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Department of the Treasury

Washington, DC 20224

[Third Party Communication:

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Person To Contact:

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PLR-136860-10

Date:

March 07, 2011

Legend:

X =

A =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Trust 1 =

Trust 2 =

Dear :

This responds to a letter dated August 13, 2010 and subsequent correspondence, submitted on behalf of X, requesting a ruling under § 1362(f) of the Internal Revenue Code (the Code).

FACTS

X submitted the following facts and representations: X incorporated on Date 1 under the laws of State. X elected to be treated as an S corporation effective Date 2. On Date 3, A, a shareholder in X, transferred stock in X to Trust 1, which X represents was an eligible shareholder of X. On Date 4, Trust 1 no longer qualified as an eligible shareholder, which resulted in a termination of X's S corporation status. On Date 5, Trust 1 completed the transfer of the stock in X to Trust 2, which X represents is an eligible shareholder of X.

X further represents that its S corporation election termination was inadvertent and was not motivated by tax avoidance or retroactive tax planning. X and its shareholders agree to make any adjustments required by the Secretary consistent with the treatment of X as an S corporation.

LAW AND ANALYSIS

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1361(b)(1)(B) provides that a small business corporation cannot 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.

Section 1361(c) provides that certain trusts are permitted shareholders. Section 1361(c)(2)(A) also provides, in part, that § 1361(c)(2) shall not apply to any foreign trust.

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 taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation. The termination is effective on and after the day of cessation. § 1362(d)(2)(B).

Section 1362(f) provides 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 consent, or (B) 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 the termination, steps were taken -

(A) so that the corporation is a small business corporation, or (B) to acquire the required 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 this subsection, agrees 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 such 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 the representations made, we conclude that the termination of X's S election as a result of Trust 1 becoming an ineligible shareholder on Date 4 constituted an "inadvertent termination" within the meaning of § 1362(f).

We conclude that, pursuant to § 1362(f), X will be treated as continuing to be an S corporation from Date 2 and thereafter, assuming X's S election is valid and not otherwise terminated under § 1362(d), and that A will be treated as the owner of the stock in X from Date 4 until Date 5.

This ruling is contingent upon X and all its shareholders treating X as having been an S corporation for the period beginning Date 2, and thereafter, and A treating himself, not Trust 1, as the owner of the stock in X from Date 4 through Date 5. The shareholders of X must include in their income their pro rata share of separately stated and nonseparately computed items of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided in § 1368. X and each of its shareholders must file any original and amended returns that are necessary to properly reflect the reporting of X's items of S corporation income consistent with the relief granted in this letter.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal tax consequences of the above-described facts under any other provision of the Code, including whether X was otherwise a valid S corporation. Specifically, no opinion is expressed regarding whether Trust 1 was otherwise a permitted shareholder of X prior to Date 4, whether Trust 2 is otherwise a permitted shareholder of X, and whether any other shareholder of X is a permitted shareholder of X.

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

Pursuant to the power of attorney on file with this office, a copy of this letter will be sent to X's authorized representative.

Sincerely,

Faith P. Colson

Faith P. Colson
Senior Counsel, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures:

Copy of this letter

Copy for § 6110 purposes