

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

Number: **202416005**  
Release Date: 4/19/2024

Third Party Communication: None  
Date of Communication: Not Applicable

Index Number: 1362.00-00, 1362.02-00,  
1362.04-00

Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:PSI:B03  
PLR-114424-23

Date:  
January 17, 2024

LEGEND

X =

A =

B =

C =

D =

E =

F =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Agreement 1 =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Dear \_\_\_\_\_ :

This letter responds to a letter dated June 8, 2023, and subsequent correspondence, submitted on behalf of X by X's authorized representatives, requesting relief under § 1362(f) of the Internal Revenue Code (Code).

### FACTS

According to the information submitted, X was organized as a limited liability company under the laws of State on Date 1. X elected to be treated as an S corporation pursuant to § 1362(a) effective Date 3. X represents that on and after Date 3 and until Date 4, the owners of X were eligible S corporation shareholders.

Agreement 1, X's operating agreement effective Date 2, did not provide for identical rights to distribution and liquidation proceeds which caused X to have more than one class of stock under § 1361(b)(1)(D), and therefore X's S corporation election made on Date 3 was ineffective. X also made disproportionate distributions to A, B, C, D, E, and F during Year 1, Year 2, and Year 3 which would also have caused the S election to terminate. Further, a reorganization in Year 4 otherwise caused X's S election to terminate.

X represents that the circumstances surrounding the ineffectiveness of X's S corporation election made on Date 3 were inadvertent and not the result of tax avoidance or retroactive tax planning. Further, X represents that X and its shareholders have filed tax returns consistent with X being an S corporation. Finally, X and its shareholders agree to make any adjustments that may be required by the Secretary as a condition of obtaining relief under § 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 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 one class of stock.

Section 1.1361-1(l)(1) of the Income Tax Regulations provides that a corporation is generally treated as having 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 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 laws, and binding agreements relating to distribution and liquidation proceeds (collectively, governing provisions).

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

Section 1362(d)(2)(A) 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 the corporation is an S corporation) such corporation ceases to be a small business corporation. Section 1362(d)(2)(B) further provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides, in 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) or (B) was terminated under § 1362(d)(2), (2) the Secretary determines that the circumstances resulting in the ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in the ineffectiveness or termination, steps were taken so that the corporation for which the election was made or the termination occurred is a small business corporation, and (4) the corporation for which the election was made or the termination occurred, 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 or termination, 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 was not effective when made on Date 3 because X had more than one class of stock. We further conclude that, even if X's S election was not ineffective on Date 3, it would have terminated in Year 1 due to disproportionate distributions made by X. We conclude that the circumstances that caused X's S election to be ineffective and subsequently terminate in Year 1 were inadvertent within the meaning of § 1362(f). Therefore, under § 1362(f), X will be treated as an S corporation from Date 3 to Date 4, provided that its S corporation election was otherwise valid and has not otherwise terminated under § 1362(d).

This ruling is contingent on X and its shareholders taking remedial steps to make corrective distributions to its shareholders to eliminate the cumulative amount of the disproportionate distributions made by X to its shareholders by filing, within 120 days from the date of this letter, all required returns (including amended returns) for all open years consistent with X's election to be treated as an S corporation from Date 3 to Date 4. A copy of this letter should be attached to any such returns.

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 on whether X was otherwise eligible to be an S corporation and any tax consequences related to the reorganization in Year 4.

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 the request for rulings, it is subject to verification on examination.

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

Sincerely,

Robert Alinsky  
Chief, Branch 3  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosure:

Copy of this letter for § 6110 purposes

cc: