

**Internal Revenue Service**

Department of the Treasury  
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LEGEND

- X =
- A =
- B =
- Y =
- State =
- Date 1 =
- Date 2 =
- Date 3 =
- Date 4 =
- Date 5 =

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

This responds to a letter dated August 31, 2022, submitted on behalf of X by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code (the Code).

FACTS

The information submitted states that X was organized under the laws of State on Date 1 and elected to be treated as an S corporation, effective Date 2. On Date 3, A

and B issued shares of X to Y, an ineligible shareholder, thereby terminating X's S election. A, B, and X were unaware that Y was an ineligible shareholder. On Date 4, X's counsel informed A, B, and X that Y was an ineligible shareholder of X. On Date 5, Y distributed its shares in X to A, B, and the remainder of the shareholders, all of which are represented by X to be eligible S corporation shareholders.

X represents that it has filed tax returns consistent with being an S corporation since Date 1. 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. 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 1362(a) 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) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1361(b)(1) provides that a "small business corporation" means a domestic corporation that is not an ineligible corporation and that 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 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which a corporation is an S corporation) such corporation ceases to be a small business corporation. Section 1362(d)(2)(B) provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides, in pertinent 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 section 1361(b), or 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 event resulting in the ineffectiveness or termination, steps were taken (A) so that the corporation for which the election was made or the termination occurred is a small business corporation, 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 information submitted and the representations made, we conclude that X's S corporation election was terminated on Date 3, under § 1362(d)(2), because of the transfer of shares of X to Y, an ineligible shareholder. We conclude, however, that the termination described in this paragraph was inadvertent within the meaning of § 1362(f). Accordingly, pursuant to the provisions of § 1362(f), X will be treated as an S corporation from Date 2 and thereafter, provided X's S corporation election was valid and was not otherwise terminated under § 1362(d).

Except for the specific ruling 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. In particular, we express or imply no opinion regarding X's eligibility to be an S corporation.

The ruling contained in this letter is based on information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by the 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.

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

Sincerely,

Laura C. Fields

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

Encl:

Copy for § 6110 purposes

cc: