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Trust =

X represents that its tax advisors were unaware that X had two classes of stock issued and outstanding. When X discovered that it had two classes of stock issued and outstanding, X submitted this request for a ruling. As corrective action, X has converted all the preferred stock to common stock.

X represents that there was no intent to knowingly make an invalid S corporation election and that the events that resulted in the invalid election were not motivated by tax avoidance or retroactive tax planning.

X and its shareholders agree to make any adjustments required by the Secretary consistent with the treatment of X as an S corporation.

### **LAW AND ANALYSIS**

Section 1361(a) provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under section 1362(a) is in effect for the year.

Section 1361(b)(1) provides that the term "small business corporation" means a domestic corporation that is not an ineligible corporation and that meets the requirements specified in section 1361(b)(1)(A) through (D).

Section 1361(b)(1)(D) provides that S corporations may not have more than one class of stock. Section 1.1361-1(l)(1) of the Income Tax Regulations provides that, except as provided in section 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 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 law, and binding agreements relating to distribution and liquidation proceeds (collectively, the governing provisions).

Section 1362(f) provides, in relevant part, that if (1) an election under section 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to section 1362(b)(2)) by reason of a failure to meet the requirements of section 1361 (b) or to obtain shareholder consents, (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 circumstances resulting in ineffectiveness, steps were taken so that the corporation is once more 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 section 1362(f), agrees to make any adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to the period, then,

notwithstanding the circumstances resulting in the ineffectiveness, the corporation shall be treated as continuing to be 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 intended S corporation election was invalid because X had two classes of stock. We further conclude that the ineffectiveness was inadvertent within the meaning of section 1362(f). Therefore, X will be treated as continuing to be an S corporation from Date 2, and thereafter, provided that X's subchapter S election is not otherwise terminated under section 1362(d).

Except as specifically set forth above, we express no opinion concerning the federal tax consequences of the facts described above under any other provision of the Code.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being mailed to your authorized representative.

Sincerely,

/s/

David R. Haglund  
Senior Technician Reviewer  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures (2)

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