

Internal Revenue Service

Number: **201909005**
Release Date: 3/1/2019

Index Numbers: 1361.03-02, 1361.03-03,
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:B03
PLR-118647-18

Date:
November 30, 2018

LEGEND

X =

Trust 1

Trust 2 =

Trust 3 =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

A =

a =

Dear :

This responds to a letter dated January 24, 2018, and subsequent correspondence submitted on behalf of X, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code.

FACTS

The information submitted states that X was incorporated under the laws of State on Date 1, and elected to be an S corporation effective Date 2.

On Date 3, A transferred a shares of X stock to Trust 1. X represents that Trust 1 was treated as a wholly-owned grantor trust under §§ 671 and 676.

On Date 4, A died and Trust 1 ceased to be a grantor trust with respect to A' s interests, but would have continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii) for the two year period beginning on the day of the deemed owner's death.

On Date 5, before the end of the two year period, Trust 1 transferred a shares of X stock to Trust 2. X represents that Trust 2 qualified to elect to be treated as an electing small business trust (ESBT), however, the trustee failed to make a timely ESBT election within the meaning of § 1361(e)(1)(A)(v) thereby causing X's S corporation election to terminate on Date 5.

On Date 6, Trust 2 distributed a shares of stock in X to Trust 3. X represents that Trust 3 qualified to elect to be treated as a qualified subchapter S trust (QSST) but the beneficiary failed to make a timely QSST election within the meaning of § 1361(d)(2). The failure to make the QSST election Date 6, would have terminated X's S corporation election had it not already been terminated Date 5.

X represents that the circumstances resulting in the termination of their respective S corporation elections were inadvertent and not motivated by tax avoidance. X further represent that it filed returns consistent with its status as an S corporation. X and its shareholders agree to make such 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)(B) provides that, for purposes of subchapter S, the term “small business corporation” means a domestic corporation which is not an ineligible corporation and which 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 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 1 of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States may be an S corporation shareholder.

Section 1361(c)(2)(A)(ii) and § 1.1361-1(b)(1)(ii) provide that, for purposes of § 1361(b)(1)(B), a trust that is described in § 1361(c)(2)(A)(i) immediately before the death of the deemed owner and that continues in existence after such death is a permitted S corporation shareholder, but only for the two-year period beginning on the day of the deemed owner’s death. Section 1.1361-1(h)(3)(i)(B) provides that if stock is held by a trust described in § 1.1361-1(h)(1)(ii), the estate of the deemed owner is generally treated as the shareholder as of the day of the deemed owner’s death.

Section 1361(c)(2)(A)(v) provides that for the purposes of § 1362(b)(1)(B), an ESBT may be a shareholder.

Section 1361(d)(1) provides, in part, 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).

Section 1362(d)(2) 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(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 circumstances resulting in such termination, steps were taken so that the corporation for which the termination occurred is a small business corporation, and (4) the corporation for which 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 such 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 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 representations made, we conclude that X's S corporation election terminated beginning on Date 5, when the stock in X was transferred to Trust 2, because the trustee of Trust 2 failed to timely file the ESBT election under § 1361(e)(1)(A)(v). We conclude that the termination was inadvertent within the meaning of § 1362(f). Moreover, had X's S corporation election not already terminated on Date 5, it would have terminated on Date 6, when stock was transferred to Trust 3 and the beneficiary of Trust 3 failed to timely file QSST election under § 1361(d)(2). Similarly, this termination was inadvertent within the meaning of § 1362(f).

Pursuant to the provisions of § 1362(f), X will be treated as an S corporation on and after Date 5, unless X's S corporation election is otherwise terminated under § 1362(d). This ruling is conditioned on (1) the trustee of Trust 2 filing an ESBT election effective Date 5, with the appropriate service center within 120 days of the date of this letter, and 2) the beneficiary of Trust 2 filing a QSST election for Trust 2 effective Date 6, within 120 days from the date of this letter. A copy of this letter should be attached the ESBT and QSST elections.

Specifically, we express or imply no opinion regarding whether X is otherwise eligible to be treated as an S corporation or whether Trust 2 is eligible to be treated as an ESBT or whether Trust 3 is eligible to be treated as a QSST.

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

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.

In accordance with a power of attorney on file with this office, we are sending a copy of this letter ruling to your authorized representatives.

Sincerely,

Richard T. Probst
Senior Technician Reviewer, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures: Copy of this letter
Copy of this letter for § 6110 purposes

cc: