Internal Revenue Service

Number: **200736003**
Release Date: 9/7/2007

Index Number: 9100.00-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:ITA:B03
PLR-106582-07
Date:
May 31, 2007

TY:

Legend

taxpayer	=
Date 1	=
Sub1	=
Year 5	=
Sub 2	=
Year 4	=
Accounting Firm 1	=
Year 1	=
Year 2	=
Year 3	=
Accounting Firm 2	=
Accounting Firm 3	=
Year 6	=
Year 7	=
Individual 1	=

Dear :

This responds to your letter of requesting an extension of time, under §§ 301.9100-1 and -3 of the Procedure and Administration Regulations, for the taxpayer to make consent dividend elections pursuant to § 565 of the Internal Revenue Code.

The taxpayer is the common parent of an affiliated group that files a federal consolidated income tax return. The taxpayer and its subsidiaries are accrual method taxpayers with a fiscal year end of Date 1.

Sub 1 was a wholly owned subsidiary of the taxpayer. Sub 1 merged with and into the taxpayer at the end of the taxable year of Year 5 in a transaction that qualified as a liquidation under § 332. Sub 1 was an operating company that owned intellectual property consisting of patents and 'know how' licensed to the taxpayer and other affiliates of the taxpayer. Sub 2 was a wholly owned subsidiary of the taxpayer. Sub 2 liquidated in Year 4 in a transaction qualifying under § 332. Sub 2 was incorporated as a holding company to facilitate the acquisition of a distribution company.

Prior to the examination by Accounting Firm 1 in connection with a potential purchase of the taxpayer's common stock, the taxpayer, its related subsidiaries, or accounting firms retained by the taxpayer were unaware that Sub 1 and Sub 2 were personal holding companies during the years at issue. Therefore, the taxpayer, the subsidiaries and the accounting firms were not aware of any need for making consent dividend elections for those years. The specific facts follow:

For the taxable years ending in Year 1, Year 2, Year 3, Year 4, and Year 5, the taxpayer failed to include Forms 972 and 973 in its federal tax returns. While the taxpayer's tax department was aware of the PHC rules, the department had no experience with these rules and believed that they were inapplicable to publicly traded operating companies. Further, the potential PHC issue was not discovered in audit by the IRS, Accounting Firm 2 or Accounting Firm 3. In November of Year 7, during the financial review and tax due diligence of the taxpayer's books, Accounting Firm 2 determined that the taxpayer may be subject to the PHC tax. Accounting Firm 2 pointed out to the taxpayer that § 542(b)(2) required the taxpayer test each separate company in the consolidated group to see if each separate company qualified as a PHC. The taxpayer immediately took steps to determine whether any of the group companies were subject to PHC tax by applying the tests of § 542(b)(2). Applying the rules on a separate company by company basis, Sub 2 and Sub 1 were identified as PHCs.

The taxpayer was not aware of the liability for PHC tax or of the need to make the consent dividend elections at the time the group's consolidated income tax returns were filed. In Year 1 and Year 4, Sub 2 was a PHC as greater than 60% of its income was PHC income. However for those tax years, Sub 2 had no undistributed PHC income as it was in a taxable loss position. In Year 2, Year 3, Year 4 and Year 5, Sub 1 qualified as a PHC. However, due to a dividend paid in Year 7 that qualified as an excess dividend under § 564(a), the dividend offset the undistributed PHC income for Year 1 and Year 2. Due to the two year limitation, the dividend can not be used to offset the undistributed PHC income for Year 3 or Year 4. As Sub 1 liquidated in Year 5, any undistributed PHC income would have been distributed at that time, so there was no undistributed PHC income in that year. The taxpayer represents that if it had known

of the PHC issue, the taxpayer would have agreed to the Sub 1's consent dividends for the taxable years of Year 3 and Year 4. The actual or deemed dividend would not have impacted the taxpayer's consolidated income tax return because the income received by the taxpayer would have been eliminated under the consolidated rules of § 1.1502-13 of the Income Tax Regulations.

The failure to make consent divided elections was due to the oversight of the taxpayer's tax department who prepared the consolidated federal income tax returns of the taxpayer and its subsidiaries. Individual 1, the manager of the tax department, acknowledges this error by a sworn affidavit.

Ruling Requested

The taxpayer requests that it be granted an extension of time under § 301.9100 to file the election under section 565(a) to declare a consent dividend for the undistributed PHC income of Sub 1 for its tax years ending Date 1, Year 3 and Year 4. The election under section 565(a) will be treated as timely made with the taxpayer's income tax return for the taxable year ending Date 1, Year 3 and Year 4.

Law and Analysis

Section 565(a) provides that if any person owns consent stock (as defined in § 565(f)(1)) in a corporation on the last day of the taxable year of such corporation and such person agrees, in a consent filed with the return of such corporation in accordance with the regulations, to treat as a dividend the amount specified in such consent, the amount so specified shall, except as provided in § 565(b), constitute a consent dividend for purposes of § 561 (relating to the deduction for dividends paid).

Section 1.565-1(a) of the Income Tax Regulations provides that the dividends paid deduction, as defined in § 561, includes the consent dividend for the taxable year. A consent dividend is a hypothetical distribution made by certain corporations to any person who owns consent stock on the last day of the taxable year of such corporation and who agrees to treat the hypothetical distribution as an actual dividend, subject to specified limitations, by filing a consent at the time and in the manner specified in § 1.565-1(b). Section 1.565-1(b)(3) provides that a consent may be filed not later than the due date of the corporation's income tax return for the taxable year for which the dividends paid deduction is claimed. Under Rev. Rul. 78-296, 1978-2 C.B. 183, the due date for purposes of § 1.565-1(b)(3) includes the extended due date of a return filed pursuant to an extension of the time to file.

Section 301.9100-3 of the Procedure and Administration regulations generally provides extensions of time for making regulatory elections. For this purpose, § 301.9100-1(b) defines the term "regulatory election" to include an election whose

deadline is prescribed by a revenue ruling, revenue procedure, notice or announcement published in the Internal Revenue Bulletin.

Sections 301.9100-1 through 301.9100-3 of the regulations provide extensions of time to make a regulatory election. Section 301.9100-2 provides an automatic 6 month extension of time to make a regulatory election, predicated upon the taxpayer's timely filing of their tax return for the relevant tax year. Section 301.9100-3 provides extensions of time for making regulatory elections that do not meet the requirements of section 301.9100-2. Section 301.9100-3(a) provides that a request for relief under section 301.9100-3 will be granted when the taxpayer provides evidence (including affidavits described in paragraph (e) of this section) to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the government.

Section 301.9100-3(b)(1) states that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer –

(i) requests relief before the failure to make the regulatory election is discovered by the Service;

(ii) inadvertently failed to make the election because of intervening events beyond the taxpayer's control;

(iii) failed to make the election because, after exercising due diligence, the taxpayer was unaware of the necessity for the election;

(iv) reasonably relied on the written advice of the Service; or

(v) reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make, the election.

Section 301.9100-3(b)(1)(v) of the regulations provides in part that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer relied on a qualified tax professional, and the tax professional failed to make the election. Section 301.9100-3(b)(2) of the regulations provides that there is no reasonable reliance if the taxpayer knew or should have known that the professional was not competent to render advice on the regulatory election or was not aware of all relevant facts.

Section 301.9100-3(b)(3) of the regulations provides in part that a taxpayer is deemed to have not acted reasonably and in good faith if the taxpayer:

i) Seeks to alter a return position for which an accuracy-related penalty has been or could be imposed under section 6662 at the time the taxpayer requests relief;

ii) Was informed in all material respects of the required election and related tax consequences but chose not to file the election; or

iii) Uses hindsight in requesting relief. If specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer, the IRS will not ordinarily grant relief. In such a case, the

IRS will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

Section 301.9100-3(c) of the regulations provides in part that the interests of the government are prejudiced if granting relief would result in the taxpayer having a lower tax liability in the aggregate, for all taxable years affected by the election, than the taxpayer would have had if the election had been timely made (taking into account the time value of money). This section also provides that the interests of the government are prejudiced if the taxable year in which the regulatory election should have been made or any taxable years that would have been affected by the election had it been timely made are closed by the period of limitations on assessments under section 6501(a) before the taxpayer's receipt of a ruling granting relief under this section.

In the present case, taxpayer has demonstrated that it acted reasonably and in good faith in that it requested relief before the failure to make the election was discovered by the IRS, and it reasonably relied on Individual 1 and its tax department who failed to make the election because although aware of the PHC rules, were unaware of the necessity to make the election.

The taxpayer is not attempting to alter a return position taken for which a penalty has been or could have been imposed under §6662. Further, the taxpayer was not informed of the need to make the elections under § 565 of the Code and so did not make any conscious choice as to whether or not to make the elections. In addition, there is no indication that taxpayer is using hindsight, as defined above, in requesting this relief. Specific facts have not changed since the original deadline that made the election advantageous to the taxpayer.

In the present case, granting the relief requested will not prejudice the interests of the government under the given criteria. The disclosed circumstances indicate that the omission the taxpayer now seeks to correct originated from a mistake on the part of its tax department, and not from a desire to avoid taxes and relief was requested before the failure was discovered by the Service. Granting this application will not prejudice the interests of the government.

Accordingly, the consent of the Commissioner is hereby granted for an extension of the time to file the forms necessary to make the § 565 consent dividend election for the taxable years ending Year 3 and Year 4. This extension shall be for a period of 45 days from the date of this ruling. Please attach a copy of this ruling to the returns, schedules, and forms filed in connection with making this election under § 565 when such forms are filled.

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.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

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.

Sincerely,

Christopher F. Kane
Branch Chief, Branch 3
(Income Tax & Accounting)

cc: