Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:

Telephone Number:

Refer Reply To:
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Date:
August 06, 2010

Legend

X =

Y =

State =

D1 =
D2 =
D3 =
D4 =
D5 =
D6 =
D7 =

Dear :

This letter responds to a letter dated, February 11, 2010, and subsequent correspondence, submitted on behalf of X, requesting a ruling under § 1362(g) of the Internal Revenue Code.

FACTS

The information submitted states that X was incorporated on D1. X elected to be an S corporation effective D2, but revoked that election effective D4.

The shareholders of Y adopted an employee stock ownership plan (ESOP) effective D3. Y acquired 100 percent of the outstanding shares of X on D5. On D6, the ESOP purchased 100 percent of the issued and outstanding shares of Y from the shareholders. Y will elect to be an S corporation effective D7.

Y is requesting permission to file Form 8869, Qualified Subchapter S Subsidiary Election, on behalf of X effective D7, which is prior to the termination of the five-year waiting period imposed by § 1362(g). Y represents that its former shareholders will not make an election under § 1042 upon selling their shares of Y stock to the ESOP. Additionally, Y represents that it will not consent to any such election under §§ 4978 and 4979A.

LAW

Section 1362(a) provides that except as provided in § 1362(g), a small business corporation may elect to be an S corporation.

Section 1361(b)(1) provides, in part, that for the purposes of subchapter S, the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not (B) have as a shareholder a person (other than an estate, trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual and (D) have more than one class of stock.

Section 1361(c)(6) provides that for purposes of § 1361(b)(1)(B), an organization which is described in §§ 401(a) or 501(c)(3), and exempt from taxation under § 501(a) may be a shareholder in an S corporation. ESOPs as defined in § 4975(e)(7) are described in § 401(a) and exempt from taxation under § 501(a).

Section 1362(d)(1)(A) provides that an election under § 1362(a) may be terminated by revocation.

Section 1362(g) provides that if a small business corporation has made an election under § 1362(a) and if such election has been terminated under § 1362(d), the corporation (and any successor corporation) is not eligible to make an election under section 1362(a) for any taxable year before its fifth taxable year which begins after its first taxable year for which the termination is effective, unless the Secretary consents to the election.

Section 1.1362-5(a) of the Income Tax Regulations provides that the corporation has the burden of establishing that under the relevant facts and circumstances, the Commissioner should consent to a new election. The fact that more than 50 percent of the stock in the corporation is owned by persons who did not own any stock in the corporation on the date of the termination tends to establish that consent should be granted. In the absence of this fact, consent ordinarily is denied unless the corporation

shows that the event causing termination was not reasonably within the control of the corporation or shareholders having a substantial interest in the corporation and was not part of a plan on the part of the corporation or of such shareholders to terminate the election.

Based solely on the facts submitted and representations made, we conclude that X has met its burden under § 1.1362-5(a). We grant permission to X to elect to be a qualified subchapter S subsidiary effective D7 and for all subsequent years unless otherwise terminated. This consent is dependent upon X successfully electing to be treated as a qualified subchapter S subsidiary and dependent upon Y successfully electing to be treated as an S corporation, both elections effective D7. This ruling is conditioned on the shareholders of Y not making an election under § 1042 concerning the sale of their Y stock to the ESOP and Y not consenting to any such election under §§ 4978 and 4979A.

Except as specifically set forth above, we express or imply no opinion concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, we express or imply no opinion as to whether Y is a small business corporation under § 1361(b), and we express or imply no opinion as to whether X is a small business corporation under § 1361(b).

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

Pursuant to a power of attorney on file with this office, a copy of this letter is being forwarded to X's authorized representative.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes