

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 shareholder 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. 94-455, title IX, § 902(b)(1), title XIX, § 1901(b)(32)(B)(iv), Oct. 4, 1976, 90 Stat. 1608, 1800, related to special rules applicable to earnings and profits of electing small business corporations, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

AMENDMENTS

- 2004—Subsec. (b)(3). Pub. L. 108-311 added par. (3).
- 1996—Subsec. (a)(2). Pub. L. 104-188, § 1306, reenacted heading without change and amended text generally. Prior to amendment, text read as follows: "Under regulations prescribed by the Secretary, if any shareholder terminates his interest in the corporation during the taxable year and all persons who are shareholders during the taxable year agree to the application of this paragraph, paragraph (1) shall be applied as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination." Subsec. (b)(1)(A) to (C). Pub. L. 104-188, § 1307(a), struck out "and" at end of subpar. (A)(ii), added subpar. (B), and redesignated former subpar. (B) as (C).
- Subsec. (b)(2)(A) to (C). Pub. L. 104-188, § 1307(b), added subpar. (A), redesignated subpar. (C) as (B), and struck out former subpars. (A) and (B) which read as follows:
 - "(A) a court decision which becomes final,
 - "(B) a closing agreement, or".

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-311 effective as if included in the provisions of the Small Business Job Protection

Act of 1996, Pub. L. 104-188, to which such amendment relates, see section 407(c) of Pub. L. 108-311, set out as a note under section 401 of this title.

EFFECTIVE DATE OF 1996 AMENDMENTS

Pub. L. 105-34, title XVI, § 1601(c)(2), Aug. 5, 1997, 111 Stat. 1087, provided that:

“(A) Notwithstanding section 1317 of the Small Business Job Protection Act of 1996 [Pub. L. 104-188, enacting provisions set out as notes under sections 641 and 1362 of this title], the amendments made by subsections (a) and (b) of section 1307 of such Act [amending this section] shall apply to determinations made after December 31, 1996.

“(B) In no event shall the 120-day period referred to in section 1377(b)(1)(B) of the Internal Revenue Code of 1986 (as added by such section 1307) expire before the end of the 120-day period beginning on the date of the enactment of this Act [Aug. 5, 1997].”

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

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.

§ 1378. Taxable year of S corporation

(a) General rule

For purposes of this subtitle, the taxable year of an S corporation shall be a permitted year.

(b) Permitted year defined

For purposes of this section, the term “permitted year” means a taxable year which—

- (1) is a year ending December 31, or
- (2) is any other accounting period for which the corporation establishes a business purpose to the satisfaction of the Secretary.

For purposes of paragraph (2), any deferral of income to shareholders shall not be treated as a business purpose.

(Added Pub. L. 97-354, § 2, Oct. 19, 1982, 96 Stat. 1685; amended Pub. L. 98-369, div. A, title VII, § 721(m), (q), July 18, 1984, 98 Stat. 969, 970; Pub. L. 99-514, title VIII, § 806(b), Oct. 22, 1986, 100 Stat. 2363.)

PRIOR PROVISIONS

A prior section 1378, added Pub. L. 89-389, § 2(a), Apr. 14, 1966, 80 Stat. 113; amended Pub. L. 91-172, title V, § 511(c)(4), Dec. 30, 1969, 83 Stat. 638; Pub. L. 94-455, title XIX, § 1901(a)(152), (b)(33)(R), Oct. 4, 1976, 90 Stat. 1789, 1802, related to tax imposed on certain capital gains, prior to the general revision of this subchapter by section 2 of Pub. L. 97-354.

AMENDMENTS

1986—Subsec. (a). Pub. L. 99-514, § 806(b)(1), amended subsec. (a) generally. Prior to amendment, subsec. (a) read as follows: “For purposes of this subtitle—

“(1) an S corporation shall not change its taxable year to any accounting period other than a permitted year, and

“(2) no corporation may make an election under section 1362(a) for any taxable year unless such taxable year is a permitted year.”

Subsec. (b). Pub. L. 99-514, § 806(b)(2), inserted at end “For purposes of paragraph (2), any deferral of income to shareholders shall not be treated as a business purpose.”

Subsec. (c). Pub. L. 99-514, § 806(b)(3), struck out subsec. (c) which required existing S corporations to use permitted year after 50-percent shift in ownership.

1984—Subsec. (c)(1). Pub. L. 98-369, § 721(m), substituted “which includes December 31, 1982 (or which is an S corporation for a taxable year beginning during 1983 by reason of an election made on or before October 19, 1982)” for “which includes December 31, 1982”.

Subsec. (c)(3)(B)(i). Pub. L. 98-369, § 721(q), substituted “who (or whose estate) held” for “who held”.

EFFECTIVE DATE OF 1986 AMENDMENT

Pub. L. 99-514, title VIII, § 806(e), Oct. 22, 1986, 100 Stat. 2364, as amended by Pub. L. 100-647, title I, § 1008(e)(7), (8), (10), Nov. 10, 1988, 102 Stat. 3441, provided that:

“(1) IN GENERAL.—The amendments made by this section [amending this section and sections 267, 441, and 706 of this title] shall apply to taxable years beginning after December 31, 1986.

“(2) CHANGE IN ACCOUNTING PERIOD.—In the case of any partnership, S corporation, or personal service corporation required by the amendments made by this section to change its accounting period for the taxpayer’s first taxable year beginning after December 31, 1986—

“(A) such change shall be treated as initiated by the partnership, S corporation, or personal service corporation,

“(B) such change shall be treated as having been made with the consent of the Secretary, and

“(C) with respect to any partner or shareholder of an S corporation which is required to include the items from more than 1 taxable year of the partnership or S corporation in any 1 taxable year, income in excess of expenses of such partnership or corporation for the short taxable year required by such amendments shall be taken into account ratably in each of the first 4 taxable years beginning after December 31, 1986, unless such partner or shareholder elects to include all such income in the the [sic] partner’s or shareholder’s taxable year with or within which the partnership’s or S corporation’s short taxable year ends.

Subparagraph (C) shall apply to a shareholder of an S corporation only if such corporation was an S corporation for a taxable year beginning in 1986.

“(3) BASIS, ETC. RULES—

“(A) BASIS RULE.—The adjusted basis of any partner’s interest in a partnership or shareholder’s stock in an S corporation shall be determined as if all of the income to be taken into account ratably in the 4 taxable years referred to in paragraph (2)(C) were included in gross income for the 1st of such taxable years.

“(B) TREATMENT OF DISPOSITIONS.—If any interest in a partnership or stock in an S corporation is disposed of before the last taxable year in the spread period, all amounts which would be included in the gross income of the partner or shareholder for subsequent taxable years in the spread period under paragraph (2)(C) and attributable to the interest or stock disposed of shall be included in gross income for the taxable year in which the disposition occurs. For purposes of the preceding sentence, the term ‘spread period’ means the period consisting of the 4 taxable years referred to in paragraph (2)(C).”

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98-369 effective as if included in 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

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.

CONSTRUCTION OF SECTION 806 OF PUB. L. 99-514

Pub. L. 100-647, title I, § 1008(e)(9), Nov. 10, 1988, 102 Stat. 3441, provided that: “Nothing in section 806 of the Reform Act [Pub. L. 99-514, amending this section and