

**§ 1.1244(d)-2**

section 1244, assuming the various requirements of such section are satisfied, and the remaining \$750 will be a capital loss.

*Example 2.* B owns property with a basis of \$20,000. The fair market value of the property unencumbered is \$15,000 but the property is subject to a \$2,000 mortgage. B transfers the encumbered property to a corporation for 100 shares of section 1244 stock in an exchange that qualifies under section 351. The basis of the shares, determined in accordance with section 358, is \$18,000 or \$180 per share, but solely for purposes of section 1244 the basis is \$13,000 (\$130 per share), which is its basis for purposes other than section 1244, reduced by \$5,000, the excess of the adjusted basis, immediately before the exchange, of the property transferred over its fair market value.

*Example 3.* C transfers business assets to a corporation for 100 shares of section 1244 stock in an exchange that qualifies under section 351. The assets transferred are as follows:

	Basis	Fair market value
Cash .....	\$10,000	\$10,000
Inventory .....	15,000	30,000
Depreciable property .....	50,000	20,000
Land .....	25,000	10,000
	100,000	70,000

The basis for the shares received by C is \$100,000, which is applied \$1,000 to each share. However, the basis of the shares for purposes of section 1244 is \$70,000 (\$700 per share), the basis for general purposes reduced by \$30,000, the excess of the aggregate adjusted basis of the property transferred over the aggregate fair market value of such property.

[T.D. 6495, 25 FR 9679, Oct. 8, 1960]

**§ 1.1244(d)-2 Increases in basis of section 1244 stock.**

(a) *In general.* If subsequent to the time of its issuance there is for any reason, including the operation of section 1376(a), an increase in the basis of section 1244 stock, such increase shall be treated as allocable to stock which is not section 1244 stock. Therefore, a loss on stock, the basis of which has been increased subsequent to its issuance, must be apportioned between the part that qualifies as section 1244 stock and the part that does not so qualify. Only the loss apportioned to the part that so qualifies may be treated as an ordinary loss pursuant to section 1244. The amount of loss apportioned to the part that qualifies is the amount which bears the same ratio to the total loss as the basis of the stock

which is treated as allocated to section 1244 stock bears to the total basis of the stock.

(b) *Example.* The provisions of paragraph (a) of this section may be illustrated by the following example:

*Example:* For \$10,000 a corporation issues 100 shares of section 1244 stock to X. X later contributes \$2,000 to the capital of the corporation and this increases the total basis of his 100 shares to \$12,000. Subsequently, he sells the 100 shares for \$9,000. Of the \$3,000 loss, \$2,500 is allocated to the portion of the stock that qualifies as section 1244 stock (\$10,000/\$12,000 of \$3,000), and the remaining \$500 is allocated to the portion of the stock that does not so qualify. Therefore, to the extent of \$2,500, the loss may be treated as an ordinary loss assuming the various requirements of section 1244 stock are satisfied. However, the remaining \$500 loss must be treated as a capital loss.

[T.D. 6495, 25 FR 9680, Oct. 8, 1960]

**§ 1.1244(d)-3 Stock dividend, recapitalizations, changes in name, etc.**

(a) *In general.* Section 1244(c)(1) provides that stock may not qualify for the benefits of section 1244 unless it is issued to the taxpayer for money or other property not including stock or securities. However, section 1244(d)(2) authorizes exceptions to this rule. The exceptions may apply in three situations: (1) The receipt of a stock dividend; (2) the exchange of stock for stock pursuant to a reorganization described in section 368(a)(1)(E); and (3) the exchange of stock for stock pursuant to a reorganization described in section 368(a)(1)(F).

(b) *Stock dividends.* (1) If common stock is received by an individual or partnership in a nontaxable distribution under section 305(a) made solely with respect to stock owned by such individual or partnership which meets the requirements of section 1244 stock determinable at the time of the distribution, then the common stock so received will also be treated as meeting such requirements. For purposes of this paragraph and paragraphs (c) and (d) of this section, the requirements of section 1244 stock determinable at the time of the distribution or exchange are all of the requirements of section 1244(c)(1) other than the one described in subparagraph (C) thereof, relating to the gross receipts test.