Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:P&SI:3 PLR-107062-00
Date:
July 11, 2000

Company:

LLC:

Partnership:

State:

M:

N:

a:

b:

c:

Dear

This letter responds to a letter from your authorized representatives dated March 24, 2000, submitted on behalf of Company, requesting a ruling under § 1362(f) of the Internal Revenue Code that the termination of Company's S corporation election, if it occurred, was inadvertent. Company represents the following facts.

Company was incorporated in State on a and elected under § 1362(a) to be an S corporation effective the same date.

Company decided to convert to a limited partnership under the State Revised Limited Partnership Act. Company represents that its motive for conversion was the reduction of its State franchise tax and not avoidance of federal tax.

To effect the conversion, M formed LLC, contributing some of his Company stock in exchange for all of the interests in LLC. On b, Company converted into Partnership. LLC was named the general partner, and M and N became limited

partners. Each unit in Partnership held by the partners, general and limited, carried the same economic rights.

On b, Partnership elected under § 301.7701-3 of the Procedure and Administration Regulations to be treated as an association taxable as a corporation. Believing that the conversion would be treated for federal income tax purposes as a reorganization under § 368(a)(1)(F) and that Company's S corporation election would be unaffected by the conversion, Partnership did not file Form 2553 to elect S corporation status.

On December 27, 1999, Rev. Proc. 99-51, 1999-52 I.R.B. 760, announced that the Internal Revenue Service would not rule on whether a state law limited partnership electing to be classified as an association for federal tax purposes has more than one class of stock under § 1361(b)(1)(D). Realizing for the first time that Company's conversion to a State limited partnership might have terminated its S corporation election, Partnership converted back to a State corporation on c. Company represents that it had no plan to terminate its S election. Company acted expeditiously to resolve the issue.

Except as provided in § 1362(g), § 1362(a)(1) provides that a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1361(b)(1)(D) provides that, for purposes of subchapter S, the term "small business corporation" means a domestic corporation that is not an ineligible corporation and that does not, among other things, have more than one class of stock.

Section 1362(d)(2)(A) provides that an election under § 1362(a) terminates whenever the corporation ceases to be a small business corporation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3); (2) the Secretary determines that the circumstances resulting in termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in termination, steps were taken so that the corporation is 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 § 1362(f), agrees to make the adjustments (consistent with the treatment of the corporation as an S corporation) as might be required by the Secretary regarding this period, then, notwithstanding the circumstances resulting in termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(b) provides that the determination of whether a termination was inadvertent is made by the Commissioner. The corporation has the burden of

establishing that under the relevant facts and circumstances the Commissioner should determine that the termination was inadvertent. The fact that the terminating event was not reasonably within the control of the corporation and was not part of a plan to terminate the election, or the fact that the event took place without the knowledge of the corporation, notwithstanding its due diligence to safeguard itself against such an event, tends to establish that the termination was inadvertent.

According to the legislative history of § 1362(f)--

> If the Internal Revenue Service determines that a corporation's subchapter S election is inadvertently terminated, the Service can waive the effect of the terminating event for any period if the corporation timely corrects the event and if the corporation and the shareholders agree to be treated as if the election had been in effect for such period.
>
> The committee intends that the Internal Revenue Service be reasonable in granting waivers, so that corporations whose subchapter S eligibility requirements have been inadvertently violated do not suffer the tax consequences of a termination if no tax avoidance would result from the continued subchapter S treatment. In granting a waiver, it is hoped that taxpayers and the government will work out agreements that protect the revenues without undue hardship to taxpayers.... It is expected that the waiver may be made retroactive for all years, or retroactive for the period in which the corporation again became eligible for subchapter S treatment, depending on the facts.

S. Rep. No. 640, 97th Cong., 2d Sess. 12-13 (1982); 1982-2 C.B. 718, 723-24.

The Internal Revenue Service is studying the issue of whether a state law limited partnership electing under § 301.7701-3 to be classified as an association taxable as a corporation has more than one class of stock for purposes of § 1361(b)(1)(D). Until the Service resolves this issue through published guidance, letter rulings will not be issued. The Service will treat any request for a ruling whether a state law limited partnership is eligible to elect S corporation status as a request for a ruling on whether the partnership complies with § 1361(b)(1)(D). Rev. Proc. 2000-3, § 5.26, 2000-1 I.R.B. 103, 113, based on Rev. Proc. 99-51, 1999-52 I.R.B. 760.

Based solely on the facts as represented by Company in this ruling request, we conclude that if Company’s conversion from a State corporation to a State limited partnership did create a second class of stock, the consequent termination of Company's S corporation election was inadvertent within the meaning of § 1362(f).

Therefore, we rule that Company will continue to be treated as an S corporation for the period from b to c, and thereafter, unless Company's S election otherwise terminates under § 1362(d).

This ruling is based on 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 ruling request, it is subject to verification on examination.

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

In accordance with the power of attorney on file with this office, we are sending a copy of this letter to your 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,
WILLIAM P. O'SHEA
Chief, Branch 3
Office of Assistant Chief Counsel
(Passthroughs and Special Industries)

enclosure: copy for § 6110 purposes