

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

Number: **202319008**  
Release Date: 5/12/2023

Third Party Communication: None  
Date of Communication: Not Applicable

Index Number: 1361.03-03, 1362.00-00,  
1362.04-00

Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:B01  
PLR-116113-22  
Date:  
February 10, 2023

LEGEND

X =  
TIN:

A =  
TIN:

Date 1 =

Date 2 =

Date 3 =

Date 4 =

State =

Dear :

This responds to a letter dated August 19, 2022, and additional correspondence, submitted on behalf of X by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code (the Code).

FACTS

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

on Date 3 and was treated as a wholly-owned grantor trust under §§ 671 and 676 as to A. Trust first acquired shares in X on Date 3.

On Date 4, Trust ceased to be a wholly-owned grantor trust as to A. X represents that Trust qualified to elect to be treated as an Electing Small Business Trust (ESBT) as of Date 4. However, the trustees of Trust failed to make a timely ESBT election under § 1361(e)(3), thereby causing X's S corporation election to terminate on Date 4.

X represents that the circumstances resulting in the failure to file an ESBT election for Trust were inadvertent and not motivated by tax avoidance or retroactive tax planning. X also represents that it has filed income tax returns consistent with having a valid S election in effect for all taxable years since its election to be an S corporation, and that Trust has filed income tax returns consistent with having an ESBT election in effect for all relevant years. X further represents that X and its shareholders agree to make any adjustments required by the Secretary as a condition of obtaining relief under the inadvertent termination rule as provided under § 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 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 of part I of subchapter J of Chapter 1 of the Code) 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)(v) provides that, for purposes of § 1361(b)(1)(B), an electing small business trust (ESBT) may be an S corporation shareholder.

Section 1361(e)(1)(A) provides that an ESBT 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 § 170(c)(2), (3), (4), or (5), 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)(1)(B) provides that the term “electing small business trust” shall not include (i) any qualified subchapter S trust (as defined in § 1361(d)(3)) if an election under § 1361(d)(2) applies to any corporation the stock of which is held by such trust, (ii) any trust exempt from tax under subtitle A, and (iii) any charitable remainder annuity trust or charitable remainder unitrust (as defined in § 664(d)).

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)(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 1362(d)(2) provides that an S corporation election will 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.

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) or was terminated under § 1362(d)(2) or (3); (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 election was made or termination occurred is a small business corporation; and (4) the corporation for which the election was made or 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 representations made, we conclude that X's S corporation election terminated on Date 4 when the trustees of Trust failed to file an ESBT election under § 1361(e)(3). We further conclude that the termination of X's S corporation election was inadvertent within the meaning of § 1362(f). Therefore, under § 1362(f), X will be treated as continuing to be an S corporation on and after Date 4,

provided X's S corporation election was otherwise valid and not otherwise terminated under § 1362(d).

This letter ruling is subject to the condition that within 120 days from the date of this letter, the trustees of Trust must file an ESBT election with respect to Trust effective Date 4 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 letter ruling is null and void.

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 or Trust's eligibility to be an ESBT.

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.

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.

Pursuant to the power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

/s/

\_\_\_\_\_  
Laura C. Fields  
Branch Chief, Branch 1  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures

Copy of this letter for Section 6110 purposes

cc: