

Dear _____ :

This letter responds to your letter dated October 6, 2004, together with subsequent correspondence, submitted on behalf of X, requesting relief under § 1362(f) of the Internal Revenue Code.

Facts

The information submitted states that X was incorporated on Date 1. X's shareholders are A and Trust. Trust is an irrevocable trust that was established on Date 2 by A. Trust qualifies as a Grantor Trust under § 678(a)(1). Trust also qualifies as a Qualified Subchapter S Trust (QSST). Trust's beneficiaries are B, C, and D.

X elected to be treated as an S corporation effective Date 3. X timely filed Form 8869, Qualified Subchapter S Subsidiary (QSUB) Election, for its wholly owned subsidiary, Y, to be effective on Date 3. However, no election was made to treat Trust as a QSST. Further, in Year 1, the shareholders' attorneys discovered that the trustee of Trust, and not B, C, and D, the beneficiaries of Trust, signed the Form 2553, Election by a Small Business Corporation, and that, consequently, X's S corporation election was ineffective.

A, as president of X, represents that for all taxable years X, and X's shareholders have filed their tax returns as if X was an S corporation. Trust has passed through all S corporation items to its beneficiaries (B, C, and D) via a K-1. For all taxable years, X has filed its tax returns consistent with Y being treated as a QSUB.

A, as president of X, also represents that the circumstances resulting in the ineffectiveness of X's election to be an S corporation were inadvertent and that X and X's shareholders did not intend to engage in tax avoidance or retroactive tax planning. X, X's shareholders, B, C, and D have agreed to make any adjustments that the Secretary may require, consistent with the treatment of X as an S corporation.

Law and Analysis

Section 1361(a)(1) defines an S corporation as a small business corporation for which an election under § 1362(a) is in effect for the taxable year .

Section 1361(b)(1)(B) provides that the term small business corporation is a domestic corporation which is not an ineligible corporation and which does not have as a shareholder a person (other than an estate and other than a trust described in § 1361(c)(2) or an organization described in § 1361(c)(6)) who is not an individual.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which 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, the Secretary determines that the circumstances resulting in such ineffectiveness were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness, 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, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts and representations submitted, we conclude that X's S corporation election was ineffective for the taxable year beginning on Date 3, because X failed to acquire the necessary consents at the time of the election. We also conclude that the ineffectiveness of X's S corporation election was inadvertent within the meaning of § 1362(f). Accordingly, we hold that under the provisions of § 1362(f), X will be treated as an S corporation effective Date 3, and thereafter, provided that X's S election was not otherwise invalid or terminated under § 1362(d). In addition, we conclude that Trust will be granted an extension of time to file a QSST election, effective Date 3, and that Y will be treated as a valid QSUB effective Date 3, and thereafter.

This ruling is contingent on X and all of its shareholders treating X as having been an S corporation for the period beginning Date 3, and thereafter. Accordingly, all of the shareholders of X, in determining their respective income tax liabilities for the period beginning Date 3, and thereafter, must include their pro rata share of the separately stated and non-separately computed items of X as provided in § 1366, make any adjustments to basis provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this ruling shall be null and void.

This ruling is also contingent on B, C, and D filing consents with the appropriate service center, indicating that the consents are to be associated with the originally filed Form 2553, within 60 days of this letter. In addition, the ruling is contingent on Trust making a valid QSST election, effective Date 3, with the appropriate service center within 60 days of this letter. A copy of this letter should be attached to B, C, and D's consents and Trust's QSST election. Copies of the letter have been provided for this purpose.

Except as specifically ruled upon above, we express no opinion concerning the federal tax consequences of the transactions described above under any other

provisions of the Code. Specifically, no opinion is expressed on whether X is otherwise eligible to be treated as an S corporation, whether Trust is eligible to elect to be treated as a QSST, or whether Y is otherwise eligible to be treated as a QSUB.

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.

Pursuant to a power of attorney on file with this office, a copy of this letter is being sent to X's authorized representative.

Sincerely,

Beverly Katz
Senior Technician Reviewer, Branch 2
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (4)
Three copies of this letter
A copy for 6110 purposes