

Internal Revenue Service

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Taxpayer =
Owner =
Trusts =

Dear :

This letter is in response to a request for a private letter ruling filed on May 18, 2007 requesting a ruling on whether Taxpayer meets the definition of a small business corporation for purposes of section 280G(b)(5)(A)(i) of the Internal Revenue Code of 1986, as amended (Code) and § 1.280G-1 Q/A-6(a)(1) of the Income Tax Regulations (regulations).

Taxpayer is a privately-held corporation. Taxpayer is entirely owned by the Owner family through the Trusts.

Taxpayer represents that it is a domestic corporation that is not an ineligible corporation within the meaning of section 1361(b)(2) of the Code and it has never had in effect an election to be treated as an S corporation under section 1362(a). Taxpayer further represents that it meets the definition of a "small business corporation" described in section 1361(b)(1)(A), (C) and (D). Taxpayer further represents that (a) an election under section 1361(e) to be an electing small business trust (ESBT) has never been filed by, been in effect for, or applied to, any of the Trusts, (b) the Trusts have never been, and currently are not, trusts described in clauses (i), (ii), (iii), (iv) or (vi) of section 1361(c)(2)(A), and (c) the Trusts have never owned, and currently do not own, any stock in any S corporation. Taxpayer also represents that each of the Trusts (a) meets

the requirements for the definition of an ESBT in clauses (i) and (ii) of section 1361(e)(1)(A) and (b) is not a trust described in subparagraph (B) of section 1361(e)(1).

Taxpayer has entered into agreements that would provide for payments to a number of its employees that would constitute parachute payments under section 280G(b)(2) of the Code. Taxpayer represents that none of such employees is (a) a shareholder of Taxpayer, (b) a trustee or beneficiary of the Trusts, or (c) a member of, or related to, the Owner family.

Taxpayer has requested a ruling that, for purposes of § 280G(b)(5)(A)(i) of the Code and the applicable regulations, Taxpayer is a “small business corporation” as defined in § 1361(b) (without regard to paragraph (1)(C) thereof).

Section 280G(a) of the Code provides that no deduction will be allowed for any excess parachute payment. Section 280G(b)(1) defines the term “excess parachute payment” as an amount equal to the excess of any parachute payment over the portion of the base amount (as defined in section 280G(b)(3)) allocated to such payment.

Section 280G(b)(2)(A) of the Code defines the term “parachute payment” as any payment in the nature of compensation to (or for the benefit of) a disqualified individual if such payment is contingent on a change in the ownership or effective control of the corporation, or in the ownership of a substantial portion of the assets of the corporation (a change in control) and the aggregate present value of the payments in the nature of compensation to (or for the benefit of) such individual that are contingent on such change equals or exceeds an amount equal to three times the base amount as defined in section 280G(b)(3).

Section 280G(b)(5)(A)(i) of the Code provides that a parachute payment does not include any payment to a disqualified individual with respect to a corporation that (immediately before a change in control) is a small business corporation (as defined in section 1361(b) but without regard to paragraph (1)(C) of that section).

Section 1.280G-1, Q/A-6(a)(1) of the regulations provides that a parachute payment does not include any payment to a disqualified individual with respect to a corporation that (immediately before the change in control) would qualify as a small business corporation (as defined in section 1361(b) of the Code without regard to paragraph (1)(C) of that section), without regard to whether the corporation had an election to be treated as a corporation under section 1361 in effect on the date of the change in control.

Section 4999(a) of the Code imposes on any person who receives an excess parachute payment an excise tax equal to 20 percent of the amount of such payment.

Under section 1361(b)(1)(B) of the Code a corporation is not a "small business corporation" if it has 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 1361(c)(2) of the Code provides that certain trusts may be shareholders of an S corporation, including an ESBT.

Section 1361(e) of the Code defines an ESBT. Section 1361(e)(1)(A) provides that, except as provided in section 1362(e)(1)(B), an ESBT means any trust if (i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (III) an organization described in section 170(c)(2), (3), (4), or (5), or (IV) an organization described in section 170(c)(1) that holds a contingent interest in such trust and is not a potential current beneficiary, (ii) no interest in such trust was acquired by purchase, and (iii) an election under section 1361(e) applies to such trust. Section 1361(e)(3) provides that an election under section 1361(e) shall be made by the trustee.

Section 1.1361-1(m)(2)(i) of the regulations provides in general that the trustee of an ESBT must make the ESBT election by signing and filing, with the service center where the S corporation files its income tax return, a statement that meets the requirements of section 1.1361-1(m)(2)(ii).

Based upon the facts submitted and the representations made, Taxpayer is eligible to make an S corporation election and in conjunction therewith, if Taxpayer made an S corporation election, each of the Trusts would be eligible to make ESBT elections. Accordingly, we rule that Taxpayer is a "small business corporation," as defined in section 1361(b) of the Code (without regard to paragraph (1)(C) thereof) for purposes of section 280G(b)(5)(A)(i) and regulation § 1.280G-1, Q/A-6(a)(1).

A copy of this letter must be attached to any of your income tax returns to which it is relevant.

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.

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.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a properly executed penalty of perjury statement. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

Sincerely yours,

WILLIAM C. SCHMIDT
Senior Counsel
Executive Compensation Branch
Office of Division Counsel/Associate
Chief Counsel (Tax Exempt and
Government Entities)