### Internal Revenue Service

Department of the Treasury Washington, DC 20224

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## Legend:

X	=
Y	=

<u>Shareholders</u> =

<u>State</u>	=
Date 1	=
Date 2	=

:

Dear

This responds to the letter dated April 21, 2003, together with subsequent correspondence, submitted on behalf of  $\underline{X}$  requesting relief under section 1362(f) of the Internal Revenue Code.

### Facts:

The following facts have been represented. <u>X</u> was incorporated on <u>Date 1</u> and made an S corporation election for its first taxable year. On <u>Date 1</u>, <u>X</u> had an ineligible shareholder, <u>Y</u>. Within <u>X</u>'s first taxable year, on <u>Date 2</u>, <u>Y</u> transferred all of its shares to <u>Shareholders</u>. Subsequently, <u>X</u> submitted this ruling request for inadvertent invalid election relief under section 1362(f).

<u>X</u> represents that there was no intent to knowingly make an invalid S election and that the events that resulted in the invalid election were not motivated by tax avoidance or retroactive tax planning. <u>X</u> and <u>Shareholders</u> agree to make any adjustments consistent with the treatment of <u>X</u> as an S corporation.

#### Law and Analysis:

Section 1361(a)(1) provides that, for purposes of the Code, 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 the year.

Section 1361(b)(1)(B) provides that, for purposes of subchapter S, the term "small business corporation" means a domestic corporation that is not an ineligible corporation and that does not 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.

Section 1362(f) provides that if (1) an election under section 1362(a) by any corporation was not effective for the tax year for which made 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 the ineffectiveness were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness, steps were taken so that the corporation is a small business corporation or 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 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 that period, then, notwithstanding the circumstances resulting in the ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

### Conclusion:

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Based solely on the representations made and the information submitted, we conclude that  $\underline{X}$ 's election to be an S corporation was ineffective for the taxable year beginning <u>Date 1</u>. We also conclude that the ineffectiveness of  $\underline{X}$ 's S corporation election constituted an inadvertent invalid election within the meaning of section 1362(f).

Therefore, we rule that  $\underline{X}$  will be treated as an S corporation beginning <u>Date 1</u> and thereafter, unless  $\underline{X}$ 's S corporation election otherwise terminates under section 1362(d), provided that  $\underline{X}$  files a new Form 2553 effective <u>Date 1</u> with the appropriate service center within 60 days of this letter. A copy of this letter should be attached to the Form 2553.

This ruling is contingent on <u>X</u> treating <u>Shareholders</u> as owning <u>X</u> stock as of <u>Date 1</u> and on <u>X</u> and <u>Shareholders</u> treating <u>X</u> as an S corporation effective <u>Date 1</u>. Accordingly, <u>Shareholders</u> must include their pro rata shares of the separately stated and nonseparately computed items of <u>X</u> as provided in section 1366, make any adjustments to basis provided in section 1367, and take into account any distributions made by <u>X</u> as provided in section 1368. If <u>X</u> or <u>Shareholders</u> fail to treat <u>X</u> as described above, this ruling will be null and void.

Except for the specific ruling above, we express or imply no opinion concerning the federal income tax consequences of the facts of this case under any other provision of the Code, including whether  $\underline{X}$  is otherwise eligible to be an S corporation.

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  $\underline{X}$ 's authorized representative.

Sincerely,

/s/ Dan Carmody

Dan Carmody Senior Counsel, Branch 1 Office of the Associate Chief Counsel (Passthroughs and Special Industries)

Enclosures (2) Copy of this letter Copy for § 6110 purposes