

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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, ID No.

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September 01, 2016

LEGEND

X =

Date 1 =

Date 2 =

Date 3 =

State =

Units =

Dear :

This responds to a letter dated March 11, 2016, submitted on behalf of X, by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code.

FACTS

According to the information and representations submitted, X was formed on Date 1 as a limited liability company under the laws of State. Effective Date 2, X elected to be treated as an association and made an election to be treated as an S corporation.

X's S corporation election was ineffective because X failed to obtain all required shareholder consents to the election. Additionally, X's governing documents could be interpreted to allow for disproportionate distributions to shareholders, possibly creating a second class of stock. On Date 3, X and its shareholders amended its governing documents to remove the provisions allowing for disproportionate distributions. However, the amendment to the governing documents could be interpreted to continue to allow for disproportionate distributions. Furthermore, on Date 3, X issued Units, which constituted a second class of stock. X represents that it has amended its operating agreement to correct all second class of stock issues and has redeemed the Units.

X represents that the invalidity of its S election was inadvertent and was not motivated by tax avoidance or retroactive tax planning. X represents that all of X's distributions to shareholders have been pro rata in accordance with their ownership interests. X also represents that X and its shareholders agree to make any adjustments required as a condition of obtaining relief under the inadvertent invalid election rule as provided under § 1362(f) that may be required by the Secretary. X and its shareholders represent that they have filed all returns consistently with X being an S corporation.

## 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 and which does not (A) have more than 100 shareholders, (B) 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, (C) have a nonresident alien as a shareholder, and (D) have more than 1 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(f) provides that if (1) an election under subsection (a) or section 1361(b)(3)(B)(ii) by any corporation (A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or (B) was terminated under paragraph (2) or (3) of subsection (d) or section 1361(b)(3)(C); (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 a qualified subchapter S subsidiary, as the case may be, 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 in such corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of such corporation as an S corporation or a qualified subchapter S subsidiary, as the case may be) 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 or a qualified subchapter S subsidiary, as the case may be during the period specified by the Secretary.

## CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that X's S election was ineffective as of Date 2 because of the missing shareholder consents and possibly because of the disproportionate distribution provisions in the governing documents. In addition, if X's S election had been effective as of Date 2, it would have terminated on Date 3 due to its issuance of Units. It also may have terminated due to the amended provisions allowing for disproportionate distributions. We further conclude that the ineffectiveness and potential termination of X's S corporation election were inadvertent within the meaning of § 1362(f). Therefore, X will be treated as an S corporation effective Date 2 and thereafter, provided X's S corporation election is otherwise valid and 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.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

Joy C. Spies

Joy C. Spies  
Senior Technician Reviewer, Branch 1  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter

Copy of this letter for section 6110 purposes

cc: