# Current Federal Tax Developments

Week of October 10, 2022

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CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF OCTOBER 10, 2022
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# Current Federal Tax Developments

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# SECTION: 164
# AICPA MAKES ADDITIONAL RECOMMENDATIONS TO IRS ON PASSTHROUGH ENTITY TAX GUIDANCE

## Citation: AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Loc

The AICPA Tax Executive Committee has released another letter[1] to the IRS regarding additional guidance needed for the state passthrough entity taxes beyond what was provided in Notice 2020-75.[2]

The AICPA summarizes their requests in this letter as follows:

> We recommend:
>
> 1. The SITP liability is deductible in accordance with the partnership or S corporation's method of accounting.
>
> 2. The SITP liability is a specifically identified tax and accordingly, a taxpayer should be entitled to adopt the recurring item exception method of accounting with respect to the liability.
>
> 3. An entity that is unable to make an entity level election until a year subsequent to the taxable year of imposition should be allowed to make a Federal election to deduct the tax in the taxable year of imposition or the following year (similar to the treatment of plan contributions made on account of a tax year but after the year they relate to under section 404(a)(6)).[3]

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[1] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[2] Notice 2020-75, November 9, 2020, https://www.irs.gov/pub/irs-drop/n-20-75.pdf (retrieved October 7, 2022)

[3] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

### *Deduction and Taxpayer's Method of Accounting*

The AICPA first deals with the issue created by the implication in Notice 2020-75 that the passthrough tax must be paid by the taxpayer's year end to obtain a deduction.

> The language in Section 3.02(3) of the Notice causes confusion amongst taxpayers and tax practitioners as the Notice indicates a SITP is deductible for the taxable year in which the payment is made. In response to a previously issued Treasury Regulation intended to address state and local government programs intended as workarounds to the Federal $10,000 state and local deduction cap, taxpayers and advisors are closely hewing to following the four corners of the Notice.
>
> The Notice does not make mention of an entity's method of accounting controlling the timing of the deduction and only references payment, leading many to question whether the deduction is to be taken on a cash basis method of accounting. However, to be a SITP the tax must be an income tax and must be directly imposed by the state (or other domestic jurisdiction) on the partnership or S corporation.[4]

The AICPA recommends:

> The AICPA recommends that Treasury and the IRS issue guidance that the deduction for a SITP is deductible in accordance with the passthrough entity's established method of accounting.[5]

After discussing the overall rules for accrual methods, the AICPA concludes:

> All told, the basis for the deduction to be claimed in accordance with the taxpayer's method of accounting and that the PTET liability is an eligible recurring item exception item is sound. Taxpayers though, in an abundance of caution, would appreciate guidance from the IRS affirmatively stating so.[6]

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[4] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[5] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[6] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

### *Recurring Item Exception*

The AICPA also makes a case that taxpayers should be allowed to use the recurring item exception for state passthrough entity taxes:

> The recurring item exception must be consistently applied to a type of item, or for all items, from one taxable year to the next to clearly reflect income. In other words, the recurring item exception is a method of accounting and as such, if a taxpayer is not on a recurring item exception method for a type of item, it must request consent of the IRS to change its method of accounting.
>
> A passthrough entity may have an established method of accounting for other taxes, such as state income, franchise, or real property taxes. However, as 29 states now have entity level tax regimes, the state income tax liability may take on more significance. In the interest of administrative benefit for both taxpayers and the IRS, the IRS should state that a SITP liability is a separate item for purposes of the ability to adopt the recurring item exception method of accounting.[7]

The AICPA recommends:

> The SITP liability is a specifically identified separate tax and, accordingly, a taxpayer should be entitled to adopt the recurring item exception method of accounting with respect to the liability.
>
> Alternatively, if the IRS disagrees that the SITP is a separate item from state income taxes, the IRS should plainly state this determination and provide an eligibility restriction waiver for a prior five-year change for the timing of incurring liabilities for state income taxes to allow taxpayers to adjust any methods of accounting for these liabilities.[8]

The AICPA provides the following analysis in support of this recommendation:

> Treasury Reg. § 1.461-5(d)(1) provides that a taxpayer is permitted to adopt the recurring item exception as part of its method of accounting for any type of item for the first taxable year in which that type of item is incurred. In addition, the recurring item exception must be

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[7] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[8] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

> consistently applied with respect to a type of item, or for all items, from one taxable year to the next in order to clearly reflect income.
>
> As the Treasury and IRS are aware, the SITP is for a tax directly imposed upon an entity without regard to whether the imposition of and liability for the income tax is the result of an election by the entity. While the item is a state income tax, the separate definition of a SITP by the IRS recognizes this tax as a separate item from a general state income tax.[9]

## *Ability to Choose Year When Election Made After Year End*

The AICPA notes that the fact that many states don't allow an election to be made until after year end creates concerns about the year of deduction:

> As noted, section 3.02(2) of the Notice states SITPs are deductible when paid. However, section 3.02(1) of the Notice defines SITPs as amounts paid to satisfy a liability for income taxes. There is confusion among practitioners about whether a taxpayer would have a liability for income taxes in the current taxable year for an elective PTE tax where the election is made after the end of the current taxable year, especially in states where the statute does not permit an election to be made any earlier than the following taxable year. Some practitioners have been advising taxpayers to enter into a binding agreement directing the passthrough entity to make an election to pay PTE tax in order to claim a deduction in the current taxable year. In the interest of administrative benefit, the IRS should allow taxpayers to make a binding election on its timely filed tax return to claim a current year deduction for SITP arising from any PTE tax imposed on current year taxable income.[10]

The AICPA recommendation is:

> The AICPA recommends that with respect to elective SITP regimes, the IRS allow taxpayers to treat the SITP as a liability for the year in which the tax is imposed (meaning a fixed liability in the case of an accrual method taxpayer and an otherwise deductible liability in the case of a cash basis taxpayer) in situations where the state does not

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[9] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[10] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

> provide a mechanism or procedure for taxpayers to elect into the PTET prior to the end of the tax year for which the tax is imposed.[11]

The AICPA describes the problem as follows:

> In situations where a state revenue authority lacks a formal procedure for a taxpayer to make an election to pay PTE tax on current year taxable income until the following year, there is uncertainty whether the all events test is met during the current taxable year. Generally, practitioners have interpreted the all events tests as denying a SITP deduction of an elective PTE tax where an affirmative election to pay PTE tax is not made on or before the end of the taxable year. However, other practitioners have suggested the fact of the liability is fixed as of the end of the year since by statute income tax is assessed on any taxable income earned by a passthrough entity as of the end of the taxable year. A PTE tax election only acts to shift the liability from the individual owners or partners to the entity itself rather than establish that a liability exists.
>
> As a work around when an election to pay PTE tax is unavailable on or before the end of the taxable year, some practitioners have been advising taxpayers to put in place binding agreements before the end of the taxable year mandating the passthrough entity make the election in the following taxable year. However, even with such an agreement in place, there is still uncertainty for taxpayers whether the IRS will respect the substance of such an agreement or what specific information would have to be included in such an agreement to avoid a challenge by the IRS. This process also places an administrative burden on taxpayers to draft such agreements, especially for smaller taxpayers who may be lacking counsel, and on the IRS to review such agreements upon examination for completeness.[12]

The letter goes on to justify the recommendation:

> PTE taxes are put in place by states to change the state tax treatment of individual owners and partners in certain passthrough entities. By issuing the Notice and treating PTE taxes as a deductible expense for Federal income tax purposes, Treasury has signaled its apparent agreement that changes to state tax laws that shift the state tax liability from the individual to the passthrough entity removes such tax from

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[11] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[12] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

> the limitation on individual SALT deductions. From a policy perspective, there seems little reason to deny similar treatment to individuals who are owners or partners in passthrough entities which conduct business in states where the taxpayer is certain of paying PTET but is only prevented from making an affirmative election to pay PTE tax during the taxable year by state statute.
>
> Therefore, for the sake of eliminating uncertainty and reducing administrative burden on both taxpayers and the IRS, the IRS should allow a passthrough entity to make a binding election on its timely filed tax return to treat any PTE tax imposed on current year taxable income as fixing a liability to pay PTE tax as of the end of the that taxable year regardless of when an actual election is allowed by the state revenue authority, and any payment of such PTE tax to be treated as a deductible SITP in the year paid.[13]

# SECTION: 401
# IRS DELAYS INITIAL EFFECTIVE DATE OF RMD PROPOSED REGULATIONS, GRANTS RELIEF FOR CERTAIN 2021 AND 2022 PAYMENTS

## Citation: Notice 2022-53, 10/7/22

The IRS in Notice 2022-53[14] has announced that the agency will not impose penalties on failures to take *specified RMDs* for 2021 and 2022 that were required under provisions of proposed regulations issued to deal with changes in required minimum distributions (RMDs) under the SECURE Act passed in late 2019.

The notice described the provisions of the proposed regulations as follows:

> In order to satisfy section 401(a)(9)(B)(i), the beneficiary of an employee who died after the employee's required beginning date must take an annual required minimum distribution beginning in the first calendar year after the calendar year of the employee's death. In order to satisfy section 401(a)(9)(B)(ii), the remaining account balance must be distributed by the 10th calendar year after the calendar year of the employee's death (subject to an exception under section 401(a)(9)(B)(iii), if applicable). In order to satisfy both of those requirements, the proposed regulations generally provide that, in the case of an employee who dies after the employee's required beginning

[13] AICPA Tax Executive Committee Letter, "RE: Additional Guidance Needed on Section 461 Accrual Basis Taxpayers and Notice 2020-75, Forthcoming Regulations Regarding the Deductibility of Payments by Partnerships and S Corporations for Certain State and Local Income Taxes," October 4, 2022

[14] Notice 2022-53, October 7, 2022, https://www.irs.gov/pub/irs-drop/n-22-53.pdf (retrieved October 7, 2022)

> date with a designated beneficiary who is not an eligible designated beneficiary (and for whom the section 401(a)(9)(B)(iii) alternative to the 10-year rule is not applicable), annual RMDs must continue to be taken after the death of the employee, with a full distribution required by the end of the 10th calendar year following the calendar year of the employee's death.
>
> In accordance with section 401(a)(9)(B)(iii), in the case of a designated beneficiary who is an eligible designated beneficiary, the proposed regulations include an alternative to the 10-year rule under which annual lifetime or life expectancy payments are made to the beneficiary beginning in the year following the year of the employee's death. Under the proposed regulations, if an eligible designated beneficiary of an employee is using the lifetime or life expectancy payment alternative to the 10- year rule, then the eligible designated beneficiary (and, after the death of the eligible designated beneficiary, the beneficiary of the eligible designated beneficiary) must continue to take annual distributions after the death of the employee (with a full distribution made no later than the 10th year after the year of the eligible designated beneficiary's death). The proposed regulations provide for similar treatment (that is, continued annual RMDs with a requirement to take a full distribution no later than the 10th year after a specified event) in the case of a designated beneficiary who is a minor child of the employee (with the specified event being the child's reaching the age of majority).[15]

The IRS noted that a number of commentators indicated that they had not interpreted the law in this fashion and, for that reason, many individuals who inherited accounts from decedents in pay status had not taken such distributions in 2021. As the IRS did not release the proposed regulations until February 24, 2022, it was too late to timely take any such required distribution for 2021:

> During that period, some individuals who are owners of inherited IRAs or are beneficiaries under qualified defined contribution plans or section 403(b) plans submitted comments indicating that they thought the new 10-year rule would apply differently than what was proposed in the proposed regulations. Specifically, commenters believed that, regardless of when an employee died, the 10-year rule would operate like the 5-year rule, under which there would not be any RMD due for a calendar year until the last year of the 5- or 10-year period following the specified event (the death of the employee, the death of the eligible designated beneficiary, or the attainment of the age of majority for the employee's child who is an eligible designated beneficiary). Commenters in those situations who are heirs or beneficiaries of

[15] Notice 2022-53, October 7, 2022

> individuals who died in 2020 explained that they did not take an RMD in 2021 and are unsure of whether they would be required to take an RMD in 2022. Commenters asserted that, if final regulations adopt the interpretation of the 10-year rule set forth in the proposed regulations, the Treasury Department and the IRS should provide transition relief for failure to take distributions that are RMDs due in 2021 or 2022 pursuant to section 401(a)(9)(H) in the case of the death of an employee (or designated beneficiary) in 2020 or 2021.[16]

## *Delayed Application of the Provision*

In the Notice, the IRS announced that the provisions in the regulations will apply no earlier than 2023:

> Final regulations regarding RMDs under section 401(a)(9) of the Code and related provisions will apply no earlier than the 2023 distribution calendar year.[17]

## *Relief from the Consequences of Failing to Make or Take an RMD*

Per the title of Section IV of the Notice, the guidance covers "Certain RMDs for 2021 and 2022."[18]

The notice first provides relief to defined contribution retirement plans that did not make a *specified RMD*:

> A defined contribution plan that failed to make a specified RMD (as defined in Section IV.C of this notice) will not be treated as having failed to satisfy section 401(a)(9) merely because it did not make that distribution.[19]

For individuals who failed to take a *specified RMD* the following relief is provided:

> To the extent a taxpayer did not take a specified RMD (as defined in Section IV.C of this notice), the IRS will not assert that an excise tax is due under section 4974. If a taxpayer has already paid an excise tax for a missed RMD in 2021 that constitutes a specified RMD, that taxpayer may request a refund of that excise tax.[20]

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[16] Notice 2022-53, October 7, 2022

[17] Notice 2022-53, October 7, 2022

[18] Notice 2022-53, October 7, 2022

[19] Notice 2022-53, October 7, 2022

[20] Notice 2022-53, October 7, 2022

The Notice defines a *specified RMD* as follows:

> For purposes of this notice only, a specified RMD is any distribution that, under the interpretation included in the proposed regulations, would be required to be made pursuant to section 401(a)(9) in 2021 or 2022 under a defined contribution plan or IRA that is subject to the rules of 401(a)(9)(H) for the year in which the employee (or designated beneficiary) died if that payment would be required to be made to:
>
> - a designated beneficiary of an employee under the plan (or IRA owner) if: (1) the employee (or IRA owner) died in 2020 or 2021 and on or after the employee's (or IRA owner's) required beginning date, and (2) the designated beneficiary is not taking lifetime or life expectancy payments pursuant to section 401(a)(9)(B)(iii); or
>
> - a beneficiary of an eligible designated beneficiary (including a designated beneficiary who is treated as an eligible designated beneficiary pursuant to section 401(b)(5) of the SECURE Act) if: (1) the eligible designated beneficiary died in 2020 or 2021, and (2) that eligible designated beneficiary was taking lifetime or life expectancy payments pursuant to section 401(a)(9)(B)(iii) of the Code.[21]

# SECTION: 1362
# IRS PROVIDES RELIEF PROCEDURES FOR S ELECTIONS, ALSO PROVIDES WILL NOT ISSUE PRIVATE LETTERING RULINGS GENERALLY IN AREAS COVERED BY THE RELIEF

## Citation: Revenue Procedure 2022-19, 10/11/19

In Revenue Procedure 2022-19[22] the IRS has issued a series of "taxpayer assistance procedures" to resolve certain issues involving S corporations and their shareholders without requiring the issuance of a private letter ruling (PLR).

The areas covered by this guidance are:

- Agreements and Arrangements with No Principal Purpose to Circumvent One Class of Stock Requirement

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[21] Notice 2022-53, October 7, 2022

[22] Revenue Procedure 2022-19, October 11, 2022, https://www.taxnotes.com/research/federal/irs-guidance/revenue-procedures/letter-rulings-not-needed-for-some-s-corp-election-requests/7f7bl (retrieved October 8, 2022)

- Governing Provisions That Provide for Identical Distribution and Liquidation Rights
- Procedures for Addressing Missing Shareholder Consents, Errors with Regard to a Permitted Year, Missing Officer's Signature, and Other Inadvertent Errors and Omissions
- Procedures for Verifying S Elections or QSub Elections
- Procedures for Addressing a Federal Income Tax Return Filing Inconsistent with an S Election or a QSub Election
- Procedures for Retroactively Correcting One or More Non-Identical Governing Provisions[23]

### *Details of the Six Areas*

The procedure provides:

> Sections 2.03(1) through 2.03(6) of this revenue procedure describe the six areas for which issues are resolvable without a PLR, and for which this revenue procedure provides taxpayer assistance procedures. With regard to the sixth area described in 2.03(6) of this revenue procedure (addressing potential retroactive correction of non-identical governing provisions), the validity or continuation of a corporation's S election is not affected in certain circumstances only if the corporation and its applicable shareholders (as defined in section 3.06(1)(a) of this revenue procedure) meet the requirements of section 3.06 of this revenue procedure.[24]

### *Agreements and Arrangements with No Principal Purpose to Circumvent One Class of Stock Requirement.*

The Procedure describes the background for the first area of relief as follows:

> **(1) One class of stock requirement and governing provisions, including "principal purpose" conditions.**
>
> **(a) Overview.** Pursuant to § 1361(b) (1)(D) and § 1.1361-1(l)(1), a corporation that has more than one class of stock does not qualify as a small business corporation. Section 1.1361-1(l)(1) provides generally that a corporation is treated as having only one class of stock if all

[23] Revenue Procedure 2022-19, October 11, 2022

[24] Revenue Procedure 2022-19, SECTION 2.03, October 11, 2022

outstanding shares of stock confer identical rights to distribution and liquidation proceeds.

**(b) Governing provisions.** Section 1.1361-1(l)(2)(i) provides that the determination of whether all outstanding shares of stock confer identical rights to distribution and liquidation proceeds is made based on the corporate charter, articles of incorporation, bylaws, applicable State law, and binding agreements relating to distribution and liquidation proceeds (collectively, governing provisions). A commercial contractual agreement is not a binding agreement relating to distribution and liquidation proceeds, and therefore is not a governing provision, unless a principal purpose of the agreement is to circumvent the one class of stock requirement. See § 1.1361-1(l)(2)(i).

**(c) Other agreements and arrangements**. The Income Tax Regulations identify a number of other agreements and arrangements between or among an S corporation and its shareholders that may or may not be treated as second classes of stock depending in part on whether a principal purpose of the agreement or arrangement was to circumvent the one class of stock requirement or otherwise alter shareholders' rights to distribution and liquidation proceeds. See § 1.1361-1(l)(2)(iii)(A) (buy-sell agreements among shareholders, agreements restricting the transferability of stock, and redemption agreements), § 1.1361-1(l)(4)(ii)(A) (special rules for instruments, obligations, or arrangements treated as equity under general principles of Federal tax law), § 1.1361-1(l)(4)(ii)(B)(1) (short-term unwritten advances that fail the safe harbor described in § 1.1361-1(l)(4)(ii)(B)(1)), and § 1.1361-1(l)(4)(ii)(B)(2) (obligations of the same class that are considered equity under general principles of Federal tax law but fail the safe harbor described in § 1.1361-1(l)(4)(ii)(B)(2)). See section 3.01 of this revenue procedure (providing that the IRS will not treat taxpayers who have entered into the agreements or arrangements described in this section 2.03(1)(c) as violating the one class of stock requirement of § 1361(b)(1)(D) so long as there was no principal purpose to use the agreement or arrangement as a means to circumvent the one class of stock requirement).[25]

The procedure provides the following relief regarding agreements and arrangements that had no principal purpose of circumventing the one class of stock requirement:

**.01 Agreements and Arrangements with No Principal Purpose to Circumvent One Class of Stock Requirement.** Certain agreements and arrangements described in section 2.03(1)(c) of this revenue procedure are not governing provisions and are not treated as second

[25] Revenue Procedure 2022-19, SECTION 2.03(1), October 11, 2022

> classes of stock so long as there was no principal purpose to use the agreement as a means to circumvent the one class of stock requirement. Accordingly, the IRS will not treat an S corporation as violating the one class of stock requirement of § 1361(b)(1)(D) as a result of an agreement or arrangement identified in section 2.03(1)(c) of this revenue procedure that does not have a principal purpose to circumvent the one class of stock requirement. Because entering into these specific agreements in these circumstances will not result in termination of S corporation status, taxpayers do not need to seek relief from the IRS. For this reason, and because the existence of a principal purpose is inherently factual in nature, the IRS will not rule in these situations. See section 4.01(1) of this revenue procedure.[26]

Essentially, the IRS has indicated that the agency will not issue a PLR with regard to such an arrangement if the principal purpose of the arrangement is not to evade the one class of stock rules *and* the procedure specifically provides the IRS will not issue a PLR on whether an arrangement has such a principal purpose:

> **(1) Principal purpose determinations regarding the one class of stock requirement**. The IRS will not issue a PLR under § 1362(f) addressing the validity or continuation of an S election in situations regarding the one class of stock requirement that require a determination of the existence of a principal purpose because such a determination is inherently factual in nature. See section 6.02 of Rev. Proc. 2022-1 (or any successor revenue procedure). Accordingly, the IRS will not issue a PLR under § 1362(f) addressing:
>
> > (a) For purposes of determining whether all outstanding shares of stock confer identical rights to distribution and liquidation proceeds under § 1.1361-1(l)(2), whether a principal purpose of a commercial contractual agreement, buy-sell agreement, an agreement restricting the transferability of stock, or a redemption agreement is to circumvent the one class of stock requirement of § 1361(b)(1)(D) and § 1.1361-1(l) (see § 1.1361-1(l)(2)(i) and (iii)(A)(1)); or
> >
> > (b) For purposes of determining whether an instrument, obligation, or arrangement is treated as a second class of stock, whether:
> >
> > > (i) A principal purpose of issuing or entering into an instrument, obligation, or arrangement is to circumvent the rights to distribution or liquidation proceeds conferred by the outstanding shares of stock

[26] Revenue Procedure 2022-19, SECTION 3.01, October 11, 2022

> or to circumvent the limitation on eligible shareholders contained in § 1.1361-1(b)(1) (see § 1.1361-1(l)(4)(ii)(A)(2)); or
>
> (ii) A principal purpose of an unwritten advance or proportionately held obligation is to circumvent the rights of the outstanding shares of stock or the limitation on eligible shareholders under § 1.1361-1(l)(4)(ii)(A)(2) (see § 1.1361-1(l)(4)(ii)(B)).[27]

### *Governing Provisions That Provide for Identical Distribution and Liquidation Rights*

The second area deemed resolvable without obtaining a private letter ruling relates to disproportionate distributions:

> **(2) Disproportionate distributions.** A "disproportionate distribution" is 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. See § 1.1361-1(l)(1) and (2). Section 1.1361-1(l)(2)(i) provides that, "[a]lthough a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical distribution and liquidation rights, any distributions (including actual, constructive, or deemed distributions) that differ in timing or amount are to be given appropriate tax effect in accordance with the facts and circumstances." Despite this regulation providing that "a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical distribution and liquidation rights," taxpayers and practitioners have indicated concern with the language of § 1.1361-1(l)(2)(i). The articulated concern is that the word "although" in combination with the subsequent language requiring that certain disproportionate distributions "be given appropriate tax effect" creates uncertainty as to whether an S corporation has created a second class of stock — even though the governing provisions provide identical distribution and liquidation rights with respect to each share. Practitioners suggest that the language in § 1.1361-1(l)(2)(i) could be clarified by removing the word "[a]lthough" and point to inconsistency in PLRs in the treatment of disproportionate distributions. See section 3.02 of this revenue procedure (providing that the IRS will not treat any disproportionate

[27] Revenue Procedure 2022-19, SECTION 4.01(1), October 11, 2022

> distributions by a corporation as violating the one class of stock requirement of § 1361(b)(1)(D) so long as the corporation's governing provisions provide for identical distribution and liquidation rights).[28]

In this case the IRS provides for the following relief and also adds this item as one on which the agency will not issue a private letter ruling:

> **.02 Governing Provisions That Provide for Identical Distribution and Liquidation Rights.** As outlined in section 2.03(2) of this revenue procedure, § 1.1361-1(l)(2)(i) provides that a corporation is not treated as having more than one class of stock so long as the governing provisions provide for identical distribution and liquidation rights. Accordingly, the IRS will not treat any disproportionate distributions made by a corporation as violating the one class of stock requirement of § 1361(b)(1)(D) so long as the governing provisions of the corporation provide for identical distribution and liquidation rights. Because disproportionate distributions made in these circumstances will not result in the termination of S corporation status, taxpayers do not need to seek relief from the IRS and the IRS will not rule in these situations. See section 4.01(2)(a) of this revenue procedure.[29]

## *Procedures for Addressing Missing Shareholder Consents, Errors with Regard to a Permitted Year, Missing Officer's Signature, and Other Inadvertent Errors and Omissions*

The next section governs inadvertent errors or omissions on the Form 2553 or Form 8869:

> **(3) Certain inadvertent errors or omissions on Form 2553 or Form 8869**. An inadvertent error or omission on Form 2553 or Form 8869 does not invalidate an S election or a QSub election, unless the error or omission is with respect to a shareholder consent, a selection of a permitted year (as defined in § 1378(b) and § 1.1378-1(b)), or an officer's signature. See generally § 1362(a)(2) (an S election is valid "only if all persons who are shareholders in such corporation on the day on which such election is made consent to such election"), § 1.1378-1 (requiring that the taxable year of an S corporation must be a permitted year, which is defined to include a calendar year or any other taxable year for which the corporation establishes a business purpose to the satisfaction of the Commissioner), and § 1.1361-3(a)(2) (a QSub election form must be signed by a person authorized to sign the S corporation's return). See section 3.03 of this revenue procedure (providing procedures for a taxpayer to correct, without the receipt of a

[28] Revenue Procedure 2022-19, SECTION 2.03(2), October 11, 2022

[29] Revenue Procedure 2022-19, SECTION 3.02, October 11, 2022

> PLR, an error, an omission, or a missing required consent on a Form 2553 or Form 8869).[30]

The Procedure provides the following procedures for specific omissions and errors.

### *Missing Shareholder Consent*

The Procedure provides a set of potential methods to correct the situation where a shareholder consent is missing, only providing for a PLR if none of the others apply:

> An S election that fails to include the consent of a shareholder may be corrected pursuant to the following:
>
> > (a) Section 1.1362-6(b)(3)(iii) (providing an extension of time for filing a shareholder consent to an S election);
> >
> > (b) Rev. Proc. 2013-30 (providing a simplified method for taxpayers to request relief for late S elections);
> >
> > (c) Rev. Proc. 2004-35, 2004-1 C.B. 1029 (providing automatic relief for certain taxpayers requesting relief for late shareholder consents for S elections in community property States); or
> >
> > (d) If the remedies listed in section 3.03(1)(a) through (c) of this revenue procedure do not apply, a taxpayer or the taxpayer's authorized representative may request relief by submitting a request for a PLR under § 1362(f) to the Associate Chief Counsel (Passthroughs and Special Industries).[31]

### *Correction of an Error With Regard to a Permitted Year*

For an error related to a permitted year, the IRS again reminds taxpayers of automatic relief options before allowing for a PLR to be issued:

> A Form 2553 that contains an inadvertent error with regard to a permitted year may be corrected pursuant to Rev. Proc. 2013-30 (providing a simplified method for taxpayers to request relief for late S elections). If a taxpayer is not eligible for relief under Rev. Proc. 2013-30, a correction may be obtained through the receipt of a PLR under §

[30] Revenue Procedure 2022-19, SECTION 2.03(3), October 11, 2022

[31] Revenue Procedure 2022-19, SECTION 3.03(1), October 11, 2022

> 1362(f) from the Associate Chief Counsel (Passthroughs and Special Industries).[32]

### *Correction of Missing Officer's Signature*

In the case of a missing officer's signature, the Procedure first directs taxpayers to the existing standard late S election relief:

> A Form 2553 or Form 8869 that is missing the signature of an authorized officer of the S corporation that affects the validity of the S election or QSub election may be corrected pursuant to Rev. Proc. 2013-30 (providing a simplified method for taxpayers to request relief for late S elections and QSub elections). If a taxpayer is not eligible for relief under Rev. Proc. 2013-30, a correction may be obtained through the receipt of a PLR under § 1362(f) from the Associate Chief Counsel (Passthroughs and Special Industries).[33]

### *Correction of Other Inadvertent Errors or Omissions*

The Procedure concludes with a simplified process to deal with other inadvertent errors or omissions not covered by the previous sections:

> Errors and omissions on Form 2553 or Form 8869, other than those addressed in section 3.03(1) through (3) of this revenue procedure, may be corrected by explaining in writing the error(s) or omission(s) and the necessary correction(s) and submitting the written explanation to one of the following addresses (depending on the Internal Revenue Submission Processing Center with which the S corporation files its Form 1120-S) or any successor address the IRS may provide:
>
> > (a) Internal Revenue Service, MS 6055, 333 W. Pershing Rd., Kansas City, MO 64108.
> >
> > (b) Internal Revenue Service, MS 6273, 1973 N. Rulon White Blvd., Ogden, UT 84404.[34]

[32] Revenue Procedure 2022-19, SECTION 3.03(2), October 11, 2022

[33] Revenue Procedure 2022-19, SECTION 3.03(3), October 11, 2022

[34] Revenue Procedure 2022-19, SECTION 3.03(4), October 11, 2022

### *No PLRs Issued for Certain Inadvertent Errors, Omissions, or Missing Required Consents*

Again the Procedure provides that the IRS will not generally issue rulings for any such issues other than those where the Procedure specifically provides that a PLR should be requested:

> The IRS will not issue a PLR under § 1362(f) regarding any error or omission described in section 3.03(4) of this revenue procedure. Such inadvertent errors or omissions do not impact a corporation's S election or QSub election. See section 2.03(3) of this revenue procedure. The IRS will also not issue a PLR under § 1362(f) for a missing required consent, errors with regard to a permitted year, or a missing officer's signature where the taxpayer qualifies for relief under any of the means of relief identified in section 3.03(1) through (3) of this revenue procedure. The Associate Chief Counsel (Passthroughs and Special Industries) will consider the issuance of a PLR only if the error or omission concerns a shareholder consent, the selection of a permitted year, or a missing officer's signature, and the taxpayer has no other means of requesting relief. See section 4.02(2) of this revenue procedure.[35]

## ***Procedures for Verifying S Elections or QSub Elections***

The Procedure discusses issues where the corporation is unable to locate the letter from the IRS accepting the S election or QSub election:

> Generally, within 90 days after the IRS receives a corporation's Form 2553, the IRS mails a CP261 Notice as an acknowledgment to the corporation that the IRS has accepted the corporation's filing. For QSub elections filed on Form 8869, the IRS mails a CP279 Notice to the filer and a CP279A Notice to the subsidiary, generally within 60 days after the IRS accepts the QSub election. A lack of written acknowledgement that the IRS has accepted the corporation's S election or its subsidiary's QSub election (for example, because it was lost or never received) creates uncertainty for some taxpayers about the validity of the election. However, neither subchapter S of the Code nor the Income Tax Regulations thereunder provide that a lack of possession of a CP261 Notice, CP279 Notice, or CP279A Notice affects the validity of an S election or a QSub election, respectively. Rather, such notices are merely administrative acknowledgments of an effective election that can be reproduced upon the taxpayer's request. See section 3.04 of this revenue procedure (providing procedures to

[35] Revenue Procedure 2022-19, SECTION 3.03(5), October 11, 2022

> replace a missing CP261 Notice, CP279 Notice, or CP279A Notice).[36]

The Procedure adds an exclusive method for requesting an additional copy of these letters:

> **(1) Availability of replacement letters**. With regard to a missing administrative acceptance letter for an S election or an administrative acceptance letter for a QSub election, as appropriate, a replacement letter may be requested:
>
> > (a) For an S corporation and shareholders of an S corporation, by contacting the IRS Business and Specialty Tax Line at 800-829-4933; and
> >
> > (b) For practitioners, by contacting the IRS Practitioner Priority Service at 866-860-4259.[37]

Not surprisingly, what cannot be done is request a PLR on the issue:

> **(2) Unavailability of a PLR.** The IRS will not issue a PLR under § 1362(f) with regard to any missing administrative acceptance letter described in section 3.04(1) of this revenue procedure. See section 4.01(2) of this revenue procedure. A missing administrative acceptance letter does not impact an S election or a QSub election. See section 2.03(4) of this revenue procedure.[38]

## *Procedures for Addressing a Federal Income Tax Return Filing Inconsistent with an S Election or a QSub Election*

The Procedure describes the following problem that sometimes arises with S corporations:

> Occasionally, a corporation files a Federal income tax return that is inconsistent with the corporation's status as an S corporation or a QSub (for example, an S corporation files a Form 1065, U.S. Return of Partnership Income, or Form 1120, U.S. Corporation Income Tax Return, instead of Form 1120-S, U.S. Income Tax Return for an S Corporation). Although an inconsistent Federal income tax return filing can create several complications for the filer, nothing in the Code or Income Tax Regulations thereunder provides that such a filing affects the validity of a corporation's S election or QSub election.

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[36] Revenue Procedure 2022-19, SECTION 3.03(5), October 11, 2022

[37] Revenue Procedure 2022-19, SECTION 3.04, October 11, 2022

[38] Revenue Procedure 2022-19, SECTION 3.04, October 11, 2022

> For example, neither § 1362(d) nor § 1.1361-5(a) lists an inconsistent Federal income tax return filing as an event that gives rise to a termination of an S election or a QSub election. See section 3.05 of this revenue procedure (providing procedures for taxpayers to address, without the receipt of a PLR, a Federal income tax return filing inconsistent with an S election or a QSub election, as appropriate).[39]

The Procedure provides the following method to resolve this issue:

> **(1) Filing a corrected original return or an amended return.** An S corporation, or a parent S corporation of a QSub, that files a Federal income tax return for a taxable year that is inconsistent with the status of the corporation as an S corporation, or inconsistent with the status of a subsidiary of the parent S corporation as a QSub, must file a Federal income tax return for open taxable years consistent with its status, as appropriate —
>
> > (a) to reflect the status of the corporation as an S corporation or parent of a QSub; or
> >
> > (b) to reflect the status of the subsidiary as a QSub.[40]

The Procedure provides the following guidance regarding the federal income tax effect of a corporation's prior transactions in this case:

> Because a corporation is not treated as having terminated its S election or QSub election, as appropriate, merely due to the filing of one or more Federal income tax returns inconsistent with its S election or QSub election, the corporation's distributions and other transactions will be treated consistent with its status as an S corporation or a QSub, as appropriate. Thus, a QSub's income or deductions will be treated as income or deductions of the parent S corporation and distributions between the QSub and its parent will be disregarded.[41]

As with prior issues, the IRS provides no private letter rulings will be issued in this area:

> The IRS will not issue a PLR under § 1362(f) with regard to any inconsistent return filing described in section 3.05(1) of this revenue procedure. See section 4.01(2) of this revenue procedure. Such an inconsistent return filing does not impact an S election or a QSub election. See section 2.03(5) of this revenue procedure.[42]

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[39] Revenue Procedure 2022-19, SECTION 2.03(5), October 11, 2022

[40] Revenue Procedure 2022-19, SECTION 3.05(1), October 11, 2022

[41] Revenue Procedure 2022-19, SECTION 3.05(3), October 11, 2022

[42] Revenue Procedure 2022-19, SECTION 3.05(2), October 11, 2022

## *Procedures for Retroactively Correcting One or More Non-Identical Governing Provisions*

The most complex taxpayer assistance procedure involves a case where the governing provisions create non-identical rights to regular or liquidating distributions, triggering a second class of stock. This can happen when standard boilerplate language is added to corporate documents when having both voting and non-voting stock that can provide for separate declarations of distributions to each type of stock. This creates a problem even if no disproportionate distribution ever takes place.

A similar problem can arise with LLC operating agreements when the "check the box" corporation takes on more than one member and the language of the operating agreement provides for any possibility of differing distribution rights.

The Procedure describes the problem as follows:

> **(6) Non-identical governing provisions.**
>
> **(a) Overview.** Section 1361(b)(1)(D) requires an S corporation to have only one class of stock. Section 1.1361-1(l) provides that a corporation is treated as having only one class of stock if all outstanding shares of the corporation's stock confer identical rights to distribution and liquidation proceeds and if the corporation has not issued any instrument or obligation, or entered into any arrangement, that is treated as a second class of stock. An S corporation in compliance with § 1.1361-1(l) is commonly referred to as having "identical governing provisions." The term "non-identical governing provision" means a governing provision, as defined by § 1.1361-1(l)(2)(i), on its own or as part of another governing provision, that for Federal income tax purposes results in the S corporation having more than one class of stock under § 1.1361-1(l)(1) (even if the S corporation never made a non-pro rata distribution or liquidating distribution).
>
> **(b) Consequences of non-identical governing provisions**. If an entity files an S election when it has more than a single class of stock, the entity does not meet the requirements to be an S corporation and its attempted election is invalid. See § 1361(a)(1). If a valid S corporation later provides for more than a single class of stock, its S election automatically terminates on the day the disqualifying event occurs. See § 1362(d)(2). See section 3.06 of this revenue procedure (providing procedures for correcting, without the receipt of a PLR, the validity or continuation of an S election with regard to one or more non-identical

> governing provisions, as defined in section 2.03(6)(a) of this revenue procedure).[43]

The relief provisions for this problem are much longer than those for the other areas.

### *Definitions*

The Procedure provides the following definitions for this relief procedures:

- *Applicable shareholder.* The term "applicable shareholder" means a current or former shareholder of a corporation who owns or owned stock of the corporation at any time during the period:
  - (i) Beginning on the date on which the non-identical governing provision was adopted (on its own or as part of another governing provision); and
  - (ii) Ending on the date on which the nonidentical governing provision was removed or modified in a manner such that the governing provision complies with the one class of stock requirement.
- *Discovered by the IRS.* The term "discovered by the IRS" has the meaning given the term in § 301.9100-3(b)(1)(i) of the Procedure and Administration Regulations (26 CFR part 301).
- *Disproportionate distribution.* The term "disproportionate distribution" is defined in section 2.03(2) of this revenue procedure.
- *Non-identical governing provision.* The term "non-identical governing provision" is defined in section 2.03(6)(a) of this revenue procedure.[44]

### *Retroactive Corrective Relief Procedures*

The Procedure provides a series of steps at Section 3.06(2) that must be followed to obtain retroactive relief. The section provides:

> **(a) Retroactive continuing validity of S election**. If an S corporation and its applicable shareholders meet the requirements of this section 3.06, an S election that is invalid or terminated solely as the result of one or more non-identical governing provisions will be treated for Federal income tax purposes as continuing from the date on which the first non-identical governing provision that invalidated or terminated the corporation's S election was adopted.[45]

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[43] Revenue Procedure 2022-19, SECTION 2.03(6), October 11, 2022

[44] Revenue Procedure 2022-19, SECTION 3.06(1), October 11, 2022

[45] Revenue Procedure 2022-19, SECTION 3.06(2)(a), October 11, 2022

To be eligible for retroactive relief, the corporation must meet the following requirements:

> **(b) Eligibility**. A small business corporation and each applicable shareholder of the corporation are eligible for corrective relief under this section 3.06 if the following requirements are satisfied:
>
> (i) The corporation has or had one or more non-identical governing provisions;
>
> (ii) The corporation has not made, and for Federal income tax purposes is not deemed to have made, a disproportionate distribution to an applicable shareholder;
>
> (iii) The corporation timely filed a return on Form 1120-S (as required under § 6037 of the Code and § 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 this section 3.06 (a corporation is treated as having timely filed a required Form 1120-S under this section 3.06(2)(b)(iii) if the Form 1120-S is filed within six months after its original due date, excluding extensions); and
>
> (iv) Before any non-identical governing provision is discovered by the IRS, all of the requirements described in section 3.06(2)(c) of this revenue procedure are satisfied.[46]

The following corrective relief statements are also required to obtain retroactive relief:

> **(c) Corrective relief statements.**
>
> **(i) Corporate governing provision and shareholder statements.** The corporation must complete a Corporate Governing Provision Statement in accordance with section 3.06(2)(c)(ii) of this revenue procedure and a Shareholder Statement signed by each applicable shareholder in accordance with section 3.06(2)(c)(iii) of this revenue procedure.
>
> **(ii) Corporate Governing Provision Statement**. The Corporate Governing Provision Statement, a sample of which

[46] Revenue Procedure 2022-19, SECTION 3.06(2)(b), October 11, 2022

is provided in Appendix A, must be completed in accordance with this section 3.06(2)(c)(ii).

(A) Designation. The Corporate Governing Provision Statement must state at the top of the document: "CORPORATE GOVERNING PROVISION STATEMENT PURSUANT TO REV. PROC. 2022-19, SECTION 3.06(2)(c)(ii)".

**(B) Information.** The Corporate Governing Provision Statement must provide the following information:

(1) The date of the Corporate Governing Provision Statement, the corporation's name, employment identification number (EIN), address, date of formation or incorporation, and State of formation or incorporation;

(2) The actual or intended effective date of the corporation's S election filed on Form 2553 (see Form 2553, Part I, line E) that is the subject of the request for corrective relief under this section 3.06;

(3) The name, address, and social security number or taxpayer identification number of each applicable shareholder; and

(4) To establish an inadvertent termination or invalidation of the S election of the corporation, a description of all relevant facts regarding why each non-identical governing provision was adopted, how each non-identical governing provision was discovered, and each action taken to correct or remove each non-identical governing provision before any non-identical governing provision is discovered by the IRS. This description must include each action taken by the corporation and each applicable shareholder to establish that the corporation and each applicable shareholder acted reasonably and in good faith in correcting or removing each non-identical governing provision upon discovery to demonstrate reasonable cause for relief.

**(C) Representations**. Except as provided in section 3.06(2)(c)(ii)(D), the corporation must provide the following four representations:

> (1) "The corporation's S election was inadvertently invalid or terminated solely because of the adoption of one or more non-identical governing provisions.";
>
> (2) "The corporation and each applicable shareholder satisfy all of the requirements set forth in section 3.06 of Rev. Proc. 2022-19.";
>
> (3) "The corporation responds in the negative to each requested statement set forth in section 7.01(4) or (5) of Rev. Proc. 2022-1, or any successor revenue procedure (statements regarding whether the same or a similar issue was previously ruled on or whether a request involving the same or a similar issue was submitted or is currently pending)."; and
>
> (4) "The corporation and each applicable shareholder acted reasonably and in good faith in correcting or removing each non-identical governing provision upon discovery.".

**(D) Explanation regarding previously ruled on, submitted, or pending PLRs.** If the corporation cannot respond in the negaive to any requested statement set forth in section 7.01(4) or (5) of Rev. Proc. 2022-1, or any successor revenue procedure (and therefore cannot make the representation described in section 3.06(2)(c)(ii)(C)(3) of this revenue procedure), the corporation must provide an explanation for each such response as part of the description of all relevant facts required by section 3.06(2)(c)(ii)(B)(4) of this revenue procedure.

**(E) Statements**. The corporation must provide the statements set forth in section 3.06(2)(c)(ii)(E)(1) through (3) of this revenue procedure:

> (1) "The corporation acknowledges that the relief provided by section 3.06 of Rev. Proc.

2022-19 is limited solely to each non-identical governing provision described in this Corporate Governing Provision Statement.";

(2) "The corporation acknowledges that the relief provided by section 3.06 of Rev. Proc. 2022-19 is based solely on the information, representations, and other statements provided by the corporation pursuant to section 3.06 of Rev. Proc. 2022-19, each of which is subject to verification during IRS examination."; and

(3) "During the period between the date on which the non-identical governing provision became effective and the date on which all of the procedures described in section 3.06 of Rev. Proc. 2022-19 are completed, each applicable shareholder has reported their income on all affected returns consistent with the S corporation election for the taxable year the non-identical governing provision became effective and for all subsequent years for which each applicable shareholder owned shares of the corporation.".

**(F) Signature**. The Corporate Governing Provision Statement must be signed under penalties of perjury by a person authorized to sign the corporation's Federal income tax return under § 6062 of the Code. The penalties of perjury statement must be provided in the following format: "Under penalties of perjury, I declare that I have examined this Corporate Governing Provision Statement for corrective relief for one or more non-identical governing provisions, as provided by Rev. Proc. 2022-19, section 3.06, including accompanying documents, and, to the best of my knowledge and belief, the request contains all the relevant facts, and such facts are true, correct, and complete.".

**(iii) Shareholder Statement**. The Shareholder Statement, a sample of which is provided in Appendix B, must be completed in accordance with this section 3.06(2)(c)(iii).

**(A) Designation**. The Shareholder Statement must state at the top of the document: "SHAREHOLDER STATEMENT PURSUANT TO REV. PROC. 2022-19, SECTION 3.06(2)(c)(iii)".

**(B) Information**. The Shareholder Statement must provide:

(1) The date of the Shareholder Statement, the corporation's name, EIN, address, date of formation or incorporation, and State of formation or incorporation;

(2) The name and address of each applicable shareholder;

(3) The social security number or taxpayer identification number of each applicable shareholder;

(4) The number of shares of stock or, in the case of a limited liability company, percentage of ownership each applicable shareholder owns or owned and the date(s) the stock was acquired and, if applicable, transferred; and

(5) The date that each applicable shareholder provided their signature, as required by section 3.06(2)(c)(iii)(D) of this revenue procedure.

**(C) Statement of consent**. Each applicable shareholder must provide the following statement of consent: "Under penalties of perjury, I declare that I consent to the election of [insert corporation's name], referred to herein as "the Corporation," located at [insert the Corporation's address], whose employment identification number (EIN) is [insert the Corporation's EIN], to be an S corporation under § 1362(a)(1) of the Code. I have examined this consent statement, including accompanying documents, and, to the best of my knowledge and belief, the request

> for corrective relief contains all the relevant facts, and such facts are true, correct, and complete. I understand that my consent is binding and may not be withdrawn after the Corporation receives relief pursuant to Rev. Proc. 2022-19, section 3.06. I also declare under penalties of perjury that I have reported my income on all affected returns consistent with the Corporation's election to be an S corporation for the taxable year for which the election would have been in effect but for the non-identical governing provision(s) described in the Corporate Governing Provision Statement for corrective relief and for all subsequent years I have owned shares of the Corporation.".
>
> **(D) Signature**. The Shareholder Statement must be signed under penalties of perjury by each applicable shareholder.[47]

Finally, there is a record retention requirement for this relief:

> **(d) Record retention requirement**. The corporation is required to retain the Corporate Governing Provision Statement, the Shareholder Statement(s), and the revised governing provisions in accordance with § 6001 of the Code and the Income Tax Regulations thereunder. The Corporate Governing Provision Statement, the Shareholder Statement(s), and the revised governing provisions must be retained by the corporation for inspection by authorized Internal Revenue officers or employees, and must be retained so long as the contents thereof may become material in the administration of any provision of the Code or the Income Tax Regulations. See § 1.6001-1(e).[48]

If the taxpayer does not qualify for the above retroactive relief, then the following procedures must be used to request a private letter ruling:

> **(e) Alternative relief.**
>
> **(i) General rule.** An S corporation or applicable shareholder that does not qualify for corrective relief under this section 3.06 may seek corrective relief through a request submitted by the S corporation, applicable shareholder, or authorized representative (as appropriate) to the Associate Chief Counsel (Passthroughs and Special Industries) for a PLR. The request must provide the required explanation described in

[47] Revenue Procedure 2022-19, SECTION 3.06(2)(c), October 11, 2022

[48] Revenue Procedure 2022-19, SECTION 3.06(2)(d), October 11, 2022

section 3.06(2)(e)(ii) of this revenue procedure. See generally Rev. Proc. 2022-1 (or any successor revenue procedure).

**(ii) Required explanation**. A request for a PLR by an S corporation or applicable shareholder, or authorized representative, under section 3.06(2)(e)(i) of this revenue procedure must include an explanation regarding each reason why the requirements for corrective relief under this section 3.06 could not be satisfied.[49]

# SECTION: ERC
# AICPA ISSUES DOCUMENT OUTLINING FACT AND FICTION WHEN DEALING WITH EMPLOYEE RETENTION CREDIT

## Citation: "Employee retention credit: Fact or fiction?," AICPA & CIMA, 10/3/22

The AICPA Tax Division has released a three page summary[50] of some key issues with the Employee Retention Credit that is available for download to AICPA Tax Section members.

The document does provide specific statements regarding some claims often heard from organizations involved in heavily marketed ERC study programs where businesses are tempted to pay for such a study with promises of large ERC payments that are claimed to be available to the business. It also provides a short summary document that can be useful to provide to clients confused by what they have been hearing.

A couple of key items found in the document are noted below.

### *The ERC Applies to Most Small Businesses*

Many of the ads promoting these studies at the very least strongly imply that most small businesses will qualify for a significant ERC payment. The document begins by labeling as fiction the claim that "[g]iven GOVID-19's wide-reaching effects, many small businesses will qualify for an employee retention credit (ERG)."

The document notes that the determination of whether a business qualifies for the credit is a complex undertaking:

> Determining whether a business is eligible for the ERG can be pretty complex. Your business must meet the gross receipts test (50% or

[49] Revenue Procedure 2022-19, SECTION 3.06(2)(e), October 11, 2022

[50] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022, https://www.aicpa.org/resources/download/employee-retention-credit-erc-fact-or-fiction (membership required)

> more reduction for 2020 or a 20% or more decline for 2021 qualifying quarters when compared to 2019 quarters) or experience a full or partial suspension of operations because of a government order. Whether a business experienced a partial suspension is a facts ·and circumstances determination and will vary depending on the location of the business and the government orders.[51]

However, the document notes that a business without a significant decline in revenues can qualify for the credit is a fact—but notes that "there must have been a full or partial suspension of operations BECAUSE OF A GOVERNMENT ORDER that limited commerce, travel or group meetings due to COVID-19." As well, that order "would need to have a more. than a nominal impact on the business to qualify for the ERC."[52]

### *Nature of Restrictions*

The documents labels as fiction many blanket claims regarding full or partial suspension some clients have reported being told by parties marketing studies to them.

These include:

- *All safety recommendations or guidelines a government agency issues should be considered government orders to suspend operation requirements.* The document notes there are requirements beyond simply recommendations to qualify as an order for these purposes, as well as noting "[n]o federal order during 2020 or 2021 would qualify businesses for the ERC…"[53]

- *My business experienced supply chain disruption, which means it qualifies for the ERC.* The document notes that merely experiencing a supply chain disruption, even if related to the pandemic in some form, wouldn't be sufficient to qualify unless all fo the following are met:

  - The business's supplier cannot made deliveries of critical goods due to a qualifying government order (which, based on the previous discussion, would need to be a state or local order),

  - The business cannot purchase these critical goods from an alternative supplier, and

  - The business must experience a more than nominal effect from this issue.[54]

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[51] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022

[52] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022

[53] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022

[54] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022

- *My business qualifies for the ERC because employees and clients had to wear masks.*[55] This requirement alone would not qualify as a full or partial suspension of business operations that had a more than nominal effect on the business.

- *My business was in a location where them was a stay-at-home order, and I adjusted operations based on this. This automatically means I can claim the ERC.* Voluntary changes made a business, even if in response to pandemic conditions, related to service demand do not qualify as a full or partial suspension.[56] If the issue is reduction in demand, the business would have to show it met the reduction in gross revenue test.

[55] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022

[56] "Employee retention credit: Fact or fiction?," AICPA & CIMA, October 3, 2022