

**Internal Revenue Service**

Department of the Treasury

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Person to Contact:

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DO:  
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LEGEND:

A =  
B =

Company =

Date 1 =  
Date 2 =  
Date 3 =  
Date 4 =  
Date 5 =  
Date 6 =

Old Parent =

New Parent =

Year 1 =  
Year 2 =

Dear :

This letter responds to your September 3, 1999, request for a private letter ruling as to whether Company timely filed its election for possessions corporation status under sections 936 and 30A of the Internal Revenue Code ("Code") pursuant to the circumstances described below.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

FACTS and REPRESENTATIONS:

Company has provided the following facts and representations in its submission.

Company was incorporated under state A law in Year 1 and has, since then, engaged in B business in Puerto Rico. Since Year 1, Company has filed its tax returns using the accrual method of accounting on the basis of a calendar year. Company's issued and outstanding shares were held indirectly by Old Parent, the common parent of an affiliated group.

For a period of approximately twenty years, Company elected possessions corporation treatment ("936 election") under Code sections 936(a) and (e). This election remained in effect until it was revoked for Company's tax year ending Date 1. Prior to its tax year ending Date 1, Company had not been included in the consolidated return of the affiliated group of which it was a member because as a 936 corporation, it was not an "includible corporation" under Code sections 1504(a) and 1504(b). Subsequent to revoking of its 936 election, Company was included in Old Parent's consolidated return for consecutive tax years ending Date 1 and Date 2, and for its short tax year ending Date 4.

On Date 4, all of Old Parent's assets were acquired by New Parent in what has been represented as a statutory merger. Company became an indirect subsidiary of New Parent as a result of the merger. Old Parent filed a short-period consolidated income tax return covering a three month period from Date 3 to Date 4, and included Company on this consolidated return. As a result, Company began a new short tax year on Date 5, a day immediately following Date 4, with its short tax year ending Date 6.

On March 15, Year 2, in the year following the Date 4 merger, New Parent filed a Form 7004 ("Application for Automatic Extension of Time to File Corporation Income Tax Return") requesting an automatic six month extension of time (until September 15, Year 2) to file its Federal income tax return for its tax year ending Date 6, which included the Date 4 merger. The request for an automatic extension of time included Company, as well as other members of New Parent's affiliated group. Company was not included in New Parent's Form 851 ("Affiliation Schedule") or its Form 1122 ("Authorization and Consent of Subsidiary Corporation to be Included in Consolidated Income Tax Return") for its tax year ending Date 6. New Parent represents that when it filed the Form 7004 on March 15, Year 2, for its tax year ending Date 6, it was not familiar with the international operations of Old Parent, and additionally was unaware that Company

would satisfy the requirements for treatment as a possessions corporation for tax year ending Date 6. New Parent claims that it became aware of a possible 936 election for Company subsequent to the filing of Form 7004 for tax year ending Date 6.

Company represents that it was an "existing credit claimant" on October 13, 1995, as required by Code section 936(j)(9) and that it is therefore able to elect possessions corporation treatment pursuant to Code sections 936 and 30A for its short tax year ending Date 6, provided its election were deemed timely filed. Company claims that it will have filed a Form 5712 ("Election to Be Treated as a Possessions Corporation Under Section 936") on or before September 15, Year 2. Additionally, Company represents that it will not join in the consolidated return for New Parent's tax year ending Date 6 and that it will file separate Forms 1120 ("U.S. Corporation Income Tax Return") and 5735 ("Possessions Corporation Tax Credit (Under Section 936 and Section 30A)") for its short tax year ending Date 6. Finally, Company represents that it has met all requirements to qualify for an automatic extension to file a Federal income tax return.

#### RULINGS REQUESTED:

Company has requested the following rulings.

1. Whether the Form 7004 filed by New Parent on March 15, Year 2, constitutes a request for an extension for Company to timely file a separate income tax return for its short tax year beginning Date 5 and ending Date 6.
2. Whether the Form 7004 filed by New Parent on March 15, Year 2, requires Company to join in the filing of a consolidated return with New Parent for the consolidated tax year ending Date 6.
3. Whether an election to claim the tax credit under Code sections 936 and 30A for Company's tax year beginning Date 5 and ending Date 6 is a timely election, if filed by Company on or before September 15, Year 2.

#### LAW and ANALYSIS:

##### A. Background

Company revoked its possessions corporation election while indirectly owned by Old Parent. As a result, Company was included on Old Parent's consolidated return for two taxable years, and a short-period reflecting the three months prior to New Parent's Date 4 acquisition of Old Parent's assets, including Company. Company now requests a ruling as to whether an election under Code sections 936 and 30A was timely filed for

its short tax year beginning Date 5 and ending Date 6, following its acquisition by New Parent.

Sections 936(a) and (e) provide for an election for a corporation to be treated as a possessions corporation under section 936. Section 936(a) generally provides a credit against U.S. income tax in an amount equal to tax attributed to non-U.S. source taxable income from the active conduct of a trade or business within a U.S. possession. The Small Business and Job Protection Act of 1996 enacted certain provisions that phase out section 936 of the Code over ten years, eliminating it entirely for taxable years beginning after December 31, 2005. Section 936(j)(1) states that, except as otherwise provided in section 936(j), the section 936 possession credit does not apply to any tax year beginning after December 31, 1995. Section 936(j)(2) further provides that “existing credit claimants” may continue to elect the credit under sections 936(a)(1)(A) or 30A(a)(1)(A), under limited conditions. For those taxpayers operating in Puerto Rico who have not elected the percentage limitation under section 936(a)(4)(B), the rules of section 30A apply for tax years beginning after December 31, 1995.

The rules of section 936 are to be used in applying section 30A. Section 30A(e)(1) states that the provisions of section 936 (including any applicable election thereunder) shall apply in the same manner as if the credit under section 30A were a credit under section 936(a)(1)(A). Section 30A(e)(2) provides that the credit under section 30A is treated in the same manner as the credit under section 936. Section 30A(e)(3) provides that a corporation to which section 30A applies shall be treated as if it were a corporation electing section 936. Finally, section 30A(f) provides that any term used in section 30A shall have the meaning given such term by section 936.

Here, Company has represented that it qualifies for the Puerto Rico economic activity credit under section 30A, and that it is an “existing credit claimant” under Code section 936(j)(9). Whether Company’s section 936 election was timely made for its tax year ending Date 6 depends on the following: first, whether the Form 7004 filed by New Parent is deemed to include Company in the request for an extension to file a Federal income tax return and Form 5735; and second, whether the Form 7004 filed by New Parent requires Company to join in the consolidated return with New Parent for tax year ending Date 6.

## B. Form 7004

### 1. Automatic Extensions of Time to File a Federal Income Tax Return

Code section 6012(a)(2) requires the filing of income tax returns by corporations subject to tax under subtitle A. Code section 6072(b) provides, in part, that returns of corporations under section 6012 made on the basis of a calendar year must be filed on or before the 15th day of March following the close of the calendar year.

Pursuant to section 6081(a), the Secretary has authority to grant extensions of up to six months for the filing of returns. Treas. Reg. section 1.6081-3(a) provides that if the following three requirements are met, a corporation will be allowed an automatic extension of time to file its income tax return to the 15th day of the sixth month following the month in which falls the date prescribed for the filing of its income tax return. First, the application for extension must be prepared on a Form 7004 and be signed by a person authorized by the corporation to request the extension. Second, the application must be filed on or before the date prescribed for filing the return of the corporation. Third, the corporation must make a remittance on or before the date prescribed for payment of the amount of the properly estimated unpaid tax liability.

Treas. Reg. section 1.6081-3(b) provides, in part, that the filing of an application for an automatic extension of time for a consolidated return shall be made by a person authorized by the parent corporation to request such an extension. A statement listing the name and address of each member of the affiliated group for which such consolidated return will be made must be attached to the application. Upon the timely filing of the Form 7004 with the Service, the six month extension shall be considered as granted to the affiliated group for the filing of its consolidated return or for the filing of each member's separate return.

In this case, Company became a remote subsidiary of New Parent on Date 4, as a result of a statutory merger in which New Parent acquired the assets of Old Parent. Subsequently, New Parent filed Form 7004 to extend the date for filing its tax return for its tax year ending Date 6. Attached to the Form 7004 was a statement listing the members of the affiliated group, including Company. Both Company and New Parent file their income tax returns on the basis of the calendar year.

Under Treas. Reg. section 1.6081-3(b), the filing of Form 7004 grants an extension both for the filing of a consolidated return and for the filing of separate returns by members of the affiliated group. Thus, provided the requirements of Treas. Reg. section 1.6081-3 were satisfied, the Form 7004 filed by New Parent was a valid extension request and, as a result, Company was granted a six month extension to file its separate return for tax year ending Date 6. Thus, the due date for Company to file its tax return for its tax year ending Date 6 is September 15, Year 2.

## 2. Filing a Consolidated Return for an Affiliated Group

Code section 1501 provides that an affiliated group of corporations shall have the privilege of making a consolidated return with respect to the income tax imposed by Chapter 1 for the tax year in lieu of filing separate returns. The making of a consolidated return shall be upon the condition that all corporations, which at any time during the tax year have been members of the affiliated group, consent to all the consolidated return regulations prescribed under section 1502 prior to the last day prescribed by law for the filing of such return. In the case of a corporation which is a

member of the affiliated group for a fractional part of the year, the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

Code section 1504(a)(1) provides that an “affiliated group” includes a common parent and includible corporations, which meet certain ownership requirements not at issue herein. Section 1504(b)(4) provides that, for purposes of Chapter 6 (Consolidated Returns), the term “includible corporation” does not include a corporation with respect to which an election under section 936 is in effect for the tax year.

Treas. Reg. section 1.1502-76(b)(1)(ii) provides that, if a corporation becomes or ceases to be a member of a group during a consolidated return year, it becomes or ceases to be a member at the end of the day on which its status as a member changes, and its tax year ends for all Federal income tax purposes at the end of that day.

Treas. Reg. section 1.1502-75(d)(1) provides that a group remains in existence for a tax year if the common parent remains as the common parent and at least one subsidiary that was affiliated with it at the end of the prior year remains affiliated with it at the beginning of the year, whether or not one or more corporations have ceased to be subsidiaries at any time after the group was formed.

Based on the facts presented and representations made by Company, Old Parent’s consolidated group terminated at the end of the day on Date 4, and the tax period of Company and all other members of Old Parent’s group closed at the end of the day on Date 4, the date of the acquisition of Old Parent’s assets by New Parent. Treas. Reg. §§ 1.1502-75(d)(1); 1.1502-76(b)(1)(ii). A new tax year of Company began on Date 5 and ended on Date 6. To the extent that Company was an includible corporation for its short tax year ending Date 6, its income would be includible in the consolidated return of New Parent for the period ending Date 6. I.R.C. § 1501.

The mere inclusion of Company on the Form 7004 filed by New Parent is not considered an exercise of the privilege of making a consolidated return. Revenue Ruling 55-560, 1955-2 C.B. 379. Nevertheless, if Company had been an includible corporation for its short tax year ending Date 6, it would have been compelled to join in the filing of any consolidated return of New Parent. I.R.C. § 1501. If, however, on or before September 15, Year 2, Company properly elects treatment as a possessions corporation under sections 936 and 30A for its short tax year ending Date 6, Company will have become a corporation that was not includible in the New Parent group for tax year ending Date 6. I.R.C. § 1504(b)(4). A possessions corporation is not an “includible corporation” under Code sections 1504(a) and 1504(b). Thus, Company would be ineligible to join in a consolidated return with New Parent for the tax period ending Date 6. I.R.C. § 1504(a).

C. Electing the Puerto Rico Economic Activity Credit Under Sections 936 and 30A

As previously noted, Company has represented that it is an existing credit claimant and that it otherwise meets the requirements to elect the Puerto Rico economic activity credit under sections 936(a) and 30A.

Treas. Reg. section 1.936-1(a) provides that a domestic corporation shall make an election under § 936(e), for any tax year beginning after December 31, 1975, by filing Form 5712 on or before the later of (1) the date on which such corporation is required, pursuant to Code sections 6072(b) and 6081, to file its Federal income tax return for the first tax year for which the election is made; or (2) April 8, 1980.

Here, we conclude that Company was required to file its Federal income tax return on or before September 15, Year 2, based on the Form 7004 filed by New Parent on March 15, Year 2. As noted above, the Form 7004 granted an extension for both the filing of New Parent's consolidated return for its tax year ending Date 6, as well as Company's filing of its separate return for its short tax year beginning Date 5 and ending Date 6. Company was not required to join in New Parent's consolidated return. Based on Company's representations that it met all requirements to qualify for an automatic six month extension to file its short period income tax return, the election will have been timely filed where Company's Forms 5712, 5735 and Federal income tax return for its short tax year were filed on or before September 15, Year 2.

RULINGS:

Based on the facts and representations received, and subject to the caveats below, we rule as follows:

1. The filing of Form 7004 by New Parent on March 15, Year 2, is considered a request for an extension of time to file a separate income tax return by Company for its short tax year beginning Date 5 and ending Date 6.
2. The filing of Form 7004 by New Parent on March 15, Year 2, does not require Company to join in the filing of a consolidated return with New Parent for the consolidated tax year ending Date 6.
3. The making of an election as described in sections 936(a) and (e) by Company on or before September 15, Year 2, is a timely election of the tax credit under sections 936 and 30A for the short tax period of Company beginning Date 5 and ending Date 6.

We express no opinion as to the Federal income tax treatment of the proposed

transaction under other provisions of the Code and regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the ruling. We specifically express no opinion as to whether the Date 4 acquisition by New Parent of all the assets of Old Parent qualifies for reorganization treatment under section 368. Further, this ruling is effective only to the extent that the Date 4 acquisition by New Parent of all the assets of Old Parent was not a reverse acquisition, as defined in Treas. Reg. § 1.1502-75(d)(3). Additionally, we express no opinion as to whether Company meets the requirements for the section 936 and section 30A credit, nor do we opine on whether Company qualifies as an existing credit claimant.

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

A copy of this letter must be attached to any income tax return to which it is relevant.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer and its authorized representative.

Sincerely,

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Anne P. Shelburne  
Assistant to the Branch Chief  
CC:INTL:BR6

cc: