D.C. and served as an Adjunct Professor of Law at Georgetown University Law Center in their Graduate Tax Law Program where he taught “IRS Practice and Procedure.” He coauthored “Limited Liability Companies,” published by BNA TAX MANAGEMENT, Portfolio No. 725-1, and has written numerous articles for professional journals.

Dan earned his B.B.A. and J.D. at Southern Methodist University, where he was an editor of the Southwestern Law Journal (Law Review), graduating from law school in 1979. He received his LL.M. in Taxation at New York University School of Law in 1984.

Dan is a member of the State Bar of Texas, where he is a member of the Sections of Taxation. Dan serves as a member of the Council of the Section of Taxation. From 2003 until 2005 he served as Chair of the State Bar Tax Section’s Continuing Legal Education Committee and as Course Director for the “2005 Advanced Tax Law Course” and the “2004 Advanced Tax Law Course.” He also served as Course Director for the inaugural running of “Representing Small Businesses Course” in December, 2004, sponsored by Texas Bar CLE Programs. He is also a member of the American Bar Association and the Dallas Bar Association. He speaks widely on a variety of business and tax law topics.
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By: Daniel G. Baucum


A. Section 9100 of the Internal Revenue Code doesn’t exist. So don’t bother looking for it. Nevertheless, Sections 301.9100-1 through 301.9100-3 of the Treasury Regulations are important tools for every tax practitioner if they either advise clients to make tax elections regarding federal tax returns or advise other professionals that advise clients to make tax elections regarding federal tax returns filed with the Internal Revenue Service (“Service”). In many circumstances, these Regulations provide taxpayers with a second chance to make an election that was missed—and may allow practitioners to avoid possible claims of malpractice for failing to make an effective tax election.

B. Most of the second chances are provided for regulatory elections—that is 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. But in rare instances (apparently) a second chance is provided for a missed statutory election—that is an election whose due date is prescribed by statute (in this case the statute is the Internal Revenue Code (“Code”)).1 This regulatory opportunity to redeem oneself is available to any Taxpayer, which means any person within the meaning of section 7701(a)(1) of the Code. In other words, corporations, partners in partnerships, estates, and trusts, etc.

C. Treasury Regulation section 301.9100-2 provides for automatic 12-month and 6-month extensions in certain well defined instances provided in section 301.9100-2. Section 301.9100-3 provides guidance for making non-automatic requests for relief and the standards that will be applied in such cases. These final Regulations are effective on or after December 31, 1997.2

D. Although the three factors set forth below are taken from the two prior iterations of Regulation section 301.9100-1, which were amended in 1993 and 1997, respectively, make note of the themes in each factor and you will likely recognize that these themes run throughout the current set of three regulations that constitute Treasury Regulations sections 301.9100-1, -2, and -3. Therefore, as a backdrop to the current regulations these factors should be kept in mind as you determine whether and how to apply the current -2 and -3 regulations in your case. (I can assure you that the senior professionals at IRS Chief Counsel’s Office in Washington, D.C., reviewing your case will remember this history and likely view the current regulations as refinements of those that went before—especially if your request for relief constitutes a request under the -3 regulations.

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1 As of the time of this writing I am still unaware of any relief granted by the Service for a missed statutory election. (But I have some time before the conference and perhaps I will discover examples have been there in front of me all the time. When I worked at the Chief Counsel’s Office too many years ago to consider, only regulatory elections were considered within the Service’s discretion to grant relief. See I.C.(i) and Author’s Comment, in this paper, infra.) Once I better understand this relatively new power, I may be able to identify applicable instances. I would point out, however, that the regulations are of little help. The regulations simply define in the -1 regulation the term “statutory election,” but the -2 regulation does not provide an example of its use. See, e.g., Treas. Reg. § 301.9100-2(e), Ex. 2.

2 Before these Regulations were promulgated, the Service granted relief for missed regulatory elections under rules similar to what has now essentially become Treasury Regulation 301.9100-3. These regulations, which were all denominated -1 regulations, were amended in 1991, 1993 and 1997. In order to reduce the burden of examining each request for relief (as required under the predecessor to the -3 regulations) the Service began to issue Revenue Procedures granting automatic relief in certain instances. From these revenue procedures evolved Treasury Regulation 301.9100-2, granting automatic 12-month and 6-month relief.
Under the prior regulations in general relief will be granted—either automatically or through the non-automatic process—provided that, at a minimum, the following three guidelines are met:

i. The time for making the election is not expressly prescribed by the Internal Revenue Code (“Code”). If a Code section specifically identifies a time for making the election, the Service takes the position that it does not have discretion to extend the time. For example, if an election is to be made no later than the due date of the return, than administrative relief is not available.

ii. The extension request is filed with the Service before the time fixed for making the election, or within any additional time that the Service considers reasonable (Author’s Note: Relief is in the Service’s discretion and is not a right but there is at least one instance where the Tax Court has reversed the Service’s decision not to grant relief); and

iii. The granting of the extension will not jeopardize the interests of the government.

Author’s Comment: Pay particular attention to the second sentence in subparagraph (i) above. This sentence is the basis underlying the Service’s mindset regarding their ability to grant regulatory relief only in certain circumstances and the fact that until the 1997 regulations, statutory relief was considered beyond the Service’s power to grant. Because Congress writes the laws and the Service merely interprets them, a statutorily provided deadline was (and maybe still is) inviolable.

II. Treasury Regulation 301.9100-2: Automatic Extensions.

A. Automatic 12-month extension. An automatic extension of 12 months from the due date for making a regulatory election is granted to taxpayers to make elections described in (a)(2) of the -2 regulations (or subsequent revenue procedures) provided the taxpayer takes corrective action as defined in section 301.9100-2(c).

i. The due date for making a regulatory election is the extended due date of the return if the due date of the election is the due date of the return or the due date of the return including extensions that the taxpayer has obtained. (This extension is available regardless of whether the taxpayer timely filed its return for the year the election should have been made).

ii. Section 301.9100-2(a)(2) contains a “laundry list” of regulatory elections eligible for the 12-month extension. The list includes taxable year elections under section 444; LIFO inventory election; exemption applications under the exempt organization rules, including a section 501(c)(3) election under section 508 and a homeowners association under section 528; partnership basis adjustments under section 754; Special Estate Tax valuation rules under section 2032A(d)(1); and qualified payment elections under chapter 14 of the Code.

B. Automatic 6-month extension. An automatic extension of 6 months from the due date of a return excluding extensions is granted to make regulatory and statutory elections with due dates of the return (with or without extensions) if the taxpayer timely filed its return for the year the election should have been made and the taxpayer takes corrective actions within that 6-month extension period. THIS REGULATORY RELIEF DOES NOT APPLY TO REGULATORY OR STATUTORY ELECTIONS THAT MUST BE MADE BY THE DUE DATE OF THE RETURN EXCLUDING EXTENSIONS.

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3 See Vines 91 CCH TCM 4283 and fn. 4, infra.
C. “Corrective action means taking the steps required to file the election in accordance with the statute or the regulation published in the Federal Register, or the revenue ruling, revenue procedure, notice, or announcement published in the Internal Revenue Bulletin... For those elections required to be filed with a return, corrective action includes filing an original or an amended return for the year the regulatory or statutory election should have been made and attaching the appropriate form or statement for making the election. Taxpayers who make an election under an automatic extension (and all taxpayers whose tax liability would be affected by the election) must file their return in a manner that is consistent with the election and comply with all other requirements for making the election for the year the election should have been made and for all affected years; otherwise, the IRS may invalidate the election.” Treas. Reg. 301.9100-2(c).

D. Certain procedural requirements must be met for the automatic extensions to apply.
   i. Each return, statement of election or other filing should be marked at the top of the document as: “FILED PURSUANT TO 301.9100-2”.
   ii. The filing should be sent to the same address that the filing to make the election would have been sent had the filing been timely made.
   iii. Since this is not a letter ruling request (it is a request for an automatic extension) no user fees apply. (Compare with -3, below).

III. Treasury Regulation 301.9100-3: Non-automatic Extensions to Make Elections.
A. An election whose deadline is prescribed by regulation or other administrative pronouncement and is not included in the -2 regulations automatic extension lists and thus does not meet the requirements for granting an automatic extension becomes subject to the general ruling request procedures and 301.9100-3 of these regulations. (Author’s Comment: Notice that statutory elections are not included herein).
   i. In other words, request for relief under the -3 Regulation is a letter ruling request under the Rev. Proc. 2007-1 (or the -1 Revenue Procedure for the year in question) and must be submitted in accordance with the applicable procedures for requests for letter rulings and must be accompanied by the applicable user fee.
   ii. Evidence must be submitted that proves that the taxpayer acted reasonably and in good faith and that the interests of the government are not prejudiced.
      1. Inadvertent failures.
      2. Catastrophic illness.
      3. Extenuating circumstances suffered by an advisor.
      4. Clerical errors made by an advisor.
      5. Errors made despite reasonable diligence.
   iii. An affidavit and declaration of the taxpayer must be submitted with the ruling request affirming under penalties of perjury that the affidavit and accompanying documents contain all of the relevant facts relating to the request and that such facts are true, correct, and complete to the best of the signatory’s knowledge and belief.
      1. The taxpayer, or the person who acts on behalf of the taxpayer with respect to tax matters, must submit a detailed affidavit describing the events that led to the failure to make the regulatory election and to the discovery of its failure. When the taxpayer relied upon a qualified tax professional for advice, the taxpayer’s affidavit must describe the engagement and responsibilities of the professional as well as the extent to which the taxpayer relied upon the professional.
2. The individual who signs for an entity must have personal knowledge of the facts and circumstances at issue.

3. Detailed affidavits must also be submitted by individuals having knowledge and information about the events that led up to the failure to make the regulatory election and the discovery of the failure. Affidavits should be submitted from the taxpayer’s return preparer, anyone who made a substantial contribution to the preparation of the return, and any accountant or attorney, knowledgeable in tax matters, who advised the taxpayer with regard to the election. These affidavits shall also describe the engagement and responsibilities of the taxpayers and also be submitted under penalties of perjury and that the letter ruling submission and accompanying documents is true, correct and complete.

4. The ruling request should include a statement regarding whether the affected return or returns are under audit, at appeals or in a federal court proceeding. Notification should also be given immediately if the Service begins an examination while the return is pending.

5. If the return, form or statement used to make the election was filed the date it should have been filed and the date actually filed should be included in the submission. This document, along with any other document referring to the election should be included as an attachment to the ruling request.

6. If the Service requests the taxpayer must submit a copy of the taxpayer’s return, or any affected parties return, for any taxable year for which the taxpayer requests an extension and any return affected thereby. This may be included with the initial letter ruling request demonstrating an effort toward full disclosure.

iv. **Helpful Hint.** Read the information regarding pre-submission conferences in the Private Letter Ruling Revenue Procedure (e.g., Rev. Proc. 2007-1) and schedule one (at least by telephone). Typically in the process of developing your case you will have identified which group at the IRS Chief Counsel’s Office in Washington, D.C. to which the letter ruling request will be submitted. Pick up the phone, call the front office of that group (e.g., corporations, passthroughs and special industries, income tax and accounting, or financial institutions & products) and identify the branch (or branches) to which the letter ruling will likely be submitted. Then I strongly suggest you schedule a pre-submission conference regarding your case; probably by telephone with a two to three page summary of facts and taxpayer information. (Don’t be silly and try to hide the identity or other pertinent information of the taxpayer.) Lay it on the line. Otherwise you will do two things wrong: (i.) You will lose the trust and confidence in your submission of the branch chief, senior technical reviewer, and attorney-advisor working with you, who will be your advocates if this is other than just a garden variety situation (and those easy cases are probably automatic under 301.9100-2 (above) so we shouldn’t be talking about them under -3); and (ii) this relief is discretionary; the IRS doesn’t have to give it to you. They can determine that relief is not in the best interest of the government and you have no recourse. To their credit, the individuals with whom you will work are true professionals and you will receive a fair and impartial hearing. If you meet the criteria for relief; you will receive it. So be totally up-front, forthcoming and above-all honest and professional with the public servants you have the privilege of working with, and you will receive the outcome that your case merits.

1. If you have a weak case, you want to know it up front. Remember, the senior individuals you work with have likely seen cases similar to yours several (if
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not dozens) of times before. They may be able to suggest facts or evidence that would be persuasive to them to overcome a weakness in your case.

2. If your case is a looser, it’s better to know it now, before you spend thousands of dollars on filing fees, private letter ruling preparation, travel and meeting costs, etc. I believe it is best to cut your losses and utilize your resources to fix the problem as best one can, if relief is likely not forthcoming.

“Requests for relief subject to this section will be granted when the taxpayer provides the evidence (including affidavits described [below] . . .) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interest of the Government.” Treas. Reg. § 301.9100-3(a). (Author’s Note: This should sound familiar if you have been paying attention.)

B. Reasonable Action and Good Faith. A taxpayer will normally be treated as having acted reasonably and in good faith if the taxpayer—
(i) requests relief before it 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 after exercising reasonable diligence because 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, but only if the taxpayer knew or should have known that the professional was not competent to render advice on the regulatory election or aware of all relevant facts. (Author’s Comment: This is otherwise known as the tax professional falling on his or her own sword to save the taxpayer. This is by far the most common “reasonable good faith” action asserted by taxpayers. Needless to say, it is also the most troublesome for tax professionals since, if it doesn’t result in relief being granted, the tax professional’s affidavit supporting this claim makes a malpractice case against the professional virtually “open and shut.” Needless to say, these situations should be handled by someone with experience as to the way the system works.) See Treas. Reg. § 301.9100-3(f), Ex. (2) (election omission discovered during audit shows that failure to satisfy one of the above good faith acts is not fatal).

There are instances, however, where the taxpayer will be deemed not to have acted in good faith, and thus such actions are typically fatal to the taxpayer’s cause. For example, if the taxpayer chooses not to make an election after being fully informed of the consequences the taxpayer will fail the good faith test. Or if the taxpayer is seeking to make a retroactive election during an audit in order to avoid the imposition of an accuracy related penalty. In such case the taxpayer will be denied relief because he will be determined not to have acted in good faith. See Treas. Reg. § 301.9100-3(f), Ex. (3). Finally, a taxpayer normally will not be deemed to have acted in good faith if, through the use of hindsight, the taxpayer seeks to take advantage of a change in facts that have occurred since the election due date that make an election advantageous. This is a strong—but rebuttable—presumption. If the taxpayer provides strong proof that taxpayer’s actions did not involve the use of hindsight, the presumption can be rebutted. Note that the regulations do not provide an example of this situation. Author’s Comment: I guess this is like Justice White’s definition of pornography, “I know it when I see it.” But in this case, at least, I haven’t ever seen strong enough proof to carry the taxpayer’s burden. But that doesn’t mean it doesn’t exist.

C. Prejudice to the Interests of the Government. If the government’s interests are prejudiced, normally the Commissioner will not grant a reasonable extension to make an election.
1. **Lower Tax Liability.** If lower tax liability results to a taxpayer in the aggregate for all taxable years affected by the failure to make the election (taking into account the time value of money) then the interests of the government are prejudiced and the relief request will be denied. Similarly, if the tax consequences of more than one taxpayer are at issue, the government’s interests will be prejudiced if in the aggregate the tax liability for the group is lowered.

2. **Closed Years.** If the statute of limitations has closed for one or more taxable years of the taxpayer affected by granting permission to make a late election, then the government’s interests are ordinarily prejudiced.

D. **Special Rules Relating to Accounting Method and Period Regulatory Elections.** Practitioners should know that special rules raising the burden of proving that the government is not prejudiced by an accounting method or accounting period regulatory election are provided, along with three out of the six examples provided by the Regulations in subparagraph (f). See Treas. Reg. § 301.9100-3(f), Ex. (3) through (6).

IV. **Conclusion.**

By far the most common of these requests for relief involve the failure of tax professionals to file required elections timely. This is seen in entity classification elections in conversions, limited liability company formations, and S corporation elections late filings, such as the election for a wholly owned corporation to be treated as a qualified subchapter S subsidiary (QSub election), to name a few. Needless to say, coordination among the tax planning and preparation team is essential so that failure to timely file an appropriate form doesn’t result in the tax practitioner “falling on one’s sword” in this forum in an attempt to avoid a malpractice claim. This is truly a place where “an ounce of prevention is worth a pound of cure.” But if a practitioner you know one day finds himself or herself in this predicament, all is not lost. The Service is professional and will grant the relief sought if the taxpayer qualifies.

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4 For further reading on this topic, it’s history and it’s relevance today, see, e.g., “S Election Relief Procedures Revamped,” J. of Tax. (Dec. 1988); “IRS Freely Grants Extensions for QTIP Elections,” J. of Tax. (Feb. 1999); “No Extension of Time to Make Election to Exclude Income from Cancellation of QRPBI,” J. of Tax. (Jan. 2006); Schechter & Pampel, “How to Lose $25 Million in Three Months and Still Get 9100 Relief,” J. of Tax (Sept. 2006)(Examining a case of first impression for the Tax Court in which they reversed the Service’s decision not to grant regulatory relief for a late election in Vines, 91 CCH TCM 4283.)