

Internal Revenue Service

Department of the Treasury

Number: **200129021**
Release Date: 7/20/2001
Index No.: 7519.00-00

Washington, DC 20224

Person to Contact:
A. Katharine J. Kiss, ID No. 50-03990
Telephone Number:
(202) 622-4920
Refer Reply To:
CC:ITA:2 – PLR-119047-00
Date:
April 19, 2001

LEGEND:

X =

B =

M =

N =

Dear _____ :

This letter is in response to your request for a ruling that the gain by the taxpayer, X, from the sale of a significant portion of its business is excludible for purposes of computing the required payment under § 7519 of the Internal Revenue Code.

FACTS:

X is an S corporation that elected under § 444(a) to have a taxable year other than its required taxable year. As such, X is obligated to comply with the requirements of § 7519 and the regulations thereunder. On M, X sold a substantial segment of its business to an unrelated third party and realized a large gain.

B, an individual whose taxable year is the calendar year and who uses the cash basis method of accounting, owns 100 percent of the issued and outstanding stock in X. Most of the gain arising from X's sale is subject to reporting on B's return due by N. Thus, this portion of the gain is deferred to B for a period of 12 months more than if X had retained its required taxable year. The remainder of the gain is subject to reporting on B's return due for the following year.

X contends that because the gain from the sale of a significant portion of its business is a one-time event, it should not be taken into account in computing X's required payment. X also contends that because B will be taxed at a rate lower than the applicable rate under § 7519, § 7519 should not be applied. X cites no authority for the ruling requested.

LAW:

Under § 444(a), an S corporation may elect a taxable year different than its required taxable year. Section 7519 provides, in general, that for any taxable year for which an election under § 444 is in effect, an S corporation may be obligated to make a required payment. Section 7519(b) requires that the highest rate of tax in effect under § 1, plus 1 percentage point, be multiplied by the entity's net base year income. The amount, if any, by which the product exceeds the net required payment balance is the required payment for the applicable election year.

In order to compute an entity's net base year income, the net income for the base year must be determined. Section 7519(d)(1). Section 7519(d)(2) provides, in part, that in computing net base year income, an S corporation's net income shall be the amount (not below zero) determined by taking into account the aggregate amount of the items described in § 1366(a), other than credits and tax-exempt income. Section 1366(a)(1)(a) provides, in general, that all items of income shall be taken into account.

Section 806 of the Tax Reform Act of 1986, 1986-3 (Vol. 1) C.B. 1, 279, generally required S corporations to conform their taxable years to the taxable years of their owners. H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. II-318, 1986-3 (Vol. 4) C.B. 318. See also H.R. Conf. Rep. 495, 100th Cong., 1st Sess. 938, 1987-3 C.B. 938. Section 444, allowing an S corporation to elect a taxable year other than the required taxable year, was added by § 10206(a) of the Omnibus Budget Reconciliation Act of 1987, 1987-3 C.B. 117. Section 10206(b) of the same act added § 7519. Required payments under § 7519 "are intended to represent the value of tax deferral obtained by the owners of those entities through the use of a taxable year different from the required taxable year." Notice 89-41, 1989-1 C.B. 682.

Congress clearly intended that required payment calculations by an S corporation include income attributable to the sale of a large segment of a business. In determining net income under § 7519(d), all items described in § 1366(a) are taken into account, except for credits and tax-exempt income. Further, the required payment calculation is made using a rate in excess of the highest rate of tax imposed by § 1, regardless of whether the income will ultimately be taxed to the shareholder at a lower rate. The ruling requested by X is clearly proscribed by § 7519.

CONCLUSION:

In determining its net income for the purpose of computing its required payment under § 7519, X must take into account the gain from the sale of a significant portion of its business.

CAVEATS:

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under § 6110.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any item discussed or referenced in this letter.

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

Sincerely,

Associate Chief Counsel
(Income Tax & Accounting)

By: _____
Robert A. Berkovsky
Chief, Branch 2

cc: Area Director, Field Compliance, SB/SE

cc: