

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **202229026**
Release Date: 7/22/2022
Index Number: 1362.04-00

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B01
PLR-121709-21
Date:
April 18, 2022

Legend

X =

A =

State =

Date 1 =

Date 2 =

Date 3 =

Trust =

Dear _____ :

This letter responds to a letter dated October 13, 2021, and subsequent correspondence, submitted on behalf of X by X's authorized representatives, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code (Code).

Facts

According to the information submitted and representations within, X was incorporated under the laws of State on Date 1. X filed a timely election under § 1362(a) of the Code to be taxed as an S corporation effective Date 1.

On Date 2, A, an individual, transferred shares of X stock to Trust, an irrevocable trust. X represents that X believed that Trust was a permissible S corporation shareholder

under § 1361(c)(2)(A)(i). Further, X represents that Trust and A filed tax returns as if Trust was treated (under subpart E of Part I of subchapter J of chapter 1 of the Code) as a grantor trust all of which was owned by A until Date 3 when A died. However, Trust by its terms did not satisfy the qualifications under § 1361(c)(2)(A)(i). Consequently, X's S corporation election terminated on Date 2.

Following A's death, X represents that Trust qualifies as an Electing Small Business Trust (ESBT) under § 1361(e)(1)(A) effective Date 3. However, the trustee of Trust failed to file an ESBT election under § 1361(e)(3) effective Date 3. Therefore, had X's S corporation election not already terminated on Date 2, it would have terminated on Date 3.

X represents that the circumstances resulting in the termination of X's S corporation election were not motivated by tax avoidance or retroactive tax planning considerations. 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 purposes of § 1361(b)(1)(B), a trust all of which is treated (under subpart E) 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(c)(2)(A)(v) provides that, for purposes of § 1361(b)(1)(B), an ESBT may be an S corporation shareholder

Section 1361(e)(1)(A) provides that 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 taxable years of such trust unless revoked with the consent of the Secretary.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1st day of the taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

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) or § 1361(b)(3)(C); (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 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 termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the information submitted and the representations made, we conclude that X's S corporation election terminated on Date 2, when shares of X were transferred to Trust. In addition, had X's S corporation election had not already terminated on Date 2, it would have terminated on Date 3 when the trustee of Trust failed to make an election under 1361(e)(3) to treat Trust as an ESBT effective Date 3. We further conclude that circumstances resulting the termination of X's S corporation were inadvertent within the meaning of § 1362(f). Accordingly, pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 2 and thereafter, provided that X's S corporation election is otherwise effective and not terminated under § 1362(d) for reasons not addressed in this letter.

Trust will be treated will be treated as a trust described in § 1361(c)(2)(A)(i) from Date 2 until Date 3. Further, Trust will be treated as a ESBT from Date 3 and thereafter, provided that the trustee of Trust files an ESBT 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 ESBT election.

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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k) 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 representatives.

Sincerely,

Jennifer Keeney
Senior Counsel, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes

cc: