

Internal Revenue Service

Number: **201615003**

Release Date: 4/8/2016

Index Number: 1362.04-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B03

PLR-123622-15

Date:

December 01, 2015

Legend

X =

State =

D1 =

D2 =

D3 =

D4 =

D5 =

D6 =

Shareholder =

Trust1 =

Trust2 =

Year1 =

Year2 =

n =

Dear _____ :

This letter responds to a letter dated June 26, 2015, and subsequent information, 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 was organized under the laws of State on D1 and elected to be an S corporation effective D2. Shareholder transferred all of the shares in X to Trust1 on D3. X represents that Trust1 was a permitted S corporation shareholder through D5. On D4, a date prior to D5, Trust1 transferred the shares in X to Trust2 for the benefit of Income Beneficiary, who is the same person as Shareholder.

X represents that Trust2 was eligible on D4 and thereafter to be a qualified subchapter S trust (QSST) within the meaning of § 1361(d), but the Income Beneficiary did not timely file a QSST election. Furthermore, from Year1 through Year2, the trustee failed to distribute all of the trust's income to the Income Beneficiary in accordance with the terms of Trust2. Therefore, on D4, X's S corporation election terminated.

X represents that the termination was not motivated by tax avoidance or retroactive tax planning, and that Trust2 will distribute all previously undistributed trust income to Income Beneficiary. X further represents that it has filed consistently as an S corporation since D2. X and its shareholder have agreed to make any adjustments that the Commissioner may require, consistent with the treatment of X as an S corporation.

LAW AND ANALYSIS

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) provides that 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 1361(c)(2)(A)(i) provides that for purposes of § 1361(b)(1)(B), a trust all

of which is treated (under subpart E of part 1 of subchapter J of Chapter 1) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(d)(1) provides that a QSST whose beneficiary makes an election under § 1361(d)(2) will be treated as a trust described in § 1361(c)(2)(A)(i), and the beneficiary of such trust shall be treated as the owner (for purposes of § 678(a)) of that portion of the trust which consists of stock in an S corporation with respect to which the election under § 1361(d)(2) is made.

Section 1361(d)(2)(A) provides that a beneficiary of a QSST (or his legal representative) may elect to have § 1361(d) apply. Section 1361(d)(2)(D) provides that an election under § 1361(d)(2) shall be effective up to 15 days and 2 months before the date of the election.

Section 1.1361-1(j)(6)(ii) of the Income Tax Regulations provides that the current income beneficiary of the trust must make the election under § 1361(d)(2) by signing and filing with the service center where the corporation files its income tax return the applicable form or a statement including the information listed in § 1.1361-1(j)(6)(ii).

Section 1362(d)(2)(A) provides that an election under § 1362(a) will 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)(A) is effective on and after the date of cessation.

Section 1362(f) provides, in relevant part, 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 the 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, 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 the 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 the representations made, we conclude that X's S corporation election terminated on D4 when X had an ineligible shareholder. We also conclude that the circumstances resulting in the termination were inadvertent within the meaning of § 1362(f). Accordingly, under § 1362(f), X will be treated as an S corporation from D4 and thereafter, provided X's S corporation election was otherwise

valid and has not otherwise terminated under § 1362(d) for reasons not addressed in this letter.

This ruling is conditioned on the estate of Income Beneficiary filing, on behalf of Income Beneficiary, a QSST election for Trust2, effective D4, with the appropriate service center within 120 days of the date of this letter. A copy of this letter should be attached to the QSST election.

In addition, this ruling is conditioned on Trust2 filing any amended returns and making adjustments that are necessary to properly reflect the treatment of Trust2 as an QSST, including the distribution of all of Trust2's previously undistributed income to Income Beneficiary, consistent with X's representation.

Furthermore, as an adjustment under § 1362(f), a payment of \$n and a copy of this letter ruling must be sent to the following address: Internal Revenue Service, Cincinnati Service Center, 201 West Rivercenter Blvd., Covington, KY 41011, Stop 31, , Manual Deposit. The payment and a copy of this letter must be sent no later than D6.

If all of the above conditions are not met, then this ruling is null and void. Furthermore, if these conditions are not met, X must send a notification that its S corporation election has terminated to the service center with which X's S corporation election was filed.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of the facts described above under any other provisions of the Code. Specifically, we express no opinion regarding X's eligibility to be an S corporation.

This ruling is directed only to the taxpayer that requested 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,

Richard T. Probst
Senior Technician Reviewer, Branch 3
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2):

Copy of this letter
Copy for § 6110 purposes