Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Index Number: 1362.04-00

Number: **199939029**
Release Date: 10/1/1999

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:P&SI:1-PLR-106229-99
Date:
July 6, 1999

Legend:

X =

A =

B =

D1 =

D2 =

D3 =

State =

This responds to the letter dated June 21, 1999, and prior correspondence, submitted on behalf of X requesting relief under § 1362(f) of the Internal Revenue Code.

FACTS

You have represented that the facts are as follows. X is a corporation organized under the laws of State which made a valid S corporation election effective D1. On D2, X stock was issued to A, a nonresident alien. Although A is married to B, a citizen of the United States, A and B did not initially elect to subject A to tax as a United States resident, but have subsequently filed an election under § 6013(g) and the accompanying Income

Tax Regulations, along with a D3 individual tax return filed jointly with B, to have A taxed as a resident of the United States effective beginning in the D3 tax year. X and its shareholders intended for X to be an S corporation before and after the issuance of the X stock to A.

LAW AND ANALYSIS

Section 1361(a)(1) defines an "S corporation" as "a small business corporation for which an election under § 1362 is in effect."

Section 1361(b)(1)(C) provides that, in order to be a small business corporation, a taxpayer cannot have a nonresident alien as a shareholder.

Section 1362(d)(2)(A) provides that an election to be treated as a subchapter S corporation terminates whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation. Under §1362(d)(2)(B), the termination is effective on and after the date the S corporation ceases to meet the requirements of a small business corporation.

Section 1362(f), in relevant part, provides that, if (1) an election under §1362(a) by any corporation was terminated under § 1362(d), (2) the Secretary determines that the termination was inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the termination, steps were taken so that the corporation is once more a small business corporation, and (4) the corporation and each person who was a shareholder of the corporation at any time during the period specified pursuant to §1362(f), agrees to make any adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to the period, then, notwithstanding the terminating event, the corporation shall be treated as continuing to be an S corporation during the period specified by the Secretary.

The committee reports accompanying the Subchapter S Revision Act of 1982 explain §1362(f) as follows:

> If the Internal Revenue Service determines that a corporation's subchapter S election is inadvertently terminated, the Service can waive the effect of the terminating event for any period if the corporation timely corrects the event and if the corporation and the shareholders agree to be treated as if the election had been in effect for such period.
>
> The committee intends that the Internal Revenue Service be reasonable in granting waivers, so that corporations whose subchapter S eligibility requirements have been inadvertently violated do not suffer the tax consequences of a termination if no tax avoidance would result from the continued subchapter S treatment. In granting a waiver, it is hoped that

> taxpayers and the government will work out agreements that protect the revenues without undue hardship to taxpayers....It is expected that the waiver may be made retroactive for all years, or retroactive for the period in which the corporation again became eligible for subchapter S treatment, depending on the facts.

S. Rep. No. 640, 97th Cong., 2d Sess. 12-13 (1982), 1982-2 C.B. 718, 723-24; H.R. Rep. No. 826, 97th Cong., 2d Sess. 12 (1982), 1982-2 C.B. 730, 735.

Section 6013(g)(1) provides that, generally, a nonresident alien individual with respect to whom this subsection is in effect for the taxable year, is treated as a resident of the United States for purposes of chapter 1 for all of the taxable year.

Section 6013(g)(2) provides that an individual with respect to whom this subsection is in effect is any individual who, at the close of the taxable year for which an election is made, is a nonresident alien individual married to a citizen or resident of the United States, if both spouses make the election to have the benefits of this subsection apply to them.

Section 6013(g)(3) provides that an election made under this subsection applies to the taxable year for which it was made and to all subsequent taxable years until terminated; except that an election shall not apply to any taxable year if neither spouse is a citizen or resident of the United States at any time during the year.

Pursuant to § 6013(g)(4), an election is terminated as the earliest of: a revocation by either taxpayer; the death of either taxpayer; the legal separation of the couple; or the termination by the Secretary of the Treasury. If an election made under § 6013(g) for any two individuals is terminated for any taxable year, the two individuals are ineligible under § 6013(g)(6) to make an election under this subsection for any subsequent tax year.

Section 1.6013-6(a)(4)(i) of the Income Tax Regulations provides that, generally, an election under this section is made by attaching a statement to a joint income tax return or a joint amended income tax return for the first taxable year for which the election is to be in effect.

CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that X's election to be treated as an S corporation terminated on D2 when X's stock was issued to A. We also conclude that the termination constituted an "inadvertent termination" within the meaning of § 1362(f). Pursuant to § 1362(f), X will be treated as continuing to

be an S corporation from D2, provided that the election to have A taxed as a resident of the United States is effective beginning in the D3 tax year and that X's S election is not otherwise terminated under § 1362(d).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed concerning whether the original election made by X to be treated as an S corporation was a valid election under § 1362.

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.

Sincerely,

Signed/Daniel J. Coburn
Daniel J. Coburn
Assistant to the Branch Chief, Branch 1
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes