

Internal Revenue Service

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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:B3

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Date:

May 09, 2016

Legend

X =

Y =

A =

B =

C =

D =

E =

Trust =

Estate =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Dear _____ :

This letter responds to a letter dated January 7, 2016, and subsequent correspondence, submitted on behalf of X by its authorized representatives, requesting a ruling under § 1362(f) of the Internal Revenue Code (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 and Date 3, shares of X were transferred from A to B, who then transferred the shares to Y, an ineligible shareholder under § 1361(b)(1). The members of Y are B and C and are eligible shareholders under § 1361(b)(1). On Date 4, B requested that the shares be treated as owned directly by B and C.

On Date 5, D died. Under § 1361(c)(2)(A)(iii), Trust was an eligible shareholder until Date 6, two years after it received the shares of X from Estate pursuant to the terms of a will. Accordingly, Trust ceased to be eligible shareholder on Date 7. Had X's S corporation election not previously terminated, X's s corporation election would have terminated on Date 7. X represents that on Date 8 Trust would have qualified as a qualified subchapter S trust ("QSST") under § 1361(d), however no QSST election was filed.

X represents that there was no tax avoidance or retroactive tax planning involved in the transfer of shares of B to Y or in the failure of Trust to timely elect to be classified as a QSST. In addition, X and its shareholders agree to make any adjustments

consistent with the treatment of X as an S corporation as may be required by the Secretary. X also represents that X and all its shareholders have filed consistently with X being treated as an S corporation. In addition, X represents that all items allocable to the shares originally acquired by Y were allocated to and reported by B and C, eligible shareholders. Trust represents that E reported the income, gain, and loss allocated to Trust by reason of ownership of X stock. X represents that Trust qualified as a QSST under section 1361(d) from Date 8.

Law and Analysis

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 the term “small business corporation” means a domestic corporation that is not an ineligible corporation and that does not, among other requirements, 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(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 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 I of subchapter J of chapter 1 of the Code) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(c)(2)(A)(iii) provides that for purposes of § 1361(b)(1)(B), a trust with respect to stock transferred to it pursuant to the terms of a will, but only for the 2-year period beginning on the day on which such stock is transferred to it, may be a shareholder.

Section 1361(d)(1) provides that in the case of a QSST with respect to which a beneficiary makes an election under § 1361(d)(2), the trust is treated as a trust described in § 1361(c)(2)(A)(i), and for purposes of § 678(a), the beneficiary of such trust shall be treated as the owner 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 may elect to have § 1361(d)(1) apply.

Section 1362(d)(2)(A) provides that an election under § 1362(a) is 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 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 circumstances resulting in such termination, steps were taken so that the corporation for which the termination occurred is a small business corporation; and (4) the corporation for which the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agree to make the adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to this period, then, notwithstanding the circumstances resulting in such termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(b) provides that the determination of whether a termination was inadvertent is made by the Commissioner. The corporation has the burden of establishing that under the relevant facts and circumstances the Commissioner should determine that the termination was inadvertent. The fact that the termination event was not reasonably within the control of the corporation and was not part of a plan to terminate the election, or the fact that the terminating event or circumstance took place without the knowledge of the corporation, notwithstanding its due diligence to safeguard itself against such an event or circumstance, tends to establish that the termination of the election was inadvertent.

Conclusion

Based solely on the facts submitted and representations made, we conclude that X's S corporation election was terminated on Date 2 and that the termination was inadvertent within the meaning of § 1362(f). We further conclude that, if X's S corporation election was not already terminated, Trust's failure to make a timely QSST election would have caused X's S corporation election to terminate on Date 7. Consequently, we rule that X will be treated as an S corporation from Date 2 and thereafter provided that X's S corporation election was otherwise valid and not otherwise terminated under § 1362(d).

This ruling is contingent on the beneficiary (or beneficiary's representative) of Trust filing a QSST election for Trust effective Date 8 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.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of the facts described above under any other provision of the Code, including whether Trust is a valid QSST.

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 for precedent.

Pursuant to a power of attorney on file, we are sending a copy of this letter to X's authorized representatives.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the rulings requested, it is subject to verification on examination.

Sincerely,

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

Enclosures (2):

Copy of this letter

Copy for §6110 purposes

cc: