

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Refer Reply To:  
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PLR-142525-11  
Date:  
December 09, 2011

Legend

X =

A =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Trust =

Dear :

This responds to a letter dated October 4, 2011 and subsequent correspondence, submitted on behalf of X by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated under the laws of State on Date 1 and elected to be an S corporation effective Date 2. A created Trust, a revocable trust, that held shares of X stock. On Date 3, A died and Trust became irrevocable. Trust was a qualifying S corporation shareholder under § 1362(c)(2)(A)(ii) until Date 4, two years after A's date of death. Trust, however, continued to hold X stock until Date 5. As such, X's S corporation election terminated on Date 4 when Trust ceased to be an eligible shareholder.

On Date 5, Trust transferred the remaining X stock held by Trust to Trust's beneficiaries, who are individuals qualified to be S corporation shareholders.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and were not motivated by tax avoidance or retroactive planning. X further represents that at all times since Date 2, X and its shareholders have treated X as an S corporation. X and its shareholders consent to make any adjustments that the Commissioner may require, consistent with the treatment of X as an S corporation.

## LAW AND ANALYSIS

Section 1361(a)(1) of the Code provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

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

Section 1361(c)(2)(A)(i) provides that, for purposes of § 1361(b)(1)(B), a trust all of which is treated (under subpart E of part 1 of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States may be an S corporation shareholder.

Section 1361(c)(2)(A)(ii) and § 1.1361-1(b)(1)(ii) provide that, for purposes of § 1361(b)(1)(B), a trust that is described in § 1361(c)(2)(A)(i) immediately before the death of the deemed owner and that continues in existence after such death is a permitted S corporation shareholder, but only for the two-year period beginning on the day of the deemed owner's death. Section 1.1361-1(h)(3)(i)(B) provides that if stock is held by a trust described in § 1.1361-1(h)(1)(ii), the estate of the deemed owner is generally treated as the shareholder as of the day of the deemed owner's death.

Section 1362(d)(2) provides that (A) in general, an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation and (B) any termination under § 1362(d)(2) shall be effective on and after the date of cessation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents or (B) was terminated under § 1362(d)(2) or (3); (2) the Secretary determines that the circumstances resulting in the ineffectiveness or termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken (A) so

that the corporation is a small business corporation or (B) to acquire the shareholder consents; and (4) the corporation and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), 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 each period, then, notwithstanding the circumstances resulting in the ineffectiveness or termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

Based solely on the facts submitted and the representations made, we conclude that X's election to be treated as an S corporation was terminated on Date 4 and that this termination was inadvertent within the meaning of § 1362(f). We further conclude that, pursuant to the provisions of § 1362(f), X will be treated as being an S corporation from Date 4 and thereafter, provided X is otherwise eligible to be an S corporation and provided that the election was not otherwise terminated under § 1362(d).

Accordingly, X's shareholders, in determining their respective income tax liabilities during the termination period and thereafter, must include their pro rata share of the separately stated items of income (including tax exempt income), loss, deduction, or credit and non-separately computed items of income or loss of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided by § 1368. If X or any of the shareholders fail to treat X as described above, this ruling shall be void.

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

Sincerely,

Charlotte Chyr  
Senior Technician Reviewer, Branch 2  
(Passthroughs & Special Industries)

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

cc: