

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.

(2) If, however, such stock dividend is received by such individual or partnership partly with respect to stock meeting the requirements of section 1244 stock determinable at the time of the distribution, and partly with respect to stock not meeting such requirements, then only part of the stock received as a stock dividend will be treated as meeting such requirements. Assuming all the shares with respect to which the dividend is received have equal rights to dividends, such part is the number of shares which bears the same ratio to the total number of shares received as the number of shares owned immediately before the stock dividend which meets such qualifications bears to the total number of shares with respect to

which the stock dividend is received. In determining the basis of shares received in the stock dividend and of the shares held before the stock dividend, section 307 shall apply as if two separate nontaxable stock dividends were made, one with respect to the shares that meet the requirements and the other with respect to shares that do not meet the requirements.

(3) The provisions of subparagraphs (1) and (2) of this paragraph may be illustrated by the following examples:

Example 1. Corporation X issues 100 shares of its common stock to B for \$1,000. Subsequently, in a nontaxable stock dividend B receives 5 more shares of common stock of Corporation X. If the 100 shares meet all the requirements of section 1244 stock determinable at the time of the distribution of the stock dividend, the 5 additional shares shall also be treated as meeting such requirements.

Example 2. In 1959, Corporation Y issues 100 shares of its common stock to C for \$1,000 and these shares meet the requirements of section 1244 stock determinable at the time of the issuance. In 1960, C purchases an additional 200 shares of such stock from another shareholder for \$3,000; however, these shares do not meet the requirements of section 1244 stock because they were not originally issued to C by the corporation. In 1961, C receives 15 shares of Corporation Y common stock as a stock dividend. Of the shares received, 5 shares, the number received with respect to the 100 shares of stock which met the requirements of section 1244 at the time of the distribution, i.e., $100/300 \times 15$, shall also be treated as meeting such requirements. The remaining 10 shares do not meet such requirements as they are not received with respect to section 1244 stock. The basis of such 5 shares is determined by applying section 307 as if the 5 shares were received as a separate stock dividend made solely with respect to shares that meet the requirements of section 1244 stock at the time of the distribution. Thus, the basis of the 5 shares is \$47.61 ($\frac{5}{105}$ of \$1,000).

(c) *Recapitalizations.* (1) If, pursuant to a recapitalization described in section 368(a)(1)(E), common stock of a corporation is received by an individual or partnership in exchange for stock of such corporation meeting the requirements of section 1244 stock determinable at the time of the exchange, such common stock shall be treated as meeting such requirements.

(2) If common stock is received pursuant to such a recapitalization partly

in exchange for stock meeting the requirements of section 1244 stock determinable at the time of the exchange and partly in exchange for stock not meeting such requirements, then only part of such common stock will be treated as meeting such requirements. Such part is the number of shares which bears the same ratio to the total number of shares of common stock so received as the basis of the shares transferred which meet such requirements bears to the basis of all the shares transferred for such common stock. The basis allocable, pursuant to section 358, to the common stock which is treated as meeting such requirements is limited to the basis of stock that meets such requirements transferred in the exchange.

(3) The provisions of subparagraphs (1) and (2) of this paragraph may be illustrated by the following examples:

Example 3. A owns 500 shares of voting common stock of Corporation X. Corporation X revises its capital structure to provide for two classes of common stock: Class A voting and Class B nonvoting. In a recapitalization described in subparagraph (E) of section 368(a)(1). A exchanges his 500 shares for 750 shares of Class B nonvoting stock. If the 500 shares meet all the requirements of section 1244 stock determinable at the time of the exchange, the 750 shares received in the exchange are treated as meeting such requirements.

Example 4. B owns 500 shares of common stock of Corporation X with a basis of \$5,000, and 100 shares of preferred stock of that corporation with a basis of \$2,500. Pursuant to a recapitalization described in section 368(a)(1)(E), B exchanges all of his shares for 900 shares of common stock of Corporation X. The 500 common shares meet the requirements of section 1244 stock determinable at the time of the exchange, but the 100 preferred shares do not meet such requirements since only common stock may qualify. Of the 900 common shares received, 600 shares (\$5,000/\$7,500×900 shares) are treated as meeting the requirements of section 1244 stock at the time of the exchange, because they are deemed to be received in exchange for the 500 common shares which met such requirements. The remaining 300 shares do not meet such requirements as they are not deemed to be received in exchange for section 1244 stock. The basis of the 600 shares is \$5,000, the basis of the relinquished shares meeting the requirements of section 1244.

(d) *Change of name, etc.* (1) If, pursuant to a reorganization described in

section 368(a)(1)(F), common stock of a successor corporation is received by an individual or partnership in exchange for stock of the predecessor corporation meeting the requirements of section 1244 stock determinable at the time of the exchange, such common stock shall be treated as meeting such requirements. If common stock is received pursuant to such a reorganization partly in exchange for stock meeting the requirements of section 1244 stock determinable at the time of the exchange and partly in exchange for stock not meeting such requirements, the principles of paragraph (c)(2) of this section apply in determining the number of shares received which are treated as meeting the requirements of section 1244 stock and the basis of those shares.

(2) For purposes of paragraphs (1)(C) and (3)(A) of section 1244(c), a successor corporation in a reorganization described in section 368(a)(1)(F) shall be treated as the same corporation as its predecessor.

[T.D. 7779, 46 FR 29472, June 2, 1981]

§ 1.1244(d)-4 Net operating loss deduction.

(a) *General rule.* For purpose of section 172, relating to the net operating loss deduction, any amount of loss that is treated as an ordinary loss under section 1244 (taking into account the annual dollar limitation of that section) shall be treated as attributable to the trade or business of the taxpayer. Therefore, this loss is allowable in determining the taxpayer's net operating loss for a taxable year and is not subject to the application of section 172(d)(4), relating to nonbusiness deductions. A taxpayer may deduct the maximum of ordinary loss permitted under section 1244(b) even though all or a portion of the taxpayer's net operating loss carryback or carryover for the taxable year was, when incurred, a loss on section 1244 stock.

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

Example: A, a single individual, computes a net operating loss of \$15,000 for 1980 in accordance with the rules of § 1.172-3, relating to net operating loss in case of a taxpayer other than a corporation. Included within