

Internal Revenue Service

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November 18, 2004

LEGEND

Company =

Date1 =

Date2 =

Date3 =

Date4 =

Date5 =

Month =

Grantor =

Trust1 =

Trust2 =

Trust3 =

State =

V =

W =

X =

W =

Dear _____ :

We received a letter dated August 4, 2003, and additional correspondence, submitted on behalf of Company requesting a ruling under § 1362(f) of the Internal Revenue Code. This letter responds to that request.

Company was incorporated under State law on Date1. Company filed an election to be treated as an S corporation under § 1362 for its taxable year beginning Date2.

On Date3, Grantor established Trust1, a grantor trust, for estate planning purposes. Prior to Date4, Grantor transferred his V shares of Company stock to Trust1. Grantor passed away on Date4.

Under the terms of the trust instrument establishing Trust1, W of the V shares of Company stock held by Trust1 on Date4 were transferred to Trust2 and X of the V shares held by Trust1 on Date4 were transferred to Trust3. These transfers occurred on Date5, within two years of Date4.

The trustee of Trust2 was not aware that an election was required to treat Trust2 as a Qualified Subchapter S Trust ("QSST") under § 1361(d). During Month, Company discovered that the election to treat Trust2 as a QSST had not been made and that as a result Trust2 was an ineligible shareholder. Shortly thereafter, Company and its shareholders requested inadvertent termination relief under § 1362(f).

Company 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, Company represents that it has filed consistent with being an S corporation at all times since Date2. Each person who was a shareholder of Company during the time period described in § 1362(f) has agreed to make any adjustment (consistent with the treatment of Company as an S corporation) as may be required by the Secretary with respect to the period.

Law

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) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 75 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 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 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 is once more a small business corporation; 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 any 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 shall be treated as continuing to be an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the information submitted and the representations made, we conclude that the transfer of Company stock to Trust2 terminated Company's S election. We also conclude that the termination of Company's S election was inadvertent within the meaning of § 1362(f). Accordingly, pursuant to the provisions of § 1362(f), Company will be treated as continuing to be an S corporation from Date5, and thereafter, provided Company's S election was valid and not otherwise terminated under § 1362(d). Therefore, the shareholders of Company, including Trust2, in determining their federal tax liability during this period, must include their pro rata shares of separately and nonseparately computed items of Company as provided in § 1366, make any adjustments to stock basis as provided in § 1367, and take into account any distributions made by Company to shareholders as provided in § 1368.

Except as specifically set forth above, we express or imply no opinion concerning the federal tax consequences of the above-described facts under any other provision of the Code. Specifically, no opinion is expressed or implied on whether Company is otherwise eligible to be treated as an S corporation.

This ruling is directed only to the taxpayer who requested 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 Company's authorized representative.

Sincerely yours,

/s/

CHRISTINE ELLISON
Chief, Branch 3
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2):

Copy of this letter

Copy for § 6110 purposes

cc: