

**Internal Revenue Service**

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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:B01  
PLR-108144-05

Date:  
April 01, 2005

Legend

X =

A =

B =

Trust =

State =

D1 =

D2 =

D3 =

D4 =

Dear :

This responds to a letter dated February 3, 2005, submitted on behalf of X, requesting inadvertent termination relief under § 1362(f) of the Internal Revenue Code.

FACTS

According to the information submitted, X was incorporated on D1 pursuant to the laws of State. X elected to be an S corporation effective on D1.

A, a shareholder of X, died on D2 and A's shares of X stock were transferred to A's estate. On D3, A's estate distributed the X stock to Trust. It was intended that Trust be treated as a qualified subchapter S trust (QSST) as defined in § 1361(d)(3). However, due to an oversight, B, the beneficiary of Trust, did not make a timely QSST election under § 1361(d)(2), thereby terminating X's S corporation election on D3.

In D4, X's counsel discovered that B had not made a QSST election for Trust. Subsequently, X submitted this ruling request for inadvertent termination relief under § 1362(f).

X and B represent that the transfer of stock to Trust and the subsequent failure to file the QSST election were not motivated by tax avoidance. Furthermore, X and its shareholders represent that from D3 until the present, X, B, and the other shareholders have all filed, or will file, returns consistent with X's status as an S corporation. X and its shareholders have agreed to make any adjustments that the Commissioner may require consistent with the treatment of X as an S corporation.

#### 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)(B) provides in part that the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1362(c)(6)) who is not an individual.

Section 1361(c)(2)(A)(i) provides that a trust all of which is treated (under subpart E of part I of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States, may be a subchapter S corporation shareholder.

Section 1361(d)(1) provides that in the case of a QSST with respect to which a beneficiary makes an election under § 1361(d)(1)(2) will be treated as a trust described in § 1362(c)(2)(A)(i), and the QSST's beneficiary will be treated as the owner (for purposes of § 678(a)) of that portion of the QSST's S corporation stock to which the election under § 1361(d)(2) applies.

Section 1361(d)(3) provides that the term "QSST" means a trust: (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only 1 income beneficiary, (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary, (iii) the income interest of the

current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust, and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary; and (B) all of the income (within the meaning of § 643(b)) of which is distributed (or required to be distributed) currently to 1 individual who is a citizen or resident of the United States.

Under § 1361(d)(2)(A), a beneficiary of a QSST (or his legal representative) may elect to have § 1361(d) apply. Under 1361(d)(2)(D), an election under § 1361(d)(2) will be effective up to 15 days and 2 months before the date of the election.

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

Section 1.1361-1(j)(6)(iii)(E) provides that if a corporation's S election terminates because of a late QSST election, the corporation may request inadvertent termination relief under § 1362(f).

Section 1362(f) provides in relevant part that if: (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2); (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 in such corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of such corporation as an S corporation, as the case may be) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

## CONCLUSION

Based solely upon the facts presented and the representations made, we conclude that X's S corporation election terminated on D3, because B failed to make a timely QSST election under § 1361(d)(2). We also conclude that the termination was inadvertent within the meaning of § 1362(f). Therefore, under § 1362(f), X will be treated as an S corporation from D3 and thereafter, assuming X's S corporation election is valid and is not otherwise terminated under § 1362(d). However, this ruling is contingent upon B filing a QSST election, with an effective date of D3, with the appropriate service center within 60 days of the date of this ruling. A copy of this letter must 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 on whether X's original election to be an S corporation was a valid election under § 1362 or whether Trust is a QSST within the meaning of § 1361(d)(3).

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's authorized representative.

Sincerely,

/s/ Dianna K. Miosi

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

Enclosures (2)

Copy of this letter  
Copy for section 6110 purposes

cc: