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Person To Contact:

ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B01

PLR-130924-16

Date:

November 17, 2016

LEGEND

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Trust 1 =

Trust 2 =

A =

Dear :

This responds to a letter dated September 22, 2016, and subsequent correspondence, submitted on behalf of X 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. X elected to be treated as an S corporation effective Date 2. On Date 3, stock in X was transferred to Trust 1 and Trust 2. X represents that Trust 1 and Trust 2 have, at all times since Date 3, met the requirements to be Electing Small Business Trusts (ESBTs), within the meaning of § 1361(e). However, no election was made under § 1361(e)(3) to treat the trusts as ESBTs. Consequently, Trust 1 and Trust 2 were ineligible shareholders, and, as a result, X's S corporation election terminated on Date 3. On Date 4, Trust 1 and Trust 2 transferred all their X stock to A, an eligible S corporation shareholder.

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 tax planning. X represents that it has filed its federal income tax returns consistent with having a valid S corporation election in effect. Additionally, for each year since Date 3, Trust 1 and Trust 2 have filed an original or amended return consistent with being an ESBT. X and its shareholders, including Trust 1 and Trust 2, have agreed to make any adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

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 that is not an ineligible corporation and that 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 one class of stock.

Section 1361(c)(2)(A)(v) provides that, for the purposes of § 1362(b)(1)(B), an ESBT is a permitted shareholder of a small business corporation.

Section 1361(e) defines an ESBT. Section 1361(e)(1)(A) provides that, except as provided in § 1362(e)(2)(B), the term "electing small business trust" means any trust

if (i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (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 § 1361(e) applies to such trust.

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 taxable years of such trust unless revoked with the consent of the Secretary.

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, in relevant part, that if (1) an election under § 1362(a) by any corporation was terminated under paragraph (2) or (3) of § 1362(d), (2) the Secretary determines that the circumstances resulting in such termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in termination, steps were taken so that the corporation is once more a small business corporation, 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 any adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to the period, then, notwithstanding the circumstances resulting in the termination, the corporation will be treated as continuing to be an S corporation during the period specified by the Secretary.

CONCLUSION

Based solely on the information submitted and the representations made, we conclude that X's S election terminated on Date 3 when Trust 1 and Trust 2 became shareholders, and that the termination was inadvertent within the meaning of § 1362(f). Therefore, X will be treated as continuing to be an S corporation from Date 3, and thereafter, provided that X's S corporation election was otherwise valid and was not otherwise terminated under § 1362(d).

This ruling is contingent upon X and all of its shareholders treating X as having been an S corporation, and Trust 1 and Trust 2 as having been ESBTs, for the period beginning Date 3, and thereafter. Within 120 days from the date of this letter, the trustee of Trust 1 and Trust 2 must file an election to treat the trusts as ESBTs, effective Date 3, with the appropriate service center. A copy of this letter should be attached to the election. If these conditions are not met, then this ruling is null and void.

Accordingly, X's shareholders, in determining their respective income tax liabilities, must include their pro rata share of the separately and non-separately computed items of X as provided in § 1366, make any adjustments to stock basis as provided in § 1367, and take into account distributions made by X as provided by § 1368.

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 concerning whether X is otherwise eligible to be treated as an S corporation, or whether Trust 1 and Trust 2 are eligible to be treated as ESBTs.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, we are sending a copy of this letter to your 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 of this letter for § 6110 purposes