

**Internal Revenue Service**

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Date:

June 09, 2005

Legend

X =

State =

D1 =

D2 =

D3 =

Trust 1 =

Trust 2 =

A =

B =

Dear :

This responds to a letter dated December 28, 2004, together with subsequent correspondence, submitted on behalf of X requesting a ruling under § 1362(f) of the Internal Revenue Code.

## FACTS

According to the information submitted, X was incorporated under the laws of State on D1. X elected to be an S corporation effective D2. Among X's shareholder are Trust 1 and Trust 2. X represents that Trust 1 and Trust 2 qualify as qualified subchapter S trusts (QSSTs). A and B are the income beneficiaries of Trust 1 and Trust 2, respectively.

On D3, the co-trustees of Trust 1 and Trust 2 discovered that the legal representatives of A and B did not timely file QSST elections for Trust 1 and Trust 2, and that, consequently, X's S corporation election was ineffective.

X represents that since D2, X and its shareholders, including Trust 1 and Trust 2, have filed their income tax returns as if X was an S corporation. X represents that its ineffective S corporation election was inadvertent. X and all its shareholders who were shareholders since D2 agree to make any necessary adjustments 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 section 1362(a) is in effect for such year.

Section 1361(b)(1) 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 section 1361(c)(2), or an organization described in section 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 1361(d)(1) provides that a QSST whose beneficiary makes an election under section 1362(d)(2) will be treated as a trust described in section 1361(c)(2)(A)(i), and the QSST's beneficiary will be treated as the owner (for purposes of section 678(a)) of that portion of the QSST's S Corporation stock to which the election under section 1361(d)(2) applies. Under section 1361(d)(2)(A), a beneficiary of a QSST may elect to have section 1361(d) apply. Under section 1361(d)(2)(D), this election will be effective up to 15 days and two months before the date of the election.

Section 1361(d)(3) defines a QSST as a trust (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust; (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 beneficiary in the trust shall terminate on the earlier of the 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 that beneficiary; and (B) all of the income (within the meaning of section 643(b) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(f) provides, in relevant part, that if (1) an election under section 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to section 1362(b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, (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 ineffectiveness, 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 section 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 the period, then, notwithstanding the circumstances resulting in the ineffectiveness, the corporation shall be treated as continuing to be an S corporation during the period specified by the Secretary.

## CONCLUSION

Based solely on the information submitted and the representations made, we conclude that X's subchapter S election was invalid, because appropriate elections were not filed for Trust 1 and Trust 2. In addition, we conclude that the election was inadvertently invalid within the meaning of § 1362(f). Therefore, X will be treated as continuing to be an S corporation from D2, and thereafter, provided that A and B or their legal representatives file QSST elections with the appropriate service center within 60 days of the date of this letter. A copy of this letter should be attached to the QSST elections.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed concerning whether X is otherwise eligible to be treated as an S corporation, or whether Trust 1 and Trust 2 are eligible to be treated as QSSTs.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Dianna K. Miosi  
Chief, Branch 1  
Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter

Copy for § 6110 purposes