

OVERVIEW:

IRS Letter Ruling Permits Taxpayer to Revoke Inadvertent Opt-Out from Installment Method in a Failed Exchange

PLR 200813019, issued on December 17, 2007, and released on March 28, 2008, dealt with the following fact pattern: Taxpayer, a limited liability company taxed as a partnership, sold relinquished property in a forward exchange in Year 1. It was unable to acquire replacement property within the 180-day exchange period, and the exchange failed in Year 2. This failed exchange qualified as an installment sale because Taxpayer did not have actual or constructive receipt of (at least some portion of) the sales proceeds in the year that the property was sold. However, taxpayer's accountant failed to recognize that the transaction qualified as an installment sale, and he reported the gain from the sale of the property on taxpayer's Year 1 tax return. Declaring the income on Taxpayer's Year 1 tax return amounted to an option to ***opt out*** of the installment method that otherwise would have permitted Taxpayer to defer payment of taxes on the proceeds from this transaction until Year 2.

Treas. Reg. 15.453-1(d)(4) provides, generally, that an election to opt out of installment sale treatment is *irrevocable*, and that: "An election may be revoked only with the consent of the Internal Revenue Service."

When Taxpayer learned of the accountant's error, it applied to the IRS for consent to revoke its opt-out election. The IRS was satisfied that the election to pay the taxes in Year 1 was inadvertent and the result of the accountant's *oversight*, rather than *hindsight* by Taxpayer. Therefore Taxpayer was permitted to revoke its election out of the installment method.

Private Letter Ruling 200813019

SUBJECT MATTER: Section 453 -- Installment Method

TEXT:

Release Date: 3/28/2008

Date: December 17, 2007

Refer Reply To: CC:ITA:B04 - PLR-131288-07

LEGEND:

Taxpayer = * * * *

Year 1 = * * * *

Date 1 = * * * *

Year 2 = * * * *

Dear * * * *:

This is in reply to your letter submitted on behalf of Taxpayer requesting consent to revoke an election out of the installment method pursuant to § 453(d)(3) of the *Internal Revenue Code* and § 15A.453-1(d)(4) of the Temporary Income Tax Regulations.

FACTS

Taxpayer is a calendar year, cash basis, limited liability company that has three members, one who owns a 50 percent interest and two others who each own a 25 percent interest. Taxpayer is engaged in the business of real estate rentals, owned a single rental property, and is treated as a partnership for federal income tax purposes.

During Year 1, Taxpayer intended to enter into a deferred like-kind exchange of its rental property under § 1031. Taxpayer entered into an exchange agreement with a professional exchange company (QI), which intended to facilitate the exchange in compliance with the regulations under § 1031. On Date 1, pursuant to the exchange [*2] agreement,

the QI sold taxpayer's rental property. The cash proceeds from the sale were retained by the QI pending Taxpayer's identification and acquisition of replacement property.

During the ensuing 180-day period, Taxpayer was unable to locate suitable replacement property. In Year 2, the QI gave the cash proceeds from the sale of the rental property to Taxpayer.

In Year 2, Taxpayer's accountant completed Taxpayer's Year 1 partnership return. The accountant, however, failed to recognize that the Year 1 sale of rental property qualified for the installment method under § 453 and reported all gain from the sale on the Year 1 partnership return. Taxpayer relied on the accountant to prepare the Year 1 return properly and to advise Taxpayer regarding all necessary tax filings, including any provision that might benefit Taxpayer. The accountant was fully aware that the intended § 1031 exchange had failed due to unavailability of suitable replacement property. Furthermore, the accountant provided an affidavit indicating that the accountant's oversight was the reason the installment method was not used.

Subsequently, other professionals advised Taxpayer that the installment method should have [*3] been used in Year 1. Taxpayer immediately took action to request consent from the Service to revoke its election not to use the installment method.

LAW AND ANALYSIS

Section 453(a) provides that, generally, a taxpayer shall report income from an installment sale under the installment method. *Section 453(b)* defines an installment sale as a disposition of property for which at least one payment is to be received after the close of the taxable year of the disposition.

Section 15A.453-1(b)(3)(i) defines "payment" to include amounts actually or constructively received in the taxable year under an installment obligation.

Section 453(d)(1) and section 15A.453-1(d)(1) provide that a taxpayer may elect out of the installment method in the manner prescribed by the regulations. Section 15A.453-1(d)(3) provides that a taxpayer who reports an amount realized equal to the selling price including the full face amount of an installment obligation on a timely filed tax return for the taxable year in which the installment sale occurs is considered to have elected out of the installment method.

Except as otherwise provided in the regulations, section 453(d)(2) requires a taxpayer who desires to elect out of [*4] the installment method to do so on or before the due date (including extensions) of the taxpayer's federal income tax return for the taxable year of the sale. Section 15A.453-1(d)(4) provides that an election under *section 453(d)(1)* is generally irrevocable. An election may be revoked only with the consent of the Internal Revenue Service. Section 15A.453-1(d)(4) provides that revocation of an election out of the installment method is retroactive and will not be permitted when one of its purposes is the avoidance of federal income taxes.

In the instant case, Taxpayer provided the accountant with all the necessary information for purposes of preparing the Year 1 partnership return, including information regarding the sale of the rental property. The accountant failed to recognize that the Year 1 sale qualified for installment method treatment. As soon as Taxpayer became aware of this oversight, Taxpayer filed a request for consent to revoke the election out of the installment method. The information submitted indicates that Taxpayer's desire to revoke the election is due to Taxpayer's accountant's [*5] oversight rather than hindsight by Taxpayer or a purpose of avoiding federal income taxes.

CONCLUSION

Based on careful consideration of all of the information submitted and the representations made, we conclude that Taxpayer will be allowed to revoke its election out of the installment method with respect to the Year 1 sale of rental property.

Permission to revoke the election out of the installment method for the Year 1 sale of rental property is granted for the period that ends 75 days after the date of this letter. In order to revoke its election out of the installment method, Taxpayer must file an amended federal income tax return for Year 1 and any other previously filed returns on which a portion of the gain from the sale is reportable under the installment method. A copy of this letter ruling must be attached to each of the amended returns.

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 letter, including the computation of gain to be reported under the installment method.

This ruling is directed only to the taxpayer who requested it. *Section 6110(k)(3) of the Code* [*6] 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 your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This ruling is conditioned upon the accuracy of that information and those representations. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

Sincerely,

Michael J. Montemurro
Branch Chief, Branch 4
(Income Tax & Accounting)