

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

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Date:
July 25, 2005

Legend:

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

A =

Trust 1 =

Trust 2 =

Trust 3 =

Trust 4 =

Dear _____ :

This responds to a letter dated February 17, 2005, submitted on behalf of X, requesting a ruling under section 1362(f) of the Internal Revenue Code.

Facts

X was incorporated on Date 1 under the laws of State. X elected to be taxed as an S corporation effective Date 2. On Date 3, A, a shareholder of X, transferred all of A's shares of X to Trust 1, a grantor trust. A retained the power to revoke, modify or alter Trust 1 in whole or in part. X represents that Trust 1 is an eligible S corporation shareholder as a grantor trust.

On Date 4, A established Trust 2. At all times relevant to this ruling, Trust 2's only asset was stock in X. X represents that Trust 2 was qualified to elect to be a qualified subchapter S trust. Inadvertently, Trust 2's income beneficiary failed to file a timely election to treat Trust 2 as a qualified subchapter S trust.

On Date 4, A established Trust 3. At all relevant times, Trust 3's only asset was stock in X. X represents that Trust 3 was qualified to elect to be a qualified subchapter S trust. Inadvertently, Trust 3's income beneficiary failed to file a timely election to treat Trust 3 as a qualified subchapter S trust.

On Date 5, A established Trust 4. At all relevant times, Trust 4's only asset was stock in X. X represents that Trust 4 was qualified to elect to be a qualified subchapter S trust. Inadvertently, Trust 4's income beneficiary failed to file a timely election to treat Trust 4 as a qualified subchapter S trust.

The income beneficiary for each trust intended to file an election for Trust 2, Trust 3, and Trust 4, respectively, to be treated as a qualified subchapter S trust (QSST) under section 1361(d). However, all income beneficiaries failed to timely file the appropriate election under 1362(d)(2). As a result of the failure to file this election, X's S corporation election terminated.

X represents that there was no intent to terminate X's S corporation election and that the failure to file timely the QSST election for Trust 2, Trust 3, and Trust 4 was not motivated by tax avoidance or retroactive tax planning. X also represents that since Date 4 and thereafter, Trust 2, Trust 3, and Trust 4 have complied with the requirements under section 1361(d), which defines a QSST.

X and its shareholders agree to make any adjustments required by the Secretary consistent with the treatment of X as an S corporation.

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 section 1362(a) is in effect for such 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 75 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in section 1361(c)(2), or an organization described in section 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(d)(1) provides that a QSST whose beneficiary makes an election under section 1362(d)(2) will be treated as a trust described in section 1361(c)(2)(A)(i), and the QSST's beneficiary will be treated as the owner (for purposes of section 678(a)) of that portion of the QSST's S Corporation stock to which the election under section 1361(d)(2) applies. Under section 1361(d)(2)(A), a beneficiary of a QSST may elect to have section 1361(d) apply. Under section 1361(d)(2)(D), this election will be effective up to 15 days and two months before the date of the election.

Section 1361(d)(3) defines a QSST as a trust (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust; (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary; (iii) the income interest of the current beneficiary in the trust shall terminate on the earlier of the beneficiary's death or the termination of the trust; and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to that beneficiary; and (B) all of the income (within the meaning of section 643(b) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(f) provides, in relevant part, that if (1) an election under section 1362(a) by any corporation was terminated under paragraph (2) or (3) of section 1362(d), (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 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 section 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 X's subchapter S election terminated because QSST elections were not filed for Trust 2, Trust 3, and Trust 4. In addition, we conclude that the termination was inadvertent within the meaning of section 1362(f). Therefore, X will be treated as continuing to be an S corporation from Date 4, and thereafter, provided that the respective beneficiaries for Trust 2, Trust 3, and Trust 4 file a QSST election with the appropriate service center, effective Date 4 for Trust 2 and Trust 3, and effective Date 5 for Trust 4, within 60 days of the date of this letter. A copy of this letter should be attached to the QSST election.

Except as specifically set forth 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 is otherwise eligible to be treated as an S corporation; whether Trust 1 is a grantor trust; or whether Trust 2, Trust 3, or Trust 4 are eligible to be treated as QSSTs.

This ruling is directed only to the taxpayer(s) requesting 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, a copy of this letter is being sent to the taxpayer representative.

Sincerely,

/s/ David R. Haglund

David R. Haglund
Senior Technician Reviewer, Branch 1
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter

Copy of this letter for section 6110 purposes

cc: