

Internal Revenue Service

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Legend:

X =

Subsidiaries =

State =

D1 =

D2 =

Dear _____ :

This responds to a letter dated February 19, 2009, submitted on behalf of X, requesting relief for inadvertent invalid subchapter S election under § 1362(f) of the Internal Revenue Code.

Facts

According to the information submitted and representations therein, X was incorporated on D1 under the laws of State and made an election to be a subchapter S corporation effective D2. In addition, X elected to treat each of Subsidiaries as a qualified subchapter S subsidiary (“QSub”). On D2, X was unaware that its two classes of stock may have prevented X from being a small business corporation eligible to elect to be treated as an S corporation. Upon discovery of the possibility of an invalid election, steps were taken immediately to qualify X as a small business corporation.

X and its shareholders agree to make any adjustments required by the Secretary consistent with the treatment of X as an S corporation.

Law and Analysis

Section 1361(a)(1) defines an “S corporation” as a small business corporation for which an election under § 1362(a) is in effect.

Section 1361(b)(1) defines a “small business corporation” as a domestic corporation which is not an ineligible corporation which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, and a trust described in subsection (c)(2), or an organization described in subsection (c)(6)) who is

not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1st day of the taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1361(b)(3)(B) defines a QSub as a domestic corporation that is not an ineligible corporation, if 100 percent of the stock of the corporation is owned by an S corporation, and the S corporation elects to treat the corporation as a QSub.

Section 1362(f) provides in part that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which made by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, (2) the Secretary determines that the circumstances resulting in such ineffectiveness were inadvertent, (3) no later than a reasonable period of time after the discovery of the circumstances resulting in such ineffectiveness, steps were taken so that the corporation for which the election was made is a small business corporation, and (4) the corporation for which the election was made, and each person who was a shareholder in such corporation at any time during the period of the ineffective S election, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness, the corporation is treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and the representations made, we conclude that X's election to be treated as an S corporation as of D2 may have been invalid and also conclude that if the election was invalid, it constitutes an inadvertent invalid election within the meaning of § 1362(f). Under the provisions of § 1362(f), X will be treated as an S corporation as of D2 and thereafter, provided that X's S corporation election is not otherwise terminated under § 1362(d). Furthermore, each of Subsidiaries will be treated as a QSub of X as of D2 and thereafter, provided that each QSub's election is otherwise valid.

This ruling is contingent upon X and all its shareholders treating X as having been an S corporation for the period beginning D2 and thereafter.

Except as specifically provided herein, no opinion is expressed or implied as to the federal tax consequences of the facts described above under any other provision of the Code. In particular, no opinion is expressed as to whether X is otherwise eligible to be an S corporation or whether Subsidiaries are otherwise eligible to be QSubs.

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.

Under a power of attorney on file in this office, a copy of this letter will be sent to your authorized representative.

Sincerely,

Faith P. Colson

Faith P. Colson
Senior Counsel, Branch 1
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2):

Copy of this letter
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cc: