

Dear _____ :

This letter responds to a letter dated August 21, 2017, submitted on behalf of X, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

The information submitted states that X was incorporated under the laws of State on Date 1 and elected to be an S corporation effective Date 2.

On Date 3, A created Trust 1 and then transferred shares of X stock to Trust 1, a revocable trust treated as a wholly-owned grantor trust under §§ 671 and 676. On Date 4, B created Trust 2 and transferred shares of X stock to Trust 2, a revocable trust treated as a wholly-owned grantor trust under §§ 671 and 676.

On Date 5, B died. Trust 2, pursuant to its terms, transferred its shares of X to Trust 4 on Date 5. On Date 6, A died. Trust 1, pursuant to its terms, transferred its shares of X to Trust 3 on Date 6.

X represents that Trust 3 and Trust 4 intended to be a qualified subchapter S trusts (QSST) described in § 1361(d)(3)(A) as of Date 5 and Date 6 respectively. However, the income beneficiary of Trust 3, failed to make a QSST election within the meaning of § 1361(d)(2) for Trust 3. Consequently, X's S corporation election terminated on Date 5. If X's S corporation election had not already terminated on Date 5, it would have terminated on Date 6 because Trust 4 failed to qualify as a QSST because of a trust provision inconsistent with QSST status and the income beneficiary failed to make a QSST election for Trust 4.

On Date 7, X redeemed all of its shares held by Trust 3 and Trust 4.

X represents that all circumstances resulting in the termination of its S corporation election were inadvertent and not motivated by tax avoidance. Further, since Date 5, X and X's shareholders have continually treated X as an S corporation. As such, all items of income, gain, loss, and deduction recognized by X since Date 5 have been allocated among the shareholders of X. X and its shareholders agreed to make such adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary.

Section 1361(b)(1)(B) provides that the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not 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.

Section 1361(d)(1) provides that in the case of a QSST for which a beneficiary makes an election under § 1361(d)(2), the trust is treated as a trust described in

§ 1361(c)(2)(A)(i), and for purposes of § 678(a), the beneficiary of the trust shall be treated as the owner of that portion of the trust that consists of stock in an S corporation with respect to which the election under § 1361(d)(2) is made.

Section 1361(d)(2)(A) provides that a beneficiary of a QSST may elect to have § 1361(d) apply. Section 1.1361-1(j)(6)(ii) provides that the current income beneficiary of a QSST must make the election under § 1361(d)(2) by signing and filing with the service center with which the corporation files its income tax returns the applicable form or a statement including the information listed in § 1.1361-1(j)(6)(ii).

Section 1362(d)(2) provides that (A) in general, an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation, and (B) any termination under § 1362(d)(2) shall be effective on and after the date of cessation.

Section 1362(f) provides, in part, 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 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 the ineffectiveness or termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election terminated on Date 5, when the X stock was transferred to Trust 4 because of the failure of the beneficiary of Trust 4 to make the required QSST election with respect to the trust. We further conclude that this termination of X's S corporation election was an inadvertent termination within the meaning of § 1362(f). Moreover, had X's S corporation election not already terminated on Date 5, it would have terminated on Date 6 when the stock was transferred to Trust 3 because of a trust provision inconsistent with QSST status and the income beneficiary's failure to make a QSST election for Trust 3. Similarly, this would have been an inadvertent termination within 1362(f). Accordingly, pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 5 and thereafter, provided X's S corporation election was valid and not otherwise terminated under § 1362(d).

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code, including whether X is a small business corporation under § 1361(b), or whether Trust 3 and Trust 4 were eligible to be treated as QSSTs within the meaning of § 1361(d)(3).

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.

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

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

Sincerely,

Bradford R Poston
Special Counsel to the Associate Chief Counsel
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures: Copy of this letter
Copy for § 6110 purposes

cc: