

## Internal Revenue Service

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Department of the Treasury  
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Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:B03  
PLR-114165-18  
Date:  
October 22, 2018

X:

Date 1:  
Date 2:  
Date 3:  
Date 4:  
State:

Dear :

This letter responds to your letter dated March 7, 2018, and subsequent correspondence, requesting relief under § 1362(f) of the Internal Revenue Code.

### FACTS

The information submitted states that X began business on Date 1 and is organized under the laws of State. Between Date 2 and Date 3, X had two owners, and was classified as a partnership for federal income tax purposes. During this time, X's Operating Agreement provided that current distributions were to be made to the two owners in accordance with their "Ownership Ratios," while distributions made upon dissolution would be made in accordance with the owners' "positive Capital Account balances." Certain distributions (the "LLC distributions") that X made to the owners between Date 2 and Date 3 caused the owners' capital accounts to become disproportionate to the owners' ownership ratios.

Effective Date 3, X elected to be classified as an S corporation, and did not make any changes to its Operating Agreement. As a result of the LLC distributions, the Operating Agreement created a right to nonproportional distributions to X's owners. This caused X to have multiple classes of stock within the meaning of § 1361(b)(1)(D), thereby causing X's S corporation election to be ineffective.

On Date 4, X amended its Operating Agreement to clarify that all liquidating distributions are to be made in accordance with the shareholders' ownership ratios. X represents that, between Date 3 and Date 4, all distributions were made in accordance with its shareholders' relative stock ownership, and that all taxable income was also allocated in a pro rata manner. X further represents that X and its shareholders intended for X to be an S corporation at all times from Date 3 and onward and that X has filed all returns consistent with X's treatment as an S corporation since Date 3. X and its shareholders agree to make any adjustments required as a condition of obtaining relief under the inadvertent termination rule as provided in § 1362(f).

### 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(a)(1) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with § 1362, to be an S corporation.

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), (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, and (4) the corporation and each person who was a shareholder of 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 the ineffectiveness, the corporation will be treated as an S corporation during the period specified by the Secretary.

### CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election on Date 3 was ineffective as a result of X having more

than one class of stock. We further conclude that this ineffectiveness was inadvertent within the meaning of § 1362(f).

X has taken corrective action so that it meets the requirements of a small business corporation under § 1361(b). Therefore, we determine that pursuant to the provisions of § 1362(f), X will be treated an S corporation effective Date 3 and thereafter, provided X's S corporation election was otherwise valid and has 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 described above under any other provision of the Code. Specifically, we express or imply no opinion regarding X's eligibility to be an S corporation.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of 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 that requested it. Section 6110(k)(3) provides that this ruling 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 your authorized representatives.

Sincerely,

James A. Quinn  
Senior Counsel, Branch 3  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures (2)

Copy of this letter

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