

Internal Revenue Service

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Third Party Communication: None

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B01

PLR-128248-04

Date:

November 17, 2004

Legend

X =

D1 =

D2 =

D3 =

D4 =

State =

Dear :

This letter responds to your letter dated May 19, 2004, requesting relief for X to be treated as continuing to be an S corporation under § 1362(f) following an inadvertent termination of its S corporation status.

FACTS

X was incorporated on D1 under the laws of State, and filed an S corporation election, effective on D1. On D2, X shares were transferred to ineligible shareholders. Also on D2, X converted from a State corporation to a State limited partnership and elected to be treated as an association taxable as a corporation and to also be treated as an S corporation. This conversion may have created a second class of stock which would have terminated X's S corporation election.

X and its owners intended that X would continue to be treated as an S corporation. On D3, after X was advised that shares had been transferred shares to

ineligible shareholders, the ineligible shareholders transferred their shares to eligible shareholders. On D4, after X was advised that the conversion to a State limited partnership may have caused its S election to terminate, X reorganized as a State limited liability partnership and elected to be classified as a corporation for federal tax purposes. X represents that it was unaware that the conversion to a State limited partnership could potentially terminate its S corporation election. X represents that it did not intend to terminate its S corporation election and that during the termination period it has timely and consistently filed its tax returns consistent with its treatment 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. Section 1361(b)(1) defines "small business corporation" as a domestic corporation that is not an ineligible corporation and that 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 (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)(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.

Under § 1362(d)(2), an election to be an S corporation will be terminated whenever the corporation ceases to be a small business corporation.

Section 1362(f) provides that a corporation will be treated as continuing to be an S corporation during the period specified by the Secretary if (1) an election under § 1362(a) by the corporation was terminated under paragraph (2) or (3) of § 1362(d), (2) the Secretary determines that the termination was inadvertent, (3) no later than a reasonable period of time after discovery of the terminating event, steps were taken so that the corporation is once more a small business corporation, 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 any adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to that period.

CONCLUSION

Based upon the information submitted and the representations set forth above, we conclude that (1) X's S corporation election terminated on D2 when X's shareholders transferred their shares to ineligible shareholders; and that (2) if X's conversion from a State corporation to a State limited partnership created a second class of stock, which

would also have terminated X's S corporation election, that the termination was inadvertent within the meaning of section 1362(f).

Pursuant to the provisions of section 1362(f), X will be treated as continuing to be an S corporation from Date 2 and thereafter, provided that X's subchapter S election is not otherwise terminated under section 1362(d).

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 whether X's original election to be an S corporation was a valid election under § 1362.

These rulings are directed only to the taxpayer who requested them. Section 6110(k)(3) provides that this letter 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 the taxpayer.

Sincerely,

/s/ David R. Haglund

David R. Haglund
Senior Technician Reviewer, Branch 1
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
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