

Revenue Procedures

Rev. Proc. 2003-43, 2003-23 IRB 998, 05/09/2003, IRC Sec(s). 1362

S corporation election—treating late elections as timely.

Headnote:

IRS revised method for taxpayers to request relief for late S corp. elections, and other late elections that might be filed by S corp, effective for all requests made or pending in national office on 6/9/2003. *Rev Proc 98-55*, 1998-2 CB 645 is superseded.

Reference(s): ¶ 13,625.01(10); 13,625.01(15); Code Sec. 1362;

Full Text:

1. Purpose

This revenue procedure provides a simplified method for taxpayers to request relief for late S corporation elections, Electing Small Business Trust (ESBT) elections, Qualified Subchapter S Trust (QSST) elections and Qualified Subchapter S Subsidiary (QSub) elections. Generally, this revenue procedure provides that certain eligible entities may be granted relief for failing to file these elections in a timely manner if the request for relief is filed within 24 months of the due date of the election. Accompanying this document is a flowchart designed to aid taxpayers in applying this revenue procedure.

2. Background

.01 S Corporation Elections.

(1) In General. Section 1361(a)(1) of the Internal Revenue Code defines an “S corporation,” with respect to any taxable year, as a small business corporation for which an S corporation election is in effect for that year.

Section 1362(b)(1) provides that a corporation may make an election to be treated as an S corporation (A) at any time during the preceding taxable year, or (B) at any time during the taxable year and on or before the 15th day of the 3rd month of the taxable year.

Section 1.1362-6(a)(2) of the Income Tax Regulations provides that a corporation makes an election to be an S corporation by filing a completed Form 2553, Election by a Small Business Corporation.

Under § 1362(b)(3), if an S corporation election is made for a taxable year after the 15th day of the 3rd month of that taxable year and on or before the 15th day of the 3rd month

of the following taxable year, then the S corporation election is treated as made for the following taxable year.

(2) Late S Corporation Elections. 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 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).

.02 QSub Elections.

(1) In General. Section 1361 generally provides that an S corporation may elect to treat certain wholly owned subsidiaries as QSubs (as defined in § 1361(b)(3)(B)).

Section 1.1361-3 describes the time and manner for a corporation to make a QSub election. Section 1.1361-3(a)(2) provides that an S corporation may make a QSub election by filing the election form with the applicable service center. Form 8869, Qualified Subchapter S Subsidiary Election, is used to make a QSub election. The election to treat a subsidiary as a QSub may be filed at any time during the taxable year under § 1.1361-3(a)(3). Section 1.1361-3(a)(4) provides that the effective date is the date specified on the form (provided the date specified is not earlier than two months and 15 days before the date of the filing and the date specified is not more than 12 months after the date of the filing) or, on the date the election form is filed if no date is specified. If an election form specifies an effective date more than two months and 15 days prior to the date on which the election form is filed, it will be effective two months and 15 days prior to the date it is filed. If an election form specifies an effective date more than 12 months after the date on which the election is filed, it will be effective 12 months after the date it is filed.

(2) Late QSub Elections. Under § 301.9100-1(c) of the Procedure and Administration Regulations, 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 certain statutory elections 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. Because a QSub election is a regulatory election, the Commissioner may permit a late QSub election under the rules set forth in § 301.9100-3.

.03 ESBT and QSST Elections.

(1) In General. Section 1361(b)(1)(B) limits the permitted shareholders of an S corporation to domestic individuals, estates, certain trusts, and certain exempt organizations.

Section 1361(d)(1)(A) provides that a QSST (as defined in § 1361(d)(3)(A)) is a permitted S corporation shareholder if the beneficiary of the QSST makes an election under § 1361(d)(2). Pursuant to § 1361(d)(2)(A) and § 1.1361-1(j)(6)(i), the election by a current income beneficiary of a QSST may be made by the beneficiary's guardian or legal representative (or a natural or an adoptive parent of the current income beneficiary if a legal representative has not been appointed) if the current income beneficiary is a minor. A QSST election is made by signing and filing an election statement with the applicable service center. Section 1.1361-1(j)(6)(iii) provides that the QSST election must be made within the 16-day-and-2-month period beginning on the day that the S corporation stock is transferred to the trust.

Section 1361(c)(2)(A)(v) provides that an ESBT (as defined in § 1361(e)) is a permitted S corporation shareholder. To qualify as an ESBT, the trustee of the trust must make an ESBT election by signing and filing an election statement with the applicable service center. Section 1.1361-1(m)(2)(iii) provides that the ESBT election must be filed within the time requirements prescribed in § 1.1361-1(j)(6)(iii) for filing a QSST election (described above).

(2) Late ESBT and QSST Elections. Failure to properly make an election to be treated as an ESBT or a QSST may result in a shareholder who is not an eligible S corporation shareholder under § 1361(b)(1)(B) holding stock of the corporation. As a result, the failure to properly file an ESBT or QSST election may result in an inadvertent invalid S corporation election, or in an inadvertent termination of an S corporation election.

Section 1362(f) grants the Secretary (or his delegate) authority to provide relief if a corporation's S corporation election was not effective for the taxable year for which it was made by reason of a failure to meet the requirements of § 1361(b) or to acquire the required shareholder consents. Under § 1362(f), the Secretary may also grant relief if the corporation's S corporation election terminated under § 1362(d)(2) or (3). A corporation is eligible for relief under this provision if (1) the Secretary determines that the circumstances resulting in the ineffectiveness or termination were inadvertent, (2) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken so that the S corporation is a small business corporation, or to acquire the required shareholder consents, and (3) 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. If a corporation is eligible for relief under this provision, then, notwithstanding the circumstances resulting in the ineffectiveness or termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4 sets forth additional guidance regarding inadvertent termination relief. Section 1.1362-4(b) provides that the corporation has the burden of establishing that under the relevant facts and circumstances the Commissioner should determine that the termination was inadvertent. The fact that the terminating event was not reasonably

within the control of the corporation and was not part of a plan to terminate the election, or the fact that the event took place without the knowledge of the corporation, notwithstanding its due diligence to safeguard against such an event, tends to establish that the termination was inadvertent.

Section 1.1362-4(c) provides that a corporation may request inadvertent termination relief by submitting a request for a letter ruling. Section 1.1362-4(d) provides that the Commissioner may condition the granting of a ruling request on any adjustments that are appropriate. Section 1.1362-4(e) requires the corporation and all persons who were shareholders of the corporation at any time during the time specified by the Commissioner to consent to any adjustments that the Commissioner may require.

The Service will grant relief for both the late QSST and ESBT election and the inadvertent termination of the S corporation election (or inadvertent invalid S corporation election) if the standard described in section 1362(f) for an inadvertent termination of an S corporation election or an inadvertent invalid S corporation election is satisfied.

3. Scope

.01 In General. This revenue procedure supersedes Rev. Proc. 98-55 and provides relief for a late Election Under Subchapter S (as defined in section 4.01(1) of this revenue procedure.)

Section 4.01 of this revenue procedure provides a glossary of certain terms as they are used in this revenue procedure. Section 4.02 of this revenue procedure provides the situations in which an entity is eligible for relief. Section 4.03 of this revenue procedure provides the procedural requirements for relief.

This revenue procedure provides procedures in lieu of the letter ruling process ordinarily used to obtain relief for a late Election Under Subchapter S filed pursuant to § 1362(b)(5), § 1362(f), or § 301.9100-1 and § 301.9100-3. Accordingly, user fees do not apply to corrective actions under this revenue procedure.

.02 Entities That Fail to Qualify for Relief Under This Revenue Procedure.

(1) Letter Rulings. A corporation or trust that does not meet the requirements for relief or is denied relief under this revenue procedure may request inadvertent termination, inadvertent invalid election, or late election relief (as appropriate) by requesting a letter ruling. The Service will not ordinarily issue a letter ruling if the period of limitations on assessment under § 6501(a) has lapsed for any taxable year for which an election should have been made or any taxable year that would have been affected by the election had it been timely made. The procedural requirements for requesting a letter ruling are described in Rev. Proc. 2003-1, 2003-1 I.R.B. 1 (or its successor).

(2) Rev. Proc. 97-48. Certain corporations may be eligible for automatic late S corporation election relief pursuant to Rev. Proc. 97-48, 1997-2 C.B. 521. Rev. Proc. 97-

48 provides special procedures to obtain automatic relief for certain late S corporation elections. Generally, relief is available in situations in which a corporation intends to be an S corporation, the corporation and its shareholders reported their income consistent with S corporation status for the taxable year the S corporation election should have been made and for every subsequent year, and the corporation did not receive notification from the Service regarding any problem with the S corporation status within 6 months of the date on which the Form 1120S for the first year was timely filed. Rev. Proc. 97-48 does not provide relief for late ESBT, QSST or QSub elections.

4. Relief For Late S Corporation, Esbt, Qsst And Qsub Elections Under This Revenue Procedure

.01 Definitions.

(1) Election Under Subchapter S: For purposes of this revenue procedure, Election Under Subchapter S refers to the filing of a Form 2553 by a corporation to be treated as a subchapter S corporation under § 1362, an election by a trustee to treat a trust as an ESBT under § 1361(e), an election by a trust beneficiary to treat a trust as a QSST under § 1361(d), or the filing of a Form 8869 by a parent S corporation to treat a subsidiary as a QSub under § 1361(b)(3).

(2) Due Date of Election Under Subchapter S: The Due Date of the Election Under Subchapter S will vary depending on the type of election sought. For a corporation that requests to be treated as a subchapter S corporation, the Due Date of the Election Under Subchapter S is specified by § 1362(b). For ESBT or QSST elections, the Due Date of the Election Under Subchapter S is specified by § 1.1361-1(m)(2)(iii) or § 1.1361-1(j)(6)(iii), respectively. The Due Date of the Election Under Subchapter S for a parent S corporation to make an election to treat a subsidiary as a QSub on a specific date is specified by § 1.1361-3(a)(3).

.02 Eligibility for Relief. Relief is available under section 4.04 of this revenue procedure if the following requirements are met:

- (1) The entity fails to qualify for its intended status as an S corporation, ESBT, QSST, or QSub on the first day that status was desired solely because of the failure to file the appropriate Election Under Subchapter S timely with the applicable service center;
- (2) Less than 24 months have passed since the original Due Date of the Election Under Subchapter S;
- (3) Either,
 - (a) the entity is seeking relief for a late S corporation or QSub election and the entity has reasonable cause for its failure to make the timely Election Under Subchapter S, or
 - (b) the S corporation and the entity are seeking relief for an inadvertent invalid S corporation election or an inadvertent termination of an S corporation election due

to the failure to make the timely ESBT or QSST election and the failure to file the timely Election Under Subchapter S was inadvertent; and

(4) Either,

(a) all of the following requirements are met: (i) the entity seeking to make the election has not filed a tax return (in the case of QSubs, the parent has not filed a tax return) for the first year in which the election was intended, (ii) the application for relief is filed under this revenue procedure no later than 6 months after the due date of the tax return (excluding extensions) of the entity seeking to make the election (in the case of QSubs, the due date of the tax return of the parent) for the first year in which the election was intended, and, (iii) no taxpayer whose tax liability or tax return would be affected by the Election Under Subchapter S (including all shareholders of the S corporation) has reported inconsistently with the S corporation election (as well as any ESBT, QSST or QSub elections), on any affected return for the year the Election Under Subchapter S was intended; or

(b) all of the following requirements are met: (i) the entity seeking to make the election has filed a tax return (in the case of QSubs, the parent has filed a tax return) for the first year in which the election was intended within 6 months of the due date of the tax return (excluding extensions), and (ii) all taxpayers whose tax liability or tax returns would be affected by the Election Under Subchapter S (including all shareholders of the S corporation) have reported consistently with the S corporation election (as well as any ESBT, QSST or QSub elections), on all affected returns for the year the Election Under Subchapter S was intended, as well as for any subsequent years.

.03 Procedural Requirements for Relief.

(1) Procedural Requirements When a Tax Return Has Not Been Filed for the First Year of the Intended Election Under Subchapter S. If the entity seeking the election has not filed a tax return for the first taxable year of the intended Election Under Subchapter S, the entity may request relief for the late Election Under Subchapter S by filing with the applicable service center the properly completed election form(s). The election form(s) must be filed within 18 months of the original Due Date of the intended Election Under Subchapter S (but in no event later than 6 months after the due date of the tax return (excluding extensions) of the entity (in the case of QSubs, the due date of the tax return of the parent) for the first year in which the election was intended) and must state at the top of the document "FILED PURSUANT TO REV. PROC. 2003-43." Attached to the election form must be a statement establishing either reasonable cause for the failure to file the Election Under Subchapter S timely (in the case of S corporation or QSub elections), or a statement establishing that the failure to file the Election Under Subchapter S timely was inadvertent (in the case of ESBT or QSST elections.)

(2) Procedural Requirements When a Tax Return Has Been Filed for the First Year of the Intended Election Under Subchapter S. If the entity seeking the election has filed a tax return for the first taxable year of the intended Election Under Subchapter S within 6 months of the due date of that tax return (excluding extensions), then the entity may request relief for the late Election Under Subchapter S by filing with the applicable

service center the properly completed election form(s) and the supporting documents described below. The election form(s) must be filed within 24 months of the original Due Date for the Election Under Subchapter S and must state at the top of the document "FILED PURSUANT TO REV. PROC. 2003-43." Attached to the election form must be a statement establishing either reasonable cause for the failure to file the Election Under Subchapter S timely (in the case of S corporation or QSub elections), or a statement establishing that the failure to file the Election Under Subchapter S timely was inadvertent (in the case of ESBT or QSST elections.) The following additional documents must be attached to the election form (if applicable):

(a) S Corporations. An entity seeking relief for a late S corporation election must file a completed Form 2553, signed by an officer of the corporation authorized to sign and all persons who were shareholders at any time during the period that began on the first day of the taxable year for which the election is to be effective and ends on the day the election is made. The completed election form must include the following material:

(i) Statements from all shareholders during the period between the date the S corporation election was to have become effective and the date the completed election was filed that they have reported their income (on all affected returns) consistent with the S corporation election for the year the election should have been made and for all subsequent years; and

(ii) A dated declaration signed by an officer of the corporation authorized to sign which states: "Under penalties of perjury, I declare that, to the best of my knowledge and belief, the facts presented in support of this election are true, correct, and complete."

(b) ESBTs and QSSTs. The trustee of an ESBT or the current income beneficiary of a QSST must sign and file the appropriate election with the applicable service center. The completed election form must include the following material:

(i) A statement from the trustee of the ESBT or the current income beneficiary of the QSST that includes the information required by § 1.1361-1(m)(2)(ii) (in the case of ESBT elections) or § 1.1361-1(j)(6)(ii) (in the case of QSST elections);

(ii) In the case of a QSST, a statement from the trustee that the trust satisfies the QSST requirements of § 1361(d)(3) and that the income distribution requirements have been and will continue to be met;

(iii) In the case of an ESBT, a statement from the trustee that all potential current beneficiaries meet the shareholder requirements of § 1361(b)(1) and that the trust satisfies the requirements of an ESBT under § 1361(e)(1) other than the requirement to make an ESBT election;

(iv) A statement from the trustee of the ESBT or the current income beneficiary of the QSST that the beneficiary or trustee acted diligently to correct the mistake upon its discovery;

(v) Statements from all shareholders during the period between the date the S corporation election terminated or was to have become effective and the date the completed election was filed that they have reported their income (on all affected returns) consistent with the S corporation election for the year the election should have been made and for all subsequent years; and

(vi) A dated declaration, signed by the trustee of the ESBT or the current income beneficiary of the QSST which states: “Under penalties of perjury, I declare that, to the best of my knowledge and belief, the facts presented in support of this election are true, correct, and complete.”

(c) QSubs. An S corporation seeking relief for a late QSub election for a subsidiary must file a completed Form 8869. The completed election form must include the following material:

(i) A statement that the corporation satisfies the QSub requirements of § 1361(b)(3)(B), and that all assets, liabilities, and items of income, deduction, and credit of the QSub have been treated as assets, liabilities, and items of income, deduction, and credit of the S corporation (on all affected returns) consistent with the QSub election for the year the election was intended and for all subsequent years;

(ii) A dated declaration signed by an officer of the S corporation authorized to sign which states: “Under penalties of perjury, I declare that, to the best of my knowledge and belief, the facts presented in support of this election are true, correct, and complete.”

.04 Relief for Late Election Under Subchapter S. Upon receipt of a completed application requesting relief under section 4.03 of this revenue procedure, the Service will determine whether the requirements for granting additional time to file the Election Under Subchapter S have been satisfied and will notify the entity of the result of this determination.

5. Effect On Other Documents

Rev. Proc. 98-55 is superseded.

6. Effective Date

.01 In general. This revenue procedure is effective June 9, 2003. Any entity that meets the requirements of this revenue procedure as of June 9, 2003, may seek relief under this revenue procedure. This revenue procedure applies to requests pending with the service center pursuant to Rev. Proc. 98-55 on June 9, 2003, and to requests received thereafter. It also applies to all letter ruling requests pending in the national office on June 9, 2003, and all future requests for relief.

.02 Transition rule for pending letter ruling requests. If an entity has filed a request for a letter ruling seeking relief for a late Election Under Subchapter S and that letter ruling request is pending in the national office on June 9, 2003, the entity may withdraw that letter ruling request and receive a refund of its user fee. However, the national office will process letter ruling requests pending on June 9, 2003, unless, prior to the earlier of July 24, 2003, or the issuance of the letter ruling, the entity notifies the national office that it will withdraw its letter ruling request.

7. Paperwork Reduction Act

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1548.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collections of information in this revenue procedure are in section 4.03. This information is required to be submitted to the applicable service center in order to obtain relief for a late Election Under Subchapter S. This information will be used to determine whether the eligibility requirements for obtaining relief have been met. The collection of information is required to obtain a benefit. The likely respondents are business or other for-profit institutions.

The estimated total annual reporting burden is 25,000 hours.

The estimated annual burden per respondent varies from .5 hours to 7 hours, depending on individual circumstances, with an estimated average burden of 1 hour to complete the statement. The estimated number of respondents is 25,000.

The estimated annual frequency of responses is on occasion.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by 26

U.S.C. 6103.

8. Drafting Information

The principal author of this revenue procedure is Jason T. Smyczek of the Office of the Associate Chief Counsel (Passthroughs and Special Industries.) For further information regarding this revenue procedure contact Mr. Smyczek at (202) 622-3050 (not a toll free call).

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