

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

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PLR-137040-16

Date:

March 01, 2017

LEGEND

X =

Y =

Trust1 =

Trust2 =

Trust3 =

Date 1 =

Date 2 =

Date 3 =

Date 4=

Date 5=

Date 6=

State =

Dear _____ :

This responds to a letter dated November 17, 2016, submitted on behalf of X, requesting relief under section 1362(f) of the Internal Revenue Code (the Code) for an inadvertent termination of its S corporation election.

FACTS

According to the information submitted and representations within, X was formed and made a valid S corporation election on Date 2, under the laws of State. Y was formed and made a valid S corporation election on Date 1, under the laws of State. On Date 3, X acquired all of the stock in Y. X made a valid Qualified Subchapter S Subsidiary (QSub) election for Y effective Date 3.

At the time of X's S corporation election, Trust1, a grantor trust, was the sole shareholder of X. On Date 4, Trust1 transferred X shares to Trust2. Trust2 made a valid Electing Small Business Trust (ESBT) election effective Date 4.

On Date 5, the assets of Trust2 were transferred to Trust3. Trust3 was not a valid S corporation shareholder, thereby causing X's S corporation election to terminate effective Date 5. X represents that Trust3 was eligible to make an Electing Small Business Trust (ESBT) election as of Date 5, however, the trustee of Trust5 inadvertently failed to file an ESBT election. X represents that Trust3 has been treated as if a valid ESBT election had been made on Date 5 and has at all times since Date 5 met the requirements of an ESBT under § 1361(d)(3). X further represents that Trust3 has filed its income tax returns consistent with being an ESBT.

X represents that the circumstances resulting in the failure to make the ESBT election was inadvertent and not motivated by tax avoidance or retroactive tax planning. X further represents that X has filed its income tax returns consistent with having a valid S election in effect for all taxable years since X elected to be an S corporation. X represents that other than the failure to make a valid ESBT election on Date 5, X has qualified as a small business corporation at all times since its election on Date 2. Lastly, X and its shareholders agree to make any adjustments required as a condition of obtaining relief under § 1362(f) that may be required by the Secretary.

LAW AND ANALYSIS

Section 1361(a) provides that an S corporation is a small business corporation for which an election under § 1362(a) is in effect.

Section 1361(b)(1) provides that the terms “small business corporation” means 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(b)(3)(A) generally provides that a QSub shall not be treated as a separate corporation and all assets, liabilities, and items of income, deduction, and credit of a QSub shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

Section 1361(b)(3)(B) defines a QSub as a domestic corporation which is not an ineligible corporation, if 100 percent of the stock of the corporation is owned by the S corporation, and the S corporation elects to treat the corporation as a Qualified subchapter S subsidiary .

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 1361(c)(2)(A)(i) of the Code provides that for purposes of section 1361(b)(1) a trust all of which is treated (under subpart E of part I of subchapter J of this chapter) 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)(v) provides that for purposes of § 1361(b)(1)(B), an ESBT is a permissible shareholder.

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 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 1.1361-1(m)(2)(iii) provides that the trustee of an ESBT must file the ESBT election within the time requirements prescribed in § 1.1361-1(j)(6)(iii) for filing a QSST election (generally within the 16-day-and-2-month period beginning on the day that the stock is transferred to the trust).

Section 1.1361-3(a) prescribes the time and manner for making an election to be classified as a QSub.

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.

CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that the failure of Trust3 to make an ESBT election effective Date 5 caused an inadvertent termination of X's S corporation election within the meaning of § 1362(f) on Date 5. Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation beginning on and after Date 2, and Y will continue to be a QSub of X effective Date 3, unless X's S corporation election is otherwise terminated under § 1362(d).

This letter ruling is subject to the condition that within 120 days from the date of this letter, an election to treat the Trust3 as an ESBT effective Date 5, must be made with the appropriate service center. A copy of this letter should be attached to the ESBT election. If this condition is not met, then this ruling is null and void. Furthermore, if this condition is not met, X must send notification that its S election has terminated to the service center with which X's S election was filed.

Except as specifically ruled upon above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation.

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 representatives.

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 of this letter for section 6110 purposes