

b. Company's Form 2553 was correctly and accurately completed except that two of Company's shareholders did not consent to Company's S corporation election. At the time of the election, the co-executors for the Estate failed to consent on behalf of the Estate to Company's S corporation election. In addition, Individual, the current income beneficiary of the Trust, for which a qualified subchapter S trust ("QSST") election was made, failed to consent to Company's S corporation election. Despite not providing all of the required shareholder consents, Company and its shareholders filed or will file their income tax returns consistent with the treatment of Company as an S corporation.

Company represents that the circumstances resulting in the invalidity of Company's S corporation election were inadvertent and were not motivated by tax avoidance. Company and its shareholders have agreed to make such adjustments, consistent with the treatment of Company as an S corporation, as may be required by the Service.

LAW AND ANALYSIS

Section 1361(a)(1) provides that for purposes of title 26, 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 for purposes of subchapter S, 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 1362(a)(1) provides that except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation. Section 1362(a)(2) provides that an election under § 1362(a) shall be valid only if all persons who are shareholders in such corporation on the day on which such election is made consent to such election.

Section 1362(f) provides that if (1) an election under § 1362(a) or § 1361(b)(3)(B)(ii) 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) or § 1361(b)(3)(C); (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 (A) so that the corporation for which the election was made or the termination occurred is a small business corporation or a qualified subchapter S subsidiary, as the case may be, or (B) 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 the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation or a qualified subchapter S subsidiary, as the case may be) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, the corporation shall be treated as an S corporation or a qualified subchapter S subsidiary, as the case may be, during the period specified by the Secretary.

Section 1.1362-6(a)(2) of the Income Tax Regulations provides that a small business corporation makes an election under § 1362(a) to be an S corporation by filing a completed Form 2553. The election form must be filed with the service center designated in the instructions applicable to Form 2553. The election is not valid unless all shareholders of the corporation at the time of the election consent to the election in the manner provided in § 1.1362-6(b). However, once a valid election is made, new shareholders need not consent to that election.

Section 1.1362-6(b)(2) provides in part that the following rules apply in determining persons required to consent: (iii) The consent of an estate must be made by an executor or administrator thereof, or by any other fiduciary appointed by testamentary instrument or appointed by the court having jurisdiction over the administration of the estate; and (iv) In the case of a trust described § 1361(c)(2)(A) (including a trust treated under § 1361(d)(1)(A) as a trust described in § 1361(c)(2)(A)(i) and excepting an election small business trust described in § 1361(c)(2)(A)(v) (ESBT)), only the person treated as the shareholder for purposes of § 1361(b)(1) must consent to the election.

CONCLUSIONS

Based solely on the facts submitted and the representations made, we conclude that Company's subchapter S election was invalid under § 1362(a)(2) because the Estate and Individual, shareholders of Company, failed to consent to Company's S corporation election.

We further conclude that the invalidity of Company's S corporation election was inadvertent within the meaning of § 1362(f). Accordingly, pursuant to provisions of § 1362(f), Company will be treated as an S corporation from b, and thereafter, provided that Company's S corporation election is otherwise valid and is not otherwise terminated under § 1362(d). In addition, the Trust will be treated as a QSST during the period of Company's inadvertent invalid S corporation election, provided that the Trust made a valid QSST election. However, this ruling is contingent on Company and its shareholders treating Company as having been an S corporation from b, and thereafter. Accordingly, Company's shareholders, in determining their income tax liabilities for the

period beginning b and thereafter, must include their pro rata shares of the separately and nonseparately computed items of Company under § 1366, make any adjustments to stock basis under § 1367, and take into account any distributions made by Company to shareholders under § 1368. If Company or any of Company's shareholders fail to treat Company as described above, this ruling will be null and void.

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 whether Company is otherwise eligible to be treated as an S corporation or whether the Trust is otherwise a valid QSST.

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.

Under a Power of Attorney on file with this office, we are sending a copy of this letter to Company's authorized representative.

Sincerely,

/s/

Christine Ellison
Chief, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes