time of the lien release described below, the servicer of the loan knew or had reason to know that the fair market value of X_{10} had been positive at origination.

(ii) At the time when the loan was originated and the liens were created, the fair market values of the ten properties securing the loan were as shown in the center column below. Except for property X_{10}>, the appraised values at that time were the same. Immediately before and after the lien release, the fair market values of properties X_2> through X_{10}> were as shown in the right-hand column below. (Except for property X_{10}>, the information in this table is the same as that in Facts (ii) of Example 2.)

Real Property Interest	Fair market value at origination	Fair market value at lien release
X_1	$20 million	n/a
X_2	$5 million	$3.25 million
X_3	$25 million	$16.25 million
X_4 through X_9	$60 million	$39 million
X_{10}	Greater than zero	Greater than zero

(iii) After Date 1 B exercised its right to demand a release of the lien on property X_{10} (the outparcel). *B* did not make any payment on the loan in connection with the lien release.

(2) *Analysis.*

(i) Under § 1.860G–2(a)(8), *R*'s release of the lien on property X_{10} causes the loan to cease to be a qualified mortgage unless the release takes place in a transaction that satisfies either paragraph (a)(8)(i) or paragraph (a)(8)(ii) of § 1.860G–2. The lien release on property X_{10} does not satisfy § 1.860G–2(a)(8)(ii) because it is not pursuant to a defeasance. The lien release on property X_{10} satisfies § 1.860G–2(a)(8)(i) only if the transaction in which it occurs meets the requirements of both § 1.860G–2(a)(8)(i)(A) and § 1.860G–2(a)(8)(i)(B).

(ii) The transaction in which the lien was released resulted from the exercise of an option that is unilateral within the meaning of § 1.1001–3(c)(3). Thus, the transaction is not a significant modification as defined in § 1.860G–2(b)(2) and therefore is described in § 1.860G–2(a)(8)(i)(A). In addition, however, to satisfy § 1.860G–2(a)(8)(i)(B), the loan must continue to be principally secured by an interest in real property as determined by § 1.860G–2(b)(7).

(iii) The release of the lien on X_{10} does not satisfy the 80-percent test in § 1.860G–2(b)(7)(ii) or the alternative test in § 1.860G–2(b)(7)(iii).

(iv) The unilateral right to release the lien on property X_{10} without paying down the loan is not a grandfathered transaction described in section 5.02 of this revenue procedure because *B* issued the loan after December 6, 2010.

(v) The release of the lien on property X_{10} is within the scope of section 5.03 of this revenue procedure only if it is pursuant to a "qualified paydown transaction." Under the loan documents, the allocated loan amount of property X_{10} may be zero, but that amount does not satisfy section 5.04(2) of this revenue procedure. Although property X_{10} was assigned no value for underwriting purposes, the servicer knew or had reason to know that, at origination, it had a value greater than $0. Therefore, the amount required by section 5.04(2) of this revenue procedure is greater than zero.

(vi) Because the transaction does not meet the requirements either of section 5 of this revenue procedure or of § 1.860G–2(b)(7)(ii)-(iii), § 1.860G–2(a)(8)(i)(B) is not satisfied, and § 1.860G-(a)(8) causes the loan to cease being a qualified mortgage on the date that the lien is released.

SECTION 8. EFFECTIVE DATE

This revenue procedure applies to releases of liens on interests in real property securing mortgage loans held by REMICs that are effected on or after September 16, 2009.

SECTION 9. DRAFTING INFORMATION

The principal author of this revenue procedure is Richard LaFalce of the Office of Associate Chief Counsel (Financial Institutions and Products). For further information, contact Mr. LaFalce at (202) 622–3930 (not a toll-free call).

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26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.
(Also Part I, §§ 301.7701–1, 301.7701–2, 301.7701–3.)

Rev. Proc. 2010–32

SECTION 1. PURPOSE

The Treasury Department and the Internal Revenue Service (IRS) have become aware that taxpayers are concerned about the validity of elections made by certain foreign eligible entities under § 301.7701–3(c) of the Procedure and Administration Regulations to be classified for federal tax purposes as a partnership or disregarded as an entity separate from its owner (a disregarded entity). The Treasury Department and IRS understand that these concerns arise due to uncertainty regarding the number of owners for federal tax purposes of the foreign eligible entity on the effective date of the election. To alleviate these concerns and simplify tax administration, this revenue procedure provides that, if the requirements of this revenue procedure are satisfied, the IRS will treat an election under § 301.7701–3(c) to classify a foreign eligible entity that is a qualified entity (as defined in section 3.02 of this revenue procedure) as a partnership or disregarded entity as an election to be treated as a partnership or disregarded entity (as appropriate) rather than as an association taxable as a corporation.

SECTION 2. BACKGROUND

.01 Section 301.7701–1(a)(1) states that the Internal Revenue Code (Code) prescribes the classification of various organizations for federal tax purposes. Whether an organization is an entity separate from its owners for federal tax purposes is a matter of federal tax law and does not depend on whether the organization is recognized as an entity under local law.

.02 Section 301.7701–1(b) provides that the classification of organizations that are recognized as separate entities is determined under §§ 301.7701–2, 301.7701–3, and 301.7701–4 unless a provision of the Code provides for special treatment of that organization.

.03 Section 301.7701–2(a) defines the term "business entity" as any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under § 301.7701–3 ("a disregarded entity")) that is not properly classified as a trust under § 301.7701–4 or otherwise subject to special treatment under the Code. A business entity with two or more members is classified for federal tax purposes as either a corporation or a partnership. A business entity with only one owner is classi-

fied as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as a sole proprietorship, branch, or division of the owner.

.04 Section 301.7701–3(a) provides that a business entity that is not classified as a corporation under § 301.7701–2(b)(1), (3), (4), (5), (6), (7), or (8) (an eligible entity) can elect its classification for federal tax purposes. An eligible entity with at least two members can elect to be classified as either an association (and thus a corporation under § 301.7701–2(b)(2)) or a partnership, and an eligible entity with a single owner can elect to be classified as an association or to be disregarded as an entity separate from its owner. Elections are necessary only if an eligible entity does not want its default classification or if an eligible entity chooses to change its classification.

.05 Section 301.7701–3(b)(2)(i) provides that, except for certain existing entities described in § 301.7701–3(b)(3), unless a foreign eligible entity elects otherwise, the entity is: (A) a partnership if it has two or more members and at least one member does not have limited liability; (B) an association if all members have limited liability; or (C) disregarded as an entity separate from its owner if it has a single member that does not have limited liability.

.06 Section 301.7701–3(c)(1)(i) provides that an eligible entity may elect to be classified other than as provided under § 301.7701–3(b) by filing Form 8832, *Entity Classification Election*, with the appropriate IRS Service Center. Under § 301.7701–3(c)(1)(iii), this election will be effective on the date specified by the entity on Form 8832 or on the date filed if no such date is specified on the election form. The effective date specified on Form 8832 cannot be more than 75 days prior to the date on which the election is filed and cannot be more than 12 months after the date on which the election is filed.

.07 Section 301.7701–3(c)(1)(ii) provides that an eligible entity required to file a federal tax or information return for the taxable year for which an election is made must attach a copy of its Form 8832 to its federal tax or information return for that year. If the entity is not required to file a return for that year, a copy of its Form 8832 must be attached to the federal income tax or information return of any direct or indirect owner of the entity for the taxable year of the owner that includes the date on which the election was effective.

.08 Section 301.7701–3(c)(1)(iv) provides in part that, if an eligible entity makes an election under paragraph (c)(1)(i) of this section to change its classification (other than an election made by an existing entity to change its classification as of the effective date of this section), the entity cannot change its classification by election again during the 60 months succeeding the effective date of the election. An election by a newly formed eligible entity that is effective on the date of formation is not considered a change for purposes of this paragraph (c)(1)(iv).

.09 Section 301.7701–3(c)(2)(i) provides that an election made under §301.7701–3(c)(1)(i) of this section must be signed by: (A) each member of the electing entity who is an owner at the time the election is filed; or (B) any officer, manager, or member of the electing entity who is authorized (under local law or the entity's organizational documents) to make the election and who represents to having such authorization under penalties of perjury.

SECTION 3. SCOPE

.01 *In General*. This revenue procedure provides guidance on the classification for federal tax purposes of a business entity that is a qualified entity (as defined in section 3.02 of this revenue procedure) and is in lieu of the letter ruling process ordinarily used to obtain relief for a late change of entity classification election filed pursuant to §§ 301.7701–3(c), 301.9100–1, and 301.9100–3. Accordingly, user fees do not apply to corrective actions under this revenue procedure.

.02 *Qualified Entity*. For purpose of this revenue procedure, a business entity is a "qualified entity" if the following conditions are satisfied:

(1) The business entity is an eligible entity under § 301.7701–3(a);

(2) The business entity is foreign under § 301.7701–5(a);

(3) The classification of the business entity, either by default under § 301.7701–3(b)(2)(i)(B) for a newly formed or newly relevant eligible entity, or by election under § 301.7701–3(c) for an existing relevant entity, would be or was an association taxable as a corporation;

(4) As permitted under §301.7701–3(c), the business entity filed an otherwise valid Form 8832 electing to be treated for federal tax purposes,

(a) As a partnership based on the reasonable assumption that it had two or more owners as of the effective date of the election; or

(b) As a disregarded entity based on the reasonable assumption that it had a single owner as of the effective date of the election;

(5) For federal tax purposes, either:

(a) The business entity and its actual and purported owners (or owner) have treated the entity consistently with the election on the otherwise valid Form 8832 on all filed information and tax returns; or

(b) No information or tax returns have been required to be filed since the effective date for the election made on the otherwise valid Form 8832; and

(6) The period of limitations on assessments (as established under section 6501(a) of the Code) has not ended for any taxable year of the business entity or its actual and purported owners (or owner) affected by the election made on the otherwise valid Form 8832.

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

A business entity that does not qualify for relief under this revenue procedure may request relief through the letter ruling process in accordance with Rev. Proc. 2010–1, 2010–1 I.R.B. 1 (or its successor).

SECTION 4. APPLICATION

.01 If a qualified entity files an otherwise valid Form 8832 to be classified as a partnership for federal tax purposes but it is later determined that the qualified entity had a single owner for federal tax purposes as of the effective date of the election, the IRS will treat the Form 8832 as an election to classify the qualified entity as a disregarded entity for federal tax purposes provided that:

(1) The qualified entity's actual single owner and purported owners as of the effective date of the election file original or amended returns consistent with the treatment of the entity as a disregarded entity for any taxable year that would have been affected if the election had been made to

treat the qualified entity as a disregarded entity for federal tax purposes;

(2) All required amended returns are filed before the close of the period of limitations on assessments under § 6501(a) for any relevant taxable year; and

(3) A corrected Form 8832 is filed with the appropriate Internal Revenue Service Center and a copy of the corrected Form 8832 is attached to the single owner's amended return for the taxable year during which the original election was made as required under § 301.7701–3(c)(1)(ii). The statement "FILED PURSUANT TO REVENUE PROCEDURE 2010–32" must be included across the top of the corrected Form 8832. Additionally, the corrected Form 8832 must satisfy the requirements of § 301.7701–3(c)(2)(i).

.02 If a qualified entity files an otherwise valid Form 8832 electing to be classified as a disregarded entity for federal tax purposes but it is later determined that the qualified entity had two or more owners for federal tax purposes as of the effective date of the election, the IRS will treat the Form 8832 as an election to classify the qualified entity as a partnership for federal tax purposes provided that:

(1) The qualified entity files information returns and its actual owners file original or amended returns consistent with the treatment of the entity as a partnership for any taxable year that would have been affected if the original election had been made to treat the qualified entity as a partnership for federal tax purposes;

(2) All required information and amended returns are filed before the close of the period of limitations on assessments under § 6501(a) for the relevant taxable year; and

(3) A corrected Form 8832 is filed with the appropriate Internal Revenue Service Center and a copy of the corrected Form 8832 is attached to the owners' amended returns for the taxable year during which the original election was made as required under § 301.7701–3(c)(1)(ii). The statement "FILED PURSUANT TO REVENUE PROCEDURE 2010–32" must be included across the top of the corrected Form 8832. Additionally, the corrected Form 8832 must satisfy the requirements of § 301.7701–3(c)(2)(i).

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective on September 7, 2010. Any qualified entity that meets the requirements of this revenue procedure as of September 7, 2010, may seek relief under this revenue procedure.

SECTION 6. DRAFTING INFORMATION

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