

106TH CONGRESS  
1ST SESSION

# S. 1904

To amend the Internal Revenue Code of 1986 to provide for an election for special tax treatment of certain S corporation conversions.

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IN THE SENATE OF THE UNITED STATES

NOVEMBER 10, 1999

Mr. THOMAS (for himself and Mr. ENZI) introduced the following bill; which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to provide for an election for special tax treatment of certain S corporation conversions.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. ELECTION FOR SPECIAL TAX TREATMENT OF**  
4       **CERTAIN S CORPORATION CONVERSIONS.**

5       (a) IN GENERAL.—A qualified electing S corporation  
6       may elect the special tax treatment provided in subsection  
7       (b) for an eligible corporate conversion in the manner set  
8       forth in subsection (e).

9       (b) SPECIAL TAX TREATMENT.—

1           (1) TRANSFERS TO PARTNERSHIP.—In the case  
 2           of transfers by a qualified electing S corporation to  
 3           a partnership in connection with an eligible cor-  
 4           porate conversion, no gain or loss shall be recognized  
 5           by shareholders of such corporation with respect to  
 6           money or property received by the partnership.

7           (2) OTHER TRANSFERS.—All other distribu-  
 8           tions of money or property by the qualified electing  
 9           S corporation shall be treated as a distribution in  
 10          part or full payment in exchange for the stock of  
 11          such corporation.

12          (c) QUALIFIED ELECTING S CORPORATION.—For  
 13          purposes of this section, the term “qualified electing S cor-  
 14          poration” means a domestic corporation which—

15                 (A) has had a valid S election continuously  
 16                 in effect for all taxable years of the corporation  
 17                 beginning on or after January 1, 1990, and

18                 (B) has never made an election under this  
 19                 section.

20          (d) ELIGIBLE CORPORATE CONVERSION.—For pur-  
 21          poses of this section—

22                 (1) IN GENERAL.—The term “eligible corporate  
 23                 conversion” means (however effected)—

24                         (A) a transfer by a qualified electing S cor-  
 25                         poration of substantially all of its assets to a

partnership (as defined in section 7701(a)(2) of the Internal Revenue Code of 1986) for not less than 80 percent of the capital and profits of the partnership in any taxable year of the corporation ending on or before December 31, 2005,

(B) the meeting of the requirement described in paragraph (2) by the partnership, and

(C) the subsequent liquidation and dissolution of the qualified S corporation within the same taxable year as the transfer.

(2) CONTINUITY OF BUSINESS REQUIREMENT.—

(A) IN GENERAL.—The requirement described in this paragraph is met if the partnership described in paragraph (1)(A) either—

(i) maintains the continuity of the qualified electing S corporation's business for 5 consecutive taxable years following the year in which the corporate conversion occurs, or

(ii) pays a corporate conversion recapture tax in the taxable year in which the failure to maintain such continuity first occurs.

1 (B) CONTINUITY OF THE QUALIFIED  
2 ELECTING S CORPORATION'S BUSINESS.—For  
3 purposes of subparagraph (A)(i), the term  
4 “continuity of the qualified electing S corpora-  
5 tion's business” means, under all the facts and  
6 circumstances, either—

7 (i) the continuation of 1 or more of  
8 the S corporation's historic lines of busi-  
9 ness, or

10 (ii) the use of a significant portion of  
11 the S corporation's historic business assets,  
12 whether or not such assets have a taxable  
13 basis, in the conduct of an active trade or  
14 business.

15 (C) CORPORATE CONVERSION RECAPTURE  
16 TAX.—For purposes of subparagraph (A)(ii),  
17 the term “corporate conversion recapture tax”  
18 means—

19 (i) a recomputation of the tax under  
20 subtitle A of the Internal Revenue Code of  
21 1986 of the partnership and the partners  
22 as if—

23 (I) the partnership were an S  
24 corporation,

1 (II) the stock of such S corpora-  
 2 tion was owned in the same manner  
 3 as the capital of the partnership, and

4 (III) the S corporation were dis-  
 5 solved and its assets distributed to its  
 6 shareholders in complete liquidation  
 7 on the last day of the taxable year,  
 8 multiplied by

9 (ii) a fraction—

10 (I) the numerator of which is the  
 11 excess (if any) of 5 over the number  
 12 of complete taxable years in which the  
 13 partnership maintains continuity of  
 14 the qualified electing S corporation's  
 15 business, and

16 (II) the denominator of which is  
 17 5.

18 (d) BASIS RULES.—In the case of an eligible cor-  
 19 porate conversion, property in the hands of the partner-  
 20 ship shall have the same basis as in the hands of the quali-  
 21 fied electing S corporation immediately prior to the eligible  
 22 corporate conversion.

23 (e) METHOD OF MAKING ELECTION.—In order to  
 24 elect the special tax treatment provided in subsection (b)  
 25 for an eligible corporate conversion, the qualified electing

1 S corporation shall file a written election claiming such  
2 treatment with the timely-filed information return of the  
3 S corporation for the taxable year in which the eligible  
4 corporate conversion occurs.

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