

Internal Revenue Service

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Person To Contact: _____, ID No.

Telephone Number:

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Date:
December 10, 2024

LEGEND

X =

A =

B =

Trust 1 =

Trust 2 =

Trust 3 =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Year =

Dear _____ :

This letter responds to a letter dated June 3, 2024, and subsequent correspondence, submitted on behalf of X by its authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code.

FACTS

According to the information submitted and representations made, X was organized on Date 1 under the laws of State. X elected to be treated as an S corporation effective Date 2.

A and B, individuals, held shares of X. On Date 3, A died, and A's shares of X were transferred to Trust 1 pursuant to the terms of A's will. Trust 1 made a timely QSST election. On Date 4, B died and per the terms of A and B's separate wills, B's shares of X and the shares of X held in Trust 1 were each divided equally and transferred to Trust 2 and Trust 3 on Date 5.

X represents that Trust 2 and Trust 3 qualified to elect to be treated as Electing Small Business Trusts as of Date 5. However, the trustees of Trust 2 and Trust 3 failed to make timely ESBT elections under § 1361(e)(3), thereby causing X's S corporation election to be ineffective.

X represents that X and its shareholders have filed tax returns consistent with being an S corporation for all relevant periods. X further 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. 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 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)(v) provides that, for purposes of § 1361(b)(1)(B), an ESBT may be an S corporation shareholder.

Section 1361(c)(2)(A)(ii) provides that a trust which was described in § 1361(c)(2)(A)(i) immediately before the death of the deemed owner and which continues in existence after such death, but only for the 2-year period beginning on the day of the deemed owner's death is a permissible 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)(1)(B) provides that an ESBT does not include (i) any qualified subchapter S trust (as defined in § 1361(d)(3)) if an election under § 1361(d)(2) applies to any corporation the stock of which is held by such trust, (ii) any trust exempt from tax under subtitle A, and (iii) any charitable remainder annuity trust or charitable remainder unitrust (as defined in § 664(d)).

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 1.1361-1(m)(2)(i) of the Income Tax Regulations provides, in part, that the trustee of an ESBT must make the ESBT 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(m)(2)(ii).

Section 1.1361-1(m)(2)(iii) provides that the trustee of an ESBT must file the ESBT election within the time requirements prescribed in § 1.1361-1(j)(6)(iii) for filing a QSST election (generally within the 16-day-and-2-month period beginning on the day that the stock is transferred to the trust).

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 1st 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 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 information submitted and the representations made, we conclude that X's S corporation election terminated on Date 5 when Trust 2 and Trust 3 became ineligible shareholders.

We further conclude that the circumstances resulting in the termination of X's S corporation election 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 beginning on and after Date 5, and thereafter, provided that X's S corporation election was valid and was not otherwise terminated under § 1362(d) for reasons not addressed in this letter.

We additionally conclude that Trust 2 and Trust 3 will be treated as ESBTs from Date 5 and thereafter. This letter is contingent on the following conditions that must occur within 120 days of the date of this letter (1) the trustees of Trust 2 and Trust 3 must each file an election to treat Trust 2 and Trust 3 as ESBTs, effective Date 5, with the appropriate service center, and (2) X and the trustees of Trust 2 and Trust 3, must file any original or amended returns and making adjustments to properly reflect the treatment of the trusts as ESBTs for Year and all subsequent taxable years. A copy of this letter should be attached to each ESBT election and return.

If the conditions are not met, this ruling is null and void. In addition, 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 5.

Except as specifically ruled 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 whether X is otherwise eligible to be an S corporation or whether Trust 2 and Trust 3 are otherwise eligible to be ESBTs.

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 representative.

Sincerely,

Holly Porter
Associate Chief Counsel
(Passthroughs & Special Industries)

By: _____
Jennifer N. Keeney
Senior Counsel, Branch 1
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy of letter for § 6110 purposes

cc: