

Internal Revenue Service

Number: **202451004**
Release Date: 12/20/2024

Index Number: 1362.00-00, 1362.01-02,
1362.02-00, 1362.04-00

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:
CC:PSI:B03
PLR-105736-24

Date:
September 24, 2024

LEGEND

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Year =

A =

B =

Trust 1 =

Trust 2 =

Dear _____ :

This letter responds to a letter dated March 21, 2024, and subsequent correspondence, submitted on behalf of X and its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

FACTS

According to the information submitted, X was incorporated under the laws of State on Date 1. X elected to be an S corporation effective Date 2. On Date 3, shareholders A and B established Trust 1 and Trust 2, and subsequently on Date 4 A and B transferred shares of X to Trust 1 and Trust 2. Trust 1 and Trust 2 were intended to be qualified subchapter S trusts (QSST) for the benefit of the children of A and B, but the governing provisions of Trust 1 and Trust 2 did not satisfy the requirements under § 1361(d)(3). Consequently, upon the transfer of shares on Date 4, Trust 1 and Trust 2 became ineligible shareholders of X and X's S corporation election terminated.

In Year, X discovered that its S corporation election terminated on Date 4, and that Trust 1 and Trust 2 were ineligible shareholders of X. Subsequently, on Date 5 the trust agreements for Trust 1 and Trust 2 were modified retroactively to ensure they each qualified as a QSST effective Date 3 pursuant to the modification agreement.

X represents that all relevant times, X and its shareholders intended for X to be an S corporation effective Date 3 and that X, and Trust 1 and Trust 2 have filed federal tax returns consistent with X being an S corporation. X represents that the termination of its S corporation election on Date 4 was inadvertent and was not motivated by tax avoidance or retroactive tax planning. X and its shareholders agree to make any 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) 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) defines a "small business corporation" as a domestic corporation, which is not an ineligible corporation, 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 the purposes of § 1362(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, may be an S corporation shareholder.

Section 1361(d)(1) provides that a QSST who beneficiary makes an election under § 1361(d)(2) will be treated as a trust described in §1361(c)(2)(A)(i), and the beneficiary of such trust will be treated as the owner (for purposes § 678(a)) of that portion of the trust which consists of stock in an S corporation with respect to which the election under § 1361(d)(2) is made.

Section 1361(d)(3) defines a QSST as a trust, (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust, (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary, (iii) the income interest of the current beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust, and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary, and (B) all of the income (within the meaning of § 643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(d)(2)(A) provides that an election under § 1362(a) 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(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 terminated under § 1362(d)(2) or (3), (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 the termination, steps were taken so that the corporation for which the termination occurred is once a small business corporation, and (4) the corporation for which the termination occurred and each person who was a shareholder in the corporation at any time during the period specified pursuant to § 1362(f), agrees to make adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to the period, then, notwithstanding the circumstances resulting in the termination, the corporation will be treated as a S corporation during the period specified by the Secretary.

Rev. Rul. 93-79, 1993-2 C.B. 269, provides that a reformation of a trust to meet the requirements of a QSST is recognized prospectively.

CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election terminated on Date 4 when Trust 1 and Trust 2 became ineligible shareholders. We further conclude that the termination of X's S corporation election on Date 4 was inadvertent with the meaning of § 1362(f). Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 4 and thereafter, provided that X's S election was otherwise valid and was not otherwise terminated under § 1362(d).

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation or Trust 1's and Trust 2's eligibility to be a QSST.

The rulings contained in this letter are 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 request for rulings, it is subject to verification on examination.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Robert D. Alinsky
Chief, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:

Copy of this letter for § 6110 purposes

cc: