

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **201343016**

Release Date: 10/25/2013

Index Number: 1362.00-00, 1362.04-00

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B01
PLR-119925-13

Date:
July 23, 2013

Legend:

X =

A =

Trust =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Year =

Dear _____ :

This letter responds to a letter dated February 13, 2013, submitted on X's behalf by X's authorized representative, requesting relief under § 1362(f) of the Internal

Revenue Code (the Code).

Facts

According to the information submitted, X was incorporated under the laws of State on Date 1 and elected to be an S corporation effective Date 2. Pursuant to an agreement dated Date 3, A established Trust, a revocable grantor trust, and transferred X stock to Trust. Trust was a qualifying shareholder of an S corporation pursuant to § 1361(c)(2)(A)(i).

On Date 4, A died and Trust ceased to be a grantor trust. Trust continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii). X represents that Trust was eligible to be an ESBT within the meaning of § 1361(e). However, the trustee of the Trust did not make an election under § 1361(e)(3) to treat Trust as an ESBT. Therefore, Trust was not a permissible shareholder and, as a result, X's S corporation election terminated on Date 5.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance. X further represents that X has filed returns consistent with X's status as an S corporation. X and its shareholders have agreed to make any adjustments the Commissioner may require, 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 75 shareholders, (B) have as a shareholder a person (other than an estate and other than a trust described in subsection (c)(2)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(c)(2)(A)(v) provides that, for purposes of § 1361(b)(1)(B), trusts that may be shareholders include an electing small business trust.

Section 1361(e)(1)(A) provides that an "electing small business trust" means any trust if (i) such trust does not have as a beneficiary any person other than an (I) individual, (II) an estate, or (III) an organization described in paragraph (2), (3), (4), or (5) of § 170(c) or (IV) an organization described in § 170(c)(1) which holds a contingent interest in such trust and is not a potential current beneficiary; (ii) no interest in such

trust was acquired by purchase, and (iii) an election under this subsection applies to such trust.

Section 1361(e)(1)(B) provides that the term “electing small business trust” shall not include (i) any qualified subchapter S trust (as defined in § 1361(d)(3)) if an election under § 1361(d)(2) applies to any corporation the stock of which is held by such trust, (ii) any trust exempt from tax under subtitle A, and (iii) any charitable remainder annuity trust or charitable remainder unitrust (as defined in § 664(d)).

Section 1361(e)(3) provides that an election under § 1361(e) shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent years of such trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) of the Income Tax Regulations provides in part that the trustee of the trust 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 paragraph (m)(2)(ii) of this section.

Under § 1.1361-1(m)(2)(iii), if S corporation stock is transferred to a trust, the ESBT election must be made within the 16-day-and-2-month period beginning on the day that the stock is transferred to the trust.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever the corporation ceases to be a small business corporation.

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 such 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.

Conclusion

Based on the information submitted and the representations made, we conclude that X's S election inadvertently terminated within the meaning of § 1362(f) on Date 5. Pursuant to the provisions of § 1362(f) and contingent on the filing of the ESBT election for Trust, X will be treated as an S corporation from Date 5 and thereafter, provided X's S corporation was valid and provided that the election was not otherwise terminated under § 1362(d).

Within 120 days from the date of this letter, an election to treat Trust as an ESBT effective Date 5 must be made with the appropriate service center. This ruling is further contingent upon Trust filing an amended return for Year within 120 days from the date of this letter. A copy of this letter should be attached to the election. A copy is enclosed for that purpose.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed on whether X was or is otherwise eligible to be treated as an S corporation or whether Trust is eligible to be an ESBT.

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

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

David R. Haglund

David R. Haglund
Branch Chief, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2):

Copy of this letter
Copy for § 6110 purposes