

**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:PSI:B03  
PLR-110689-07  
Date:  
August 29, 2007

Legend:

Parent =

Subsidiary =

Partnership =

A =

B =

C =

D =

State =

Date1 =

Date2 =

Date3 =

Dear :

This letter responds to your letter dated March 1, 2007, and subsequent correspondence, submitted on behalf of Parent, requesting rulings under §§ 1362(b)(5) and 1362(f) of the Internal Revenue Code and § 301.9100-3 of the Procedure and Administration Regulations.

### Facts

On Date1, Parent incorporated under the laws of State. The shareholders of Parent intended Parent to be treated as an S corporation effective Date2, but Parent inadvertently failed to timely file an S corporation election. In addition, Parent discovered that one of the shareholders of record on Date2 (Partnership) was an ineligible S corporation shareholder. Immediately thereafter, Parent redeemed the shares of Parent's stock held by Partnership for cash on Date3. Parent also intended to file an election to treat Subsidiary, its wholly-owned subsidiary, as a qualified subchapter S subsidiary (QSub) effective Date2, but Parent failed to timely file the QSub election.

Parent represents that, with the exception of having an ineligible shareholder for the period beginning Date2 and ending Date3, it meets all of the requirements to be a small business corporation under § 1361(b) effective Date2. Moreover, Parent represents that the presence of an ineligible shareholder was inadvertent. Parent and its shareholders agree to make any adjustments consistent with the treatment of Parent as an S corporation as may be required by the Secretary.

Parent requests a ruling under § 1362(b)(5) that it will be treated as an S corporation effective Date2 and a ruling under § 1362(f) that the effect of Parent's invalid § 1362(a) election will be waived. In addition, Parent requests an extension of time under § 301.9100-3 to make a QSub election for Subsidiary effective Date2.

### Law

#### **Section 1362(b)(5) Ruling**

Section 1362(a)(1) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1362(b)(1) provides that an election under § 1362(a) may be made by a small business corporation for any taxable year (A) at any time during the preceding taxable year, or (B) at any time during the taxable year and on or before the 15<sup>th</sup> day of the third month of the taxable year.

Section 1362(b)(2) provides that if (A) an election under § 1362(a) is made for any taxable year during such year and on or before the 15<sup>th</sup> day of the third month of such year, but (B) either (i) on one or more days in such taxable year before the day on which the election was made the corporation did not meet the requirements of § 1361(b), or (ii) one or more of the persons who held stock in the corporation during such taxable year and before the election was made did not consent to the election, then such election shall be treated as made for the following taxable year.

Section 1362(b)(3) provides that if (A) a small business corporation makes an election under § 1362(a) for any taxable year, and (B) the election is made after the 15<sup>th</sup> day of the third month of the taxable year and on or before the 15<sup>th</sup> day of the third month of the following taxable year, then the election shall be treated as made for the following taxable year.

Section 1362(b)(5) provides that if (A) an election under § 1362(a) is made for any taxable year (determined without regard to § 1362(b)(3)), after the date prescribed by § 1362(b) for making the election for the taxable year or no § 1362(a) election is made for any taxable year, and (B) the Secretary determines that there was reasonable cause for the failure to timely make the election, the Secretary may treat the election as timely made for the taxable year (and § 1362(b)(3) shall not apply).

### **Section 1362(f) Ruling**

Section 1361(a) provides that the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) provides, in part, that the term “small business corporation” means a domestic corporation that is not an ineligible corporation and that does not have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1362(f) provides, in part, that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, (2) the Secretary determines that the circumstances resulting in such ineffectiveness were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness, steps were taken so that the corporation for which the election was made is a small business

corporation, and (4) the corporation for which the election was made, and each person who was a shareholder in such corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

### **Section 301.9100-3 Ruling**

Section 1361(b)(3)(A) provides that, except as provided in regulations prescribed by the Secretary, for purposes of Title 26, (i) a corporation which is a QSub shall not be treated as a separate corporation, and (ii) all assets, liabilities, and items of income, deduction, and credit of a QSub shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

Section 1361(b)(3)(B) provides that, for purposes of § 1361(b)(3), the term "qualified subchapter S subsidiary" means any domestic corporation which is not an ineligible corporation (as defined in § 1361(b)(2)), if (i) 100 percent of the stock of such corporation is held by the S corporation, and (ii) the S corporation elects to treat such corporation as a QSub.

A taxpayer makes a QSub election with respect to a subsidiary by filing Form 8869 (Qualified Subchapter S Election) with the appropriate service center.

Section 1.1361-3(a)(4) of the Income Tax Regulations provides that a QSub election will be effective on the date specified on the election form or on the date the election form is filed if no date is specified. The effective date specified on the form cannot be more than two months and 15 days prior to the date of filing and cannot be more than 12 months after the date of filing.

Under § 301.9100-1(c) the Commissioner may grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make a regulatory election, or a statutory election (but no more than six months except in the case of a taxpayer who is abroad), under all subtitles of the Code, except subtitles E, G, H, and I. Section 301.9100-1(b) defines the term "regulatory election" as 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.

Sections 301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make an election.

Section 301.9100-2 provides automatic extensions of time for making certain elections. Section 301.9100-3 provides extensions of time for making regulatory elections that do not meet the requirements of § 301.9100-2.

Section 301.9100-3(a) provides that requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides the evidence (including affidavits described in § 301.9100-3(e)) 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 interests of the Government.

### Conclusions

#### **Section 1362(b)(5) Ruling**

Based solely on the facts submitted and representations made, we conclude that Parent has established reasonable cause for failing to make an S corporation election. Thus, we conclude that Parent is eligible for relief under § 1362(b)(5). Accordingly, if Parent makes an election to be an S corporation by filing with the appropriate service center a completed Form 2553 that contains an effective date of Date2, within 60 days following the date of this letter, the election shall be treated as timely made. A copy of this letter should be attached to Form 2553.

#### **Section 1362(f) Ruling**

Parent failed to timely file an election to be treated as an S corporation effective Date2. Had Parent timely filed the election, it would have been ineffective because Parent had an ineligible S corporation shareholder on Date2. Based solely on the facts submitted and representations made, we conclude that Parent's election to be treated as an S corporation effective Date2 would have been ineffective and also conclude that the ineffectiveness would have been inadvertent within the meaning of § 1362(f).

Under the provisions of § 1362(f), Parent will be treated as an S corporation effective Date2 and thereafter, provided that Parent's S corporation election is not otherwise terminated under § 1362(d). From Date2 through Date3, the partners of Partnership, A, B, C, and D, will be treated as if they held shares in Parent directly. Accordingly, Parent's shareholders, in determining their respective income tax liabilities, must include their pro rata share of the separately and nonseparately computed items of Parent under § 1366, make any adjustments to stock basis under § 1367, and take into account any distributions made by Parent under § 1368. If Parent or Parent's shareholders fail to treat Parent as described above, this letter ruling will be null and void.

#### **Section 301.9100-3 Ruling**

Based solely on the facts submitted and representations made, we conclude that Parent has satisfied the requirements of §§ 301.9100-1 and 301.9100-3. Accordingly, Parent is granted an extension of time of 60 days from the date of this letter to elect to treat Subsidiary as a QSub effective Date2. The election should be made by filing Form 8869 with the appropriate service center. A copy of this letter should be attached to Form 8869.

Except as expressly provided herein, we express or imply no opinion concerning the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion concerning whether Parent is otherwise eligible to be an S corporation, or whether Subsidiary is a valid QSub.

This 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.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

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 the request for rulings, it is subject to verification on examination.

Sincerely,

/s/

William P. O'Shea  
Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)

A copy of this letter

A copy for § 6110 purposes

cc: