

SUPPORTING STATEMENT
Internal Revenue Service
Form 7203, S Corporation Shareholder Stock and Debt Basis Limitations

OMB Control Number 1545-2302

1. CIRCUMSTANCES NECESSITATING COLLECTION OF INFORMATION

Internal Revenue Code (IRC) section 1366 determines the shareholder's tax liability from an S corporation. IRC section 1367 details the adjustments to basis including the increase and decrease in basis, income items included in basis, the basis of indebtedness, and the basis of inherited stock.

Treasury Regulations section 1.1366-2 provides rules and guidance on limitations on deductions of passthrough items of an S corporation to its shareholders. Section 1.1367-1 provides rules relating to adjustments to the basis of a shareholder's stock in an S corporation and a shareholder's election option to decrease the basis. Section 1.1367-2 provides rules relating to adjustments to the basis of indebtedness of an S corporation to a shareholder.

Form 7203 is used by S corporation shareholders to figure potential limitations of their share of the S corporation's deductions, credits, and other items that can be deducted on the shareholder's tax return.

2. USE OF DATA

The information is used by the Internal Revenue Service (IRS) and taxpayers to verify the stock and debt basis limitations claimed by shareholders, ensuring the proper basis computations are reported and claimed.

3. USE OF IMPROVED INFORMATION TECHNOLOGY TO REDUCE BURDEN

Electronic filing of Form 7203 is currently available.

4. EFFORTS TO IDENTIFY DUPLICATION

The information obtained through this collection is unique and is not already available for use or adaptation from another source.

5. METHODS TO MINIMIZE BURDEN ON SMALL BUSINESSES OR OTHER SMALL ENTITIES

The IRS proactively works with both internal and external stakeholders to minimize the burden on small businesses, while maintaining tax compliance. The Agency also seeks input regarding the burden estimates from the public via notices and tax product instructions. This information collection is for individual, trust/estates, and tax-exempt taxpayers; therefore, there will be minimal if any impact to small businesses. The forms can be filed electronically, which further reduces any burden to small businesses.

6. CONSEQUENCES OF LESS FREQUENT COLLECTION ON FEDERAL PROGRAMS OR POLICY ACTIVITIES

A less frequent collection would result in the IRS being unable to ensure shareholders are claiming the correct stock and debt basis limitations per federal tax rules under sections 1366 and 1367, thereby engendering the inability of the IRS to meet its mission.

7. SPECIAL CIRCUMSTANCES REQUIRING DATA COLLECTION TO BE INCONSISTENT WITH GUIDELINES IN 5 CFR 1320.5(d)(2)

There are no special circumstances requiring data collection to be inconsistent with Guidelines in 5 CFR 1320.5(d)(2).

8. CONSULTATION WITH INDIVIDUALS OUTSIDE OF THE AGENCY ON AVAILABILITY OF DATA, FREQUENCY OF COLLECTION, CLARITY OF INSTRUCTIONS AND FORMS, AND DATA ELEMENTS

In response to the Federal Register notice (86 FR 38204), dated July 19, 2021, the IRS received two comment submissions during the comment period for this collection of information. Below are the Agency's responses:

From: Jeff Alberty, Managing Director, Grant Thornton LLP

Comment 1: Aggregate loss versus any loss, deduction, and credit (including prior year losses, deductions, and credits).

Response: We can't always guarantee that that the basis will be properly carried forward from the prior year. This is especially true when the shareholder changes advisors. Also, qualifying the reporting requirement with another exception will only add a layer of confusion. The purpose of the Form is to not only ensure there is sufficient basis for losses, deductions, and distributions, in the current year, but to also ensure that the basis is properly maintain and tracked from year to year.

The additional costs seem minimal when you consider the fact that the shareholder's basis needs to be maintained year over year anyway. Most returns are prepared on software that will maintain the form and basis and add the additional activity each year as a normal course of calculating the shareholder's return. In the end, the extra cost (calculating basis in the tax return preparation software vs separate basis software) if any, would be nominal since the calculation will be done contemporaneously (when the information is readily available) verses looking back through historical records to determine basis. This benefit both the shareholder and the IRS. Some shareholders have several years pass before being audited. Only then do they realize they may have a basis issue. At that time, it is very time consuming and costly for the shareholder to recreate their basis. Had they reported it more frequently, the computation would be readily available and indeed, there may not be an audit issue if the basis was reported on a regular basis. In essence, it forces advisors and tax return software companies to provide a consistent and current basis calculation which will increase compliance.

Where there are inconsistencies with other form instructions, they will be updated. We have updated Form 7203 instructions to be consistent with Schedule E (Form 1040).

Comment 2: Disposition of stock.

Response: Agree, the instructions should be updated to include the requirement that the shareholder report stock and debt basis when the stock is disposed through sale or gift. Also, we agree that the shareholder should report stock and debt basis when the shareholder has a worthless stock loss, or the S corporation is liquidated.

IRC § 904(f)(3)B – defines disposition as “as sale, exchange, distribution, or gift of property, whether or not gain or loss is recognized on the transfer.” It is important for the shareholder to report events that materially impact the basis computation, not merely events that trigger gain recognition.

Instructions revised under Who Must File on page one.

Comment 3: Receipt of a loan payment.

Response: Agree should require basis computation when there is a repayment of a reduced basis loan. Instructions revised under Who Must File on page one.

From: Richard J. Salter, Partner, WIPFLI on practical utility

Comment 1: Receipt of loan repayments.

Response: Agree. Instructions revised under Who Must File on page one.

Comment 2: AMT calculation reminder.

Response: We will take it under advisement as a possible TIP for subsequent instruction updates.

Comment 3: Consider suggesting in the instructions that it is prudent to complete and retain the form even in years for which it is not required to be filed.

Response: Agree. Instructions revised to add a TIP under Who Must file on page one.

Comment 4: Clarify basis of inherited property.

Response: Agree. Instructions revised at paragraph four under Line 2 on page two.

Comment 5: Add reference to Treasury Regulations section 1.1366-2(a)(6) in instructions and an optional line to the form reflecting the excess of donor’s basis over FMV.

Response: Agree to add reference, and instructions revised at paragraph five under Line 2 on page two. We will take adding an optional information line to the form under advisement as a possible update when the form is revised.

Comment 6: Clarify exclusion of C corporation from Form 1099-DIV on Line 6.

Response: Agree. Instructions revised at paragraph four under Line 6 on page two.

Comment 7: Consider adding lines to reflect a reduction for the basis of stock and/or of debt disposed of by sale or exchange or by gift.

Response: We can't change the form/instructions at this time. We will take this under advisement when the form is revised.

Comment 8: Consider including in the specific instructions for line 17 that it includes the face value of loans received by gift or inheritance in addition current year loans made by the taxpayer.

Response: We can't change the form/instructions at this time. We will take this under advisement when the form is revised.

Comment 9: Consider including in the specific instructions for line 22 that if the FMV of loans received by gift or inheritance during the year is less than face value, line 22 should not include the excess of face over FMV.

Response: We can't change the form/instructions at this time. We will take this under advisement when the form is revised.

Comment 10: Add a separate box to line 34 with instructions to distinguish formal notes from those deemed as formal notes under Treasury Regulations section 1.1367-2(a)(2)(ii).

Response: Agree to add reference, and instructions revised at paragraph three under Line 34 on page four. We will take adding a separate box to the form under advisement as a possible update when the form is revised.

From: Richard J. Salter, Partner, WIPFLI on enhancements

Comment 1: Use the term "reportable" on the K-1 rather than "reported" in instructions to address certain instances.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 2: Include references to the related forms on which at-risk, passive activity, and excess business loss limitations are calculated.

Response: Agree. Instructions revised under Limitations on Losses, Deductions, and Credits on page one.

Comment 3: Item 1 under Basis Limitations.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 4: Item 2 under Basis Limitations.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 5: Add box for Treasury Regulations section 1.1367-1(g) election.

Response: We can't change the form at this time. We will take this under advisement when the form is revised.

Comment 6: Separate basis calculations.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 7: Specify loan repayments do not decrease stock basis.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 8: Specify that additional capital contributions do not increase loan basis.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 9: Rectify conflicting directive for filing more than one Form 7203.

Response: This is a TIP, not a directive, for the shareholder to consider preparing two Forms 7203 if they dispose of some, but not all, of their stock during the year. As a result, the shareholder is free to decide what is best for them.

Comment 10: Use additional columns on form to allow tracking of basis in different blocks of stock.

Response: We can't change the form at this time. In addition, although the shareholder may have different basis in different blocks of stock, the passthrough items are generally allocated pro-rata to all shares, regardless of their different bases. As a result, there seems to be a limited benefit in adding columns for the different blocks when the columns will generally be identical, other than the beginning and ending balances. It is up to the shareholder to maintain the different basis in the different blocks.

Comment 11: Retention of Forms K-1 and other documentation reflected on Form 7203.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances. This may also send the wrong message about Form 7203.

Comment 12: Unreported gains from non-dividend distributions.

Response: This is basic information that an advisor should already be aware of or will become self-evident depending on the facts and circumstances.

Comment 13: Change columns in Part III of Form 7203 to available and allowable losses and deductions.

Response: We can't change the form at this time. We will take this under advisement when the form is revised.

Comment 14: Add additional line for non-deductible expenses.

Response: We can't change the form at this time. We will take this under advisement when the form is revised.

From: Richard J. Salter, Partner, WIPFLI on instructions for calculations based on year.

Comments 1 through 5: Instructions for basis calculations in previous years.

Response: We will take this under advisement when the form is revised.

9. EXPLANATION OF DECISION TO PROVIDE ANY PAYMENT OR GIFT TO RESPONDENTS

No payment or gift will be provided to any respondents.

10. ASSURANCE OF CONFIDENTIALITY OF RESPONSES

Generally, tax returns and tax return information are confidential as required by 26 U.S.C. 6103.

11. JUSTIFICATION OF SENSITIVE QUESTIONS

A privacy impact assessment (PIA) has been conducted for information collected under this request as part of the "Individual Master File (IMF)" system and a Privacy Act System of Records notice (SORN) has been issued for these systems under Treasury/IRS 22.062 - Electronic Filing Records; Treasury/IRS 24.030 - Customer Account Data Engine (CADE) Individual Master File; IRS 24.046 - CADE Business Master File (BMF); Treasury/IRS 34.037 - Audit Trail and Security Records. The Internal Revenue Service PIAs can be found at <https://www.irs.gov/privacy-disclosure/privacy-impact-assessments-pia>.

Title 26 U.S.C. 6109 requires inclusion of identifying numbers in returns, statements, or other documents for securing proper identification of persons required to make such returns, statements, or documents and is the authority for social security numbers (SSNs) in IRS systems.

This is an attachment to the federal tax return. The Privacy Act statement associated with this form is listed in the federal tax return instructions.

12. ESTIMATED BURDEN OF INFORMATION COLLECTION

The estimated burdens for individual and tax-exempt filers are included in the estimates for OMB control numbers 1545-0074 and 1545-0047.

This collection includes the estimated burden for estate and trust filers required to file Form 7203 with their tax return. The IRS anticipates that there will be approximately 70,000 respondents annually, with a total estimated burden of 265,300 hours annually. The estimated burden is shown below.

Authority	Description	# of Respondents	# Responses per Respondent	Annual Responses	Hours per Response	Total Burden
IRC 1366 and 1367	Form 7203	70,000	1	70,000	3.79	265,300
Totals		70,000		70,000		265,300

The following regulations impose no additional burden. Please continue to assign OMB number 1545-7203 to these regulations.

1.1366-2

1.1367-1

1.1367-2

13. ESTIMATED TOTAL ANNUAL COST BURDEN TO RESPONDENTS

To ensure more accuracy and consistency across its information collections, the IRS is currently in the process of revising the methodology it uses to estimate burden and costs. Once this methodology is complete, the IRS will update this information collection to reflect a more precise estimate of burden and costs.

14. ESTIMATED ANNUALIZED COST TO THE FEDERAL GOVERNMENT

Form 7203 was a new tax product for tax year 2021. The product cost will be captured in the next collection update from IRS Chief Financial Office and Media and Publications.

15. REASONS FOR CHANGE IN BURDEN

There is no change in the paperwork burden previously approved by OMB. The IRS is making this submission to renew the OMB approval.

16. PLANS FOR TABULATION, STATISTICAL ANALYSIS AND PUBLICATION

There are no plans for tabulation, statistical analysis and publication.

17. REASONS WHY DISPLAYING THE OMB EXPIRATION DATE IS INAPPROPRIATE

The IRS believes that displaying the OMB expiration date is inappropriate because it could cause confusion by leading taxpayers to believe that the form sunsets as of the expiration date. Taxpayers are not likely to be aware that the IRS intends to request renewal of the OMB approval and obtain a new expiration date before the old one expires.

18. EXCEPTIONS TO THE CERTIFICATION STATEMENT

There are no exceptions to the certification statement for this collection.

Note: The following paragraph applies to all of the collections of information in this submission:

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number. Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.