

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:

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Date:

December 3, 1999

LEGEND:

X =

Y =

Z =

Dear

This letter responds to your letter, dated July 22, 1999, written on behalf of X, requesting a ruling under § 1362(d)(2)(A) of the Internal Revenue Code that X's S election will not terminate if X transfers shares of its stock to employees of a limited partnership in which it is the general partner.

FACTS

According to the information submitted, X is an S corporation that is the sole general partner of Y, a limited partnership. In accordance with a proposed deferred compensation plan (the Plan), X plans to transfer shares of its stock to a select number of Y's employees, Z.

The transfer under the Plan will be between X and Z and will not directly involve Y. However, X is concerned that Y will be treated as a momentary shareholder of X under § 1361(b) because the stock will be used to compensate employees of Y.

X requests a ruling that its proposed transaction will not cause its S election to be terminated under § 1362(d)(2)(A).

LAW

Section 1361(a) defines an S corporation as a small business corporation for which an election under §1362(a) is in effect.

Section 1361(b) defines a small business corporation as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 75 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 1362(a)(1) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of this section, to be an S corporation.

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) such corporation ceases to be a small business corporation.

CONCLUSIONS

After applying the law to the facts submitted and the representations made, we conclude that, solely for purposes of § 1361, Y will not be treated as a momentary shareholder in connection with the transfer of its stock to Z under the Plan. As a result, we conclude that the transfer of stock to Z will not cause X's S election to be terminated under § 1362(d)(2).

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 including § 1032 and § 83. Specifically, no opinion is expressed concerning whether X is an S corporation for federal tax purposes.

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

Under the power of attorney on file with this office, we are sending a copy of this letter to X.

Sincerely yours,

Jeffrey A. Erickson
Assistant to the Branch Chief, Branch 3
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter

Copy for § 6110 purposes