

Part III

Administrative, Procedural, and Miscellaneous

26 CFR 301.7701-3: Classification of certain business entities.
(Also § 301.7701-2.)

Rev. Proc. 2002-69

SECTION 1. PURPOSE

The Treasury Department and the Internal Revenue Service have become aware that taxpayers are unsure of the classification for an entity that is owned solely by a husband and wife as community property under the laws of a state, a foreign country, or a possession of the United States. To alleviate this uncertainty and in the interest of administrative simplicity, this revenue procedure provides that the Internal Revenue Service will respect a taxpayer's treatment of these entities as either disregarded entities or partnerships.

This revenue procedure provides guidance on the classification for federal tax purposes of a qualified entity (described in section 3.02 of this revenue procedure) that is owned solely by a husband and wife as community property under the laws of a state, a foreign country, or a possession of the United States.

SECTION 2. BACKGROUND

Section 301.7701-1(a)(1) states that the Code prescribes the classification of various organizations for federal tax purposes. Whether an organization is an entity

separate from its owners for federal tax purposes is a matter of federal tax law and does not depend on whether the organization is recognized as an entity under local law.

Section 301.7701-1(b) provides that the classification of organizations that are recognized as separate entities is determined under §§ 301.7701-2, 301.7701-3, and 301.7701-4 unless a provision of the Code provides for special treatment of that organization.

Section 301.7701-2(a) defines the term “business entity” as any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under § 301.7701-3) that is not properly classified as a trust under § 301.7701-4 or otherwise subject to special treatment under the Code. A business entity with two or more members is classified for federal tax purposes as either a corporation or a partnership. A business entity with only one owner is classified as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as a sole proprietorship, branch, or division of the owner.

SECTION 3. SCOPE

.01 In General. This revenue procedure provides guidance on the classification for federal tax purposes of a qualified entity (described in section 3.02 of this revenue procedure).

.02 Qualified Entity. A business entity is a qualified entity if:

(1) The business entity is wholly owned by a husband and wife as community property under the laws of a state, a foreign country, or a possession of the United States;

(2) No person other than one or both spouses would be considered an owner for federal tax purposes; and

(3) The business entity is not treated as a corporation under § 301.7701-2.

SECTION 4. APPLICATION

.01 If a qualified entity (as described in section 3.02 of this revenue procedure), and the husband and wife as community property owners, treat the entity as a disregarded entity for federal tax purposes, the Internal Revenue Service will accept the position that the entity is a disregarded entity for federal tax purposes.

.02 If a qualified entity (as described in section 3.02 of this revenue procedure), and the husband and wife as community property owners, treat the entity as a partnership for federal tax purposes and file the appropriate partnership returns, the Internal Revenue Service will accept the position that the entity is a partnership for federal tax purposes.

.03 A change in reporting position will be treated for federal tax purposes as a conversion of the entity.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective on the date published in the Internal Revenue Bulletin.

SECTION 6. DRAFTING INFORMATION

The principal author of this revenue procedure is Laura Nash of the Office of the Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure contact Ms. Nash or Ms. Rebekah Myers at (202) 622-3050 (not a toll free call).