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	Person to Contact:
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Legend	
Taxpayer	=
A	=
В	=
С	=
D	=
Firm 1	=
Firm 2	=
Date 1	=
Date 2	=
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Dear

This letter responds to your letter dated August 8, 1999, written on behalf of Taxpayer, requesting a ruling regarding Taxpayer's status as an S corporation

FACTS

According to the information submitted, Taxpayer was incorporated on Date 1. On Date 2, Taxpayer elected to be treated as an S corporation, effective as of Date 1.

On Date 3, Taxpayer's sole shareholders were A and B, each of whom owned x percent of Taxpayer's outstanding shares. In that same year, Year 1, Taxpayer made distributions totaling \$K to A and \$L to B.

On or about Date 4, Taxpayer retained Firm 1 to assist Taxpayer in forming D, a British limited company. Firm 1 informed Taxpayer that Taxpayer's method of accounting may not have been in accordance with generally accepted accounting procedures.

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On Date 5, Taxpayer declared a stock dividend and then sold some of its stock to C. The dividend and sale left A and B each with y percent of Taxpayer's outstanding stock and C with Z percent of it. That same year, Year 2, Taxpayer made distributions totaling \$M to A, \$N to B, and \$O to C. Later in Year 2, Taxpayer retained Firm 2 to review Taxpayer's method of accounting.

Early in the following year, Year 3, Taxpayer made distributions totaling \$P to A, \$Q to B, and \$R to C. Early that year, Firm 2 informed A that in Years 1, 2, and 3 Taxpayer had made disproportionate dividends to shareholders and that the distributions may have terminated Taxpayer's S corporation election.

On the advice of Firm 2, Taxpayer took the following steps. Taxpayer submitted a request for waiver of any inadvertent termination of its S corporation election under § 1362(f). Additionally, Taxpayer determined that remedial distributions needed to be made so that distributions to shareholders in Years 1, 2, and 3 would be proportionate to each shareholder's shares. On Date 6, the following remedial distributions were made: a total of \$S to A and \$T to C.

Taxpayer represents that, before Firm 2's notification of A, Taxpayer had no knowledge that its distributions might have terminated its S corporation election and that Taxpayer and its principal officers (A and B) possessed no knowledge of S corporation taxation. Taxpayer represents that it has only a single class of stock. Finally, shareholders A, B, and C represent that, despite the difference in timing between the disproportionate distributions and the remedial distributions, the shareholders intended that they each would benefit from the Corporation in proportion to their ownership interests in the Corporation.

DISCUSSION

Section 1361(a)(1) provides that the term "S corporation" means, with respect to any tax year, a small business corporation for which an election under § 1362(a) is in effect for that year.

Under § 1361(b)(1)(D), a small business corporation cannot have more than one class of stock. Section 1.1361-1(l)(2)(i) of the Income Tax Regulations provides that the determination of whether all outstanding shares of stock confer identical rights to distribution and liquidation proceeds is based on the governing provisions of a corporation. Such provisions include binding agreements relating to distribution and liquidation proceeds.

Although a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical rights to operating and liquidating distributions, any distributions (including actual, constructive, or deemed distributions) that differ in timing or amount are to be given appropriate tax effect in accordance with

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the facts and circumstances. Example 2 of § 1.1361-1(I)(2)(v) illustrates a determination of whether, when distributions by a corporation differ in timing, the difference in timing causes the corporation to be treated as having more than one class of stock. In the example, S, a corporation, has two equal shareholders. Under the corporation's bylaws, the shareholders are entitled to equal distributions. S distributes \$50,000 to one shareholder in the current year, but does not distribute \$50,000 to other shareholder until one year later. The example determines that such circumstances indicate that the difference in timing was not due to a binding agreement relating to distributions. Accordingly, the example concludes that the difference in timing did not cause S to be treated as having more than one class of stock.

Similarly, here, Taxpayer's stock will not be treated as having other than identical distribution rights because of the difference in timing between Taxpayer's disproportionate and remedial distributions. Accordingly, Taxpayer did not cease to be a small business corporation due to the difference in timing between Taxpayer's distributions in Years 1, 2, and 3.

CONCLUSION

After applying the relevant law and regulations to the representations made, we conclude that Taxpayer's S corporation election did not terminate due to the timing difference between Taxpayer's disproportionate distributions in Years 1, 2, and 3 and the remedial distributions.

Except as specifically ruled above, we express no opinion concerning the federal tax consequences of the transactions described above under any other provision of the Code. Specifically, we express no opinion on the tax consequences of the above facts under § 7872.

This letter is issued only to the taxpayer who requested it. Under 6110(k)(3), it may be used or cited as precedent.

Taxpayer should attach a copy of this letter to its next federal income tax return. We enclose a copy for that purpose.

Pursuant to a power of attorney on file with this office, copies of this ruling are being sent to your representatives.

Sincerely yours, Jeff Erickson Assistant to the Branch Chief, Branch 3 Office of the Assistant Chief Counsel (Passthroughs and Special Industries)

encl: copy for § 6110 purposes