

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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CC:PSI:3 PLR-107624-06

Date: November 9, 2006

Company =

State =

Shareholders
Agreement =

a =

b =

Dear :

This letter responds to a letter dated January 27 2006, submitted on behalf of Company requesting a ruling under § 1361(b)(1)(D) of the Internal Revenue Code.

FACTS

Company was incorporated under the laws of State and filed an S corporation election effective for its taxable year beginning a. Company, its shareholders, and its option holders entered into the Shareholders Agreement effective as of b. Section 3 of the Shareholders Agreement contains provisions relating to minimum distributions to shareholders by Company. Distributions under those provisions are made based on the shareholders' varying interests in Company's income in the current or immediately preceding taxable year (or earlier if such earlier year's taxable income is adjusted by Company or the Service) ("Varying Interests Distributions"). Company's Varying Interests Distributions entail year-end and quarterly distributions that enable shareholders to make timely estimated and final tax payments. The distributions are

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made directly to the shareholders rather than to their respective taxing authorities on behalf of the shareholders.

In addition to Varying Interests Distributions, Company declares dividends and makes pro rata distributions to its shareholders based on the number of shares owned by the shareholders as of the record date ("Record Date Distributions"). Company's Record Date Distributions are made in accordance with the corporate laws of State, which provides that all shares of the same class are equal. The Shareholders Agreement and applicable corporate laws of State constitute the governing provisions of Company.

LAW

Section 1361(a)(1) provides that for purposes of the Code, the term "S corporation" means, with respect to the 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 the term "small business corporation" means a domestic corporation that, among other things, does not have more than one class of stock. Accordingly, S corporations may not have more than one class of stock.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides that a corporation that has more than one class of stock does not qualify as a small business corporation. Except as provided in § 1.1361-1(l)(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, in part, that the determination 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). 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)(iv) provides that a governing provision does not, within the meaning of § 1.1361-1(l)(2)(i), alter the rights to liquidation and distribution proceeds conferred by an S corporation's stock merely because the governing provision provides that, as a result of a change in stock ownership, distributions in a taxable year are to be

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made on the basis of the shareholders' varying interests in the S corporation's income in the current or immediately preceding taxable year. If distributions pursuant to the provision are not made within a reasonable time after the close of the taxable year in which the varying interests occur, the distribution may be recharacterized depending on the facts and circumstances, but will not result in a second class of stock.

CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that Company's governing provisions relating to Varying Interests Distributions and to Record Date Distributions do not cause Company to have more than one class of stock for purposes of § 1361(b)(1)(D).

Except for the specific ruling above, we express or imply no opinion concerning the federal income tax consequences of the facts of this case under any other provision of the Code. Specifically, we express or imply no opinion regarding Company's eligibility to be an S corporation.

Under a power of attorney on file with this office, we are sending a copy of this letter to Company's authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

/s/

CHRISTINE ELLISON
Chief, Branch 3
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure: copy of this letter for § 6110 purposes