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# Quick Guide to Section 338(h)(10) and Section 336(e) Elections

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From a nontax standpoint, the purchaser of a corporate business often prefers buying the target corporation's stock rather than its assets. A stock purchase is usually easier to accomplish than an asset purchase and is often necessary to avoid interruption of contractual and other relationships of the target corporation. For federal income tax purposes, however, the purchaser may prefer to buy the assets of the business to obtain a cost basis for those assets, often referred to as a basis "step-up."[\[1\]](#)

Section 338(h)(10) of the Internal Revenue Code (the "Code") affords a corporate purchaser the convenience of a stock purchase with the tax benefits of an asset purchase by allowing the purchaser to elect to treat a stock purchase as an asset purchase for federal income tax purposes.[\[2\]](#) As you will see below, Section 338(h)(10) election is available only in limited situations. Similarly, Section 336(e) provides an election by the seller (or sellers) to achieve similar tax consequences as a section 338(h)(10) election. This guideline will briefly discuss the requirements of both elections and provide a simple comparison of them.

## Section 338(h)(10) Election

### When can an election be made?

- QSP - "qualified stock purchase".

The term "qualified stock purchase" means any transaction or series of transactions in which 80% of target stock is acquired by the purchasing corporation during the "12-month acquisition period."[\[3\]](#)

### Who can make the election?

- Buyer must be a corporation making a QSP.[\[4\]](#)
- Target must be a S-Corp or a member of an affiliated or consolidated group of corporations.[\[5\]](#)
- Buyer and Target (all shareholder of S-Corp) must jointly make the election. [\[6\]](#)

### How does the election impact the tax treatment?

- The transaction is treated as a taxable acquisition of 100% of the Target's asset for tax purpose.[\[7\]](#)
- Step up in the tax basis of the Target's assets to fair market value.
- Buyer gets more depreciation and/or amortization deductions.
- The purchase price allocated to goodwill can generally be amortized ratably over 15 years.
- Seller could incur increased tax liability in the following situations:
- The recognition of gain on ordinary income type assets and "1374 gain" from prior years as a

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C-Corp;[8]

- Tax basis of stock exceeding tax basis of assets;[9] or
- Additional state income taxes due to asset location

## How does the election impact the purchase agreement?

- Tax Reps
- When buying an S-Corp, Buyer needs confidence that Target is in fact an S-Corp, otherwise the 338(h)(10) election cannot be made
- Purchase Price Allocations
- S-Corp Sellers will want to avoid ordinary income from gain on assets such as inventory, accounts receivable, and depreciation recapture and may seek a gross-up for incremental tax liability

**Related Article:** [Franchise Tax Board Audits Sale of S Corp in 338\(h\)\(10\) Transaction](#)

## Section 336(e) Election

### When can an election be made?

- QSD - “qualified stock disposition”
- A QSD is any transaction or series of transactions in which 80% stock of Target is sold, exchanged, or distributed, or any combination thereof, by another domestic corporation or by S-Corp shareholders in a “disposition” during the “12-month disposition period.” [10]

### Who can make the election?

- Buyer can take the form of corporations, partnerships, LLCs or individuals; For the purpose of QSD, there can be multiple acquirers.
- Target must be S-Corp or domestic corporations that are members of a consolidated group.[11]
- Seller must be a domestic corporation or shareholders of S-Corp that makes a QSD.[12]
- Seller (or the S corporation shareholders) and Target must enter into a binding written agreement to make the election.[13]

### How does the election impact the tax treatment? (Same as section 338(h)(10) election)

- The transaction is treated as a taxable acquisition of 100% of the Target’s asset for tax purpose.[14]
- Step up in the tax basis of the Target’s assets to fair market value.
- Buyer gets more depreciation and/or amortization deductions.
- The purchase price allocated to goodwill can generally be amortized ratably over 15 years.
- Seller could incur increased tax liability in the following situations: The recognition of gain on ordinary income type assets and “1374 gain” from prior years as a C-Corp;[15] Tax basis of stock exceeding tax basis of assets.[16]

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## How does the election impact the purchase agreement?

- Tax Repts
- Buyer should address issues relating to the making, or not making, of a §336(e) election in the purchase agreement.

### Comparisons Chart

	<b>338(H)(10)</b>	<b>336(e)</b>
<b>Buyer</b>	Must be a single corporation (C or S); Can be domestic or foreign	Can be Partnership, LLC or individuals; can have multiple purchasers
<b>Target</b>	Domestic Corporation; Must be a member of the selling consolidated group, or a S corporation	Domestic Corporation or S-Corp
<b>SELLER</b>	N/A	Domestic corporation that makes a QSD of stock; or shareholders of S-Corp
<b>election</b>	Joint election by buyer and seller (all shareholders of target S corporation)	The Seller and Target must enter into a binding, written agreement to make the election
<b>triggering event</b>	QSP - Only sales and exchanges	