Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:INTL:BR2 – PLR-131651-03
Date:
February 06, 2004

In Re:

Legend

A =

B =

C1 =
C2 =
C3 =
D =
E =
F =
Firm X =
Firm Y =
Firm Z =
Country W =
Country X =
Country Y =
Country Z =
W percent =
X percent =
Y percent =
Z percent =
Date A =
amount M =

Dear :

This is in response to your letter dated May 6, 2003 requesting an extension of time to file a qualified electing fund (“QEF”) election on behalf of A with respect to A’s investments in C1, C2, C3, and D.

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

FACTS

A is a U.S. limited liability company with 32 members, 28 of whom are U.S. citizens or residents. A is the sole general partner of B, a Country W limited partnership. A owns approximately W percent of B.

C1, C2 and C3 are Country Y entities that are classified as corporations for U.S. tax law. Each was formed by B on Date A to serve as a holding company for investment in certain active companies. B made an equity contribution to C2 in exchange for a 100% interest in C2. C2 contributed the same amount to its direct, wholly-owned subsidiary, C3, and C3 contributed the same amount to its direct, wholly-owned subsidiary, C1. C1, C2 and C3 have been passive foreign investment companies ("PFICs") under Section 1297 since the date of their formation.

In June 2000, C1 obtained an X percent interest in F, a Country Z operating company. Prior to this acquisition, in February 2000, the advice of Firm X, a law firm competent to render international tax advice, was sought concerning the potential investment in F. Firm X had previously been involved in the formation of both A and B and therefore was aware of A's ownership interest in B. Firm X was consulted whether the investment in F could be made directly through the Country Y entities (C1, C2 and C3) or whether the investment needed to be made though a holding company organized in the U.S. or elsewhere. Firm X focused on B's ownership of the Country Y entities and failed to recall that the Country Y entities were indirectly owned by A through B and therefore failed to advise A that C1, C2, and C3 qualified as PFICs with regard to A. A was therefore not advised to make a QEF election for C1, C2 and C3 and made no QEF election for C1, C2, or C3 for the 2000 tax year.

In February 2001, C1 obtained a Y percent interest in the common equity of D, a Country X holding company, and D acquired Z percent of the common equity of E, a Country X operating company, and approximately amount M of convertible bonds of E. Prior to these acquisitions, in January 2001, Firm X was consulted concerning the potential investment in E. Firm X was informed that the investment in E would be made through D. Firm X failed to advise that investing in E through D would cause D to qualify as a PFIC with regard to A and therefore failed to advise A to make a QEF election for D.

Firm Y, an accounting firm, also provided tax advice with respect to the formation and structuring of A and B and prepared A and B's tax returns since their formation including the 2000 and 2001 tax returns. Firm Z was hired in 2002 to complete the preparation of A and B's 2001 tax returns. Neither Firm Y nor Firm Z advised A and B about the potential status of C1, C2, C3, or D as a PFIC or the availability of the QEF election.

In January 2003, while rendering advice with respect to the consequences of a redemption by E of the convertible bonds held by D, Firm X reviewed the overall organizational structure and realized that A held indirect interests in four PFICs: C1, C2, C3 and D. At this time, Firm X noted for the first time the fact that these entities were PFICs and recommended the submission of a ruling request to make retroactive QEF elections under Treas. Reg. § 1.1295-3.

RULING REQUESTED

A requests the consent of the Commissioner of the Internal Revenue Service to make a retroactive QEF election under Treas. Reg. § 1.1295-3(f) with respect to C1, C2, C3, for A's 2000 tax year and with respect to D for A's 2001 tax year.

LAW AND ANALYSIS

Section 1295(a) provides that any PFIC shall be treated as a QEF with respect to a taxpayer if (1) an election by the taxpayer under section 1295(b) applies to such company for the taxable year and (2) the company complies with such requirements as the Secretary may prescribe for purposes of determining the ordinary earnings and net capital gains of such company. Under section 1295(b)(2), a QEF election may be made for any taxable year at any time on or before the due date (determined with regard to extensions) for filing the return for such taxable year. To the extent provided in regulations, such an election may be made after such due date if the taxpayer failed to make an election by the due date because the taxpayer reasonably believed the company was not a PFIC.

Under Treas. Reg. § 1.1295-3(f), the taxpayer may request the consent of the Commissioner to make a retroactive QEF election for a taxable year. The Commissioner will grant relief under Treas. Reg. § 1.1295-3(f) only if four conditions are satisfied. The first requirement is that the shareholder reasonably relied on a qualified tax professional who failed to identify the foreign corporation as a PFIC or failed to advise the shareholder of the consequences of making, or failing to make, a section 1295 election. Treas. Reg. § 1.1295-3(f)(2) provides that a shareholder will not be considered to have reasonably relied on a qualified tax professional if the shareholder

knew, or reasonably should have known, that the foreign corporation was a PFIC and knew of the availability of a section 1295 election. In addition, a shareholder cannot claim reliance upon a tax professional if he knew or reasonably should have known that the qualified tax professional was not competent to render tax advice with respect to the ownership of shares of a foreign corporation or did not have access to all relevant facts and circumstances.

During the years at issue, A sought U.S. tax advice from its regular outside tax counsel, Firm X, prior to the formation of and investment in C1, C2, C3 and D. Firm X's tax department was competent to render tax advice with respect to stock ownership of a foreign corporation and had access to all the relevant facts and circumstances. Firm X's tax department failed to identify C1, C2, C3 and D as PFICs and therefore failed to advise A of the consequences of making or failing to make a QEF election. Thus, A reasonably relied on a qualified tax professional within the meaning of Treas. Reg. § 1.1295-3(f)(1)(i) and (2) for the taxable years at issue.

The second requirement of Treas. Reg. § 1.1295-3(f) is that granting consent will not prejudice the interests of the U.S. government. Under Treas. Reg. § 1.1295-3(f)(3)(i), the interests of the U.S. government are prejudiced if granting relief would result in the shareholder having a lower tax liability, taking into account applicable interest charges, in the aggregate for all years affected by the retroactive election (other than by a de minimis amount) than the shareholder would have had if the shareholder had made the section 1295 election by the election due date. The time value of money is taken into account for purposes of this computation. If granting relief would prejudice the interests of the U.S. government, the Commissioner may, in his sole discretion, grant consent to make the election provided the shareholder enters into a closing agreement with the Commissioner that requires the shareholder to pay an amount sufficient to eliminate any prejudice to the U.S. government as a consequence of the shareholder's inability to file amended returns for closed taxable years. Treas. Reg. § 1.1295-3(f)(3)(ii).

This requirement is met in this case because all of the affected years are still open and A has already reported the amounts owed for 2000 through 2002 on its partnership return and on the Schedules K-1 for its members.

The third requirement of Treas. Reg. § 1.1295-3(f) is that the request must be made before a representative of the Internal Revenue Service raises upon audit the PFIC status of the corporation for any taxable year of the shareholder. Treas. Reg. § 1.1295-3(f)(1)(iii). In this case, the PFIC status of the C1, C2, C3, and D has not been raised upon audit.

The final requirement of Treas. Reg. § 1.1295-3(f) is that the procedural requirements set forth in Treas. Reg. § 1.1295-3(f)(4) must be met. These include filing a request for consent to make a retroactive election with, and submitting a user fee to, the Office of the Associate Chief Counsel (International). Treas. Reg. § 1.1295-3(f)(4)(i). Additionally, affidavits signed under penalties of perjury must be submitted by the shareholder and any qualified tax professional upon whose advice the shareholder relied. Treas. Reg. § 1.1295-3(f)(4)(ii), (iii). These affidavits must describe the events that led to the failure to make a QEF election by the election due date, the discovery of such failure, and the engagement and responsibilities of the qualified tax professional and the extent to which the shareholder relied on such professional. Here, affidavits meeting the requirements set forth in Treas. Reg. § 1.1295-3(f)(4)(ii) and (iii) as to the failure of Firm X to inform A of its need to make QEF elections have been submitted and A has otherwise satisfied the procedural requirements of Treas. Reg. § 1.1295-3(f)(4).

Based on the information submitted and representations made:

Consent is granted to A to make retroactive elections for A's 2000 taxable year with respect to C1, C2 and C3, and for A's 2001 taxable year with respect to D, under Treas. Reg. § 1.1295-3(f), provided that A complies with the rules under Treas. Reg. § 1.1295-3(g) regarding the time and manner for making the retroactive QEF election.

This private letter ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this ruling must be attached to any tax return to which it is relevant.

In accordance with the power of attorney on file with this office, a copy of this ruling is being sent to the taxpayer.

Sincerely,

Valerie A. Mark Lippe
Senior Technician Reviewer, CC:INTL:Br2
Office of Associate Chief Counsel
(International)