

**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:

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PLR-116738-19

Date:

January 13, 2020

LEGEND

X =

State =

A =

B =

Trust 1 =

Trust 2 =

Trust 3 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Dear :

This responds to a letter dated May 14, 2019, and subsequent information, submitted on behalf of X by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code.

#### FACTS

According to the information submitted and representations within, X was incorporated on Date 1, under the laws of State. Effective Date 2, X elected to be taxed as an S corporation.

On Date 3, A established Trust 1, a revocable trust treated as a wholly-owned grantor trust under §§ 671 and 676. On Date 4, Trust 1 acquired shares in X.

On Date 5, A died and Trust 1 ceased to be a grantor trust with respect to A's interest, but continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii) for the 2 year period beginning on the day of the deemed owner's death. On Date 6, by operation of the governing instrument of Trust 1, shares of X were transferred to Trust 2. X represents that Trust 2 qualified to elect to be treated as qualified subchapter S trusts (QSST). However, the sole income beneficiaries of the separate shares of Trust 2 failed to make timely QSST elections within the meaning of § 1361(d)(2), thereby causing X's S corporation election to terminate on Date 6.

On Date 7, B established Trust 3, a revocable trust treated as a wholly-owned grantor trust under §§ 671 and 676. On Date 4, Trust 3 acquired shares in X.

On Date 8, B died and Trust 3 ceased to be a grantor trust with respect to B's interest, but continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii) for the 2 year period beginning on the day of the deemed owner's death. X represents that Trust 3 qualified to elect to be treated as a QSST. However, the sole income beneficiaries of the separate shares of Trust 3 failed to make timely QSST elections within the meaning of § 1361(d)(2). The failure to make the QSST elections would have terminated X's S corporation election on Date 9 had it not already been terminated.

X represents that the circumstances resulting in the failure to file the QSST elections for Trust 2 and Trust 3 were 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 and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as 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 1361(c)(2)(A)(i) provides that for purposes of § 1361(b)(1)(B), a trust all of which is treated (under subpart E) as owned by an individual who is a citizen or resident of the United States may be a shareholder of an S corporation.

Section 1361(c)(2)(A)(ii) provides that a trust may be an S corporation shareholder if it was described in section 1361(c)(2)(A)(i) immediately before the death of the deemed owner and it continues in existence after such death, but only for the 2-year period beginning on the day of the deemed owner's death.

Section 1361(d)(1) provides that in the case of a QSST with respect to 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 is treated as the owner of that portion of the trust which consists of stock in a S corporation with respect to which the election under § 1361(d)(2) is made.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3) or § 1361(b)(3)(C); (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 such 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 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 representations made, we conclude that X's S corporation election terminated beginning on Date 6, when the stock in X was transferred to Trust 2 because the income beneficiaries of Trust 2 failed to timely file the required QSST elections under § 1361(d)(2). We conclude that the termination was inadvertent within the meaning of § 1362(f). Moreover, had X's S corporation election not already terminated on Date 6, it would have terminated on Date 9 as a result of the income beneficiaries of Trust 3 failing to timely file the required QSST elections under § 1361(d)(2). Similarly, this would have been inadvertent termination within the meaning of § 1362(f). Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation beginning on and after Date 6, 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, the income beneficiaries of Trust 2 must file a QSST election effective Date 6 and the income beneficiaries of Trust 3 must file a QSST election effective Date 9. All elections must be filed with the appropriate service center. A copy of this letter should be attached to the QSST elections. 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. Further, no opinion is expressed or implied concerning whether Trust 2 and Trust 3 meet the requirements of a QSST under § 1361(d)(3).

The ruling contained in this letter is based on information and representations submitted by the taxpayer and is 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 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 X's authorized representative.

Sincerely,

*Laura C. Fields*

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

Enclosures (2)

Copy of this letter

Copy of this letter for section 6110 purposes

cc: