

ACRS-Subchapter S Corporation Shareholders

This memo should be used in conjunction with TSB-M-83-(2)-I, Modification for Federal Accelerated Cost Recovery System. Numerous inquiries have been received concerning the effect of the modifications to federal adjusted gross income under section 612 on shareholders of federal subchapter S Corporations.

Under federal law, prior to the Subchapter S Revision Act of 1982, a subchapter S corporation was not treated as a conduit, except for the excess of net long-term capital gains over net short-term capital losses. The character of income and deductions did not flow through to the shareholders. (Internal Revenue Code Sections 1373 and 1375(a))

Accordingly, since the character of the accelerated cost recovery deduction does not pass through to the shareholders of an electing New York State subchapter S corporation the modifications provided in sections 612(b)(25) and 612(c)(26) are not to be made.

In the case of shareholders in a subchapter S corporation which has not made an election under 660 to be treated as a subchapter S corporation for New York State tax purposes no modification to adjust the accelerated cost recovery deduction are to be made. This is based on both the above reasoning and the fact that the shareholder would not include his share of federal subchapter S corporation undistributed taxable income or loss in his New York state personal income tax return. However, the corporation itself would have to make the modifications provided in Article 9-A, of the New York State Tax Law.

This memorandum does not apply to tax years beginning after 1982, due to the substantial changes made in the treatment of S corporation shareholders by the Subchapter S Revision Act of 1982. A memorandum will be issued at a later date which will explain the full effect of this Act for New York State tax purposes.

For the modifications to be made by non-electing corporations for the accelerated cost recovery deduction see TSB-M-82-(16)-C. For the treatment of the shareholders of subchapter S corporation where an election under section 660 was or was not made see TSB-M-81-(11), Income and Corporation Taxes.