



## FACTS

X was formed under the laws of State on D1 and elected to be an S corporation effective as of that date. Prior to D2, Trust was a trust all of which was treated as owned by Grantors, and thus an eligible S Corporation shareholder under § 1361(c)(2)(A)(i). On D2, Grantors amended Trust, resulting in Trust no longer being an eligible shareholder under § 1361(c)(2)(A)(i). X represents that Trust was eligible to be an electing small business trust (ESBT) within the meaning of § 1361(e) on D2, but the trustees did not timely file an ESBT election. Therefore, because Trust was not a permitted shareholder, X's S corporation election terminated on D2.

X represents that the termination of its S corporation election was not motivated by tax avoidance or retroactive tax planning. X further represents that X and its shareholders have filed consistently with the treatment of X as an S corporation since D2. X and its shareholders 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)(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(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 I 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(c)(2)(A)(v) provides that for purposes of § 1361(b)(1)(B) an ESBT may be a shareholder.

Section 1361(e)(1)(A) provides that, except as provided in § 1361(e)(1)(B), 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)(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 years of the trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) of the Income Tax Regulations 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 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) 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 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), 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 D2. 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 D2 and thereafter, provided X's S corporation election was otherwise valid and has not otherwise terminated under § 1362(d).

This ruling is conditioned on the trustee of Trust filing an ESBT election, effective D2, with the appropriate service center within 120 days of the date of this letter. A copy of this letter should be attached to the ESBT election. X and its shareholders must file any original and amended returns for all open years consistent with the relief granted in this letter. If these conditions are not met, then this ruling is null and void.

Except as specifically ruled above, we express 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, or Trust's eligibility to be an ESBT.

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

The ruling contained in this letter is 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 ruling request, it is subject to verification on examination.

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

Sincerely,

/s/

Joy C. Spies  
Senior Technician Reviewer, Branch 1  
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes

cc: