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section 34 (4 percent of \$200, the amount of the dividends received after July 31, 1954, that is, \$100 received on September 1, 1954, and \$100 received on December 1, 1954).

(b) *Tax credit.* The credit is used to reduce the tax imposed by Subtitle A of the Code, including the alternative tax under section 1201 in the case of capital gains and the self-employment tax under chapter 2 of the Code; however, it may not be used by the taxpayer as a credit against penalties, additions to the tax, or interest on delinquent taxes.

(c) *Joint return of husband and wife.*

(1) In the case of a joint return the credit is determined on the basis of the dividends received by both the husband and wife after taking into account the exclusion allowed by section 116. See § 1.116-1. The credit is allowable in the case of a joint return on account of the dividends received by each spouse without regard to whether the spouse would be liable for the tax imposed by Subtitle A if the joint return had not been filed. However, the limitations on amount of credit in section 34(b) are determined by reference to the tax and the credit under section 33 required to be shown on the joint return and to the combined taxable income of husband and wife. For this purpose, it makes no difference whether the tax, the credit, or the taxable income is attributable to one or the other spouse. If both the husband and wife are entitled to the credit, their combined credit shall not exceed the amount so computed.

(2) The application of subparagraph (1) of this paragraph may be illustrated by the following examples:

Example 1. H and W, husband and wife, make a joint return for the calendar year 1954. The only dividend received by either of them during the year is a dividend received by H on September 1 in the amount of \$400. Subject to the limitations of section 34(b), the credit amounts to \$14 (4 percent of \$350, the dividends included in gross income after allowance of the exclusion of \$50 under section 116).

Example 2. The facts are the same as in example (1) except that W also received a dividend on September 1 of \$30. Since this dividend (being less than the maximum amount allowable as an exclusion under section 116(a)) is excluded from W's gross income, it does not affect the computation of the tax credit and the tax credit is the same as in example (1).

Example 3. H and W, husband and wife, make a joint return for the calendar year 1954. H and W each received a \$400 dividend on September 1, 1954, and these were the only dividends received by them in 1954. Since H and W may each exclude \$50 of the dividends received by them, \$700 of dividend income is included in gross income. Subject to the limitations in section 34(b), the credit against the tax of H and W amounts to \$28 (4 percent of \$700).

(d) *Individuals receiving dividends.* Where two or more persons hold stock as tenants in common, as joint tenants, or as tenants by the entirety, the dividends received with respect to such stock shall be considered as being received by each tenant to the extent that he is entitled under local law to a share of such dividends. Where dividends constitute community property under local law each spouse shall be considered as receiving one-half of such dividends.

(e) *Time dividends are received.* In cases where it is necessary to determine the time of receipt of dividends, the rules established to determine in which taxable year dividends must be included in gross income apply, including the rules relating to constructive receipt. See section 451 and regulations thereunder.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6777, 29 FR 17806, Dec. 16, 1964]

§ 1.34-2 Limitations on amount of credit.

(a) Under section 34(b) the credit may not exceed the lesser of either—

(1) The amount of the tax imposed by chapter 1 of the Code for the taxable year reduced by the foreign tax credit allowable under section 33, or

(2) Whichever of the following is applicable:

(i) In the case of a taxable year ending before January 1, 1955, or beginning after December 31, 1963, 2 percent of the taxable income for such taxable year;

(ii) In the case of a taxable year ending after December 31, 1954, and beginning before January 1, 1964, 4 percent of the taxable income for such taxable year. In the case of a taxpayer who computes his tax under section 3 or

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who uses the standard deduction provided by section 141, the taxable income for the taxable year is the adjusted gross income for the taxable year reduced by the standard deduction prescribed in section 141 and the deductions for personal exemptions provided in section 151. Where the alternative tax on capital gains is imposed under section 1201(b), the taxable income for such taxable year is the taxable income as defined in section 63, which includes 50 percent of the excess of net long-term capital gain over net short-term capital loss.

(b) The application of the limitations in paragraph (a) of this section may be illustrated by the following example:

Example. Assume the following facts in the case of an individual whose taxable year is the calendar year:

1954

Computation of tax liability without regard to the dividend received credit:

(1) Gross income	\$7,500
(2) Deductions	2,900
(3) Taxable income	4,600
(4) Income tax liability	996
(5) Foreign tax credit	16
(6) Income tax liability minus foreign tax credit ..	980

Computation of limitation under section 34(b)(1):

(7) Dividends for which credit is allowable	\$2,500
(8) Dividends received credit under section 34(a); (2,500×0.04)	100
(9) Dividends received credit, as limited by section 34(b)(1); (item (6) or item (8) whichever is lesser)	100

Computation of limitation under section 34(b)(2):

(10) Taxable income	\$4,600
(11) Dividends received credit under section 34(b)(2); (4,600×0.02)	92

Dividends received credit allowable:
Item (6), item (9), or item (11), whichever is lesser

	\$92
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1955

Computation of tax liability without regard to the dividend received credit:

(12) Gross income	\$7,500
(13) Deductions	2,900
(14) Taxable income	4,600
(15) Income tax liability	996
(16) Foreign tax credit	816
(17) Income tax liability minus foreign tax credit ..	180

Computation of limitation under section 34(b)(1):

(18) Dividends for which credit is allowable	\$2,500
(19) Dividends received credit under section 34(a); (2,500×0.04)	100

(20) Dividends received credit as limited by section 34(b)(1); (item (17) or item (19) whichever is lesser)

	100
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Computation of limitation under section 34(b)(2):

(21) Taxable income	\$4,600
(22) Dividends received credit under section 34(b)(2); (4,600×0.04)	184

Dividends received credit allowable:
Item (17), item (19), or item (22), whichever is lesser

	\$100
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[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6777, 29 FR 17807, Dec. 16, 1964]

§ 1.34-3 Dividends to which the credit and exclusion apply.

(a) *General rule.* The credit under section 34 and the exclusion under section 116 apply only to distributions of property defined as dividends by section 316. Thus, the credit and the exclusion are not allowed with respect to patronage dividends paid by either exempt or taxable farm cooperatives. Nor are they allowed for distributions to non-stockholding policyholders by an insurance company having shares of stock or for any distribution by a mutual insurance company. See paragraph (b) of this section for an additional restriction with respect to stock life insurance companies. The credit and the exclusion are, however, allowed with respect to dividends paid on capital stock by nonexempt cooperatives and with respect to dividends paid on capital stock by building and loan associations. However, see paragraph (b) of this section with respect to so-called dividends paid by building and loan associations ineligible for the credit and the exclusion. The credit and the exclusion are allowed with respect to distributions from any organization taxed as a corporation if the distribution falls within the definition of a dividend in section 316.

(b) *Dividends from certain corporations.* (1) Section 34 (c) and (d) contains further restrictions on the type of distributions which are treated as dividends for purposes of the credit and exclusion. Thus, no credit or exclusion is applicable with respect to dividends received from a corporation organized under the China Trade Act, 1922; from stock life insurance companies before January 1, 1959, in taxable years ending