

**Internal Revenue Service**Number: **201743006**

Release Date: 10/27/2017

Index Number: 1361.01-02, 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-103242-17

Date:

July 28, 2017

**LEGEND**X =Y =State =A =B =C =D =Date 1 =Date 2 =Date 3 =Date 4 =

Agreement 1 =

Agreement 2 =

n =

Dear :

This letter responds to a letter dated January 19, 2017, and subsequent correspondence, submitted on behalf of X by X's authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

#### FACTS

The information submitted states that X is a limited liability company organized under the laws of State on Date 1. X elected to be an S corporation effective Date 1. Several years later, one of X's unitholders desired to sell his interest in X to A. The other members of X approved the sale of the units to A, subject to the condition that A purchase all of the seller's units, as the other members did not want any additional members of X.

A did not have the financial resources to acquire all of the unitholder's units in X. A sought the funds from B, C, and D. They agreed to assist him in acquiring the units, but they wanted to own a percentage of the units acquired. Under advice from their attorney, on Date 2, B, C, and D formed Y, a limited liability company organized under the laws of State and taxed as a partnership for Federal income tax purposes. B, C, and D each owned a one-third interest in Y. A and Y then entered into Agreement 1, later modified by Agreement 2 (collectively the agreements), whereby Y provided a loan to A for the purchase of the units in X, and B, C, and D, through Y, also took a long-term beneficial ownership of n% of the interests in the X units that A purchased on Date 3.

Y, as a partnership, was an ineligible shareholder and, as a result, X's S corporation election was terminated as of Date 3. After becoming aware of the termination, Y was dissolved and its rights under the agreements were distributed to B, C, and D. Subsequently, on Date 4, A contributed the X units and B, C, and D contributed their rights under the agreements to a voting trust, and the agreements were terminated. The voting trust issued certificates evidencing the separate interests of X that are beneficially owned by each of A, B, C, and D.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance or retroactive

tax planning. X and X's unitholders agree to make any adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary under § 1362(f).

## 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) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 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 1 class of stock.

Section 1.1361-1(e)(1) of the Income Tax Regulations provides, in pertinent part, that ordinarily the person who would have to include in gross income dividends distributed with respect to the stock of the corporation (if the corporation were a C corporation) is considered to be the shareholder of the corporation. The person for whom stock of a corporation is held by a nominee, guardian, custodian, or an agent is considered to be the shareholder of the corporation for purposes of § 1.1361-1(e)(1) and (f). For example, a partnership may be a nominee of S corporation stock for a person who qualifies as a shareholder of an S corporation. However, if the partnership is the beneficial owner of the stock, then the partnership is the shareholder, and the corporation does not qualify as a small business corporation.

Section 1.1361-1(f) provides that, except as otherwise provided in § 1.1361-1(e)(1) (relating to nominees), § 1.1361-1(h) (relating to certain trusts), and § 1361(c)(6) (relating to certain exempt organizations), a corporation in which any shareholder is a corporation, partnership, or trust does not qualify as a small business corporation.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1<sup>st</sup> day of the 1<sup>st</sup> taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in relevant part, 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 of the corporation at any

time during the period specified pursuant to § 1362(f), agrees to make the 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 such termination, the 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 terminated on Date 3. We further conclude that the termination was inadvertent within the meaning of § 1362(f). Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 3, and thereafter, provided that X's S corporation election was otherwise valid and has not otherwise terminated under § 1362(d).

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 request for ruling, it is subject to verification on examination.

Except as specifically ruled above, we express or imply no opinion concerning the federal tax consequences of the facts described above under any other provisions of the Code.

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 a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

/s/

Holly Porter  
Chief, Branch 3  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter  
Copy for § 6110 purposes

cc: