

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B02
PLR-151156-07

Date:
April 16, 2008

X =

D1 =

D2 =

D3 =

D4 =

D5

State =

Dear

This letter responds to a letter dated October 19, 2007, submitted on behalf of X by X's authorized representative, requesting relief under § 1362(f) of the Internal Revenue Code.

The information submitted states that X was incorporated on D1 and elected to be an S corporation effective D2. On D3, X's shareholders entered into a Distribution Agreement. Paragraph 1 of the Distribution Agreement provides that X will distribute a substantial portion of its real estate assets in accordance with drawings and legal descriptions to be determined in the future. Paragraph 2 of the Distribution Agreement provides that it is the intent of the Distribution Agreement to provide that the parcels of land that X will distribute to each shareholder are approximately equivalent even though each shareholder does not hold equivalent ownership interests in X. Therefore, the

Distribution Agreement alters the rights to distribution and liquidation proceeds conferred by the outstanding stock of X so that those rights are not identical. Accordingly, the Distribution Agreement may have caused X to have more than one class of stock.

X represents that the circumstances resulting in the possible termination of X's election to be an S corporation were inadvertent and not motivated by tax avoidance or retroactive tax planning. X represents that since D3, X and each person who is or was a shareholder of X have filed federal income tax returns consistent with X's S corporation election. On D4, X was informed by their new legal counsel that the existence of the Distribution Agreement may have caused a termination of X's S corporation election. Thereafter, X's shareholders terminated the Distribution Agreement pursuant to a Termination Agreement dated D5. X represents that no distributions were made to X's shareholders under the terms of the Distribution Agreement. X and its shareholders have agreed to make such adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary.

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1361(b)(1)(B) provides that a "small business corporation" means a domestic corporation that is not an ineligible corporation and that does not have as a shareholder a person (other than an estate, a trust described in §1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides that, except as provided in § 1.1361-1(i)(4) (relating to instruments, obligations, or arrangements treated as a second class of stock), a corporation is 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 based on the governing provisions of a corporation. Such provisions include binding agreements relating to distribution and liquidation proceeds.

Section 1362(d)(2) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which a corporation is an S corporation) such corporation ceases to be a small business corporation. A termination of an S corporation election under § 1362(d)(2) is effective on and after the date of cessation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3), (2) the Secretary determines that the circumstances resulting in such termination were inadvertent, (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness,

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 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 such ineffectiveness, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Based solely on the information submitted and the representations made we conclude that X's S election may have terminated on D3 when X's shareholders entered into the Distribution Agreement. We conclude, however, that if X's S corporation election terminated because the Distribution Agreement created a second class of stock, then it was inadvertent within the meaning of § 1362(f). Therefore, X will be treated as an S corporation from D3 and thereafter.

X's shareholders must include their pro rata share of the separately and nonseparately computed items of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this ruling shall be null and void.

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. Specifically, no opinion is expressed on whether X was or is otherwise eligible to be treated as an S corporation.

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 forwarded to X's authorized representative.

Sincerely,

J. Thomas Hines
Chief, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

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