

**Internal Revenue Service**

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Washington, DC 20224

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April 23, 2014

**LEGEND**

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

A =

Dear :

This responds to a letter dated February 13, 2013, submitted on behalf of X by X's authorized representative, requesting inadvertent S corporation election termination relief pursuant to § 1362(f) of the Internal Revenue Code.

**FACTS**

According to the information submitted and representations within, X incorporated under the laws of State and elected to be treated as an S corporation effective Date 1. X's S corporation election terminated when it transferred shares of X to A, an ineligible shareholder, on Date 2 and again on Date 3. On Date 4, X discovered that it had

effectively terminated its S corporation election and took corrective action; the shares of X were transferred to A's owner, an eligible shareholder. X represents that its shareholders were unaware that A was prohibited from owning shares of X, and that such a transaction would terminate X's S corporation election. X also represents that its shareholders did not intend to terminate X's S corporation election.

## **LAW**

Section 1362(a) 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 1361(a)(1) 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)(B) 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 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 1362(d)(2) 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, and that any termination under § 1362(d)(2) shall be 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 was terminated under § 1362(d)(2); (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 such termination, steps were taken so that the corporation for which the termination occurred is a small business corporation, or to acquire the required shareholder consents; and (4) the corporation for which 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 such 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 termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

## **CONCLUSION**

Based solely upon the facts submitted and the representations made, we conclude that X's S corporation election terminated when it transferred shares of X to A, an ineligible shareholder, on Date 2. We further conclude that the termination of X's S corporation election constituted an inadvertent termination within the meaning of § 1362(f). Under § 1362(f), X will be treated as an S corporation from Date 2 and thereafter, notwithstanding the transfer on Date 3 (the subsequent transfer on Date 3 will not preclude X from being treated as an S corporation from Date 2), provided that X's S corporation election was otherwise valid and has not otherwise terminated under § 1362(d). 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, once again, notwithstanding the transfer on Date 3.

Except as specifically ruled upon above, no opinion is expressed as to the federal income tax consequences of the facts described above under any other provision of the Code, including whether X was otherwise eligible to be an S corporation or whether the shareholders of X were otherwise eligible S corporation shareholders.

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. In accordance with the Power of Attorney on file with this office, copies of this letter ruling will be sent to your authorized representatives.

Sincerely,

*David R. Haglund*  
David R. Haglund  
Branch Chief, Branch 1  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter.  
Copy of this letter for §6110 purposes.

cc: