Internal Revenue Service

Index Number: 362.02-00

Number: **199935035**
Release Date: 9/3/1999

Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:P&SI:2 - PLR-104797-99
Date:
June 4, 1999

X =

Y =

A =

B =

C =

D1 =

D2 =

D3 =

State =

Court =

Dear :

This letter responds to your February 24, 1999, and subsequent correspondence, submitted on behalf of X, requesting a ruling as to whether X's subchapter S election was terminated on D2.

The information submitted states that X is a corporation organized under the laws of State. A is the majority shareholder of X. In D1, B and C were issued shares of X and all of the shareholders executed a cross stock purchase agreement which provided that the shareholders of X could not sell their shares of stock in X without first giving the other shareholders written notice of their intent to sell, providing the terms of the proposed sale to the other shareholders, and allowing the other shareholders a period of time to purchase the offered shares.

On D2, B and C attempted to transfer their shares in X to Y, a C corporation owned and controlled by B and C. B and C did not give notice of their intent to sell, or offer the right to purchase the shares, to A.

After learning of the attempted transfer of X stock to Y, A filed suit in Court of State, seeking to have the stock transfer declared void. On D3, the Court in State entered an order holding that the attempted transfer of X stock to Y was void from its inception.

Section 1362(a) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

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

Based solely on the facts and representations submitted, because under the cross stock purchase agreement and under State law as determined by Court, B and C's attempted stock transfer is void, we conclude that X's election did not terminate on D2. Accordingly, as the C corporation was never a shareholder of X, X will be treated as continuing to be an S corporation from D2, and thereafter, provided X's S election was valid, and has not otherwise been terminated under the provisions of § 1362(d).

X and all its current and prior shareholders, including B and C must treat X as having been an S corporation for the period from D2, to the present. In addition, as X will be treated as continuing to be an S corporation, X and its shareholders must treat B and C as the owners of any shares that B and C attempted to transfer to Y and amend any prior tax returns that are

inconsistent with this treatment of X as an S corporation.

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, including whether X was or is a small business corporation under § 1361(b) of the Code.

This ruling is directed only to the taxpayer who requested 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.

Sincerely yours,

J. THOMAS HINES
Senior Technician Reviewer
Branch 2
Office of the Assistant
Chief Counsel
(Passthroughs and
Special Industries)

Enclosures: 2
Copy of this letter
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