*26 CFR 1.671-2: Applicable principles.*
*(Also Sections 643, 671, 678; 1.671-3.)*

**Gain or loss; sale of S stock by QSST.** If a "qualified subchapter S trust" (QSST) sells all or part of its stock in an S corporation, the beneficiary rather than the trust is the taxpayer who recognizes gain or loss on the sale of the stock, even if under local trust law gain or loss on the sale is allocable to corpus rather than to income.

## Rev. Rul. 92-84

### ISSUE

If a "qualified subchapter S trust" (QSST) sells all or part of its stock in an S corporation, and under local trust law any gain or loss on the sale is allocable to corpus rather than to income, is the taxpayer who recognizes gain or loss on the sale of the stock the trust or the beneficiary?

### FACTS

*TR* is a trust that meet all of the requirements of a QSST under section 1361(d)(3) of the Internal Revenue Code. *TR* owns shares of stock of *M* corporation.

*M* Corporation is a small business corporation that has in effect an election to be an S corporation. *A*, the sole income beneficiary of *TR*, has made an election under section 1361(d)(2) of the Code with respect to *TR* and *M* corporation. *A*'s election took effect on the same date as *M* corporation's S election.

*TR* sells all or part of its *M* corporation stock. Under applicable local trust law gain or loss on the sale of the stock is properly allocable to corpus rather than to income.

### LAW AND ANALYSIS

Section 1361(a)(1) of the Code provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under section 1362(a) is in effect for such year. Section 1361(b)(1)(B) permits only individuals, estates, and certain trusts to be shareholders of a small business corporation.

Section 1361(c)(2)(A)(i) of the Code provides that a trust, all of which is treated under the grantor trust provisions of sections 671 through 679 (subpart E of part I of subchapter J of chapter 1) as owned by an individual who is a citizen or resident of the United States, is a permissible shareholder for purposes of section 1361(b)(1)(B).

Section 1361(d)(1)(A) of the Code provides that, in the case of a QSST with respect to which a beneficiary makes an election under section 1361(d)(2), such trust shall be treated as a trust described in section 1361(c)(2)(A)(i).

Section 1361(d)(1)(B) of the Code provides that, for purposes of section 678(a), which sets forth the rules for when a person other than the grantor will be treated as a substantial owner, the beneficiary of a QSST shall be treated as the owner of that portion of the trust which consists of stock in an S corporation with respect to which the election under section 1361(d)(2) is made.

A QSST is defined in section 1361(d)(3) of the Code. Under section 1361(d)(3)(A), the terms of a trust must contain certain requirements for the trust to be a QSST. In addition, section 1361(d)(3)(B) provides that a trust is a QSST only if all of the income of the trust (within the meaning of section 643(b)) is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

*A* has made the election under section 1361(d)(2) of the Code with respect to *TR* and *M* corporation. Therefore, under section 1361(d)(1)(B), *A* is treated as the owner of that portion of *TR* that consists of stock in corporation *M* for purposes of section 678(a).

Section 671 of the Code provides that, where the grantor or another person is treated as the owner of any portion of a trust, there shall be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account under chapter 1 in computing taxable income or credits against the tax of an individual.

Section 678(a) is within subpart E of subchapter J of the Code. Therefore, the provisions of section 671 are applicable to the stock of an S corporation with respect to which the beneficiary has made an election under section 1361(d)(2).

Section 1.671-2(b) of the Income Tax Regulations provides that when it is stated in the regulations under subpart E that "income" is attributed to the grantor or another person, the reference, unless specifically limited, is to income determined for tax purposes and not to income for trust accounting purposes.

Section 1.671-2(c) of the regulations provides that an item of income, deduction, or credit included in computing the taxable income and credits of a grantor or another person under section 671 is treated as if it had been received or paid directly by the grantor or other person (whether or not an individual).

Section 1.671-3(a)(2) of the regulations provides that, if the portion treated as owned by a grantor or another person consists of specific trust property and its income, all items directly related to that property are attributable to that portion.

Accordingly, where a grantor or another person is treated as the owner of property constituting corpus under subpart E, the trust is disregarded as a separate entity and any gain or loss on the sale of such corpus is treated as gain or loss of such person.

The gain or loss on the sale of *M* corporation stock by *TR* is directly related to that stock. Therefore, pursuant to the provisions of section 1361 and subpart E of subchapter J of the Code, any gain or loss on the sale by *TR* of its stock in *M* corporation is included in computing the taxable income of *A*.

### HOLDING

If a "qualified subchapter S trust" (QSST) sells all or part of its stock in an S corporation, the beneficiary rather than the trust is the taxpayer who recognizes gain or loss on the sale of the stock, even if under local trust law gain or loss on the sale is allocable to corpus rather than to income.