

§ 1.926(a)-1

26 CFR Ch. I (4-1-02 Edition)

R's direct labor	100.00
<hr/>	
Total	(550.00)
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Maximum combined taxable income	500.00
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Overall profit percentage (see example 4)	43.17%
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Overall profit percentage limitation (determined under paragraph (c)(2) of this section) (R's gross receipts from sale (\$1,050.00) times the overall profit percentage (43.17%))	453.29
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R's direct labor	200.00
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Total	(830.00)
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Maximum combined taxable income	220.00
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Overall profit percentage limitation calculation (determined under paragraph (c)(2) of this section):	
Gross receipts of R and F from all domestic and foreign sales	\$3,500.00
R's cost of goods sold	(1,880.00)
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Combined gross income	1,620.000
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Less:	
R's total expenses	259.00
F's total expenses	140.00
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Total	(399.00)
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Total taxable income from all sales computed on a full costing method	\$1,221.00
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Overall profit percentage (total taxable income (\$1,221) divided by total gross receipts (\$3,500))	34.89%
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Overall profit percentage limitation—overall profit percentage times R's gross receipts from the sale of export property (i.e., 34.89% times \$1,050)	\$366.35
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Since maximum combined taxable income (\$500) is greater than the overall profit percentage limitation (\$453.29), combined taxable income under marginal costing and for purposes of computing F's commission is limited to \$453.29. Under these marginal costing rules, F will have a profit attributable to the sales of \$104.26, i.e., 23% of combined taxable income (23% of \$453.29). Accordingly, the commission F receives from R is \$234.26, i.e., F's expenses (\$130) plus F's profit (\$104.26).

Example 6. Assume the same facts as in *Example 5*, except that F has expenses of \$140 and R's cost of goods sold for the export sale was \$900. R does not incur any direct selling expenses. Since cost of goods sold has increased by \$280, R's total gross income has been reduced from \$1,900 to \$1,620. For purposes of applying the combined taxable income method, R and F may compute their combined taxable income under the marginal costing rules as follows:

<i>Combined taxable income—full costing:</i>	
R's gross receipts from the sale of export property	\$1,050.00
R's cost of goods sold	(900.00)
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Combined gross income	150.00
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Less:	
F's expenses	140.00
Apportionment of R's G/A expenses \$50 x \$150/\$1,620	4.63
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Total	(144.63)
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Combined taxable income (loss)	5.37
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Maximum combined taxable income (determined under paragraph (b)(1) of this section):	
R's gross receipts from the sale of export property	\$1,050.00
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Less:	
R's direct materials	630.00

Since the overall profit percentage limitation (\$366.35) is greater than the maximum combined taxable income (\$220), combined taxable income under marginal costing and for purposes of computing F's commission is limited to \$220. Under these marginal costing rules, F will have a profit attributable to the sale of \$50.60, i.e., 23% of combined taxable income as determined under the marginal costing rules (23% of \$220). If the transaction occurred in 1987, F's profit would be limited, however, by paragraph (b)(4) of this section to the full costing combined taxable income of \$5.37.

[T.D. 8126, 52 FR 6455, Mar. 3, 1987, as amended by T.D. 8764, 63 FR 10306, Mar. 3, 1998; T.D. 8944, 66 FR 13429, Mar. 6, 2001]

§ 1.926(a)-1 Distributions to shareholders.

(a) *Treatment of distributions.* [Reserved] For guidance, see § 1.926(a)-1T(a).

(b) *Order of distribution*—(1) *In general*—(i) *Distributions by a FSC received by a shareholder in a taxable year of the shareholder beginning before January 1, 1990.* Any actual distribution to a shareholder by a FSC (all references to a FSC in this section shall include a small FSC and a former FSC) that is received by the shareholder in a taxable year of the shareholder beginning before January 1, 1990, and made out of earnings and profits shall be treated as made in the following order, to the extent thereof—

(A) Out of earnings and profits attributable to exempt foreign trade income determined solely because of operation of section 923(a)(4),

(B) Out of earnings and profits attributable to other exempt foreign trade income,

(C) Out of earnings and profits attributable to non-exempt foreign trade income determined under either of the administrative pricing methods of section 925(a)(1) or (2),

(D) Out of earnings and profits attributable to section 923(a)(2) non-exempt income, and

(E) Out of other earnings and profits.

(ii) *Distributions by a FSC received by a shareholder in a taxable year of the shareholder beginning after December 31, 1989.* Any actual distribution to a shareholder by a FSC that is received by the shareholder in a taxable year beginning after December 31, 1989, and that is made out of earnings and profits shall be treated as made in the following order, to the extent thereof—

(A) Out of earnings and profits attributable to exempt foreign trade income determined solely because of the operation of section 923(a)(4),

(B) Out of earnings and profits attributable to foreign trade income (other than exempt foreign trade income determined solely because of the operation of section 923(a)(4)) allocable to the marketing of agricultural or horticultural products (or the providing of related services) by a qualified cooperative which is a shareholder of the FSC,

(C) Out of earnings and profits attributable to non-exempt foreign trade income and other exempt foreign trade income determined under either of the administrative pricing methods of sec-

tion 925(a)(1) and (2). Distributions out of this classification will be made on a pro rata basis so that 15/23 (16/23 with regard to distribution to a non-corporate shareholder) of each distribution will be out of earnings and profits attributable to exempt foreign trade income and the remainder will be out of earnings and profits attributable to non-exempt foreign trade income. To the extent the distributions are out of earnings and profits attributable to the disposition of, or services related to, military property, 7.5/23 (8/23 with regard to distributions to a non-corporate shareholder) of each distribution will be out of earnings and profits attributable to exempt foreign trade income and the remainder will be out of earnings and profits attributable to non-exempt foreign trade income,

(D) Out of earnings and profits attributable to other exempt foreign trade income determined under the transfer pricing method of section 925(a)(3),

(E) Out of earnings and profits attributable to section 923(a)(2) non-exempt income,

(F) Out of earnings and profits attributable to effectively connected income, as defined in section 245(c)(4)(B), and

(G) Out of other earnings and profits.

(2) *Determination of earnings and profits.* [Reserved] For guidance, see § 1.926(a)-1T(b)(1).

(c) *Definition of “former FSC”.* [Reserved] For guidance, see § 1.926(a)-1T(c).

(d) *Personal holding company income.* [Reserved] For guidance, see § 1.926(a)-1T(d).

(e) *Sale of stock if section 1248 applies.* [Reserved] For guidance, see § 1.926(a)-1T(e).

[T.D. 8340, 56 FR 11093, Mar. 15, 1991]

§ 1.926(a)-1T Temporary regulations; distributions to shareholders.

(a) *Treatment of distributions.* Any distribution by a FSC (or former FSC) to its shareholder with respect to its stock will be includible in the shareholder's gross income in accordance with the provisions of section 301. (Any further reference to a FSC in this section shall include a small FSC unless indicated otherwise.) See section 245(c)