



# TaxNewsFlash

United States



No. 2022-310  
October 11, 2022

## Rev. Proc. 2022-19: Taxpayer assistance procedures for S corporations under section 1362(f)

The IRS released an advance version of [Rev. Proc. 2022-19](#) [PDF 871 KB], which describes procedures that allow S corporations and their shareholders to resolve frequently encountered issues with certainty and often without requesting a private letter ruling (PLR).

The issues addressed by the revenue procedure are those that the IRS historically has identified as not affecting the validity or continuation of a corporation's election under section 1362(a) to be treated as an S corporation (S election) or under section 1361(b)(3)(B)(ii) to treat its subsidiary as a qualified subchapter S subsidiary (a QSub). The revenue procedure also provides areas in which the IRS will not rule, or will not ordinarily rule, regarding the validity or continuation of an S election or a QSub election.

One of the more significant elements of the revenue procedure is the description of certain situations in which taxpayers may retroactively validate or preserve an S election invalidated or terminated solely as the result of one or more "non-identical governing provisions" that for federal income tax purposes results in the S corporation having more than one class of stock under section 1.1361-1(l)(1) (even if the S corporation never made a non-pro rata distribution or liquidating distribution).

Generally, a small business corporation is eligible for retroactive corrective relief under the revenue procedure if all of the following requirements are met:

- The corporation has (or had) one or more non-identical governing provisions
- The corporation has not made, and for federal income tax purposes is not deemed to have made, a disproportionate distribution to an applicable shareholder. For purposes of the revenue procedure, "disproportionate distribution" is defined as any distribution (including an actual distribution, a constructive distribution, or a deemed distribution) of property by a corporation with respect to shares of its stock that differs in timing or amount from the distribution with respect to any other shares of its stock.

**KPMG observation:** Disproportionate distributions by a corporation generally do not constitute a second class of stock so long as the corporation's governing provisions provide for identical distribution and liquidation rights. However, in order to meet the requirements for relief under this revenue procedure—

when the governing provisions are, by definition, not identical—presumably all distributions must be identical as to timing and amount.

- The corporation timely filed a return on Form 1120-S (as required under section 6037 of the Code and section 1.6037-1 of the Income Tax Regulations) for each taxable year of the corporation beginning with the taxable year in which the first non-identical governing provision was adopted and through the taxable year immediately preceding the taxable year in which the corporation made a request for corrective relief under the revenue procedure (a corporation is treated as having timely filed a required Form 1120-S for purposes of the revenue procedure if the Form 1120-S is filed within six months after its original due date, excluding extensions); and
- Before any non-identical governing provision is discovered by the IRS, all of the requirements described in the revenue procedure are satisfied.

If a corporation satisfies the requirements for relief under this provision, the IRS generally will not issue a PLR relating to the validity of the corporation's S election.

The revenue procedure also identifies the following issues for which a PLR will not be available or will not ordinarily be issued either because IRS does not believe there is an existing concern with the validity of the entity's S election (or QSub election) (and perhaps the issuance of the PLR would simply comprise a "comfort ruling") or because there are other avenues to address the matter outside of the PLR process:

- Rulings that require a determination of the existence of a principal purpose is to circumvent the one class of stock requirement or the limitation on eligible shareholders.
- Rulings regarding the termination of S corporation status because of a disproportionate distribution made by a corporation so long as the governing provisions of the corporation provide for identical distribution and liquidation rights.

**KPMG observation:** A question may remain as to the type of arrangement that may constitute a governing provision. For example, could a long-standing pattern of behavior in making disproportionate distributions amount to a governing provision?

- Rulings as to whether a missing administrative letter relating to the IRS's acceptance of an election affect the validity of that election.
- Rulings relating to the validity or continuation of an S corporation election when the corporation has filed a federal income tax return that is inconsistent with the corporation's status as an S corporation or a QSub.
- Rulings regarding the validation of an S election (or QSub election) solely because of certain errors or omissions on the election form.

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