On March 3, 1970, M corporation, pursuant to a plan to acquire the assets of N corporation, purchased all of the stock of N corporation through a tender offer accepted by the shareholders of N. On April 1, 1970, N was liquidated and all of its property was distributed to M. M had in force an election to be taxed as a Subchapter S corporation. The Code provided the general rule that an election under subsection (a) made by a small business corporation, shall terminate if the corporation ceases to be a small business corporation. The Code provided that the term "small business corporation" means a domestic corporation which is not a member of an affiliated group as defined in section 1504.

In the instant case, M purchased the stock of N for the purpose of acquiring N's assets. While M, as a matter of form briefly owned N's stock, that ownership was merely a momentary control since it was the initial step of a plan to acquire the assets of N. Accordingly, although an affiliated group, as defined in section 1504, consisting of M and N came into existence when M completed its acquisition of at least 80 percent of the outstanding stock of N, for purposes of qualifying as an S corporation momentary control will not be considered as terminating M's election as a small business corporation since the liquidation of N under section 334(b)(2) occurred within 30 days of M's acquisition of N's stock. Note that in 1997, section 1361(b)(2) was amended to eliminate the affiliated group prohibition.

Compare Rev. Rul. 72-320, which holds that since one corporation never contemplated more than momentary control of a second corporation, such affiliation will not be considered as terminating the first corporation's election under Subchapter S.

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