



STATE OF DELAWARE
DEPARTMENT OF FINANCE
DIVISION OF REVENUE
CARVEL STATE BUILDING
820 N. FRENCH STREET
P.O. Box 8911
WILMINGTON, DELAWARE 19899-8911

DIVISION OF REVENUE

TECHNICAL INFORMATION MEMORANDUM 98-2 FINAL

AUGUST 7, 1998

SUBJECT: EFFECT OF FEDERAL SMALL BUSINESS JOB PROTECTION ACT

Purpose of Regulation -- The purpose of this regulation is to explain the effect of the Small Business Job Protection Act of 1996, Pub. L. No. 104-188, 110 Stat 1755 (the Act), as it relates to Subchapter S corporations, the relationship between the classification of organizations for federal and state tax purposes and the procedures for electing entity classification.

The Act amended Subchapter S of the IRC by revising the manner in which Federal S corporations may organize. The revisions affected among other things, the number of permissible shareholders, the types of shareholders, affiliations with other corporations, elections and reelections. In general, such revisions are applicable to the State treatment of S corporations.

Authority to make regulations; general information --

- (i) The Director of Revenue is charged with the administration and enforcement of all state tax laws unless such duties are expressly conferred upon another agency. 30 Del. C. §563
- (ii) Published regulations are made and promulgated pursuant to authority vested in the Director. 30 Del. C. §563
- (iii) As used in published regulations, references to a section (§) number refer to a section of the Delaware Code. References to a section (§) number preceded by a "1", as in §1.1900.2, refer to sections of regulations published by the Division of Revenue of this State.

REGULATION:

§1.1900.2 In general; Classification of organizations for state tax purposes; election of entity classification.

- (a) Meaning of terms -- Any term used in these regulations shall have the same meaning as when used in a comparable context in the laws and income tax regulations of the United States referring to federal income taxes, unless a different meaning is clearly required. Any reference to the laws of the United States or to the Internal Revenue Code shall mean the Internal Revenue Code of 1986 [26 U.S.C. § 1 et seq.] as amended and regulations and amendments thereto and other laws of the United States relating to federal income taxes, as the same may be or become effective, for the taxable year.
- (b) Classification of entities -- The classification of entities for Delaware tax purposes shall be as prescribed for federal tax purposes. Unless inconsistent with Delaware law, the provisions of Sections 1361 through 1379 of the Regulations to the Internal Revenue Code of 1986 are hereby adopted for Delaware purposes.
- (c) Section 1361(b)(3)(B) defines the term "qualified subchapter S subsidiary" (QSSS) as a domestic corporation that is not an ineligible corporation, if (1) an S corporation holds 100 percent of the stock of the corporation, and (2) that S corporation elects to treat the subsidiary as a QSSS. Section 1361(b)(3)(A) provides that a corporation that is a QSSS is not treated as a separate corporation, and all assets, liabilities, and items of income, deduction, and credit of the QSSS are treated as assets, liabilities, and items of income, deduction, and credit of the parent S corporation.
- (d) Notice of election to be classified as a QSSS -- A valid election under the rules prescribed by the Internal Revenue Service by a parent S corporation to treat a wholly owned subsidiary as a QSSS shall be valid for State purposes upon making the federal election.
- (e) Tax return requirements -- Entities carrying on a trade or business within this State are subject to the provisions of Title 30 of the Delaware Code and are required to file income tax returns for such years. An S corporation which has elected to treat a subsidiary which is conducting business in this State as a QSSS shall be a taxable entity in this State and the items of income, deductions and apportionment factors of the QSSS shall be included on the income tax return of the S corporation.
- (f) Notwithstanding subsection (e), a QSSS is subject to the licensing and gross receipts provisions of Title 30 of the Delaware Code with respect to its business activities conducted within the State.
- (g) Effective date of this regulation -- This regulation is effective as of January 1, 1997.
- (h) Contact Person -- For more information about these regulations or the classification of entities, contact **John J. Maciejewski, Jr., Assistant Director, Office of Business Taxes, State of Delaware Division of Revenue, 820 N. French Street, Wilmington, Delaware 19801** or phone (302) 577-8450.


William M. Remington
Director of Revenue