Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B01 – PLR-147928-03
Date:
Feb 23 2004

Legend:

Subsidiary =

Parent =

State =

D1 =

D2 =

Dear :

This letter responds to the letter received by our office on June 16, 2003, and related correspondence, written on behalf of Subsidiary, requesting relief under § 1362(b)(5) of the Internal Revenue Code.

FACTS

The information submitted discloses that Parent was incorporated under the laws of State and is an S corporation. Parent elected to treat Subsidiary, wholly owned by Parent as of D1, as a qualified subchapter S subsidiary ("QSub"), effective D1. On D2, Parent distributed its stock in Subsidiary to Parent's shareholders. Consequently, Subsidiary's QSub election terminated as of D2.

Subsidiary and its shareholders intended that Subsidiary be an S corporation immediately after the termination of its QSub election. However, an election to treat Subsidiary as an S corporation effective D2 was not filed.

LAW AND ANALYSIS

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)(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 1.1361-5(a)(1)(iii) of the Income Tax Regulations 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.

CONCLUSION

Based solely on the facts submitted and representations made, we conclude that Subsidiary has established reasonable cause for failing to make a timely election to be an S corporation. As a result, provided that Subsidiary otherwise qualifies as an S corporation, Subsidiary will be recognized as an S corporation effective D2. Within 60 days from the date of this letter, Subsidiary should submit a properly completed Form 2553, with a copy of this letter attached, to the relevant service center. A copy of this letter is enclosed for that purpose.

This ruling is contingent upon Subsidiary and all its shareholders treating Subsidiary as having been an S corporation for the period beginning D2, and thereafter.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed regarding whether Subsidiary is otherwise eligible to be an S corporation.

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 mailed to the taxpayer.

Sincerely,

/s/ Dianna K Miosi

Dianna K. Miosi
Chief, Branch 1
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter
Copy for § 6110 purposes

cc: