

Internal Revenue Service, Treasury

§ 1.301-1

CORPORATE DISTRIBUTIONS AND
ADJUSTMENTS

DISTRIBUTIONS BY CORPORATIONS

EFFECTS ON RECIPIENTS

§ 1.301-1 Rules applicable with respect to distributions of money and other property.

(a) *General.* Section 301 provides the general rule for treatment of distributions on or after June 22, 1954, of property by a corporation to a shareholder with respect to its stock. The term *property* is defined in section 317(a). Such distributions, except as otherwise provided in this chapter, shall be treated as provided in section 301(c). Under section 301(c), distributions may be included in gross income, applied against and reduce the adjusted basis of the stock, treated as gain from the sale or exchange of property, or (in the case of certain distributions out of increase in value accrued before March 1, 1913) may be exempt from tax. The amount of the distributions to which section 301 applies is determined in accordance with the provisions of section 301(b). The basis of property received in a distribution to which section 301 applies is determined in accordance with the provisions of section 301(d). Accordingly, except as otherwise provided in this chapter, a distribution on or after June 22, 1954, of property by a corporation to a shareholder with respect to its stock shall be included in gross income to the extent the amount distributed is considered a dividend under section 316. For examples of distributions treated otherwise, see sections 116, 301(c)(2), 301(c)(3)(B), 301(e), 302(b), 303, and 305. See also part II (relating to distributions in partial or complete liquidation), part III (relating to corporate organizations and reorganizations), and part IV (relating to insolvency reorganizations), subchapter C, chapter 1 of the Code.

(b) *Time of inclusion in gross income and of determination of fair market value.* A distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands. However, if such distribution is a distribution other than in cash, the

fair market value of the property shall be determined as of the date of distribution without regard to whether such date is the same as that on which the distribution is includible in gross income. For example, if a corporation distributes a taxable dividend in property (the adjusted basis of which exceeds its fair market value on December 31, 1955) on December 31, 1955, which is received by, or unqualifiedly made subject to the demand of, its shareholders on January 2, 1956, the amount to be included in the gross income of the shareholders will be the fair market value of such property on December 31, 1955, although such amount will not be includible in the gross income of the shareholders until January 2, 1956.

(c) *Application of section to shareholders.* Section 301 is not applicable to an amount paid by a corporation to a shareholder unless the amount is paid to the shareholder in his capacity as such.

(d) *Distributions to corporate shareholders.* (1) If the shareholder is a corporation, the amount of any distribution to be taken into account under section 301(c) shall be:

(i) The amount of money distributed,

(ii) An amount equal to the fair market value of any property distributed which consists of any obligations of the distributing corporation, stock of the distributing corporation treated as property under section 305(b), or rights to acquire such stock treated as property under section 305(b), plus

(iii) In the case of a distribution not described in subdivision (iv) of this subparagraph, an amount equal to (a) the fair market value of any other property distributed or, if lesser, (b) the adjusted basis of such other property in the hands of the distributing corporation (determined immediately before the distribution and increased for any gain recognized to the distributing corporation under section 311 (b), (c), or (d), or under section 341(f), 617(d), 1245(a), 1250(a), 1251(c), 1252(a), or 1254(a)), or

(iv) In the case of a distribution made after November 8, 1971, to a shareholder which is a foreign corporation, an amount equal to the fair market value of any other property distributed, but only if the distribution received by

such shareholder is not effectively connected for the taxable year with the conduct of a trade or business in the United States by such shareholder.

(2) In the case of a distribution the amount of which is determined by reference to the adjusted basis described in subparagraph (1)(iii)(b) of this paragraph:

(i) That portion of the distribution which is a dividend under section 301(c)(1) may not exceed such adjusted basis, or

(ii) If the distribution is not out of earnings and profits, the amount of the reduction in basis of the shareholder's stock, and the amount of any gain resulting from such distribution, are to be determined by reference to such adjusted basis of the property which is distributed.

(3) Notwithstanding paragraph (d)(1)(iii), if a distribution of property described in such paragraph is made after December 31, 1962, by a foreign corporation to a shareholder which is a corporation, the amount of the distribution to be taken into account under section 301(c) shall be determined under section 301(b)(1)(C) and paragraph (n) of this section.

(e) *Adjusted basis.* In determining the adjusted basis of property distributed in the hands of the distributing corporation immediately before the distribution for purposes of section 301(b)(1)(B)(ii), (b)(1)(C)(i), and (d)(2)(B), the basis to be used shall be the basis for determining gain upon a sale or exchange.

(f) *Examples.* The application of this section (except paragraph (n)) may be illustrated by the following examples:

Example (1). On January 1, 1955, A, an individual owned all of the stock of Corporation M with an adjusted basis of \$2,000. During 1955, A received distributions from Corporation M totaling \$30,000, consisting of \$10,000 in cash and listed securities having a basis in the hands of Corporation M and a fair market value on the date distributed of \$20,000. Corporation M's taxable year is the calendar year. As of December 31, 1954, Corporation M had earnings and profits accumulated after February 28, 1913, in the amount of \$26,000, and it had no earnings and profits and no deficit for 1955. Of the \$30,000 received by A, \$26,000 will be treated as an ordinary dividend; the remaining \$4,000 will be applied against the adjusted basis of his stock; the \$2,000 in excess of the adjusted basis of his

stock will either be treated as gain from the sale or exchange of property (under section 301(c)(3)(A)) or, if out of increase in value accrued before March 1, 1913, will (under section 301(c)(3)(B)) be exempt from tax. If A subsequently sells his stock in Corporation M, the basis for determining gain or loss on the sale will be zero.

Example (2). The facts are the same as in Example 1 with the exceptions that the shareholder of Corporation M is Corporation W and that the securities which were distributed had an adjusted basis to Corporation M of \$15,000. The distribution received by Corporation W totals \$25,000 consisting of \$10,000 in cash and securities with an adjusted basis of \$15,000. The total \$25,000 will be treated as a dividend to Corporation W since the earnings and profits of Corporation M (\$26,000) are in excess of the amount of the distribution.

Example (3). Corporation X owns timber land which it acquired prior to March 1, 1913, at a cost of \$50,000 with \$5,000 allocated as the separate cost of the land. On March 1, 1913, this property had a fair market value of \$150,000 of which \$135,000 was attributable to the timber and \$15,000 to the land. All of the timber was cut prior to 1955 and the full appreciation in the value thereof, \$90,000 (\$135,000 - \$45,000), realized through depletion allowances based on March 1, 1913, value. None of this surplus from realized appreciation had been distributed. In 1955, Corporation X sold the land for \$20,000 thereby realizing a gain of \$15,000. Of this gain, \$10,000 is due to realized appreciation in value which accrued before March 1, 1913 (\$15,000 - \$5,000). Of the gain of \$15,000, \$5,000 is taxable. Therefore, at December 31, 1955, Corporation X had a surplus from realized appreciation in the amount of \$100,000. It had no accumulated earnings and profits and no deficit at January 1, 1955. The net earnings for 1955 (including the \$5,000 gain on the sale of the land) were \$20,000. During 1955, Corporation X distributed \$75,000 to its stockholders. Of this amount, \$20,000 will be treated as a dividend. The remaining \$55,000, which is a distribution of realized appreciation, will be applied against and reduce the adjusted basis of the shareholders' stock. If any part of the \$55,000 is in excess of the adjusted basis of a shareholder's stock, such part will be exempt from tax.

(h) *Basis.* The basis of property received in the distribution to which section 301 applies shall be—

(1) If the shareholder is not a corporation, the fair market value of such property;

(2) If the shareholder is a corporation—

(i) In the case of a distribution of the obligations of the distributing corporation or of the stock of such corporation or rights to acquire such stock (if such stock or rights are treated as property under section 305(b)), the fair market value of such obligations, stock, or rights;

(ii) In the case of the distribution of any other property, except as provided in subdivision (iii) (relating to certain distributions by a foreign corporation) or subdivision (iv) (relating to certain distributions to foreign corporate distributees) of this subparagraph, whichever of the following is the lesser—

(a) The fair market value of such property; or

(b) The adjusted basis (in the hands of the distributing corporation immediately before the distribution) of such property increased in the amount of gain to the distributing corporation which is recognized under section 311(b) (relating to distributions of LIFO inventory), section 311(c) (relating to distributions of property subject to liabilities in excess of basis), section 311(d) (relating to appreciated property used to redeem stock), section 341(f) (relating to certain sales of stock of consenting corporations), section 617(d) (relating to gain from dispositions of certain mining property), section 1245(a) or 1250(a) (relating to gain from dispositions of certain depreciable property), section 1251(c) (relating to gain from disposition of farm recapture property), section 1252(a) (relating to gain from disposition of farm land), or 1254(a) (relating to gain from disposition of interest in natural resource recapture property);

(iii) In the case of the distribution by a foreign corporation of any other property after December 31, 1962, in a distribution not described in subdivision (iv) of this subparagraph, the amount determined under paragraph (n) of this section;

(iv) In the case of the distribution of any other property made after November 8, 1971, to a shareholder which is a foreign corporation, the fair market value of such property, but only if the distribution received by such shareholder is not effectively connected for the taxable year with the conduct of a

trade or business in the United States by such shareholder.

(i) [Reserved]

(j) *Transfers for less than fair market value.* If property is transferred by a corporation to a shareholder which is not a corporation for an amount less than its fair market value in a sale or exchange, such shareholder shall be treated as having received a distribution to which section 301 applies. In such case, the amount of the distribution shall be the difference between the amount paid for the property and its fair market value. If property is transferred in a sale or exchange by a corporation to a shareholder which is a corporation, for an amount less than its fair market value and also less than its adjusted basis, such shareholder shall be treated as having received a distribution to which section 301 applies, and—

(1) Where the fair market value of the property equals or exceeds its adjusted basis in the hands of the distributing corporation the amount of the distribution shall be the excess of the adjusted basis (increased by the amount of gain recognized under section 311 (b), (c), or (d), or under section 341(f), 617(d), 1245(a), 1250(a), 1251(c), 1252(a), or 1254(a) to the distributing corporation) over the amount paid for the property;

(2) Where the fair market value of the property is less than its adjusted basis in the hands of the distributing corporation, the amount of the distribution shall be the excess of such fair market value over the amount paid for the property. If property is transferred in a sale or exchange after December 31, 1962, by a foreign corporation to a shareholder which is a corporation for an amount less than the amount which would have been computed under paragraph (n) of this section if such property had been received in a distribution to which section 301 applied, such shareholder shall be treated as having received a distribution to which section 301 applies, and the amount of the distribution shall be the excess of the amount which would have been computed under paragraph (n) of this section with respect to such property over the amount paid for the property. In all cases, the earnings and

profits of the distributing corporation shall be decreased by the excess of the basis of the property in the hands of the distributing corporation over the amount received therefor. In computing gain or loss from the subsequent sale of such property, its basis shall be the amount paid for the property increased by the amount of the distribution.

If property is transferred in a sale or exchange after December 31, 1962, by a foreign corporation to a shareholder which is a corporation for an amount less than the amount which would have been computed under paragraph (n) of this section if such property had been received in a distribution to which section 301 applied, such shareholder shall be treated as having received a distribution to which section 301 applies, and the amount of the distribution shall be the excess of the amount which would have been computed under paragraph (n) of this section with respect to such property over the amount paid for the property. Notwithstanding the preceding provisions of this paragraph, if property is transferred in a sale or exchange after November 8, 1971, by a corporation to a shareholder which is a foreign corporation, for an amount less than its fair market value, and if paragraph (d)(1)(iv) of this section would apply if such property were received in a distribution to which section 301 applies, such shareholder shall be treated as having received a distribution to which section 301 applies and the amount of the distribution shall be the difference between the amount paid for the property and its fair market value. In all cases, the earnings and profits of the distributing corporation shall be decreased by the excess of the basis of the property in the hands of the distributing corporation over the amount received therefor. In computing gain or loss from the subsequent sale of such property, its basis shall be the amount paid for the property increased by the amount of the distribution.

(k) *Application of rule respecting transfers for less than fair market value.* The application of paragraph (j) of this section may be illustrated by the following examples:

Example (1). On January 1, 1955, A, an individual shareholder of corporation X, purchased property from that corporation for \$20. The fair market value of such property was \$100, and its basis in the hands of corporation X was \$25. The amount of the distribution determined under section 301(b) is \$80. If A were a corporation, the amount of the distribution would be \$5 (assuming that sections 311 (b) and (c), 1245(a), and 1250(a) do not apply), the excess of the basis of the property in the hands of corporation X over the amount received therefor. The basis of such property to corporation A would be \$25. If the basis of the property in the hands of corporation X were \$10, the corporate shareholder, A, would not receive a distribution. The basis of such property to corporation A would be \$20. Whether or not A is a corporation, the excess of the amount paid over the basis of the property in the hands of corporation X (\$20 over \$10) would be a taxable gain to corporation X.

Example (2). On January 1, 1963, corporation A, which is a shareholder of corporation B (a foreign corporation engaged in business within the United States), purchased one share of corporation X stock from B for \$20. The fair market value of the share was \$100, and its adjusted basis in the hands of B was \$25. Assume that if the share of corporation X stock had been received by A in a distribution to which section 301 applied, the amount of the distribution under paragraph (n) of this section would have been \$55. The amount of the distribution under section 301 is \$35, i.e., \$55 (amount computed under paragraph (n) of this section) minus \$20 (amount paid for the property). The basis of such property to A is \$55.

(1) *Transactions treated as distributions.* A distribution to shareholders with respect to their stock is within the terms of section 301 although it takes place at the same time as another transaction if the distribution is in substance a separate transaction whether or not connected in a formal sense. This is most likely to occur in the case of a recapitalization, a reincorporation, or a merger of a corporation with a newly organized corporation having substantially no property. For example, if a corporation having only common stock outstanding, exchanges one share of newly issued common stock and one bond in the principal amount of \$10 for each share of outstanding common stock, the distribution of the bonds will be a distribution of property (to the extent of their fair market value) to which

section 301 applies, even though the exchange of common stock for common stock may be pursuant to a plan of reorganization under the terms of section 368(a)(1)(E) (recapitalization) and even though the exchange of common stock for common stock may be tax free by virtue of section 354.

(m) *Cancellation of indebtedness.* The cancellation of indebtedness of a shareholder by a corporation shall be treated as a distribution of property.

(n) [Reserved]

(o) *Distributions of certain property by DISC's to corporate shareholders.* See § 1.997-1 for the rule that if a corporation which is a DISC or former DISC (as defined in section 992(a)(1) or (3) as the case may be) makes a distribution of property (other than money and other than the obligations of the DISC or former DISC) out of accumulated DISC income (as defined in section 996(f)(1)) or previously taxed income (as defined in section 996(f)(2)), such distribution of property shall be treated as if it were made to an individual and that the basis of the property distributed, in the hands of the recipient corporation, shall be determined as if such property were distributed to an individual.

(p) *Cross references.* For certain rules relating to adjustments to earnings and profits and for determining the extent to which a distribution is a dividend, see sections 312 and 316 and regulations thereunder.

(q) *Split-dollar and other life insurance arrangements—(1) Split-dollar life insurance arrangements—(i) Distribution of economic benefits.* The provision by a corporation to its shareholder pursuant to a split-dollar life insurance arrangement, as defined in § 1.61-22(b)(1) or (2), of economic benefits described in § 1.61-22(d) or of amounts described in § 1.61-22(e) is treated as a distribution of property, the amount of which is determined under § 1.61-22(d) and (e), respectively.

(ii) *Distribution of entire contract or undivided interest therein.* A transfer (within the meaning of § 1.61-22(c)(3)) of the ownership of a life insurance contract (or an undivided interest therein) that is part of a split-dollar life insurance arrangement is a distribution of

property, the amount of which is determined pursuant to § 1.61-22(g)(1) and (2).

(2) *Other life insurance arrangements.* A payment by a corporation on behalf of a shareholder of premiums on a life insurance contract or an undivided interest therein that is owned by the shareholder constitutes a distribution of property, even if such payment is not part of a split-dollar life insurance arrangement under § 1.61-22(b).

(3) *When distribution is made—(i) In general.* Except as provided in paragraph (q)(3)(ii) of this section, paragraph (b) of this section shall apply to determine when a distribution described in paragraph (q)(1) or (2) of this section is taken into account by a shareholder.

(ii) *Exception.* Notwithstanding paragraph (b) of this section, a distribution described in paragraph (q)(1)(ii) of this section shall be treated as made by a corporation to its shareholder at the time that the life insurance contract, or an undivided interest therein, is transferred (within the meaning of § 1.61-22(c)(3)) to the shareholder.

(4) *Effective date—(i) General rule.* This paragraph (q) applies to split-dollar and other life insurance arrangements entered into after September 17, 2003. For purposes of this paragraph (q)(4), a split-dollar life insurance arrangement is entered into as determined under § 1.61-22(j)(1)(ii).

(ii) *Modified arrangements treated as new arrangements.* If a split-dollar life insurance arrangement entered into on or before September 17, 2003 is materially modified (within the meaning of § 1.61-22(j)(2)) after September 17, 2003, the arrangement is treated as a new arrangement entered into on the date of the modification.

[T.D. 6500, 25 FR 11607, Nov. 26, 1960, as amended by T.D. 6752, 29 FR 12701, Sept. 9, 1964; T.D. 7084, 36 FR 267, Jan. 8, 1971; T.D. 7209, 37 FR 20800, Oct. 5, 1972; 38 FR 20824, Aug. 3, 1973; 38 FR 32794, Nov. 28, 1973; T.D. 7556, 44 FR 1376, Jan. 5, 1979; T.D. 8474, 58 FR 25557, Apr. 27, 1993; T.D. 8586, 60 FR 2500, Jan. 10, 1995; T.D. 8924, 66 FR 725, Jan. 4, 2001; T.D. 8964, Sept. 27, 2001, 66 FR 49276; T.D. 9092, 68 FR 54352, Sept. 17, 2003]

§ 1.302-1 General.

(a) Under section 302(d), unless otherwise provided in subchapter C, chapter