

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:B01  
PLR-113904-22

Date:  
January 13, 2023

Legend

X =

A =

B =

C =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Trust =

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

This letter responds to a letter dated July 20, 2022, submitted on behalf of X by its authorized representatives, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code (Code).

#### Facts

X was organized on Date 1, under the laws of State. Effective Date 1, X elected to be taxed as an S corporation.

On Date 2, A and B established Trust for the benefit of C. On Date 3, shares of X were issued to Trust. Trust remained a shareholder until Date 4. X represents that Trust was eligible to be a qualified subchapter S trust (QSST) under § 1361(c)(2)(A)(i); however, the beneficiary of Trust failed timely to file such a QSST election.

X represents that the failure to file the QSST election for Trust was inadvertent and not motivated by tax avoidance or retroactive tax planning. X further represents that: (1) X has filed its income tax returns consistent with having a valid S corporation election in effect for all taxable years since X elected to be an S corporation; (2) Trust continuously qualified as a QSST from Date 3 through Date 4, and has filed all relevant U.S. federal income tax returns on a basis consistent with having a valid QSST election in effect as of Date 3; (3) C has filed C's federal income tax returns for all relevant periods on a basis consistent with Trust having a valid QSST election in effect as of Date 3; and (4) X has continuously qualified as a small business corporation from Date 1 until Date 5. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as 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)(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) 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, in pertinent part, 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 the trust is 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)(3) provides that the term “qualified subchapter S trust” means a trust (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only 1 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 such 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 such beneficiary, and (B) all of the income (within the meaning of section 643(b)) of which is distributed (or required to be distributed) currently to 1 individual who is a citizen or resident of the United States. A substantially separate and independent share of a trust within the meaning of § 663(c) shall be treated as a separate trust for purposes of § 1361(d)(3) and § 1361(c).

Section 1.1361-1(j)(7)(i) of the Income Tax Regulations provides that the income beneficiary who makes the QSST election and is treated (for purposes of § 678(a)) as the owner of that portion of the trust that consists of S corporation stock is treated as the shareholder for purposes of §§ 1361(b)(1), 1366, 1367, and 1368.

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); (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 3, when Trust became an ineligible shareholder. We also conclude that the termination of X's S corporation election on Date 3 was inadvertent within the meaning of § 1362(f). Accordingly, under § 1362(f), X will be treated as continuing to be an S corporation on and after Date 3, provided that X's S corporation election was valid and not otherwise terminated under § 1362(d).

This ruling is contingent upon C, as the beneficiary of Trust, filing a QSST election for Trust within 120 days of the date of this letter with the appropriate service center. A copy of this letter should be attached to the QSST 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 or whether Trust was or is otherwise a valid QSST.

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.

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/

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Caroline E. Hay  
Senior Technician Reviewer, Branch 1  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes

cc: