

Internal Revenue Service

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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
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Date:
October 19, 2005

LEGEND

X =
TIN:

A =

B =
SSN:

Estate =
TIN:

Date 1 =

Date 2 =

Date 3 =

Year 1 =

Dear

This letter responds to a letter dated June 9, 2005, submitted on behalf of X, requesting relief for an inadvertent invalid subchapter S election under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated on Date 1. On Date 2, A, a shareholder of X, died. On Date 3, X elected to be treated as an S corporation by filling Form 2553, Small Business Corporation Election. B, a dependent administrator with limited rights to act for Estate without court approval, consented to the election on Estate's behalf. In Year 1, X's attorney notified X that B may not have been authorized

to consent on Estate's behalf to the election to treat X as an S corporation. Accordingly, X's S corporation election may have been ineffective.

X represents that if there was an ineffective S corporation election, it was inadvertent and was not motivated by tax avoidance or retroactive tax planning. Further, since Date 3, X and its shareholders have treated X as an S corporation. 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 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 an S corporation cannot 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)(A) provides that an election under § 1362(a) will 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(d)(2)(B) provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides 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 subsection (b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, (2) the Secretary determines that the circumstances resulting in such ineffectiveness were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in such 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 in the corporation at any time during the period specified pursuant to this subsection, 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, such 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 may have been ineffective for the taxable year beginning Date 3, because B may not have been eligible to consent to the S corporation

election on behalf of Estate. We also conclude that if the S corporation election was ineffective, the ineffectiveness of X's S election constituted an inadvertent invalid election within the meaning of § 1362(f). Therefore, we rule that X will be treated as an S corporation from Date 3, and thereafter, provided that X's S election was valid and was not otherwise terminated.

Accordingly, all of the shareholders of X, in determining their respective income tax liabilities for the period beginning Date 3 and thereafter must include their pro rata share of the separately stated and non-separately computed items of X as provided in § 1366, make any adjustments to basis provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this ruling shall be null and void.

Except as specifically ruled upon above, we express no opinion concerning the federal tax consequences of the transactions described above under any other provisions of the Code. Specifically, no opinion is expressed on 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) 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 X's authorized representative.

Sincerely yours,

J. Thomas Hines
Chief, Branch 2
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes