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Department of the Treasury
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Third Party Communication: None
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Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B02
PLR-103716-08
Date:
July 10, 2008

X =

State =

A =

B =

Trust1 =

Trust2 =

D1 =

D2 =

D3 =

D4 =

D5 =

D6 =

Dear

This responds to a letter dated January 23, 2008, and subsequent correspondence submitted on behalf of X by X's authorized representative, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated under the laws of State on D1 and elected to be an S corporation effective D2. Pursuant to an agreement dated D3, A established Trust1, a revocable trust treated as a wholly-owned grantor trust under §§ 671 and 676. A transferred A's shares of X stock to Trust1. On D4, A died and Trust1 continued to hold the X stock but ceased to qualify as a grantor trust. B, A's spouse, and B's accountants mistakenly assumed that X stock, along with other closely held stock, had been transferred to B effective the date of A's death on D4. From D4, B reported the income of X as if B owned X stock. Trust1 continued to qualify as an eligible S corporation shareholder under § 1361(c)(2)(A)(ii) for the 2 year period beginning on the day of the deemed owner's death and ending on D5. On D5, Trust1 became an ineligible S corporation shareholder and X's S corporation election terminated because Trust1 did not make an ESBT election or distribute X stock. On D6, X stock was transferred to Trust2, a marital trust, created under the terms of Trust1. Trust2 qualified as a qualified subchapter S trust (QSST) under § 1361(d) with B as the beneficiary. Since B believed that B was the owner of X stock, B failed to file a QSST election required under § 1361(c)(2). Consequently, X's S corporation election would have terminated on D6, due to the failure of B to file a QSST election for Trust2, had the election not already terminated on D5.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance. X further represents that from D3, X and its shareholders have filed all returns consistent with X's status as an S corporation. X and its shareholders have agreed to make such adjustments (consistent with the treatment of X as an S corporation) as may be required by the Secretary.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which it was made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness or termination, 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 of the corporation at any time during the period specified pursuant to § 1362(f), 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 or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election terminated on D5 because Trust1 was no longer an eligible shareholder of X. We also conclude that this termination of X's S election on D5 was an inadvertent termination within the meaning of § 1362(f). Moreover, had X's S corporation election not terminated, it would have terminated on D6, due to B's failure to file a QSST election for Trust2. Similarly, this termination of X's S election on D6 would have been an inadvertent termination within the meaning of § 1362(f).

Therefore, we conclude that X will continue to be treated as an S corporation for the period from D5 and thereafter, provided that X's S corporation election was valid and was not otherwise terminated under § 1362(d). During the period from D5 to D6, B will be treated as the owner of the X stock acquired by Trust1. After D6, Trust2 will be treated as if it was a QSST described in § 1361(c)(2)(A)(i), and B will be treated as the owner of the portion of Trust2 consisting of X stock.

This ruling is contingent upon Trust2 beneficiary filing a QSST election for the trust, with an effective date of D6, with the appropriate service center within 60 days of the date of this ruling and upon X's S corporation election being valid and not otherwise terminated under § 1362(d). A copy of this letter should be attached to the QSST election.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed regarding X's eligibility to be an S corporation or the validity of its S corporation election. Further, no opinion is expressed as to whether Trust2 qualifies as a QSST.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, copies of this letter are being sent to X's authorized representatives.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

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

cc: