

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:3 PLR-118271-02

Date:

January 16, 2003

Legend

Parent =

Subsidiary =

Shareholders =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Year 1 =

Dear :

This letter responds to a letter dated February 8, 2002, and subsequent correspondence, requesting a ruling under § 301.9100-3(a) of the Procedure and Administration Regulations for an extension of time to file an election to be treated as a qualified S corporation subsidiary (QSub) and for late S election relief under § 1362(b)(5) of the Internal Revenue Code.

#### Facts

Parent is an S corporation. Parent created Subsidiary on Date 1. Parent was the sole owner of Subsidiary from Date 1 to Date 2. On Date 2, Parent distributed Subsidiary to the shareholders of Parent, Shareholders, in proportion to Shareholders' ownership interests in Parent.

On or about Date 4, subsequent to the filing of Subsidiary's Form 1120S for the Year 1 taxable year, the Internal Revenue Service issued a notice to Subsidiary indicating that the Service had no record of Subsidiary ever filing a Form 2553, Election By a Small Business Corporation, to elect S corporation status. Further, a Form 8869, Qualified Subchapter S Subsidiary Election, was never filed with the appropriate Service Center. It is represented that Parent intended to elect to treat Subsidiary as a QSub effective Date 1 and that Subsidiary intended to elect to be an S corporation effective Date 3 but inadvertently neither election was timely filed.

### Law and Application

Section 1361(a)(1) 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 that the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not (A) have more than 75 shareholders, (B) 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, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(b)(3)(A) provides that a corporation which is a QSub shall not be treated as a separate corporation and all assets, liabilities, and items of income, deduction, and credit of a QSub shall be treated as assets, liabilities, and such items of the S corporation.

Section 1361(b)(3)(B) defines a QSub as a domestic corporation that is not an ineligible corporation, if 100 percent of the stock of the corporation is owned by an S corporation, and the S corporation elects to treat the corporation as a QSub.

Section 1361(b)(3)(C) provides that, when a QSub election terminates, such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such termination from the S corporation in exchange for its stock.

Section 1.1361-3(a) of the Income Tax Regulations provides that an S corporation may elect to treat an eligible subsidiary as a QSub by filing the form prescribed by the IRS and that the election may be effective no more than two months and 15 days prior to the date of the filing and cannot be more than 12 months after the date of filing. Notice 2000-58, 2000-2 C.B. 491, provides that Form 8869, Qualified Subchapter S Subsidiary Election, should be used to elect QSub treatment.

Section 1.1361-5(a)(1)(iii) provides that the termination of a QSub election is effective at the close of the day on which an event occurs that renders the subsidiary ineligible for QSub status under § 1361(b)(3)(B).

Section 1.1361-5(c)(1) provides that absent the Commissioner's consent, and except as provided in § 1.1361-5(c)(2), a corporation whose QSub election has terminated (or a successor corporation) may not make an S election or have a QSub election made with respect to it for five taxable years.

Section 1.1361-5(c)(2) provides that in the case of S and QSub elections effective after December 31, 1996, if a corporation's QSub election terminates, the corporation may, without requesting the Commissioner's consent, make an S election or have a QSub election made with respect to it before the expiration of the five-year period, provided that (i) immediately following the termination, the corporation (or its successor corporation) is otherwise eligible to make an S election or have a QSub election made for it; and (ii) the relevant election is made effective immediately following the termination of the QSub election.

Section 1362(a) generally provides that a small business corporation may elect to be an S corporation for federal tax purposes.

Section 1362(b) governs the timeliness of an S election as well as its effective date. Generally, if an election to be treated as an S corporation is made within the first two and one-half months of a corporation's taxable year, then the corporation will be treated as an S corporation beginning in the year in which the election was made. If the election is made after the first two and one-half months of a corporation's taxable year, then the corporation will not be treated as having made an effective election to be treated as an S corporation for federal tax purposes until the following taxable year.

Section 1362(b)(5) provides that if an election to be treated as an S corporation for federal tax purposes is either made untimely, or not made at all, and the Secretary determines that there was reasonable cause for the failure to make a timely election, then the Secretary may treat the corporation as having made a timely election.

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of time 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 E, G, H, and I, if the taxpayer demonstrates to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and that granting the relief will not prejudice the interests of the government.

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 elections that do not meet the requirements of § 301.9100-2.

Requests for relief under § 301.9100-3 will be granted when the taxpayer provides evidence to establish that the taxpayer acted reasonably and in good faith, and that granting relief will not prejudice the interests of the government.

### Conclusion

Based solely on the facts and the representations submitted, we conclude that the requirements of § 301.9100-3 have been satisfied. As a result, Parent is granted an extension of time of 60 days from the date of this letter to file a Form 8869 to elect to treat Subsidiary as a QSub effective Date 1. A copy of this letter should be attached to the Form 8869 and is enclosed for that purpose. Further, we conclude that Subsidiary has established reasonable cause for failing to make a timely election to be an S corporation. As a result, provided Subsidiary files a completed Form 2553 effective Date 3 with the appropriate Service Center within 60 days from the date of this letter, such election will be treated as timely made. A copy of this letter should be attached to the Form 2553 and is enclosed for that purpose.

Except for the specific rulings above, no opinion is expressed or implied concerning the federal income tax consequences of the facts of this case under any other provision of the Internal Revenue Code.

Pursuant to your request, we are sending a copy of this letter to your authorized representative.

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

Sincerely,

/s/

Heather C. Maloy  
Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures (3)

Copies (2) of this letter

Copy for § 6110 purposes