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Date 5 =

The information submitted states that X was formed under the laws of State on Date 1 and elected to be treated as an S corporation effective Date 2. Prior to Date 3, eligible S corporation shareholders owned all of the stock of X. On Date 3, however, two of X's shareholders contributed their stock in X to A, a partnership, which is an ineligible S corporation shareholder under § 1361(b)(1)(B). X represents that upon discovery of its

error, it promptly took remedial action. On Date 4, A executed a document transferring all of its X shares to eligible S corporation shareholders.

X represents that the transfer of X stock to A, an ineligible shareholder, was not motivated by avoidance or retrospective tax planning. X and its shareholders have continued to treat X as an S corporation at all times. X and its shareholders agree to make any adjustments (consistent with the treatment of X as an S corporation) that the Secretary may require.

Law

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)(B) provides that a “small business corporation” means a domestic corporation that is not an ineligible corporation and that does not 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.

Section 1362(d)(2) 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. A termination of an S corporation election under § 1362(d)(2) is effective on and after the date of cessation.

Section 1362(f) provides 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 event resulting in the ineffectiveness, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, 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, 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 terminated on Date 3, when X stock was transferred to A, an ineligible shareholder. We also conclude that this termination was inadvertent within the meaning of § 1362(f), and that under the provisions of § 1362(f), X will be treated as

an S corporation from Date 3 until Date 5, when X was restructured, provided that X's S election was valid and was not otherwise terminated.

Except for the specific ruling above, we express no opinion concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed concerning whether X was otherwise eligible to be treated as an S corporation.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, a copy of this letter is being sent to X's authorized representatives.

Sincerely,

Joy C. Spies

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

Enclosures (2)
Copy of this letter
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cc: