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Person To Contact:
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Date:
November 03, 2021

LEGEND

X =

State =

A =

B =

Trust 1 =

Trust 2 =

Date 1 =

Date 2 =

Date 3 =

Dear :

This responds to a letter dated May 11, 2021, and subsequent correspondence, submitted on behalf of X by X's authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code (Code).

FACTS

The information submitted states that X was incorporated under the laws of State on Date 1 and elected to be treated as an S corporation on Date 2. On Date 3, A and B, shareholders of X, transferred shares of X's outstanding stock to Trust 1 and Trust 2, respectively. X represents that Trust 1 and Trust 2 each were eligible to make an Electing Small Business Trust (ESBT) election as of Date 3 and thereafter. However, the trustees of Trust 1 and Trust 2 failed to file an ESBT election under § 1361(e)(3). Therefore, Trust 1 and Trust 2 were ineligible shareholders of X and X's S corporation election terminated on Date 3.

X represents that the failure to file ESBT elections for Trust 1 and Trust 2 was inadvertent. Further, X represents that X and its shareholders agree to make any adjustments (consistent with the treatment of X as an S corporation and Trust 1 and Trust 2 as ESBTs) that may be required by the Secretary.

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 one class of stock.

Section 1361(c)(2)(A)(v) provides that, for purposes of § 1362(b)(1)(B), an ESBT may be an S corporation shareholder.

Section 1361(e)(1)(A) provides that an ESBT means any trust if: (i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (III) an organization described in § 170(c)(2), (3), (4), or (5), 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 § 1361(e) applies to such trust.

Section 1361(e)(3) provides that an election under § 1361(e) shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

Section 1.1361-1(m)(2)(i) of the Income Tax Regulations provides that the trustee of the trust must make the ESBT election by signing and filing, with the service center where

the S corporation files its income tax return, a statement that meets the requirements of § 1.1361-1(m)(2)(ii).

Section 1.1361-1(m)(2)(iii) provides that the trustee of an ESBT must file the ESBT election within the time requirements prescribed in § 1.1361-1(j)(6)(iii) for filing a qualified subchapter S trust election (generally within the 16-day-and-2-month period beginning on the day that the stock is transferred to the trust).

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall 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) 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 of § 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 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 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 such termination, such corporation will be treated as an S corporation during the period specified by the Secretary.

CONCLUSION

Based solely on the facts submitted and representation made, we conclude X's S corporation election terminated on Date 3 when Trust 1 and Trust 2 became shareholders because the trustees of each of Trust 1 and Trust 2 failed to timely file the required ESBT election. We further conclude that the termination of X's S corporation election 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 is not otherwise terminated under § 1362(d).

This letter ruling is subject to the following conditions. No later than 120 days from the date of this letter: (1) the trustees of each of Trust 1 and Trust 2 must file an ESBT election effective Date 3 with the appropriate service center; and (2) X and its shareholders (in particular, Trust 1 and Trust 2) must also file any original or amended returns for all open taxable years consistent with the relief granted in this letter and the treatment of Trust 1 and Trust 2 as ESBTs. A copy of this letter should be attached to the ESBT election. If these conditions are not met, then this ruling is null and void. In addition, if these conditions are not met, X must send notification that its S corporation

election has terminated to the service center with which X's S corporation election was filed.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion regarding whether X is otherwise eligible to be an S corporation or whether Trust 1 and Trust 2 are otherwise eligible to be an ESBTs.

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, we have sent a copy of this letter to X's authorized representative.

Sincerely,

/s/ Caroline E. Hay

Caroline E. Hay
Senior Counsel, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:
Copy for 6110 purposes

cc: