

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—

(1) accumulated earnings and profits at the close of such taxable year, and

(2) gross receipts more than 25 percent of which are passive investment income,

then there is hereby imposed a tax on the income of such corporation for such taxable year. Such tax shall be computed by multiplying the excess net passive income by the highest rate of tax specified in section 11(b).

(b) Definitions

For purposes of this section—

(1) Excess net passive income

(A) In general

Except as provided in subparagraph (B), the term “excess net passive income” means an amount which bears the same ratio to the net passive income for the taxable year as—

(i) the amount by which the passive investment income for the taxable year exceeds 25 percent of the gross receipts for the taxable year, bears to

(ii) the passive investment income for the taxable year.

(B) Limitation

The amount of the excess net passive income for any taxable year shall not exceed the amount of the corporation’s taxable income for such taxable year as determined under section 63(a)—

(i) without regard to the deductions allowed by part VIII of subchapter B (other than the deduction allowed by section 248, relating to organization expenditures), and

(ii) without regard to the deduction under section 172.

(2) Net passive income

The term “net passive income” means—

(A) passive investment income, reduced by

(B) the deductions allowable under this chapter which are directly connected with the production of such income (other than deductions allowable under section 172 and part VIII of subchapter B).

(3) Passive investment income, etc.

The terms “passive investment income” and “gross receipts” have the same respective meanings as when used in paragraph (3) of section 1362(d).

(4) Coordination with section 1374

Notwithstanding paragraph (3), the amount of passive investment income shall be determined by not taking into account any recognized built-in gain or loss of the S corporation for any taxable year in the recognition period. Terms used in the preceding sentence shall have the same respective meanings as when used in section 1374.

(c) Credits not allowable

No credit shall be allowed under part IV of subchapter A of this chapter (other than section 34) against the tax imposed by subsection (a).

(d) Waiver of tax in certain cases

If the S corporation establishes to the satisfaction of the Secretary that—

(1) it determined in good faith that it had no accumulated earnings and profits at the close of a taxable year, and

(2) during a reasonable period of time after it was determined that it did have accumulated earnings and profits at the close of such taxable year such earnings and profits were distributed,

the Secretary may waive the tax imposed by subsection (a) for such taxable year.

(Added Pub. L. 97-354, § 2, Oct. 19, 1982, 96 Stat. 1684; amended Pub. L. 98-369, div. A, title IV, § 474(r)(28), title VII, § 721(v), July 18, 1984, 98 Stat. 844, 971; Pub. L. 99-514, title VI, § 632(c)(3), Oct. 22, 1986, 100 Stat. 2277; Pub. L. 100-647, title I, § 1006(f)(5)(B)-(D), Nov. 10, 1988, 102 Stat. 3406; Pub. L. 104-188, title I, § 1311(b)(2)(A)-(C), Aug. 20, 1996, 110 Stat. 1784; Pub. L. 109-135, title IV, § 412(qq), Dec. 21, 2005, 119 Stat. 2640.)

PRIOR PROVISIONS

A prior section 1375, added Pub. L. 85-866, title I, § 64(a), Sept. 2, 1958, 72 Stat. 1654; amended Pub. L. 88-272, title II, §§ 201(d)(13), 233(b), Feb. 26, 1964, 78 Stat. 32, 112; Pub. L. 89-389, §§ 1(a), (b), 2(b)(4), Apr. 14, 1966, 80 Stat. 111, 114; Pub. L. 91-172, title III, § 301(b)(11), Dec. 30, 1969, 83 Stat. 586; Pub. L. 94-455, title XIX, § 1901(a)(151), (b)(33)(Q), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1788, 1802, 1834; Pub. L. 95-600, title VII, § 703(j)(6), Nov. 6, 1978, 92 Stat. 2941, related to special rules applicable to distributions of electing small business corporations, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

A prior section 1376, added Pub. L. 85-866, title I, § 64(a), Sept. 2, 1958, 72 Stat. 1655, related to adjustment to basis of stock of, and indebtedness owing, shareholders, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

AMENDMENTS

2005—Subsec. (d)(1), (2). Pub. L. 109-135 substituted “accumulated” for “subchapter C”.

1996—Pub. L. 104-188, § 1311(b)(2)(C), substituted “accumulated” for “subchapter C” in section catchline.

Subsec. (a)(1). Pub. L. 104-188, § 1311(b)(2)(A), substituted “accumulated” for “subchapter C”.

Subsec. (b)(3). Pub. L. 104-188, § 1311(b)(2)(B), amended par. (3) generally. Prior to amendment, par. (3) read as follows:

“(3) PASSIVE INVESTMENT INCOME; ETC.—The terms ‘subchapter C earnings and profits’, ‘passive investment income’, and ‘gross receipts’ shall have the same respective meanings as when used in paragraph (3) of section 1362(d).”

1988—Subsec. (b)(1)(B). Pub. L. 100-647, § 1006(f)(5)(B), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: “The amount of the excess net passive income for any taxable year shall not exceed the corporation’s taxable income for the taxable year (determined in accordance with section 1374(d)(4)).”

Subsec. (b)(4). Pub. L. 100-647, § 1006(f)(5)(C), added par. (4).

Subsec. (c). Pub. L. 100-647, § 1006(f)(5)(D), amended subsec. (c) generally, in heading substituting “Credits not allowable” for “Special rules”, and in text substituting “No credit” for “(1) DISALLOWANCE OF CREDIT.—No credit”, and striking out par. (2) which related to coordination with section 1374.

1986—Subsec. (b)(1)(B). Pub. L. 99-514 substituted “section 1374(d)(4)” for “section 1374(d)”.

1984—Subsec. (c)(1). Pub. L. 98-369, § 474(r)(28), substituted “section 34” for “section 39”.

Subsec. (d). Pub. L. 98-369, § 721(v), added subsec. (d).

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by Pub. L. 104-188 applicable to taxable years beginning after Dec. 31, 1996, see section 1317(a) of Pub. L. 104-188, set out as a note under section 641 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, with exceptions and special 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 474(r)(28) 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(v) 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

This section applicable to taxable years beginning after Dec. 31, 1982, except that in the case of a taxable year beginning during 1982, this section and sections 1362(d)(3) and 1366(f)(3) of this title shall apply, and section 1372(e)(5) of this title as in effect on the day before Oct. 19, 1982, shall not apply, see section 6(a), (b)(3) of Pub. L. 97-354, set out as a note under section 1361 of this title.

PART IV—DEFINITIONS; MISCELLANEOUS

Sec.	
1377.	Definitions and special rule.
1378.	Taxable year of S corporation.
1379.	Transitional rules on enactment.

§ 1377. Definitions and special rule

(a) Pro rata share

For purposes of this subchapter—

(1) In general

Except as provided in paragraph (2), each shareholder's pro rata share of any item for any taxable year shall be the sum of the amounts determined with respect to the shareholder—

(A) by assigning an equal portion of such item to each day of the taxable year, and

(B) then by dividing that portion pro rata among the shares outstanding on such day.

(2) Election to terminate year

(A) In general

Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders and the corporation agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

(B) Affected shareholders

For purposes of subparagraph (A), the term "affected shareholders" means the share-

holder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term "affected shareholders" shall include all persons who are shareholders during the taxable year.

(b) Post-termination transition period

(1) In general

For purposes of this subchapter, the term "post-termination transition period" means—

(A) the period beginning on the day after the last day of the corporation's last taxable year as an S corporation and ending on the later of—

(i) the day which is 1 year after such last day, or

(ii) the due date for filing the return for such last year as an S corporation (including extensions),

(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and

(C) the 120-day period beginning on the date of a determination that the corporation's election under section 1362(a) had terminated for a previous taxable year.

(2) Determination defined

For purposes of paragraph (1), the term "determination" means—

(A) a determination as defined in section 1313(a), or

(B) an agreement between the corporation and the Secretary that the corporation failed to qualify as an S corporation.

(3) Special rules for audit related post-termination transition periods

(A) No application to carryovers

Paragraph (1)(B) shall not apply for purposes of section 1366(d)(3).

(B) Limitation on application to distributions

Paragraph (1)(B) shall apply to a distribution described in section 1371(e) only to the extent that the amount of such distribution does not exceed the aggregate increase (if any) in the accumulated adjustments account (within the meaning of section 1368(e)) by reason of the adjustments referred to in such paragraph.

(c) Manner of making elections, etc.

Any election under this subchapter, and any revocation under section 1362(d)(1), shall be made in such manner as the Secretary shall by regulations prescribe.

(Added Pub. L. 97-354, § 2, Oct. 19, 1982, 96 Stat. 1685; amended Pub. L. 104-188, title I, §§ 1306-1307(b), Aug. 20, 1996, 110 Stat. 1780; Pub. L. 108-311, title IV, § 407(a), Oct. 4, 2004, 118 Stat. 1190.)

PRIOR PROVISIONS

A prior section 1377, added Pub. L. 85-866, title I, § 64(a), Sept. 2, 1958, 72 Stat. 1656; amended Pub. L.