

Internal Revenue Service

Number: **202345006**

Release Date: 11/10/2023

Index Number: 1361.01-02, 1361.03-00,
1361.03-02, 1362.00-00,
1362.01-00, 1362.02-00,
1362.02-02, 1362.04-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B01

PLR-103484-23

Date:

August 15, 2023

Legend

X =

Y

A =

a =

b =

c =

Trust 1 =

Trust 2 =

Trust 3 =

Trust 4 =

Trust 5 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

State =

Dear :

This letter responds to a letter dated February 10, 2023, and subsequent correspondence, submitted on behalf of X, by X's authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code.

FACTS

According to the information submitted, Y was formed as a limited liability company under the laws of State on Date 1 and elected to be treated as an S corporation effective Date 2. As of Date 2, A owned a% of the membership interests in Y.

On Date 3, A transferred b% of the membership interests in Y to each of Trust 1, Trust 2, Trust 3, and Trust 4. However, the beneficiaries of Trust 1, Trust 2, Trust 3, and Trust 4 failed to timely make Qualified Subchapter S Trust (QSST) elections, and the governing documents of Trust 1, Trust 2, Trust 3, and Trust 4 did not satisfy the requirements to qualify the trusts as QSSTs.

A died on Date 4. On Date 5, A's estate transferred c% of the membership interests in Y to Trust 5 pursuant to the terms of A's will. Trust 5 qualified as an eligible S corporation

shareholder for the two-year period beginning on the day the membership interests in Y were transferred to it under § 1361(c)(2)(A)(iii). Y represents that beginning on Date 6, Trust 5 met the requirements of a QSST. However, the beneficiary of Trust 5 failed to timely make a QSST election.

X was formed as a corporation under the laws of State on Date 7. On Date 8, as part of what X represents was a reorganization under § 368(a)(1)(F), (1) the owners of all membership interests in Y, including Trust 1, Trust 2, Trust 3, Trust 4, and Trust 5, contributed all such membership interests to X, and (2) X elected to treat Y as a Qualified Subchapter S Subsidiary within the meaning of § 1361(b)(3)(B) effective Date 8. Consistent with Rev. Rul. 2008-18, 2008-1 C.B. 674, X was treated as the successor S corporation to Y for federal income tax purposes and therefore did not make a new S election.

On Date 9, the beneficiaries of Trust 1, Trust 2, Trust 3, and Trust 4 entered into a binding non-judicial settlement agreement under State law to qualify the trusts as QSSTs as of Date 3.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance or retroactive tax planning. Additionally, X represents that it has filed its federal income tax returns consistent with having a valid S corporation election in effect for X. X and its shareholders have agreed to make any adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

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)(iii) provides that, for purposes of § 1361(b)(1)(B), a trust with respect to stock transferred to it pursuant to the terms of a will may be a shareholder, but only for the 2-year period beginning on the day on which such stock is transferred to it.

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) apply. Section 1.1361-1(j)(6)(ii) provides that the current income beneficiary of a QSST must make the election under § 1361(d)(2) by signing and filing with the service center with which the corporation files its income tax returns the applicable form or a statement including the information listed in § 1.1361-1(j)(6)(ii).

Section 1362(d)(2) provides that (A) in general, 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 the corporation is an S corporation) such corporation ceases to be a small business corporation, and (B) any termination under § 1362(d)(2) shall be 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.

Rev. Rul. 2008-18, situation 1, holds that, consistent with Rev. Rul. 64-250, 1964-2, C.B. 333, a reorganization under § 368(a)(1)(F) did not cause the termination of an S corporation election under § 1362. In Rev. Proc. 2008-18, B, an individual, owns all of the stock in Y, an S corporation. In Year 1, B forms Newco and contributes all of the Y stock to Newco. Newco meets the requirements for qualification as a small business corporation and timely elects to treat Y as a qualified subchapter S subsidiary (QSub), effective immediately following the transaction. The transaction meets the requirements of a reorganization under § 368(a)(1)(F). Y's original S election does not terminate but continues for Newco. Newco must obtain a new EIN. Y must retain its EIN even though a QSub election is made for it and must use its original EIN any time the QSub is

otherwise treated as a separate entity for federal tax purposes (including for employment and certain excise taxes) or if the QSub election terminates.

CONCLUSIONS

Based solely on the facts submitted and representations made, we conclude that Y's S corporation election terminated on Date 3 due to the failure to file QSST elections for Trust 1, Trust 2, Trust 3, and Trust 4. We further conclude that, if Y's S election had not terminated on Date 3, it would have terminated on Date 6, two years after the transfer of Y stock to Trust 5. We conclude that the terminations were inadvertent within the meaning of § 1362(f). Accordingly, X will be treated as continuing to be an S corporation from Date 3, and thereafter, provided that its S corporation election was otherwise valid and was not otherwise terminated under § 1362(d).

This ruling is contingent upon (1) the beneficiaries of Trust 1, Trust 2, Trust 3, and Trust 4 filing QSST elections effective on Date 3, (2) the beneficiary of Trust 5 filing a QSST election effective on Date 6, and (3) Trust 1, Trust 2, Trust 3, Trust 4, and Trust 5 and their beneficiaries filing timely amended federal income tax returns for all open years consistent with the treatment of the trusts as QSSTs. The elections must be made and the amended returns must be timely filed with the appropriate service center within 120 days of the date of this ruling. A copy of this letter should be attached to the QSST elections and returns. If these conditions are not met, this ruling is null and void.

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 Trust 1, Trust 2, Trust 3, Trust 4, and Trust 5's eligibility to be QSSTs. Further, we express or imply no opinion on the validity of the reorganization under § 368(a)(1)(F) and its tax consequences.

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 who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, we are sending a copy of this letter to X's authorized representative.

Sincerely,

Joy Spies, Senior Technician Reviewer
Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure

Copy for § 6110 purposes

cc: