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Washington, DC 20224

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Person To Contact:

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PLR-107811-23

Date:

October 06, 2023

Legend:

X =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

State =

Trust 1 =

Trust 2 =

A =

Dear :

This letter responds to a letter dated March 23, 2023, and subsequent correspondence, submitted on behalf of X by its authorized representatives, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

FACTS

According to the information submitted, X was incorporated under the laws of State on Date 1 and elected to be an S corporation effective Date 2. On Date 3, Trust 1 was formed and subsequently became a shareholder of X.

X represents that Trust 1 was a grantor trust and eligible S corporation shareholder under § 1361(c)(2)(A)(i) at all times since it first acquired shares of X until Date 4, at which point Trust 1 no longer qualified as an eligible S corporation shareholder under § 1361(c)(2)(A)(i). On Date 4, the shares of X held by Trust 1 were transferred to Trust 2. X represents that Trust 2 was eligible to elect to be treated as a qualified subchapter S trust (QSST) under § 1361(d). However, A, Trust 2's income beneficiary, failed to make an election under § 1361(d)(2) to treat Trust 2 as a QSST effective Date 4. Therefore, X's S election terminated on Date 4.

X represents that the circumstances resulting in the termination of its S corporation election were inadvertent and were not motivated by tax avoidance or retroactive tax planning. Further, X represents that since inception X and its shareholders have filed tax returns consistent with X being an S corporation, and Trust 2 being a QSST since Date 4. Finally, X and its shareholders agree to make any 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 the 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 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 an S corporation shareholder.

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) — (A) such trust shall be treated as a trust described in § 1361(c)(2)(A)(i), (B) 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, and (C) for purposes of applying §§ 465 and 469 to the beneficiary of the trust, the disposition of the S corporation stock by the trust shall be treated as a disposition by such beneficiary.

Section 1361(d)(2) provides that a beneficiary of a QSST (or his legal representative) may elect to have § 1361(d) 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 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)(2)(A) 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 such 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 once more a small business corporation, and (4) the corporation for which the termination occurred and each person who was a shareholder in the corporation at any time during the period specified pursuant to § 1362(f), agrees to make adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to the 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 Date 4 when Trust 2 became an ineligible shareholder. We also conclude that the circumstances resulting in the termination of X's S corporation election were inadvertent within the meaning of § 1362(f). Therefore, X will be treated as continuing to be an S corporation from Date 4 and thereafter, provided that X's S election was otherwise valid and was not otherwise terminated under § 1362(d).

This ruling is contingent on A filing a QSST election for Trust 2 effective Date 4, with the appropriate service center within 120 days from the date of this letter. A copy of this letter should be attached to the QSST election.

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation or Trust 2's eligibility to be 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 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 to X's authorized representatives.

Sincerely,

Robert D. Alinsky
Branch Chief, Branch 3
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:

Copy of letter for § 6110 purposes

cc: