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INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR GERALD J. O'TOOLE, NEW ENGLAND
DISTRICT COUNSEL
Attn: John Mikalchus

CC:NER:NED:BOS

FROM: Nancy Romano, Senior Technician
Reviewer, Branch 3 (Administrative
Provisions & Judicial Practice)

CC:PA:APJP:Br.03

SUBJECT: Computation of the Assessment Statute
for a Short Year Return

This Field Service Advice responds to your memorandum dated August 4, 2000. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

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issues discussed in the document require inspection or disclosure of the Field Service Advice.

LEGEND

corporation A =

corporation B =

year 1 =

year 2 =

year 5 =

S short year =

C short year =

ISSUE

When does (did) the period of limitations for the assessment of tax with respect to corporation A's S short year expire.

CONCLUSIONS

It is not free from doubt, but we think that the period of limitations for the assessment of tax with respect to corporation A's S short year expired on April 21, year 5.

FACTS

Prior to year 1, corporation A properly elected to be treated as a small business corporation under section 1362(a). On July 1, year 1, corporation B purchased corporation A's outstanding stock, which terminated corporation A's election to be treated as a small business corporation. Corporation B properly filed an election to treat its purchase of corporation A stock as a purchase of corporation A's assets under section 338 (h)(10).

Corporation A and corporation B are calendar year taxpayers. Corporation B and its subsidiaries, including corporation A, timely filed a request for an automatic extension of time to file their consolidated return for year 1. Corporation A filed its

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Form 1120S for its S short year on April 21, year 2. On October 22, year 2, corporation A amended its Form 1120S for its S short year. Corporation B and its subsidiaries timely filed a consolidated income tax return for year 1, which included corporation A's C short year, on September 15, year 2.

The former shareholders of corporation A extended the statute of limitations on their individual returns for year 1, to December 31, year 5, but corporation A will not agree to extend the period of limitations on assessment of tax for its S short year.

The Service is auditing corporation A with respect to its S short year. In the audit, issues have been raised with respect to substantial adjustments that flow through to corporation A's shareholders and with respect to a built-in gains tax liability, which is taxable at the entity level.

As we understand your request for advice, you need our assistance only in determining the period of limitations on assessment of any tax at the entity level.

LAW AND ANALYSIS

The amount of any tax imposed by the Internal Revenue Code generally must be assessed within 3 years after the return was filed (whether or not such return was filed on or after the date prescribed. Sec. 6501(a). A return of tax imposed by the Internal Revenue Code, except tax imposed by chapters 3, 21, or 24, of the Internal Revenue Code, received before the last day prescribed by law or regulation is considered filed on such last day. Sec. 6501(b). For purposes of section 6501(b), the last day prescribed by law or regulation for filing a return is determined without regard to any extension of time for filing the return. Treas. Reg. § 301.6501(b)-1.

Section 1362(e)(4) provides that any taxable year of a corporation in which a termination of an election to be treated as a small business corporation under section 1362(a) takes effect (unless the termination takes place on the 1st day of such year) is an "S termination year." In the case of an S termination year, the portion of such year ending before the 1st day for which the termination is effective shall be treated as a short taxable year for which the corporation is an S corporation. Sec. 1362(e)(1)(A). The portion of the S termination year beginning on the 1st day that the termination is effective shall be treated as a short taxable year for which the corporation is a C corporation. Sec. 1362(e)(1)(B). The due date for filing the return for the short taxable year for which the corporation is an S corporation under section 1362(e)(1)(A) is the same date by which the return for the short taxable year for which the corporation is a C corporation (including any extensions thereof) must be filed. Sec. 1362(e)(6)(B); Treas. Reg. § 1.1362-3(c)(5). The intent of section 1362(e)(6)(B) is to make certain that the S

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short year return is not due before the C short year return. H. Rep. 97-826, p. 11 (1982) (“The return for the short subchapter S year will be due on the same date as the return for the short subchapter C year is due”).

Similarly, if a small business corporation becomes a member of an affiliated group of corporations filing consolidated returns in a transaction other than a qualified stock purchase for which an election under section 338(g) is made, the S short year ends on the day before the 1st day for which the termination is effective. Treas. Reg. § 1.1502-76(b)(1)(ii)(A)(2). In such cases, the small business corporation generally must file a separate return for any portion of its taxable year for which income is not included in the consolidated return filed by its common parent on or before the due date, including any extensions of time thereof, for filing the consolidated return. Treas. Reg. § 1.1502-76(c)(1). Treasury Regulation § 1.1502-76(b)(1)(ii)(A)(2) applies to transactions occurring after November 10, 1999.

In general, a corporation that is a calendar year taxpayer is required to file any return made under section 6012 by the 15th day of March of the year immediately following the close of the calendar year. Sec. 6072(b). Corporations subject to taxation under subtitle A are required to file a return under section 6012. Sec. 6012(a)(2). The Secretary may grant a reasonable extension of time for filing any return, although such extension of time may not exceed 6 months unless the taxpayer is abroad. Sec. 6081(a). In the case of a corporation, the Secretary must grant an automatic 3 month extension if the corporation requests such extension on the prescribed form and if the corporation pays the amount properly estimated as tax before the date prescribed for payment of tax. Sec. 6081(b).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

Corporation A filed its return for its S short year on April 21, year 2. Thus, unless the S short year return was filed before the last day prescribed for filing such return without regard to any extension of time for filing the return, the period of limitations for the assessment of the tax against corporation A expired 3 years after the date on which the return was filed or April 21, year 5. See sec. 6501(a) and (b).¹

Corporation A’s election to be treated as a small business corporation terminated after the first day of its year 1 taxable year. Therefore, the due date for corporation A to file its S short year return is the same date by which its C short year is due to

¹ Subsections (c) through (m), inclusive, of section 6501 set forth exceptions to the 3-year period of limitations set forth in subsection (a), none of which are applicable to this case.

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be filed including any extension thereof. See sec.1362(e)(6)(B); see also, Treas. Reg. § 1.1502-76(c)(1).² As a calendar year taxpayer, corporation A would have had until March 15, year 2, to file its C short year return except that corporation B and its subsidiaries, including corporation A, received an extension of time to file their consolidated year 1 return, including corporation A's C short year, until September 15, year 2. See secs. 6072(b) and 6081. Thus, corporation A also had until September 15, year 2, to timely file its S short year return.

Notwithstanding the above, any extension of time for filing the return is disregarded when determining the last day for filing the return for purposes of section 6501. Treas. Reg. § 301.6501(b)-1. Thus, for purposes of section 6501, the period of limitations for the assessment of a tax for corporation A's C short year return expires on March 15, year 5, or the date 3 years after the date on which the return was filed, whichever is later. Further, inasmuch as any extension of time is disregarded for purposes of section 6501, the period of limitations for the assessment of tax for corporation A's S short year also expires on March 15, year 5, or the date 3 years after the date on which the return was actually filed, whichever is later. In this case, corporation A filed its S short year return on April 21, year 2. Accordingly, we think that the period of limitations for assessment of tax expired on April 21, year 5.

We note, however, that our answer is not free from doubt. As stated above, statutory due date for filing the S short year return is the due date for filing the C short year return including any extension thereof. Sec. 1362 (e)(6)(B). It, therefore, is arguable that the unextended due date for the S short year return includes the extension provided for the C short year return and that, for purposes of section 6501, the period of limitations for the assessment of a tax for corporation A's C short year return expires on September 15, year 5, or the date 3 years after the date on which the return was filed, whichever is later. Inasmuch as April 21, year 5, precedes September 15, year 5, the assessment period would not expire before September 15, year 5.

There are no cases that discuss the interplay between section 1362(e)(6)(B) and the statute of limitations under section 6501. Nevertheless, we do not think that Congress intended to provide the Service with additional time to assess the tax with respect to the S short year where the S short year and C short year returns were filed on the same day. See H. Rep. 97-826, at 11. The statute is clear that, if the C short year return had been filed on April 21, year 2, the assessment period would

² We note that Treasury Regulation § 1.1502-76(b)(1)(ii)(A)(2) is not applicable to the instant case because it is not effective for transactions occurring before November 11, 1999.

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have expired on April 21, year 5. Accordingly, we think it is likely that a court would hold that the assessment period for the S short year return expired on April 21, year 5, which date is 3 years after the date on which the S short year return was filed.

Please call if you have any further questions.

cc: Michael P Corrado
Assistant Regional Counsel (TL)
Northeast Region