

## 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:B01

PLR-138489-16

Date:

June 12, 2017

## LEGEND

X =

A =

Trust =

Date 1=

Date 2=

Date 3=

Date 4=

Date 5=

Date 6=

Years1=

State =

\$a =

Dear \_\_\_\_\_ :

This responds to a letter dated December 7, 2016, and supplemental correspondence, submitted on behalf of X, by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code (the Code).

## FACTS

According to the information submitted and representations within, X was incorporated on Date 1, under the laws of State. On Date 1, A was a shareholder of X. A died on Date 2 at which time A's estate became a shareholder of X. Effective Date 3, X elected to be taxed as an S corporation. On Date 4, A's shares of X stock were transferred to Trust, pursuant to the terms of A's will. Trust qualified under § 1361(c)(2)(A)(iii) as an eligible shareholder for a two-year period beginning on the day the shares of X were transferred to it. A timely election to treat Trust as an Electing Small Business Trust (ESBT) was not made, thus causing X's S election to terminate on Date 5.

X represents that Trust has at all times met the requirements of an ESBT within the meaning of § 1361(e), except that the trustee of Trust did not file a timely ESBT election under § 1361(e)(3). X represents that Trust made a distribution of the X stock on Date 6. X also represents that the failure to file an ESBT election for Trust was inadvertent and was not motivated by tax avoidance or retroactive tax planning.

X represents that, other than the failure of the trustee of Trust to file a timely ESBT election on Date 4, X has qualified as a small business corporation at all times since its election on Date 3. In addition, X represents that it has filed its returns consistent with being an S corporation. X represents that its S corporation election termination was inadvertent and was not motivated by tax avoidance or retroactive tax planning. Further, X represents that X and its shareholders agree to make any adjustments required as a condition of obtaining relief under the inadvertent termination rule as provided under § 1362(f) of the Code that may be required by the Secretary.

## 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)(v) provides that, for purposes of § 1362(b)(1)(B), an electing small business trust (ESBT) may be an S corporation shareholder.

Section 1361(e) an ESBT means any trust if (i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (III) an organization described in § 170(c)(2), (3), (4), or (5), or (IV) an organization described in § 170(c)(1) which holds a contingent interest in such trust and is not a potential current beneficiary, (ii) no interest in such trust was acquired by purchase, and (iii) an election under § 1361(e) applies to such trust.

Section 1361(e)(1)(B) provides that the term “electing small business trust” shall not include (i) any qualified subchapter S trust (as defined in § 1361(d)(3)) if an election under § 1361(d)(2) applies to any corporation the stock of which is held by such trust, (ii) any trust exempt from tax under subtitle A, and (iii) any charitable remainder annuity trust or charitable remainder unitrust (as defined in § 664(d)).

Section 1361(e)(3) provides that an election under § 1361(e) shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) provides that the trustee of an ESBT must make the ESBT election by signing and filing, with the service center where the S corporation files its income tax return, a statement that meets the requirements of § 1.1361-1(m)(2)(ii).

Section 1.1361-1(m)(2)(iii) provides that the trustee of an ESBT must file the ESBT election within the time requirements prescribed in § 1.1361-1(j)(6)(iii) for filing a QSST election (generally within the 16-day-and-2-month period beginning on the day that the stock is transferred to the trust).

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or was terminated under § 1362(d)(2) or (3); (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 circumstances resulting in such ineffectiveness or termination, steps were taken so that the corporation for which the election was made or termination occurred is a small business corporation; and (4) the corporation for which the election was made or 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 the 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 ineffectiveness or termination, such corporation shall 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 election terminated on Date 5 because of the failure of the trustee to timely file an ESBT election for Trust. We further conclude that the termination of X's S election was inadvertent within the meaning of § 1362(f). Therefore, X will be treated as an S corporation effective Date 5 and thereafter, provided X's S corporation election is otherwise valid and not otherwise terminated under § 1362(d).

This letter ruling is subject to the following conditions being met within 120 days from the date of this letter: (1) an adjustment payment in the amount of \$a and a copy of this letter must be sent to the following address: Internal Revenue Service, Cincinnati Service Center, 201 West Rivercenter Blvd., Covington, KY 41011, Stop 31, Terri Lackey, Manual Deposit; (2) X, X's shareholders, Trust and Trust's beneficiary must file any original and amended returns for Years1 and make such adjustments that are both consistent with treating Trust as an ESBT and that are necessary to properly reflect the reporting of X's items of S corporation income; and (3) the trustee of Trust filing an ESBT election under § 1361(e)(3), with the appropriate service center, to treat Trust as an ESBT effective Date 4. A copy of this letter should be attached to the ESBT election. If these conditions are not met, then this ruling is null and void. Furthermore, if these conditions are not met, X must send notification that its S election has terminated to the service center with which X's S election was filed.

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

This ruling is directed only to the taxpayer requesting 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, a copy of this letter is being sent to your 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 of this letter for section 6110 purposes

cc: