Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B02
PLR-119676-08
Date:
September 22, 2008

X =

Date 1=

Date 2=

Date 3=

Date 4=

Date 5=

Dear :

This responds to a letter dated April 24, 2008, submitted on behalf of X by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code.

X was incorporated on Date 1 and made an election to be treated as an S corporation effective Date 2. X's election may have been inadvertently terminated effective Date 3 when X issued notes to a number of individuals, since these notes were convertible to X stock on Date 4. X discovered this problem on Date 5, by which time the notes had already converted to X stock.

X represents that the termination was not motivated by tax avoidance or retroactive tax planning. X and its shareholders have agreed to make any adjustments that the Commissioner may require, consistent with the treatment of X as an S corporation.

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)(4)(iv) provides that a convertible debt instrument is considered a second class of stock if: (1) it would be treated as a second class of stock under § 1.1361-1(l)(4)(ii); or (2) it embodies rights equivalent to those of a call option that would be treated as a second class of stock under § 1.1361-1(l)(4)(iii).

Section 1362(f) provides 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 to obtain shareholder consents or (B) was terminated under § 1362(d)(2) or (3), (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 (A) so that the corporation is a small business corporation or (B) to acquire the 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 the ineffectiveness or termination, the corporation will be treated as an S corporation during the period specified by the Secretary.

Based solely on the facts submitted and the representations made, we conclude that the possible termination of X’s S corporation election on Date 3 was inadvertent within the meaning of § 1362(f). We further conclude that, pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation from Date 3 and thereafter, provided X’s S corporation election was valid and provided that the election was not otherwise terminated under § 1361(d).

This ruling is conditioned upon the shareholders of X including in income their pro rata share of the separately stated and nonseparately computed items of X as provided in § 1366, making any adjustments to basis as provided in § 1367, and taking into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this letter ruling shall be null and void.

Except as specifically ruled above, we express no opinion concerning the federal tax consequences of the transactions described above under any other provisions of the Code.

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

Pursuant to a power of attorney on file, a copy of this letter is being sent to X's authorized representatives.

Sincerely,

Michael Skeen
Acting Chief, Branch 2
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures: 2
Copy of this letter
Copy for § 6110 purposes

cc: