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Person To Contact:
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Telephone Number:

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Date:
August 16, 2013

LEGEND

X =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Year =

Dear :

This letter is in response to your request, dated July 25, 2013, on behalf of X, seeking relief under § 1362(f) of the Internal Revenue Code.

FACTS

Based on the materials submitted and representations within, we understand the relevant facts to be as follows. X was organized as a limited liability company under the

laws of State on Date 1. X made elections to be treated as an association taxable as a corporation and to be treated as an S corporation effective Date 2.

At the time of its organization, X represents that its owners entered into an Operating Agreement (the "Original Operating Agreement"). X is unable to locate a copy of this agreement. X arranged for a new operating agreement to be entered into effective as of Date 3 (the "Restated Operating Agreement").

Section 6.1(a) of the Restated Operating Agreement provides that "[n]et Cash Flow From Operations and Net Cash Flow From Sales, Refinancings and Other Extraordinary Items shall be distributed to the members at such times and in such amounts as determined by the managers; provided, however, that the Company shall distribute Net Cash Flow From Operations to the members at least annually. All cash flow distributions shall be in proportion to the members' Profit-Sharing Percentages unless all members otherwise consent."

Section 6.1(b) of the Restated Operating Agreement provides that "[i]n the case of the liquidation or termination of the Company, distributions shall be made in accordance with Article XI hereof."

Section 11.4(a) of Article XI, in relevant part, provides that "[a]ll cash and other property remaining for distribution to members pursuant to Section 11.3 following satisfaction of all debts and liabilities after an Event of Termination shall be divided among and distributed to the members in accordance with their positive capital accounts, after giving effect to all contributions, distributions, and allocations for all periods. If any member has a deficit Capital Account balance (after giving effect to all contributions, distributions, and allocations for all period [sic]), such member shall have no obligation to make any contribution to the capital of the Company with respect to such deficit, and such deficit shall not be considered a debt owed to the Company or to any other person for any purpose whatsoever. The foregoing provision and the other provisions of this Agreement relating to distributions are intended to comply with Regulation Section 1.704-1(b)(2)(ii)(b) and shall be interpreted and applied in a manner consistent with such regulation."

Exhibit A to the Restated Operating Agreement has provisions relating to the allocation of profits and losses and the maintenance of capital accounts. While these provisions were included in contemplation of X being treated as a partnership, their applicability was not limited to such being the case. Thus, such provisions applied during the period of time in which X intended to be treated as an S corporation for U.S. federal income tax purposes.

X maintains a separate capital account for each owner on its books and records. These capital accounts are not proportionate based on each owner's ownership percentage in X, although the disproportionality is slight. X believes the disproportionality relates to an

adjusting journal entry in the year following the S election, but is unable to locate an explanation for the entry. However, X represents that the disproportionate capital accounts were not as a result of any transaction that had as a principal purpose circumvention of the small business corporation one class of stock requirement in § 1361(b)(1)(D).

On Date 4, an unrelated third party (the "Purchaser"), acquired all of the outstanding interests in X. Purchaser, who, together with the owners, intends to file an election under § 338(h)(10) with respect to its acquisition of X's member interests. Prior to the acquisition, during the purchaser's due diligence, the Purchaser's advisors reviewed the Restated Operating Agreement and the books and records of X and advised the Purchaser that X could be viewed has having more than one class of stock for purposes of the small business corporation requirement of § 1361(b)(1)(D). Specifically, the purchaser's advisors noted that because the Restated Operating Agreement provided for liquidating distributions to the owners based on each owner's capital account balance and that the capital account balances were disproportionate, each outstanding member interest in X did not have identical rights to liquidation proceeds. Furthermore, the Purchaser's advisors also noted that because the Original Operating Agreement could not be located, it was not possible to determine if X satisfied the one class of stock requirement at the time it filed its S election.

To eliminate the potential second class of stock X and the owners entered into a Second Restated Operating Agreement effective as of Date 5.

Section 11.4(a) of the Second Restated Operating Agreement provides that "[f]or so long as the Company maintains its election to be classified as an association taxable as a corporation for federal income tax purposes pursuant to Treasury Regulation Section 301.7701-3(c) (including, without limitation, taxation as an "S Corporation" within the meaning of Section 1361 and 1362 of the Code), all cash and other property remaining for distribution to members pursuant to Section 11.3 following satisfaction of all debts and liabilities after an Event of Termination shall be divided among and distributed to the Members pro rata in proportion to their respective membership units of the Company."

Section 11.4(b) of the Second Restated Operating Agreement provides that "[t]his Section 11.4(b) shall apply only if, at the time of the dissolution and liquidation of the Company, the Company is classified as a partnership for federal income tax purposes. In such case, all cash and other property remaining for distribution to members pursuant to Section 11.3 following satisfaction of all debts and liabilities after an Event of Termination shall be divided among and distributed to members in accordance with their positive capital accounts, after giving effect to all contributions, distributions, and allocations for all periods. If any member has a deficit capital account balance (after giving effect to all contributions, distributions, and allocations for all period [sic]), such member shall have no obligation to make any contribution to the capital of the Company

with respect to such deficit, and such deficit shall not be considered a debt owed to the Company or to any other person for any purpose whatsoever. The foregoing provision and the other provisions of this Agreement relating to distributions are intended to comply with Treasury Regulation Section 1.704-1(b)(2)(ii)(b) and shall be interpreted and applied in a manner consistent with such regulation."

In accordance with § 1362(f) and § 1.1362-4, X and each person who has been a shareholder of X at any time after Date 4 through the date of the ruling request have consented to any adjustments as may be required by the Secretary.

X requests a ruling that if certain provisions of X's operating agreements caused it to have more than one class of stock for purposes of § 1361(b)(1)(D), then the resulting ineffectiveness or subsequent termination of its S election was inadvertent within the meaning § 1362(f). Furthermore, notwithstanding the potential invalidity or termination of its S election, pursuant to § 1362(f), X will be treated an S corporation from Date 2 and thereafter.

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 § 1362(a) is in effect for the year.

Section 1361(b)(1)(D) 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, among other things, have more than one class of stock.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides that a corporation is generally treated as having only one class of stock if all outstanding shares of stock of the corporation confer identical rights to distribution and liquidation proceeds.

Section 1.1361-1(l)(2)(i) provides that the determination of whether all outstanding shares of stock confer identical rights to distribution and liquidation proceeds is made based on the corporate charter, articles of incorporation, bylaws, applicable state law, and binding agreements relating to distribution and liquidation proceeds (collectively, the "governing provisions"). A commercial contractual agreement, such as a lease, employment agreement, or loan agreement, is not a binding agreement relating to distribution and liquidation proceeds and thus is not a governing provision unless a principal purpose of the agreement is to circumvent the one class of stock requirement. Although a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical distribution and liquidation rights, any distributions (including actual, constructive, or deemed distributions) that differ in timing or amount are to be given appropriate tax effect in accordance with the facts and circumstances.

Section 1.1361-1(l)(2)(iii)(B) provides that bona fide agreements to redeem or purchase stock at the time of death, divorce, disability, or termination of employment are disregarded in determining whether a corporation's shares of stock confer identical rights.

Section 1362(d)(2)(A) provides that an election under § 1362(a) will be terminated 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.

Section 1362(d)(2)(B) provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or (B) was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents, and (4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

CONCLUSION

Based on the information submitted and the representations made, we conclude that X's S corporation election may have been ineffective or subsequently terminated because X may have had more than one class of stock. However, we conclude that, if X's S election was ineffective or subsequently terminated, such ineffectiveness or termination was inadvertent within the meaning of § 1362(f) of the Code.

Further, we conclude that the corrective action taken by X and its shareholders does not create a second class of stock under § 1361. Consequently, we rule that X will be treated as continuing to be an S corporation from Date 2, and thereafter, provided that X's S election otherwise is not terminated under § 1362(d).

Except as specifically ruled upon above, no opinion is expressed as to the federal income tax consequences of the facts described above under any other provision of the code. In particular, no opinion is expressed or implied as to whether X otherwise qualifies as a subchapter S corporations under § 1361.

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

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.

In accordance with the Power of Attorney on file with this office, a copy of this letter ruling will be sent to the taxpayer representative.

Sincerely,

Bradford R. Poston
Senior Counsel, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure (1)
Copy of Letter for § 6110 purposes