

Internal Revenue Service

Number: **201716003**

Release Date: 4/21/2017

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:B01

PLR-121903-16

Date:

January 05, 2017

X =

A =

B =

Trust 1 =

Trust 2 =

Trust 3 =

State =

Date 1 =

Date 2 =

Date 3 =

Dear

This letter responds to a letter dated June 27, 2016, and subsequent correspondence, submitted on behalf of X, requesting relief under § 1362(f) of the Internal Revenue Code.

Facts

The information submitted states that X was formed under the laws of State on Date 1. X filed a timely election under § 1362(a) to be taxed as an S corporation effective Date 1. Shares of X stock were transferred to Trust 1 on Date 2. Trust 1 was treated (under subpart E of part I of subchapter J of chapter 1 of the Internal Revenue Code) as owned by spouses A and B. Thus, Trust 1 was a permitted S corporation shareholder pursuant to § 1361(c)(2)(A)(i). A died on Date 3.

Trust 1's agreement provides that, upon the death of either A or B, the trustee shall divide Trust 1 into two separate trusts, designated as Trust 2 and Trust 3. Effective Date 3, the trustee distributed the X stock held by Trust 1 to Trust 2 and Trust 3. Trust 2 was treated (under subpart E of part I of subchapter 1) as owned by B. Thus, Trust 2 was a permitted S corporation shareholder pursuant to § 1361(c)(2)(A)(i).

X represents that Trust 3 has at all times qualified to elect to be a Qualified Subchapter S Trust (QSST) within the meaning of § 1361(d)(3); however, B, the beneficiary of Trust 3, failed to timely file a QSST election for Trust 3.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and were not motivated by tax avoidance or retroactive tax planning. Additionally, X represents that X and its shareholders have filed their federal income tax returns consistent with having a valid S corporation election in effect for X. X and its shareholders have agreed to make any adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

Law and Analysis

Section 1361(a)(1) of the Code 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) defines a "small business corporation" as 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 1 class of stock.

Section 1361(c)(2)(A)(i) provides that, for the purposes of §1362(b)(1)(B), a trust all of which is treated (under title 26, subtitle A, chapter 1, subchapter J, part I, subpart E of the United States Code) as owned by an individual who is a citizen or resident of the United States may be a shareholder of an S corporation.

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), (A) such trust will be treated as a trust described in § 1361(c)(2)(A)(i), and (B) 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 (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 1361(d)(3) defines a QSST as a trust (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust; (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary; (iii) the income interest of the current income beneficiary in the trust shall terminate on the earlier of the beneficiary's death or the termination of the trust; and (iv) upon the termination of the trust during the life of the current income beneficiary; the trust shall distribute all of its assets to that beneficiary; and (B) all of the income (within the meaning of § 643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the tax 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 consents, or (B) was terminated under paragraph (2) or (3) of § 1362(d); (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 event resulting in the ineffectiveness or 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 § 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 or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and representations made, we conclude X's S election terminated on Date 3 resulting from the failure of B, as the beneficiary of Trust 3, to make the election under § 1361(d)(2).

We further conclude that the termination was inadvertent within the meaning of § 1362(f). Accordingly, X will be treated as continuing to be an S corporation from Date 3 and thereafter, provided that its S corporation election was otherwise valid and was not otherwise terminated under § 1362(d). Trust 3 will be treated as a QSST from Date 3 and thereafter, provided that B files a QSST election effective Date 3 with the appropriate service center within 120 days from the date of this letter. A copy of this letter should be attached the QSST election.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed or implied concerning the eligibility of X to be an S corporation.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

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

Sincerely,

Laura C. Fields

Laura C. Fields
Senior Technician Reviewer, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes