

(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.)

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.

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.

§ 1374. Tax imposed on certain built-in gains

(a) General rule

If for any taxable year beginning in the recognition period an S corporation has a net recognized built-in gain, there is hereby imposed a tax (computed under subsection (b)) on the income of such corporation for such taxable year.

(b) Amount of tax

(1) In general

The amount of the tax imposed by subsection (a) shall be computed by applying the highest rate of tax specified in section 11(b) to the net recognized built-in gain of the S corporation for the taxable year.

(2) Net operating loss carryforwards from C years allowed

Notwithstanding section 1371(b)(1), any net operating loss carryforward arising in a taxable year for which the corporation was a C corporation shall be allowed for purposes of this section as a deduction against the net recognized built-in gain of the S corporation for the taxable year. For purposes of determining the amount of any such loss which may be carried to subsequent taxable years, the amount of the net recognized built-in gain shall be treated as taxable income. Rules similar to the rules of the preceding sentences of this paragraph shall apply in the case of a capital loss carryforward arising in a taxable year for which the corporation was a C corporation.

(3) Credits

(A) In general

Except as provided in subparagraph (B), no credit shall be allowable under part IV of subchapter A of this chapter (other than under section 34) against the tax imposed by subsection (a).

(B)¹ Business credit carryforwards from C years allowed

Notwithstanding section 1371(b)(1), any business credit carryforward under section 39 arising in a taxable year for which the corporation was a C corporation shall be allowed as a credit against the tax imposed by subsection (a) in the same manner as if it were imposed by section 11. A similar rule shall apply in the case of the minimum tax credit under section 53 to the extent attributable to taxable years for which the corporation was a C corporation.

(c) Limitations

(1) Corporations which were always S corporations

Subsection (a) shall not apply to any corporation if an election under section 1362(a) has been in effect with respect to such corporation for each of its taxable years. Except as provided in regulations, an S corporation and any predecessor corporation shall be treated as 1 corporation for purposes of the preceding sentence.

(2) Limitation on amount of net recognized built-in gain

The amount of the net recognized built-in gain taken into account under this section for any taxable year shall not exceed the excess (if any) of—

(A) the net unrealized built-in gain, over

(B) the net recognized built-in gain for prior taxable years beginning in the recognition period.

(d) Definitions and special rules

For purposes of this section—

(1) Net unrealized built-in gain

The term “net unrealized built-in gain” means the amount (if any) by which—

(A) the fair market value of the assets of the S corporation as of the beginning of its 1st taxable year for which an election under section 1362(a) is in effect, exceeds

(B) the aggregate adjusted bases of such assets at such time.

(2) Net recognized built-in gain

(A) In general

The term “net recognized built-in gain” means, with respect to any taxable year in the recognition period, the lesser of—

(i) the amount which would be the taxable income of the S corporation for such taxable year if only recognized built-in gains and recognized built-in losses were taken into account, or

(ii) such corporation’s taxable income for such taxable year (determined as provided in section 1375(b)(1)(B)).

(B) Carryover

If, for any taxable year described in subparagraph (A), the amount referred to in clause (i) of subparagraph (A) exceeds the amount referred to in clause (ii) of subparagraph (A), such excess shall be treated as a

¹ See Amendment of Subsection (b)(3)(B) note below.

recognized built-in gain in the succeeding taxable year. The preceding sentence shall apply only in the case of a corporation treated as an S corporation by reason of an election made on or after March 31, 1988.

(3) Recognized built-in gain

The term “recognized built-in gain” means any gain recognized during the recognition period on the disposition of any asset except to the extent that the S corporation establishes that—

(A) such asset was not held by the S corporation as of the beginning of the 1st taxable year for which it was an S corporation, or

(B) such gain exceeds the excess (if any) of—

(i) the fair market value of such asset as of the beginning of such 1st taxable year, over

(ii) the adjusted basis of the asset as of such time.

(4) Recognized built-in losses

The term “recognized built-in loss” means any loss recognized during the recognition period on the disposition of any asset to the extent that the S corporation establishes that—

(A) such asset was held by the S corporation as of the beginning of the 1st taxable year referred to in paragraph (3), and

(B) such loss does not exceed the excess of—

(i) the adjusted basis of such asset as of the beginning of such 1st taxable year, over

(ii) the fair market value of such asset as of such time.

(5) Treatment of certain built-in items

(A) Income items

Any item of income which is properly taken into account during the recognition period but which is attributable to periods before the 1st taxable year for which the corporation was an S corporation shall be treated as a recognized built-in gain for the taxable year in which it is properly taken into account.

(B) Deduction items

Any amount which is allowable as a deduction during the recognition period (determined without regard to any carryover) but which is attributable to periods before the 1st taxable year referred to in subparagraph (A) shall be treated as a recognized built-in loss for the taxable year for which it is allowable as a deduction.

(C) Adjustment to net unrealized built-in gain

The amount of the net unrealized built-in gain shall be properly adjusted for amounts which would be treated as recognized built-in gains or losses under this paragraph if such amounts were properly taken into account (or allowable as a deduction) during the recognition period.

(6) Treatment of certain property

If the adjusted basis of any asset is determined (in whole or in part) by reference to the

adjusted basis of any other asset held by the S corporation as of the beginning of the 1st taxable year referred to in paragraph (3)—

(A) such asset shall be treated as held by the S corporation as of the beginning of such 1st taxable year, and

(B) any determination under paragraph (3)(B) or (4)(B) with respect to such asset shall be made by reference to the fair market value and adjusted basis of such other asset as of the beginning of such 1st taxable year.

(7) Recognition period

(A) In general

The term “recognition period” means the 5-year period beginning with the 1st day of the 1st taxable year for which the corporation was an S corporation. For purposes of applying this section to any amount includible in income by reason of distributions to shareholders pursuant to section 593(e), the preceding sentence shall be applied without regard to the phrase “5-year”.

(B) Installment sales

If an S corporation sells an asset and reports the income from the sale using the installment method under section 453, the treatment of all payments received shall be governed by the provisions of this paragraph applicable to the taxable year in which such sale was made.

(8) Treatment of transfer of assets from C corporation to S corporation

(A) In general

Except to the extent provided in regulations, if—

(i) an S corporation acquires any asset, and

(ii) the S corporation’s basis in such asset is determined (in whole or in part) by reference to the basis of such asset (or any other property) in the hands of a C corporation,

then a tax is hereby imposed on any net recognized built-in gain attributable to any such assets for any taxable year beginning in the recognition period. The amount of such tax shall be determined under the rules of this section as modified by subparagraph (B).

(B) Modifications

For purposes of this paragraph, the modifications of this subparagraph are as follows:

(i) In general

The preceding paragraphs of this subsection shall be applied by taking into account the day on which the assets were acquired by the S corporation in lieu of the beginning of the 1st taxable year for which the corporation was an S corporation.

(ii) Subsection (c)(1) not to apply

Subsection (c)(1) shall not apply.

(9) Reference to 1st taxable year

Any reference in this section to the 1st taxable year for which the corporation was an S

corporation shall be treated as a reference to the 1st taxable year for which the corporation was an S corporation pursuant to its most recent election under section 1362.

(e) Regulations

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section including regulations providing for the appropriate treatment of successor corporations.

(Added Pub. L. 97-354, §2, Oct. 19, 1982, 96 Stat. 1683; amended Pub. L. 97-448, title III, §305(d)(3), Jan. 12, 1983, 96 Stat. 2400; Pub. L. 98-369, div. A, title I, §102(d)(1), title IV, §474(r)(27), title VII, §721(u), July 18, 1984, 98 Stat. 623, 844, 971; Pub. L. 99-514, title VI, §632(a), Oct. 22, 1986, 100 Stat. 2275; Pub. L. 100-647, title I, §1006(f)(1)-(5)(A), Nov. 10, 1988, 102 Stat. 3403, 3404; Pub. L. 101-239, title VII, §7811(c)(4), (5)(B), (8), Dec. 19, 1989, 103 Stat. 2407, 2408; Pub. L. 105-34, title XVI, §1601(f)(5)(B), Aug. 5, 1997, 111 Stat. 1091; Pub. L. 111-5, div. B, title I, §1251(a), Feb. 17, 2009, 123 Stat. 342; Pub. L. 111-240, title II, §2014(a), Sept. 27, 2010, 124 Stat. 2556; Pub. L. 112-240, title III, §326(a), (b), Jan. 2, 2013, 126 Stat. 2334; Pub. L. 113-295, div. A, title I, §138(a), Dec. 19, 2014, 128 Stat. 4020; Pub. L. 114-113, div. Q, title I, §127(a), Dec. 18, 2015, 129 Stat. 3054; Pub. L. 115-97, title I, §§12002(c), 13001(b)(2)(N), Dec. 22, 2017, 131 Stat. 2095, 2097.)

AMENDMENT OF SUBSECTION (b)(3)(B)

Pub. L. 115-97, title I, §12002(c), (d), Dec. 22, 2017, 131 Stat. 2095, amended subsection (b)(3)(B) of this section, applicable to taxable years beginning after Dec. 31, 2021. After amendment, subsection (b)(3)(B) reads as follows:

(B) Business credit carryforwards from C years allowed

Notwithstanding section 1371(b)(1), any business credit carryforward under section 39 arising in a taxable year for which the corporation was a C corporation shall be allowed as a credit against the tax imposed by subsection (a) in the same manner as if it were imposed by section 11.

See 2017 Amendment note below.

PRIOR PROVISIONS

A prior section 1374, added Pub. L. 85-866, title I, §64(a), Sept. 2, 1958, 72 Stat. 1653; amended Pub. L. 86-376, §2(b), Sept. 23, 1959, 73 Stat. 699; Pub. L. 94-455, title XIX, §1901(a)(150), Oct. 4, 1976, 90 Stat. 1788, related to allowance to shareholders of corporation net operating loss, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

AMENDMENTS

2017—Subsec. (b)(3)(B). Pub. L. 115-97, §12002(c), struck out at end “A similar rule shall apply in the case of the minimum tax credit under section 53 to the extent attributable to taxable years for which the corporation was a C corporation.”

Subsec. (b)(4). Pub. L. 115-97, §13001(b)(2)(N), struck out par. (4). Text read as follows: “For purposes of section 1201(a)—

“(A) the tax imposed by subsection (a) shall be treated as if it were imposed by section 11, and

“(B) the amount of the net recognized built-in gain shall be treated as the taxable income.”

2015—Subsec. (d)(7). Pub. L. 114-113 amended par. (7) generally. Prior to amendment, par. (7) defined recogni-

tion period, with special rules for certain years and for distributions to shareholders.

2014—Subsec. (d)(7)(C). Pub. L. 113-295 substituted “2012, 2013, and 2014” for “2012 and 2013” in heading and “2012, 2013, or 2014” for “2012 or 2013” in text.

2013—Subsec. (d)(2)(B). Pub. L. 112-240, §326(b), inserted “described in subparagraph (A)” after “for any taxable year”.

Subsec. (d)(7)(C), (D). Pub. L. 112-240, §326(a)(1), (2), added subpar. (C) and redesignated former subpar. (C) as (D).

Subsec. (d)(7)(E). Pub. L. 112-240, §326(a)(3), added subpar. (E).

2010—Subsec. (d)(7)(B). Pub. L. 111-240 amended subpar. (B) generally. Prior to amendment, text read as follows: “In the case of any taxable year beginning in 2009 or 2010, no tax shall be imposed on the net recognized built-in gain of an S corporation if the 7th taxable year in the recognition period preceded such taxable year. The preceding sentence shall be applied separately with respect to any asset to which paragraph (8) applies.”

2009—Subsec. (d)(7). Pub. L. 111-5 amended par. (7) generally. Prior to amendment, text read as follows: “The term ‘recognition period’ means the 10-year period beginning with the 1st day of the 1st taxable year for which the corporation was an S corporation. For purposes of applying this section to any amount includible in income by reason of section 593(e), the preceding sentence shall be applied without regard to the phrase ‘10-year’.”

1997—Subsec. (d)(7). Pub. L. 105-34 inserted at end “For purposes of applying this section to any amount includible in income by reason of section 593(e), the preceding sentence shall be applied without regard to the phrase ‘10-year’.”

1989—Subsec. (b)(3)(B). Pub. L. 101-239, §7811(c)(8), inserted at end “A similar rule shall apply in the case of the minimum tax credit under section 53 to the extent attributable to taxable years for which the corporation was a C corporation.”

Subsec. (d)(2)(A)(i). Pub. L. 101-239, §7811(c)(4), struck out “(except as provided in subsection (b)(2))” after “taxable year if”.

Subsec. (d)(5)(B). Pub. L. 101-239, §7811(c)(5)(B)(i), inserted “(determined without regard to any carryover)” after “during the recognition period”.

Subsec. (d)(5)(C). Pub. L. 101-239, §7811(c)(5)(B)(ii), substituted “which would be treated as recognized built-in gains or losses under this paragraph if such amounts were properly taken into account (or allowable as a deduction) during the recognition period” for “treated as recognized built-in gains or losses under this paragraph”.

1988—Subsec. (a). Pub. L. 100-647, §1006(f)(1), inserted “net” before “recognized”.

Subsec. (b)(1). Pub. L. 100-647, §1006(f)(2), added par. (1) and struck out former par. (1) which read as follows: “The tax imposed by subsection (a) shall be a tax computed by applying the highest rate of tax specified in section 11(b) to the lesser of—

“(A) the recognized built-in gains of the S corporation for the taxable year, or

“(B) the amount which would be the taxable income of the corporation for such taxable year if such corporation were not an S corporation.”

Subsec. (b)(2). Pub. L. 100-647, §1006(f)(2), added par. (2) and struck out former par. (2) which read as follows: “Notwithstanding section 1371(b)(1), any net operating loss carryforward arising in a taxable year for which the corporation was a C corporation shall be allowed as a deduction against the lesser of the amounts referred to in subparagraph (A) or (B) of paragraph (1). For purposes of determining the amount of any such loss which may be carried to subsequent taxable years, the lesser of the amounts referred to in subparagraph (A) or (B) of paragraph (1) shall be treated as taxable income.”

Subsec. (b)(4)(B). Pub. L. 100-647, §1006(f)(3), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: “the lower of the amounts specified in

subparagraphs (A) and (B) of paragraph (1) shall be treated as the taxable income.”

Subsec. (c)(2). Pub. L. 100-647, §1006(f)(4), which directed amendment of par. (2) by substituting “net recognized built-in gain” for “recognized built-in gains” wherever appearing, was executed by making the substitution in heading as well as in introductory provisions and in subpar. (B), to reflect the probable intent of Congress.

Subsec. (d)(2) to (9). Pub. L. 100-647, §1006(f)(5)(A), added pars. (2) to (9) and struck out former pars. (2), (3), and (4), which related to recognized built-in gain, recognition period, and taxable income, respectively.

Subsec. (e). Pub. L. 100-647, §1006(f)(5)(A), added subsec. (e).

1986—Pub. L. 99-514 amended section generally, substituting provisions imposing tax on certain built-in gains for provisions imposing tax on certain capital gains which had declared in: subsec. (a), general rule for capital gains tax on S corporations; subsec. (b), amount of tax; subsec. (c), general rule as to exceptions from subsec. (a) in par. (1), exception as to new corporations in par. (2), provisions relating to property with substituted basis in par. (3), and treatment of certain gains of options and commodities dealers in par. (4); and subsec. (d), determination of taxable income of corporation.

1984—Subsec. (b). Pub. L. 98-369, §474(r)(27), substituted “section 34” for “section 39” in provisions following par. (2).

Subsec. (c)(2). Pub. L. 98-369, §721(u), struck out “(and any predecessor corporation)” before “has been in existence” in subpar. (A), and inserted provision that to the extent provided in regulations, an S corporation and any predecessor corporation shall be treated as 1 corporation for purposes of this paragraph and paragraph (1).

Subsec. (c)(4). Pub. L. 98-369, §102(d)(1), added par. (4).

1983—Subsec. (d). Pub. L. 97-448 substituted “this section” for “subsections (a)(2) and (b)(2)”.

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by section 12002 of Pub. L. 115-97 applicable in general to taxable years beginning after Dec. 31, 2017, and amendment by section 12002(c) applicable to taxable years beginning after Dec. 31, 2021, see section 12002(d) of Pub. L. 115-97, set out as a note under section 53 of this title.

Amendment by section 13001(b)(2)(N) of Pub. L. 115-97 applicable to taxable years beginning after Dec. 31, 2017, see section 13001(c)(1) of Pub. L. 115-97, set out as a note under section 11 of this title.

EFFECTIVE DATE OF 2015 AMENDMENT

Pub. L. 114-113, div. Q, title I, §127(b), Dec. 18, 2015, 129 Stat. 3054, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2014.”

EFFECTIVE DATE OF 2014 AMENDMENT

Pub. L. 113-295, div. A, title I, §138(b), Dec. 19, 2014, 128 Stat. 4020, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2013.”

EFFECTIVE DATE OF 2013 AMENDMENT

Pub. L. 112-240, title III, §326(c), Jan. 2, 2013, 126 Stat. 2334, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2011.”

EFFECTIVE DATE OF 2010 AMENDMENT

Pub. L. 111-240, title II, §2014(b), Sept. 27, 2010, 124 Stat. 2556, provided that: “The amendment made by this section [amending this section] shall apply to taxable years beginning after December 31, 2010.”

EFFECTIVE DATE OF 2009 AMENDMENT

Pub. L. 111-5, div. B, title I, §1251(b), Feb. 17, 2009, 123 Stat. 342, provided that: “The amendment made by this

section [amending this section] shall apply to taxable years beginning after December 31, 2008.”

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105-34 effective as if included in the provisions of the Small Business Job Protection Act of 1996, Pub. L. 104-188, to which it relates, see section 1601(j) of Pub. L. 105-34, set out as a note under section 23 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-514 applicable to taxable years beginning after Dec. 31, 1986, but only in cases where the return for the taxable year is filed pursuant to an S election made after Dec. 31, 1986, and with provision that, in the case of any taxable year of an S corporation which begins after Dec. 31, 1986, and to which the amendments by section 632 (other than subsec. (b) thereof) of Pub. L. 99-514 do not apply, subsec. (b)(1) of this section (as in effect on the date before Oct. 22, 1986) shall apply as if it read as follows: “an amount equal to 34 percent of the amount by which the net capital gain of the corporation for the taxable year exceeds \$25,000, or”, and with other exceptions and transitional rules, see section 633 of Pub. L. 99-514, as amended, set out as an Effective Date note under section 336 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 102(d)(1) of Pub. L. 98-369 applicable to positions established after July 18, 1984, in taxable years ending after that date, except as otherwise provided, see section 102(f), (g) of Pub. L. 98-369 set out as a note under section 1256 of this title.

Amendment by section 474(r)(27) of Pub. L. 98-369 applicable to taxable years beginning after Dec. 31, 1983, and to carrybacks from such years, see section 475(a) of Pub. L. 98-369, set out as a note under section 21 of this title.

Amendment by section 721(u) of Pub. L. 98-369 effective as if included in the Subchapter S Revision Act of 1982, Pub. L. 97-354, see section 721(y)(1) of Pub. L. 98-369, set out as a note under section 1361 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97-448 effective on date of enactment of Subchapter S Revision Act of 1982 [Oct. 19, 1982], see section 311(c)(4) of Pub. L. 97-448, set out as a note under section 1368 of this title.

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.

§ 1375. Tax imposed when passive investment income of corporation having accumulated earnings and profits exceeds 25 percent of gross receipts

(a) General rule

If for the taxable year an S corporation has—