

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

Number: **201243009**

Release Date: 10/26/2012

Index Number: 1362.00-00, 1362.02-00,  
1362.04-00

Third Party Communication: None  
Date of Communication: Not Applicable

Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:2  
PLR-113389-12  
Date: June 8, 2012

**Legend**

X =

Trust =

State =

D1 =

D2 =

Dear :

This responds to a letter dated March 26, 2012 submitted on behalf of X by X's authorized representative, requesting inadvertent invalid election relief under § 1362(f) of the Internal Revenue Code (the Code).

According to the information submitted and representations made, X was incorporated on D1, under the laws of State. X filed a timely election under § 1362(a) to be treated as an S corporation effective D2. On D2, the Trust's assets included X stock. The sole income beneficiary of the Trust filed an election under § 1361(d)(2) to be treated as a qualified subchapter S trust ("QSST") effective on D2; however, the Trust did not meet the requirements of a QSST within the meaning of 1361(d)(3). However, X represents that the Trust is eligible to be an electing small business trust ("ESBT") within the meaning of § 1361(e) effective D2 but that the trustees mistakenly failed to file an

election to treat the Trust as an ESBT. Therefore, the Trust was not an eligible shareholder and X's S corporation election was ineffective.

X represents that the circumstances resulting in the ineffectiveness of X's S corporation election were inadvertent and were not motivated by tax avoidance or retroactive tax planning. Additionally, X represents that X and its shareholders have filed their federal income tax returns consistent with having made a valid S corporation election in effect for X. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as may be required by the Secretary. X represents that the sole income beneficiary of the Trust has reported all the income of the Trust on the beneficiary's Form 1040, U.S. Individual Income Tax Return since D2. X further represents that the aggregate total income tax liability of the Trust and its beneficiary would not have been different had the Trust been treated as an ESBT.

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) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 shareholders, (B) 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, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(d)(1)(A) provides that a QSST, within the meaning of § 1361(d)(3), may be a shareholder for purposes of 1361(b)(1)(B). The beneficiary of the trust makes the QSST election pursuant to § 1361(d)(2).

Section 1361(c)(2)(A)(v) provides that an ESBT, within the meaning of § 1361(e)(1), may be a shareholder for purposes of § 1361(b)(1)(B). The trustee of the trust makes the ESBT election pursuant to § 1361(e)(3). Section 1.1361-1(m)(2)(i) provides that the trustee of an ESBT must make the ESBT election by signing and filing, with the service center where the S corporation files its income tax return, a statement that meets the requirements of § 1.1361-1(m)(2)(ii).

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the tax 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 paragraph (2) or (3) of § 1362(d); (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required 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 such period, then, notwithstanding the circumstances resulting in such ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Based on the information submitted and the representations made, we conclude that X's S corporation election was inadvertently invalid on D2 because X had an ineligible shareholder. Pursuant to the provisions of § 1362(f), X will be treated as an S corporation from D2 and thereafter, provided that X's election to be an S corporation was not otherwise ineffective and was not terminated under § 1362(d), so long as the trustees of the Trust file an effective ESBT election effective D2, pursuant to the procedures set forth in § 1.1361-1(m)(2), with the appropriate service center within 120 days of the date of this letter. A copy of this letter should be attached to the ESBT election.

Except for the specific ruling above, no opinion is expressed or implied concerning the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, no opinion is expressed or implied regarding X's eligibility to be an S corporation or the Trust's eligibility to be an ESBT.

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,

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

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