



Basis, Basis, Basis for S-Corp Shareholders How it affects the Client!

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Learning Objectives

Upon completion of this course, you will be able to:

- Define shareholder basis and how it is calculated
- Determine the impact of shareholder loans and distributions on basis
- Identify when deductible losses are limited by basis
- Understand the importance of tracking shareholder basis

What is S-Corp stock basis?

- The amount of investment in stock for tax purposes
- It is adjusted annually § 1367
- It is used to figure amounts that are included or excluded from tax
- It is used to calculate the gain or loss on the sale of stock

Who's Keeping Track?

- It is the shareholder's responsibility!
 - § 1.6001-1(a)
- But wait...

Who's Keeping Track?

- Inside Basis:
 - Maintained on Books of Entity
 - AAA, PTI, AE&P
- Outside Basis
 - Maintained by shareholder
 - Different than inside basis

Initial Stock Basis

- Shares received when S-Corp is formed
 - § 351
- Purchase of shares – Cost
 - Active participant interest deduction
- C Corporation electing S status
 - Basis at time of conversion

Initial Stock Basis

- Gift of shares - donor's basis
 - IRC § 1015
 - FMV limits basis for loss
- Inheritance - FMV at date of death
- Shares received in exchange for services
 - Measured by stock's FMV

Basis Adjustments

- Ordering Rules
 - First – Increase for income items and excess depletion
 - Second – Decrease for distributions
 - Third – Decrease for nondeductible, noncapital expenses
 - Fourth – Decrease for items of loss and deduction

Basis Adjustments

- Buy / sell stock
- Capital contributions
- Adjusted annually § 1367
- Uniqueness of S-Corp Basis
- Ordering Rules Election
- Increase / Decrease chart

Basis - Increase

Item	Stock Basis	AAA	Sch. K-1
Purchase Stock	Increase	No Effect	N/A
Contribute Property	Increase	No Effect	N/A
Contribute Cash	Increase	No Effect	N/A
Ordinary Income	Increase	Increase	Box 1



Basis - Increase

Item	Stock Basis	AAA	Sch. K-1
Separately Stated Income	Increase	Increase	Box 2 - 6
Capital Gains	Increase	Increase	Box 7 - 10
Nontaxable Income	Increase	No Effect	Box 16 Code A & B
Depletion In Excess of Basis	Increase	Increase	Box 15 Code C

Basis - Decrease

Item	Stock Basis	AAA	Sch. K-1
Distributions	Decrease	Decrease	Box 16 Code D
Ordinary Loss	Decrease	Decrease	Box 1
Separately Stated Losses	Decrease	Decrease	Box 2 - 6
Capital Losses	Decrease	Decrease	Box 7 - 10
Deductible Expenses	Decrease	Decrease	Box 11 – 12 Box 14 Code L & M
Nondeductible Expenses	Decrease	Decrease	Box 16 Code C



Basis – Other?

Items	Stock Basis	AAA	Sch. K-1
Tax-Exempt Income Related Expenses	Decrease	No Effect	Box 16 Code C
Depletion Not In Excess of Basis	Decrease	Decrease	Box 17 Code R
Taxable Distributions of AE&P	No Effect	No Effect	N/A

Schedule M-2 Analysis

- What is...
 - AAA - Accumulated adjustments account
 - Cumulative total of undistributed net income items
 - Can be negative from losses
 - Belongs to corporation, not shareholder

Schedule M-2 Analysis

- AE&P - Accumulated earnings & profits
 - From C-Corp
- OAA – Other adjustments account
 - IRS record keeping account

Limitation to S-Corp Losses

- Stock & Debt limitations
 - Basis!
- At Risk limitations
 - IRC § 465
- Passive Activity Loss limitations
 - IRC § 469

Debt Basis

- Must be directly from shareholder to S-Corp
 - Shareholder guarantee of S-Corp loan does not create basis!
- Document! Document!
 - Note with interest and terms
 - Actually pay!
 - Approve at Annual Meeting

Debt Basis

- Only relevant in utilizing losses
- Only utilized after stock basis has been reduced to zero
- Restore debt basis before stock basis
- Repayment of reduced basis debt = capital gains!
- Suspended losses

Shareholder Distributions

- Distributions are not mandatory
 - Even when there is a profit
- Non-dividend vs. dividend distributions
 - Schedule K-1 or Form 1099-DIV
- Must be proportionate to ownership
- Distributions in excess of basis
- Distributions can be recharacterized

Ordering rules for Distributions

From:	Taxation	Basis
AAA	Usually tax-free	Reduce
AE & P	Taxable dividend	No effect
OAA	Usually tax-free	Reduce
Other capital	Usually tax-free up to basis	Reduce
Other capital	Capital gain in excess of basis	None remains



Real World Basis Example

- S Corporation from day one
- Sole shareholder
- 01/01/20XX Stock Basis = \$25,000
- Ordinary loss = <\$15,000>
- Interest income = \$500
- M&E expenses = \$1,500
- Non-dividend distribution = \$15,000

01/01/20XX Beginning Basis	\$25,000
Interest Income	+ \$500
Stock Basis before distributions	= \$25,500
Non-Dividend distribution	<\$15,000>
Stock Basis after distribution	= \$10,500
Nondeductible expenses (M&E)	<\$1,500>
Basis after nondeductible expenses	= \$9,000
Ordinary loss	<\$15,000>
Allowable loss	= \$9,000
12/31/20XX Ending Basis	= \$0.00
Suspended loss	= <\$6,000>

What we did for the last hour?

- Define shareholder basis and how it is calculated
- Determine the impact of shareholder loans and distributions on basis
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- Understand the importance of tracking shareholder basis



For More Information

National Society of Accountants

More information is available including additional materials at:

Booth in Vendor Hall

Or Table in Lobby

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