

Internal Revenue Service

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Person To Contact:
, ID No.

Telephone Number:

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Date:
July 12, 2023

LEGEND

X =

A =

N1 =

Trust 1 =

Date 1

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

State =

Dear _____ :

This letter responds to a letter dated December 21, 2022, submitted on behalf of X by its authorized representatives, requesting relief under § 1362(f) of the Internal Revenue Code (Code).

FACTS

The information submitted states that X was incorporated under the laws of State on Date 1. X filed an election under § 1362(a) to be taxed as an S corporation effective Date 2.

On Date 3, A established Trust 1, a grantor trust, and on Date 4, transferred N1 shares of X to Trust 1. A died on Date 5. Trust 1 continued to qualify as an eligible S corporation shareholder for the two-year period beginning on Date 5. The beneficiary did not file a timely election for Trust 1 to be treated as a qualified subchapter S trust (QSST) with the appropriate service center, and Trust 1 ceased to qualify as a shareholder under § 1361(c)(2)(A)(i). Therefore, the S election for X terminated on Date 6. Furthermore, the terms of Trust 1 provided for more than one income beneficiary.

X represents that it has always operated consistent with a validly filed QSST election for Trust 1. X represents that the terms of Trust 1 have been amended such that the terms of Trust 1 satisfy the requirements of a QSST under § 1361(d)(3) and further represents that income of the QSST was fully reported by the sole beneficiary. X further represents that 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 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) 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 of the Code) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(c)(2)(A)(ii) provides that, for purposes of § 1361(b)(1)(B), a trust which was described in clause § 1361(c)(2)(A)(i) immediately before the death of the deemed owner and which continues in existence after such death may be a shareholder, but only for the 2-year period beginning on the day of the deemed owner's death.

Section 1361(d)(1) provides 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 such trust shall be 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)(2)(A) provides that a beneficiary of a QSST may elect to have § 1361(d)(1) apply.

Section 1361(d)(3) defines a QSST as a trust, (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one 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 § 643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1.1361-1(j)(6)(ii) provides that the beneficiary of a QSST must make the QSST 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(j)(6)(ii).

Section 1.1361-1(j)(7)(i) 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 1.1362-6(b)(2)(iv) of the Income Tax Regulations provides that in the case of a trust described in § 1361(c)(2)(A) (including a trust treated under § 1361(d)(1)(A) as a trust described in § 1361(c)(2)(A)(i) and excepting an electing small business trust

described in §1361(c)(2)(A)(v)), only the person treated as the shareholder for purposes of §1361(b)(1) must consent to the election.

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 to obtain shareholder consents or was terminated under § 1362(d)(2), (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 the termination occurred is a small business corporation or to acquire the required shareholder consents, and (4) the corporation for which the election was made or 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 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 corporation election terminated on Date 6, when the beneficiary of Trust 1 failed to submit a QSST election with the appropriate service center on or before Date 6. Even if the S election had been submitted to the appropriate service center, we conclude that the terms of Trust 1 failed to satisfy the requirements of a QSST under § 1361(d)(3). We further conclude that the circumstances resulting in the termination of X's S corporation election were inadvertent within the meaning of § 1362(f). Therefore, pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 6, and thereafter, provided that a valid QSST election is submitted for Trust 1 with the appropriate service center, and all trusts therein created, and provided further that X's S corporation election was not otherwise terminated under § 1362(d) for reasons not addressed in this letter.

This ruling is contingent on the beneficiary of Trust 1 filing within 120 days from the date of this letter a valid QSST election effective Date 6, with the appropriate service center. A copy of this letter should be attached to such QSST election.

If the above conditions are not met, then this ruling is null and void. Furthermore, if these conditions are not met, X must notify the service center with which it filed its S corporation election that its election terminated on Date 6.

Except as specifically set forth above, we express or imply no opinion concerning the federal tax consequences of the facts described above under any other provision of the

Code. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation. In addition, we express or imply no opinion as to whether Trust 1 is eligible to elect to be treated as a QSST.

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 upon examination.

This ruling is directed only to the taxpayer who requested 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, we are sending copies of this letter to X's authorized representatives.

Sincerely,

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

Enclosure
Copy for § 6110 purposes

cc: