

Internal Revenue Service

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PLR-146615-14

Date:

March 09, 2015

Legend

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

A =

P =

Trust 1 =

Trust 2 =

Dear :

This responds to a letter dated December 8, 2014, and subsequent correspondence, submitted on behalf of X by its authorized representatives, requesting a ruling relating to X's status as an S corporation under §§ 1361 and 1362 of the Internal Revenue Code.

FACTS

The information submitted states that X was incorporated under the laws of State on Date 1 and elected to be an S corporation effective Date 1. On Date 2, A, a shareholder, transferred shares of X were transferred to P, a State limited liability company taxable as a partnership for federal income tax purposes. Therefore, X's

election terminated on Date 2. Trust 1 and Trust 2 have at all times been partners in P. A was not aware that P was an ineligible shareholder of an S corporation and that the transfer would terminate X's S corporation election. On Date 3, X engaged new accountants to prepare its tax returns, who discovered shares of X had been transferred to P and that this transfer terminated X's S corporation election.

On Date 4, P distributed all of its shares of X stock to Trust 1 and Trust 2. X represents that Trust 1 and Trust 2 are Electing Small Business Trusts (ESBTs) under § 1361(e)(3) as of Date 4.

X represents that the termination of its S corporation election was inadvertent and not motivated by tax avoidance or retroactive tax planning. Further, since Date 2, X and X's shareholders have continually treated X as an S corporation. As such, all items of income, gain, loss, and deduction recognized by X since Date 2 have been allocated among the shareholders of X, including P. X and its shareholders have agreed to make such adjustments as the Service may require with respect to all periods since Date 2.

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" means a domestic corporation that is not an ineligible corporation and that 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 first day of the first taxable year for which a corporation is an S corporation) such corporation ceases to be a small business corporation. A termination of an S corporation election under § 1362(d)(2) is effective on and after the date of cessation.

Section 1362(f) provides 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 event resulting in the ineffectiveness, 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 § 1362(f), 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

ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

CONCLUSION

Based solely on the information submitted and the representations made, we conclude that X's S corporation election was terminated on Date 2 when shares of X were transferred to P, an ineligible shareholder. We conclude, however, that this termination was inadvertent within the meaning of § 1362(f). Accordingly, pursuant to the provisions of § 1362(f), X will be treated as an S corporation effective Date 2 and thereafter.

During the termination period, Trust 1 and Trust 2 will be treated as if they held their respective shares in X directly. Accordingly, in determining their respective income tax liabilities during the termination period and thereafter, X's shareholders must include their pro rata share of the separately 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.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed on whether X was or is otherwise eligible to be treated as an S corporation.

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 a power of attorney on file with this office, a copy of this letter is being forwarded to X's authorized representatives.

Sincerely,

Laura C. Fields

Laura C. Fields

Senior Technician Reviewer, Branch 1
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter

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