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Department of the Treasury
Washington, DC 20224

[Third Party Communication:
Date of Communication: Month DD, YYYY]

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B01
PLR-105111-24

Date:
September 12, 2024

LEGEND

X =

Y =

A =
State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Trust =

Dear _____ :

This letter responds to a letter dated March 13, 2024, and subsequent correspondence, submitted on behalf of X by its authorized representatives requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

FACTS

The information submitted states that X was incorporated on Date 1 under the laws of State and filed an election under § 1362(a) to elect to be treated as an S corporation effective Date 2. Trust was formed on Date 3 and was treated (under subpart E of part I of subchapter J of the Code) as a wholly-owned grantor trust as to A. A transferred all of A's shares in X to Trust on Date 4. Trust ceased to be a grantor trust upon A's death on Date 5. Trust continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii) for the two-year period beginning on the day of A's death and ending Date 6.

X represents that at all times beginning on Date 6, Trust met the requirements of an Electing Small Business Trust (ESBT) within the meaning of § 1361(e)(1)(A). However, the trustee of Trust failed to file a timely election under § 1361(e)(3) for Trust to be treated as an ESBT, thus causing X's S corporation election to terminate effective Date 6.

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 further 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. 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) of the Code 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) provides that the term "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 one 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) as owned by an individual who is a citizen or resident of the United States is a permitted S corporation shareholder.

Section 1361(c)(2)(A)(ii) provides that, for purposes of § 1361(b)(1)(B), a trust that was described in § 1361(c)(2)(A)(i) immediately before the death of the deemed owner and that continues in existence after such death is a permitted S corporation shareholder, but only for the two-year period beginning on the day of the deemed owner's death.

Section 1361(c)(2)(A)(v) provides that for purposes of § 1361(b)(1)(B), an ESBT is a permissible 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)-(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 § 1362(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 subsequent taxable years of such trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) of the Income Tax Regulations provides, in part, 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 ESBT election must be filed 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)(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(d)(2)(B) provides that any termination under § 1362(d)(2)(A) is effective on and after the date of cessation.

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 to obtain shareholder consents or was terminated under § 1362(d)(2), (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 the termination occurred is a small business corporation or to acquire the required shareholder consents, and (4) the corporation for which the election was made or 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 representations made, we conclude that X's S corporation election terminated on Date 6 due to the failure to file a timely ESBT election for Trust, thereby making it an ineligible shareholder. We further conclude that the termination of X's S corporation election was inadvertent within the meaning of § 1362(f). Accordingly, under the provisions of § 1362(f), X will be treated as continuing to be an S corporation on Date 6 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 the trustee of Trust filing an appropriately completed ESBT election for Trust effective Date 6, and upon Trust and its beneficiaries filing amended federal income tax returns for all open years consistent with the treatment of Trust as an ESBT effective Date 6. The election must be made and the amended returns must be timely filed with the appropriate service center within 120 days following the date of this letter, and a copy of this letter should be attached to the returns. If these conditions are not met, this 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 X's authorized representative.

Sincerely,

Christiaan T. Cleary
Assistant to the Branch Chief, Branch 1
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure (1)
Copy for § 6110 purposes

CC: