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:
, ID No:
Telephone Number:

Refer Reply To:
CC:PSI:B01
PLR-124764-13

Date:
October 23, 2013

LEGEND

X =

IRA =

A =

B =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

State =

Dear :

This responds to a letter dated May 28, 2013, submitted on behalf of X by its authorized representative, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code (the Code).

FACTS

According to the information submitted and representations within, X was incorporated and elected to be treated as an S corporation on Date 1, under the laws of State. On Date 2, A indirectly acquired X stock from B using a self-directed IRA, an ineligible shareholder, thus causing X's S corporation election to terminate on Date 2.

On Date 3, X's tax professional discovered that the IRA had purchased X stock and immediately notified X to take corrective action. On Date 4, the IRA distributed its X shares to A. X requests inadvertent S corporation termination relief under section 1362(f) and that it be treated as an S corporation at all times since Date 2.

X represents that it has always intended to maintain its S corporation status and that the termination of X's S election was inadvertent and did not involve retroactive tax planning or tax avoidance. X further represents that X and its shareholders continued to consistently treat X as an S corporation and that X and its shareholders agree to make any adjustments required as a condition of obtaining relief under the inadvertent termination rule of § 1362(f) that may be required by the Secretary.

LAW AND ANALYSIS

Section 1361(a)(1) 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 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 1st taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation 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); (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 circumstances resulting in such ineffectiveness or termination, steps were taken so that the corporation for which the termination occurred is a small business corporation; and (4) the corporation for which the termination occurred, and each person who was a shareholder in such corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of such 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 or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(b) provides, in relevant part, that the determination of whether a termination was inadvertent is made by the Commissioner. The corporation has the burden of establishing that under the relevant facts and circumstances the Commissioner should determine that the termination was inadvertent. The fact that the terminating event was not reasonably within the control of the corporation and, in the case of a termination, was not part of a plan to terminate the election, or the fact that the terminating event or circumstance took place without the knowledge of the corporation, notwithstanding its due diligence to safeguard itself against such an event or circumstance, tends to establish that the termination of the election was inadvertent.

Section 1.1362-4(d) provides that the Commissioner may require any adjustments that are appropriate. In general, the adjustments required should be consistent with the treatment of the corporation as an S corporation during the period specified by the Commissioner.

CONCLUSION

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 2 because the IRA, by purchasing and holding stock in X, was an ineligible shareholder. We also hold that the termination of X's S corporation election was inadvertent within the meaning of section 1362(f). Therefore, pursuant to section 1362(f), X will be treated as an S corporation from Date 2 and thereafter, provided that X's S corporation election is not otherwise terminated under section 1362(d).

Accordingly, X's shareholders, in determining their federal tax liability, must include their pro rata share of the separately and non-separately computed items of X under section 1366, make any adjustments to stock basis under section 1367, and take into account any distributions made by X to shareholders under section 1368. This ruling shall be null and void if the requirements of this paragraph are not met.

As a condition for this ruling, for any tax periods between Date 2 and Date 4 in which X reported a net loss, IRA will be treated as the shareholder of the shares of stock at issue. For any tax periods between Date 2 and Date 4 in which X reported a net gain, A will be treated as the shareholder of the shares of stock at issue.

Except as specifically set forth above, we express or imply no opinion concerning the federal tax consequences of the above-described facts under any other provision of the Code. Specifically, no opinion is expressed on whether X is otherwise eligible to be treated as an S corporation.

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

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the ruling request, it is subject to verification on examination.

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

Sincerely,

Laura C. Fields
Laura C. Fields
Senior Technician Reviewer, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

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

cc: