

26 USC Subtitle A, CHAPTER 1, Subchapter S: Tax Treatment of S Corporations and Their Shareholders

From Title 26—INTERNAL REVENUE CODE

Subtitle A—Income Taxes

CHAPTER 1—NORMAL TAXES AND SURTAXES

Subchapter S—Tax Treatment of S Corporations and Their Shareholders

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PART I—IN GENERAL

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- 1363. Effect of election on corporation.

§1361. S corporation defined

(a) S corporation defined

(1) In general

For purposes of this title, 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 such year.

(2) C corporation

For purposes of this title, the term "C corporation" means, with respect to any taxable year, a corporation which is not an S corporation for such year.

(b) Small business corporation

(1) In general

For purposes of this subchapter, the term "small business corporation" means 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 subsection (c)(2), or an organization described in subsection (c)(6)) who is not an individual,
- (C) have a nonresident alien as a shareholder, and
- (D) have more than 1 class of stock.

(2) Ineligible corporation defined

For purposes of paragraph (1), the term "ineligible corporation" means any corporation which is—

- (A) a financial institution which uses the reserve method of accounting for bad debts described in section 585,
- (B) an insurance company subject to tax under subchapter L, or
- (C) a DISC or former DISC.

(3) Treatment of certain wholly owned subsidiaries

(A) In general

Except as provided in regulations prescribed by the Secretary, for purposes of this title—

- (i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and
- (ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

26 USC 1362: Election; revocation; termination

Text contains those laws in effect on March 20, 2022

From Title 26-INTERNAL REVENUE CODE

Subtitle A-Income Taxes

CHAPTER 1-NORMAL TAXES AND SURTAXES

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PART I-IN GENERAL

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§1362. Election; revocation; termination

(a) Election

✓(1) In general

Except as provided in subsection (g), a small business corporation may elect, in accordance with the provisions of this section, to be an S corporation.

✓(2) All shareholders must consent to election

An election under this subsection shall be valid only if all persons who are shareholders in such corporation on the day on which such election is made consent to such election.

(b) When made

(1) In general

An election under subsection (a) may be made by a small business corporation for any taxable year-

(A) at any time during the preceding taxable year, or

(B) at any time during the taxable year and on or before the 15th day of the 3d month of the taxable year.

(2) Certain elections made during 1st 2½ months treated as made for next taxable year

If-

(A) an election under subsection (a) is made for any taxable year during such year and on or before the 15th day of the 3d month of such year, but

(B) either-

(i) on 1 or more days in such taxable year before the day on which the election was made the corporation did not meet the requirements of subsection (b) of section 1361, or

(ii) 1 or more of the persons who held stock in the corporation during such taxable year and before the election was made did not consent to the election,

then such election shall be treated as made for the following taxable year.

(3) Election made after 1st 2½ months treated as made for following taxable year

If-

(A) a small business corporation makes an election under subsection (a) for any taxable year, and

(B) such election is made after the 15th day of the 3d month of the taxable year and on or before the 15th day of the 3rd month of the following taxable year,

then such election shall be treated as made for the following taxable year.

(4) Taxable years of 2½ months or less

For purposes of this subsection, an election for a taxable year made not later than 2 months and 15 days after the first day of the taxable year shall be treated as timely made during such year.

(5) Authority to treat late elections, etc., as timely

If-

(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this subsection for making such election for such taxable year or no such election is made for any taxable year, and

(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such an election as timely made for such taxable year (and paragraph (3) shall not apply).

(c) Years for which effective

An election under subsection (a) shall be effective for the taxable year of the corporation for which it is made and for all succeeding taxable years of the corporation, until such election is terminated under subsection (d).

(d) Termination

26 USC 1363: Effect of election on corporation

Text contains those laws in effect on March 10, 2022

From Title 26-INTERNAL REVENUE CODE

Subtitle A-Income Taxes

CHAPTER 1-NORMAL TAXES AND SURTAXES

Subchapter S-Tax Treatment of S Corporations and Their Shareholders

PART I-IN GENERAL

Jump To:Source CreditMiscellaneousAmendmentsEffective Date**§1363. Effect of election on corporation****(a) General rule**

Except as otherwise provided in this subchapter, an S corporation shall not be subject to the taxes imposed by this chapter.

(b) Computation of corporation's taxable income.

The taxable income of an S corporation shall be computed in the same manner as in the case of an individual, except that-

- (1) the items described in section 1366(a)(1)(A) shall be separately stated,
- (2) the deductions referred to in section 703(a)(2) shall not be allowed to the corporation,
- (3) section 248 shall apply, and
- (4) section 291 shall apply if the S corporation (or any predecessor) was a C corporation for any of the 3 immediately preceding taxable years.

(c) Elections of the S corporation**(1) In general**

Except as provided in paragraph (2), any election affecting the computation of items derived from an S corporation shall be made by the corporation.

(2) Exceptions

In the case of an S corporation, elections under the following provisions shall be made by each shareholder separately-

- (A) section 617 (relating to deduction and recapture of certain mining exploration expenditures), and
- (B) section 901 (relating to taxes of foreign countries and possessions of the United States).

(d) Recapture of LIFO benefits**(1) In general**

If-

- (A) an S corporation was a C corporation for the last taxable year before the first taxable year for which the election under section 1362(a) was effective, and
- (B) the corporation inventoried goods under the LIFO method for such last taxable year,

the LIFO recapture amount shall be included in the gross income of the corporation for such last taxable year (and appropriate adjustments to the basis of inventory shall be made to take into account the amount included in gross income under this paragraph).

(2) Additional tax payable in installments**(A) In general**

Any increase in the tax imposed by this chapter by reason of this subsection shall be payable in 4 equal installments.

(B) Date for payment of installments

The first installment under subparagraph (A) shall be paid on or before the due date (determined without regard to extensions) for the return of the tax imposed by this chapter for the last taxable year for which the corporation was a C corporation and the 3 succeeding installments shall be paid on or before the due date (as so determined) for the corporation's return for the 3 succeeding taxable years.

(C) No interest for period of extension

Notwithstanding section 6601(b), for purposes of section 6601, the date prescribed for the payment of each installment under this paragraph shall be determined under this paragraph.

(3) LIFO recapture amount

For purposes of this subsection, the term "LIFO recapture amount" means the amount (if any) by which-

- (A) the inventory amount of the inventory asset under the first-in, first-out method authorized by section 471, exceeds
- (B) the inventory amount of such assets under the LIFO method.

For purposes of the preceding sentence, inventory amounts shall be determined as of the close of the last taxable year referred to in paragraph (1).

(4) Other definitions

For purposes of this subsection-

(A) LIFO method

The term "LIFO method" means the method authorized by section 472.

(B) Inventory assets

The term "inventory assets" means stock in trade of the corporation, or other property of a kind which would properly be included in the inventory of the corporation if on hand at the close of the taxable year.

(C) Method of determining inventory amount

The inventory amount of assets under a method authorized by section 471 shall be determined-

- (i) if the corporation uses the retail method of valuing inventories under section 472, by using such method, or
- (ii) if clause (i) does not apply, by using cost or market, whichever is lower.

(D) Not treated as member of affiliated group

Except as provided in regulations, the corporation referred to in paragraph (1) shall not be treated as a member of an affiliated group with respect to the amount included in gross income under paragraph (1).

(5) Special rule

Sections 1367(a)(2)(D) and 1371(c)(1) shall not apply with respect to any increase in the tax imposed by reason of this subsection.

(Added Pub. L. 97-354, §2, Oct. 19, 1982, 96 Stat. 1676 ; amended Pub. L. 98-369, div. A, title VII, §721(a), (b)(1), (p), July 18, 1984, 98 Stat. 966 , 970; Pub. L. 99-514, title V, §511(d)(2)(C), title VI, §632(b), title VII, §701(e)(4)(J), Oct. 22, 1986, 100 Stat. 2249 , 2277, 2343; Pub. L. 100-203, title X, §10227(a), Dec. 22, 1987, 101 Stat. 1330-416 ; Pub. L. 100-647, title I, §1006(f)(7), title II, §2004(n), Nov. 10, 1988, 102 Stat. 3407 , 3608; Pub. L. 109-135, title IV, §411(a), Dec. 21, 2005, 119 Stat. 2636 .)

EDITORIAL NOTES

AMENDMENTS

2005-Subsec. (d)(5). Pub. L. 109-135 added par. (5).

1988-Subsec. (d). Pub. L. 100-647, §1006(f)(7), struck out subsec. (d) which related to distributions of appreciated property.

Subsec. (d)(4)(D). Pub. L. 100-647, §2004(n), added subpar. (D).

Subsec. (e). Pub. L. 100-647, §1006(f)(7), struck out subsec. (e) which provided that subsec. (d) not apply to reorganizations, etc.

1987-Subsec. (d). Pub. L. 100-203 added subsec. (d) relating to recapture of LIFO benefits.

1986-Subsec. (a). Pub. L. 99-514, §701(e)(4)(J), struck out "and in section 58(d)" after "this subchapter".

Subsec. (c)(2). Pub. L. 99-514, §511(d)(2)(C), redesignated subpars. (B) and (C) as (A) and (B), respectively, and struck out former subpar. (A) which read as follows: "section 163(d) (relating to limitation on interest on investment indebtedness)".

Subsec. (e). Pub. L. 99-514, §632(b), amended subsec. (e) generally, substituting "reorganizations, etc." for "complete liquidations and reorganizations", in heading and in text struck out reference to property in complete liquidation of the corporation.

1984-Subsec. (b)(4). Pub. L. 98-369, §721(p), added par. (4).

Subsec. (c)(2). Pub. L. 98-369, §721(b)(1), redesignated subpars. (B) to (D) as (A) to (C), respectively, and struck out subpar. (A) which provided "subsection (b)(5) or (d)(4) of section 108 (relating to income from discharge of indebtedness)".

Subsec. (d). Pub. L. 98-369, §721(a)(2), substituted "Except as provided in subsection (e), if" for "If".

Subsec. (e). Pub. L. 98-369, §721(a)(1), added subsec. (e).

26 USC Subtitle A, CHAPTER 1, Subchapter S, PART II: TAX TREATMENT OF SHAREHOLDERS**From Title 26—INTERNAL REVENUE CODE**

Subtitle A—Income Taxes

CHAPTER 1—NORMAL TAXES AND SURTAXES

Subchapter S—Tax Treatment of S Corporations and Their Shareholders

PART II—TAX TREATMENT OF SHAREHOLDERS

Sec

1366.

Pass-thru of items to shareholders.

1367.

Adjustments to basis of stock of shareholders, etc.

1368.

Distributions.

§1366. Pass-thru of items to shareholders**(a) Determination of shareholder's tax liability****(1) In general**

In determining the tax under this chapter of a shareholder for the shareholder's taxable year in which the taxable year of the S corporation ends (or for the final taxable year of a shareholder who dies, or of a trust or estate which terminates, before the end of the corporation's taxable year), there shall be taken into account the shareholder's pro rata share of the corporation's—

(A) items of income (including tax-exempt income), loss, deduction, or credit the separate treatment of which could affect the liability for tax of any shareholder, and

(B) nonseparately computed income or loss.

For purposes of the preceding sentence, the items referred to in subparagraph (A) shall include amounts described in paragraph (4) or (6) of section 702(a).

(2) Nonseparately computed income or loss defined

For purposes of this subchapter, the term "nonseparately computed income or loss" means gross income minus the deductions allowed to the corporation under this chapter, determined by excluding all items described in paragraph (1)(A).

(b) Character passed thru

The character of any item included in a shareholder's pro rata share under paragraph (1) of subsection (a) shall be determined as if such item were realized directly from the source from which realized by the corporation, or incurred in the same manner as incurred by the corporation.

(c) Gross income of a shareholder

In any case where it is necessary to determine the gross income of a shareholder for purposes of this title, such gross income shall include the shareholder's pro rata share of the gross income of the corporation.

(d) Special rules for losses and deductions**(1) Cannot exceed shareholder's basis in stock and debt**

The aggregate amount of losses and deductions taken into account by a shareholder under subsection (a) for any taxable year shall not exceed the sum of—

(A) the adjusted basis of the shareholder's stock in the S corporation (determined with regard to paragraphs (1) and (2)(A) of section 1367(a) for the taxable year), and

(B) the shareholder's adjusted basis of any indebtedness of the S corporation to the shareholder (determined without regard to any adjustment under paragraph (2) of section 1367(b) for the taxable year).

(2) Indefinite carryover of disallowed losses and deductions**(A) In general**

Except as provided in subparagraph (B), any loss or deduction which is disallowed for any taxable year by reason of paragraph (1) shall be treated as incurred by the corporation in the succeeding taxable year with respect to that shareholder.

(B) Transfers of stock between spouses or incident to divorce

In the case of any transfer described in section 1041(a) of stock of an S corporation, any loss or deduction described in subparagraph (A) with respect such stock shall be treated as incurred by the corporation in the succeeding taxable year with respect to the transferee.

(3) Carryover of disallowed losses and deductions to post-termination transition period**(A) In general**

If for the last taxable year of a corporation for which it was an S corporation a loss or deduction was disallowed by reason of paragraph (1), such loss or deduction shall be treated as incurred by the shareholder on the last day of any post-termination transition period.

(B) Cannot exceed shareholder's basis in stock

The aggregate amount of losses and deductions taken into account by a shareholder under subparagraph (A) shall not exceed the adjusted basis of the shareholder's stock in the corporation (determined at the close of the last day of the post-termination transition period and without regard to this paragraph).

(C) Adjustment in basis of stock

The shareholder's basis in the stock of the corporation shall be reduced by the amount allowed as a deduction by reason of this paragraph.

(D) At-risk limitations

To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a).

(4) Application of limitation on charitable contributions

In the case of any charitable contribution of property to which the second sentence of section 1367(a)(2) applies, paragraph (1) shall not apply to the extent of the excess (if any) of—

- (A) the shareholder's pro rata share of such contribution, over
- (B) the shareholder's pro rata share of the adjusted basis of such property.

(e) Treatment of family group

If an individual who is a member of the family (within the meaning of section 704(e)(2)) of one or more shareholders of an S corporation renders services for the corporation or furnishes capital to the corporation without receiving reasonable compensation therefor, the Secretary shall make such adjustments in the items taken into account by such individual and such shareholders as may be necessary in order to reflect the value of such services or capital.

(f) Special rules**(1) Subsection (a) not to apply to credit allowable under section 34**

Subsection (a) shall not apply with respect to any credit allowable under section 34 (relating to certain uses of gasoline and special fuels).

(2) Treatment of tax imposed on built-in gains

If any tax is imposed under section 1374 for any taxable year on an S corporation, for purposes of subsection (a), the amount so imposed shall be treated as a loss sustained by the S corporation during such taxable year. The character of such loss shall be determined by allocating the loss proportionately among the recognized built-in gains giving rise to such tax.

(3) Reduction in pass-thru for tax imposed on excess net passive income

If any tax is imposed under section 1375 for any taxable year on an S corporation, for purposes of subsection (a), each item of passive investment income shall be reduced by an amount which bears the same ratio to the amount of such tax as—

- (A) the amount of such item, bears to
- (B) the total passive investment income for the taxable year.

(Added Pub. L. 97-354, §2, Oct. 19, 1982, 96 Stat. 1677; amended Pub. L. 98-369, div. A, title IV, §474(r)(26), title VII, §735(c)(16), July 18, 1984, 98 Stat. 844, 985; Pub. L. 99-514, title VI, §632(c)(2), title VII, §701(e)(4)(K), Oct. 22, 1986, 100 Stat. 2277, 2343; Pub. L. 100-647, title I, §1006(f)(5)(E), Nov. 10, 1988, 102 Stat. 3406; Pub. L. 101-239, title VII, §7811(c)(7), Dec. 19, 1989, 103 Stat. 2407; Pub. L. 104-188, title I, §§1302(e), 1307(c)(3)(A), 1309(a)(1), 1312, Aug. 20, 1996, 110 Stat. 1779, 1782, 1783, 1784; Pub. L. 108-357, title II, §235(a), Oct. 22, 2004, 118 Stat. 1435; Pub. L. 110-172, §3(b), Dec. 29, 2007, 121 Stat. 2474; Pub. L. 115-141, div. U, title IV, §401(a)(192), Mar. 23, 2018, 132 Stat. 1193.)

26 USC Subtitle A, CHAPTER 1, Subchapter S, PART III: SPECIAL RULES**From Title 26—INTERNAL REVENUE CODE**

Subtitle A—Income Taxes

CHAPTER 1—NORMAL TAXES AND SURTAXES

Subchapter S—Tax Treatment of S Corporations and Their Shareholders

PART III—SPECIAL RULES

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1371.

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1375.

Tax imposed when passive investment income of corporation having accumulated earnings and profits exceeds 25 percent of gross receipts.

EDITORIAL NOTES**AMENDMENTS**

1996—Pub. L. 104–188, title I, §1311(b)(2)(D), Aug. 20, 1996, 110 Stat. 1784, substituted "accumulated" for "subchapter C" in item 1375.

1986—Pub. L. 99–514, title VI, §632(d), Oct. 22, 1986, 100 Stat. 2277, substituted "built-in" for "capital" in item 1374.

§1371. Coordination with subchapter C**(a) Application of subchapter C rules***SEE IRC 312 AND REG 1.312-6(b)*

Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders.

(b) No carryover between C year and S year**(1) From C year to S year**

No carryforward, and no carryback, arising for a taxable year for which a corporation is a C corporation may be carried to a taxable year for which such corporation is an S corporation.

(2) No carryover from S year

No carryforward, and no carryback, shall arise at the corporate level for a taxable year for which a corporation is an S corporation.

(3) Treatment of S year as elapsed year

Nothing in paragraphs (1) and (2) shall prevent treating a taxable year for which a corporation is an S corporation as a taxable year for purposes of determining the number of taxable years to which an item may be carried back or carried forward.

(c) Earnings and profits**(1) In general**

Except as provided in paragraphs (2) and (3) and subsection (d)(3), no adjustment shall be made to the earnings and profits of an S corporation.

(2) Adjustments for redemptions, liquidations, reorganizations, divisives, etc.

In the case of any transaction involving the application of subchapter C to any S corporation, proper adjustment to any accumulated earnings and profits of the corporation shall be made.

(3) Adjustments in case of distributions treated as dividends under section 1368(c)(2)

Paragraph (1) shall not apply with respect to that portion of a distribution which is treated as a dividend under section 1368(c)(2).

(d) Coordination with investment credit recapture**(1) No recapture by reason of election**

Any election under section 1362 shall be treated as a mere change in the form of conducting a trade or business for purposes of the second sentence of section 50(a)(4).

(2) Corporation continues to be liable

Notwithstanding an election under section 1362, an S corporation shall continue to be liable for any increase in tax under section 49(b) or 50(a) attributable to credits allowed for taxable years for which such corporation was not an S corporation.

(3) Adjustment to earnings and profits for amount of recapture

Paragraph (1) of subsection (c) shall not apply to any increase in tax under section 49(b) or 50(a) for which the S corporation is liable.

26 USC 1373: Foreign income

Text contains those laws in effect on March 10, 2022

From Title 26-INTERNAL REVENUE CODE

Subtitle A-Income Taxes

CHAPTER 1-NORMAL TAXES AND SURTAXES

Subchapter S-Tax Treatment of S Corporations and Their Shareholders

PART III-SPECIAL RULES

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Prior Provisions

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✓ **§1373. Foreign income**

(a) S corporation treated as partnership, etc.

✓ For purposes of subparts A and F of part III, and part V, of subchapter N (relating to income from sources without the United States)-

- (1) an S corporation shall be treated as a partnership, and
- (2) the shareholders of such corporation shall be treated as partners of such partnership.

(b) Recapture of overall foreign loss

For purposes of section 904(f) (relating to recapture of overall foreign loss), the making or termination of an election to be treated as an S corporation shall be treated as a disposition of the business.

(Added Pub. L. 97-354, §2, Oct. 19, 1982, 96 Stat. 1682 .)

EDITORIAL NOTES

PRIOR PROVISIONS

A prior section 1373, added Pub. L. 85-866, title I, §64(a), Sept. 2, 1958, 72 Stat. 1652 ; amended Pub. L. 89-389, §2(b)(3), Apr. 14, 1966, 80 Stat. 114 ; Pub. L. 91-172, title III, §301(b)(10), Dec. 30, 1969, 83 Stat. 586 , related to taxation of corporation undistributed taxable income to shareholders, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

STATUTORY NOTES AND RELATED SUBSIDIARIES

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97-354, set out as a note under section 1361 of this title.