Internal Revenue Service

Number: **201528025**
Release Date: 7/10/2015

Index Number: 1361.01-04, 1362.04-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B03
PLR-138483-14

Date:
April 09, 2015

LEGEND

X =

State =

A =

B =

Agreement 1 =

Agreement 2 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Dear :

This letter responds to a letter dated September 23, 2014, submitted on behalf of X by X's authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code (the Code).

FACTS

X was organized on Date 1 as a limited liability company under the laws of State. Effective Date 2, X elected to be treated as a corporation. On Date 3, A and B, the members of X, signed a new operating agreement, Agreement 1, that included provisions in contemplation of X being treated as a partnership; however, the applicability of those provisions was not limited to such treatment. Effective Date 4, X elected to be treated as an S corporation. The provisions in Agreement 1 thus applied during the period of time when X intended to be treated as an S corporation until Date 5, as explained herein.

Section 4 of Agreement 1 provided for the maintenance of capital accounts in accordance with regulations under § 704 of the Code.

Section 5 of Agreement 1 allowed for allocations to be made first to members with positive capital accounts, as well as for special and curative allocations.

Section 10 of Agreement 1 provided rules regarding how the dissolution and wind up of the business would be handled. Section 10.2(c) provided that distributions would be made to members with positive capital accounts, to the extent of their respective capital accounts. Section 10.2(d) provided that distributions to members would be based on their distributive shares, except that a distribution to a member with a negative capital account would be reduced.

After A and B were informed that, based on the provisions in Agreement 1, they might not have identical rights to liquidation proceeds, X, A, and B entered into Agreement 2 on Date 5 to remove or amend those provisions. Agreement 2 instead provides for allocations of profits and losses in accordance with the shareholders' distributive shares (their interests in the S corporation). Agreement 2 also provides that all distributions will be proportionate to their distributive shares.

X represents that X and its shareholders intended for X to be an S corporation effective Date 4 and X has filed all returns consistent with X's status as an S corporation since Date 4. X further represents that all items of income (including tax-exempt income), loss, deduction, or credit (the separate treatment of which could affect the liability for tax of any shareholder) and all distributions have been pro rata based on ownership percentage as required under the S corporation rules. Lastly, X and its shareholders agree to make any adjustments required as a condition of obtaining relief under the inadvertent termination rule as provided under § 1362(f) of the Code.

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) defines a “small business corporation” as a domestic corporation which is not an ineligible corporation which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, and a trust described in § 1361(c)(2), or an organization described in § 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 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1st day of the taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation. Section 1362(d)(2)(B) further provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides, in relevant part, 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 for which the election was made or the termination occurred is a small business corporation, or (B) to acquire the required shareholder consents; and (4) the corporation for which the election was made or the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to this period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides, in part, 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 laws, and binding agreements relating to distribution and liquidation proceeds (collectively, governing provisions).

CONCLUSION

Based on the facts submitted and the representations made, we conclude that X's S corporation election may have been ineffective because X may have had more than one class of stock. However, we conclude that if X's S corporation election was ineffective, such ineffectiveness was inadvertent within the meaning of § 1362(f). Therefore, X will be treated as an S corporation effective Date 4 and thereafter, provided X's S corporation election is not otherwise terminated under § 1362(d).

Except as specifically ruled upon above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation.

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 who requested it. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited as precedent.

Pursuant to a power of attorney on file with this office, we are sending copies of this letter to your authorized representatives.

Sincerely,

/s/

Holly Porter
Chief, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

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

cc: