

Internal Revenue Service

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Department of the Treasury

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Third Party Communication: None

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B3

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Date:

October 25, 2024

LEGEND

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

A =

B =

C =

D =

E =

n =

LLC =

Trust =

Dear _____ :

This letter responds to a letter dated April 26, 2024, and subsequent correspondence, submitted on behalf of X by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

FACTS

The information submitted states that X, a State corporation, elected to be an S corporation effective Date 1. On Date 2, LLC, a State limited liability company classified as a partnership for federal tax purposes, acquired shares of X stock from A. A's grandchildren, B, C, D, and E, each own a n percent interest in LLC. Because LLC was an ineligible shareholder under § 1361(b)(1)(B), X's S corporation election terminated on Date 2.

Shortly after A died on Date 3, X learned that its S corporation election had terminated on Date 2. Subsequently, on Date 4, LLC transferred its shares of X stock to Trust. X represents that Trust is eligible to be an electing small business trust (ESBT) under § 1361(e)(1) effective Date 4. However, the trustee(s) of Trust failed to make an election under § 1361(e)(3) treating Trust as an ESBT effective Date 4. Consequently, X's S corporation election would have terminated on Date 4, had it not previously terminated on Date 2.

X represents that the circumstances resulting in the termination of its S corporation election were inadvertent and were not the result of tax avoidance or retroactive tax planning. X further represents that it has filed its federal tax returns consistent with X being an S corporation effective Date 1. Finally, 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) states 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 the taxable year.

Section 1361(b)(1) provides that the term "small business corporation" means a domestic corporation that is not an ineligible corporation and 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)(v) provides that, for purposes of § 1361(b)(1)(B), an 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)(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)(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 1362(d)(2)(A) provides that 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. Section 1362(d)(2)(B) provides that any termination under § 1362(d)(2) is 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 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), agree 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.

CONCLUSION

Based solely on the facts submitted and representations made, we conclude that X's S corporation election terminated on Date 2 when LLC, an ineligible S corporation shareholder, acquired shares of X stock. We also conclude that had X's S corporation election not terminated on Date 2, it would have terminated on Date 4 as described in

this letter. We further conclude that the circumstances resulting in the termination of X's S corporation election were inadvertent within the meaning of § 1362(f). Therefore, under § 1362(f), X will continue to be treated as an S corporation from Date 2, and thereafter, provided X's S corporation election was valid and has not otherwise terminated under § 1362(d) for reasons not addressed in this letter.

This ruling is contingent on the trustee(s) of Trust filing an ESBT election for Trust effective Date 4 with the appropriate service center within 120 days from the date of this letter and attaching a copy of this letter to the ESBT election.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of the facts discussed or referenced in this letter under any other provision of the Code. Specifically, we express or imply no opinion on X's eligibility to be an S corporation or Trust's eligibility to be an ESBT.

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 requested ruling, 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 a power of attorney on file with this office, we are sending a copy of this letter to X's authorized representative.

Sincerely,

Mary Beth Carchia
Senior Technician Reviewer, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:

Copy of this letter for § 6110 purposes

cc: