

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

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Date:

October 4, 1999

X =

Y =

A =

D1 =

D2 =

D3 =

D4 =

D5 =

D6 =

Dear :

This letter responds to a letter dated June 1, 1999, and subsequent correspondence submitted by you as X's authorized representative on behalf of X, concerning a waiver of the five-year waiting period imposed by § 1361(b)(3)(D) of the Internal Revenue Code in order to permit X to make an S corporation election under § 1362(a).

The information submitted states that X was incorporated D1, but it did not have any shareholders, assets, or business activities until D2. On D2, Y acquired all of the shares of X and distributed them to Y's shareholders, applying the rules of § 1368 of the Code. A, the secretary and treasurer of X, represents that Y has been an S corporation since D6. On D4, Y filed a qualified subchapter S subsidiary (QSub) election under § 1361(b)(3)(B)(ii) for X, effective for D2. On D5, X filed a Form 2553, Election by a Small Business Corporation. A represents that the Form 2553 was intended to be effective D3, but no effective date was listed on the Form 2553.

Section 1362(a) 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, in general, 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 3d month of the taxable year.

Section 1.1362-6(a)(2)(i) of the Income Tax Regulations provides that a small business corporation makes an election under § 1362(a) to be an S corporation by filing a completed Form 2553. The election form must be filed with the service center designated in the instructions applicable to Form 2553. The election is not valid unless all shareholders of the corporation at the time of the election consent to the election in the manner provided in § 1.1362-6(b). However, once a valid election is made, new shareholders need not consent to that election.

In Thompson v. Commissioner, 66 T.C. 737 (1976), acq., 1977-1 C.B. 1, the court held that an S corporation election filed timely for the corporation's taxable year beginning December 1, 1969, but showing an erroneous effective date of January 1, 1969, was valid for the taxable year beginning December 1, 1969, which was the corporation's second taxable year.

Section 1361(b)(3)(A) provides that except as provided in regulations prescribed by the Secretary, for purposes of the Code (i) a corporation which is a qualified subchapter S subsidiary (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) defines a QSub as a domestic corporation that is not an ineligible corporation, as defined in § 1361(b)(2), if 100 percent of the stock of the corporation is owned by the S corporation, and the S corporation elects to treat the corporation as a QSub.

Section 1361(b)(3)(C) provides that for purposes of the Code, if any corporation which was a QSub ceases to meet the requirements of § 1361(b)(3)(B), the corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before the cessation from the S corporation in exchange for its stock.

Section 1361(b)(3)(D) provides that if a corporation's status as a QSub terminates, such corporation (and any successor corporation) shall not be eligible to make (i) an election under § 1361(b)(3)(B)(ii) to be treated as a QSub, or (ii) an election under § 1362(a) to be treated as an S corporation, before the 5<sup>th</sup> taxable year which begins after the 1<sup>st</sup> taxable year for which the termination was effective, unless the Secretary consents to the election.

In explaining § 1361(b)(3)(D), the Joint Committee on Taxation states as follows:

It is expected that the Secretary will provide waivers of the five-year rule in appropriate instances. For example, if the stock of the qualified subchapter S subsidiary is distributed to the individual shareholders of the subsidiary's parent, the subsidiary will no longer be a qualified subchapter S subsidiary and would be subject to the five-year rule. If the parent corporation retains its subchapter S election and the Secretary determines that the distribution was not made for purposes of tax avoidance, it would seem appropriate for the Secretary to waive the five-year rule.

Joint Committee on Taxation Staff, General Explanation of Tax Legislation Enacted in the 104<sup>th</sup> Congress (JCS-12-96), 104<sup>th</sup> Cong., 2d Sess. 120 (1996).

Based solely on the facts and representations submitted, the Service waives the five-year waiting period imposed by § 1361(b)(3)(D) and consents to X's S corporation election under § 1362(a), effective D3, and thereafter unless otherwise terminated.

We further conclude that X's S corporation election, filed D5 to be effective D3, will not be considered invalid because of the lack of an effective date on the Form 2553. X should, within 60 days following the date of this letter, re-file the Form 2553 with the correct effective date included. A copy of this letter should be attached to the Form 2553.

Temporary or final regulations pertaining to one or more issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked if the adopted temporary or final regulations are inconsistent with any conclusion in the ruling. See § 12.04 of Rev. Proc. 99-1, 1999-1 I.R.B. 6, 47. However, when the criteria in § 12.05 of Rev. Proc. 99-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

Except as specifically set forth above, we express no opinion concerning the federal tax consequences of the facts described above under any other provision of the Code.

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

Pursuant to a power of attorney on file with this office, a copy of this letter is being forwarded to X.

Sincerely yours,

H. GRACE KIM  
Assistant to the Chief  
Branch 2  
Office of the Assistant  
Chief Counsel  
(Passthroughs and  
Special Industries)

Enclosures: 2  
Copy of this letter  
Copy for § 6110 purposes