

Internal Revenue Service

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Person To Contact:
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Telephone Number:

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Legend:

X =

A =
Trusts =

State =

a =

D1 =

D2 =

D3 =

D4 =

Dear :

This responds to your letter dated August 26, 2005, submitted on behalf of X, requesting a ruling under § 1362(f) of the Internal Revenue Code.

Facts

According to the information submitted, X was incorporated on D1 under the laws of State. X elected to be treated as a subchapter S corporation effective D1. Trusts were created by A on D2. On D3, a shares of X stock were transferred in varying amounts to Trusts, which were eligible shareholders. On D4, Trusts became ineligible

shareholders. Because of miscommunication and administrative oversight, Trusts failed to timely make an Electing Small Business Trust election, and X's S election was terminated on D4.

X and its shareholders represent that X filed Form 1120S for all relevant years and that each of X's shareholders, including Trusts, continued to file its tax returns for all relevant years, treating X as an S corporation. X and its shareholders consent to make any 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) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect.

Section 1361(b)(1) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation which does not (A) have more than 75 shareholders, (B) have as a shareholder a person (other than an estate and other than a trust described in subsection (c)(2)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(c)(2)(A)(v) provides that, for purposes of § 1361(b)(1)(B), trusts that may be shareholders include an electing small business trust.

Section 1361(e)(1)(A) provides that an "electing small business trust" means any trust if (i) such trust does not have as a beneficiary any person other than an (I) individual, (II) an estate, or (III) an organization described in paragraph (2), (3), (4), or (5) of § 170(c) or (IV) an organization described in § 170(c)(1) which holds a contingent interest in such trust and is not a potential current beneficiary; (ii) no interest in such trust was acquired by purchase, and (iii) an election under this subsection applies to such trust.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever the corporation ceases to be a small business corporation.

Section 1362(f) provides in part that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d), (2) the Secretary determines that the circumstances resulting in the termination were inadvertent, (3) no later than a reasonable period of time after the discovery of the circumstances resulting in the termination, steps were taken so that the corporation is a small business corporation, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period of inadvertent termination of the S election, 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 the termination, the corporation is treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and the representations made, we conclude that X's election to be treated as an S corporation terminated on D4. We also conclude that the termination constituted an "inadvertent termination" within the meaning of § 1362(f). Under the provisions of § 1362(f), X will be treated as continuing to be an S corporation from D4 and thereafter, provided that X's S corporation election is not otherwise terminated under § 1362(d) and provided further that the trustee of Trusts file an ESTB election for Trusts with the appropriate service center, effective D4, within 60 days of the date of this letter. A copy of this letter should be attached to the election.

Except as specifically provide herein, no opinion is expressed or implied as to the federal tax consequences of the facts described above under any other provision of the Code. In particular, no opinion is expressed as to whether X is an S corporation for federal tax purposes or whether Trusts are ESBTs under § 1361(e).

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.

Under a power of attorney on file in this office, a copy of this letter will be sent to your authorized representatives.

Sincerely,

Dianna K. Miosi
Chief, Branch 1
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter
Copy for § 6110 purposes