

§ 1.1552-1

26 CFR Ch. I (4-1-04 Edition)

considerations which prompted the transfer.

[T.D. 6911, 32 FR 3214, Feb. 24, 1967, as amended by T.D. 7376, 40 FR 42745, Sept. 16, 1975]

§ 1.1552-1 Earnings and profits.

(a) *General rule.* For the purpose of determining the earnings and profits of each member of an affiliated group which is required to be included in a consolidated return for such group filed for a taxable year beginning after December 31, 1953, and ending after August 16, 1954, the tax liability of the group shall be allocated among the members of the group in accordance with one of the following methods, pursuant to an election under paragraph (c) of this section:

(1)(i) The tax liability of the group shall be apportioned among the members of the group in accordance with the ratio which that portion of the consolidated taxable income attributable to each member of the group having taxable income bears to the consolidated taxable income.

(ii) For consolidated return years beginning after December 31, 1965, a member's portion of the tax liability of the group under the method of allocation provided by subdivision (i) of this subparagraph is an amount equal to the tax liability of the group multiplied by a fraction, the numerator of which is the taxable income of such member, and the denominator of which is the sum of the taxable incomes of all the members. For purposes of this subdivision the taxable income of a member shall be the separate taxable income determined under § 1.1502-12, adjusted for the following items taken into account in the computation of consolidated taxable income:

(a) The portion of the consolidated net operating loss deduction, the consolidated charitable contributions deduction, the consolidated dividends received deduction, the consolidated section 247 deduction, the consolidated section 582(c) net loss, and the consolidated section 922 deduction, attributable to such member;

(b) Such member's capital gain net income (net capital gain for taxable years beginning before January 1, 1977) (determined without regard to any net

capital loss carryover attributable to such member);

(c) Such member's net capital loss and section 1231 net loss, reduced by the portion of the consolidated net capital loss attributable to such member; and

(d) The portion of any consolidated net capital loss carryover attributable to such member which is absorbed in the taxable year.

If the computation of the taxable income of a member under this subdivision results in an excess of deductions over gross income, then for purposes of this subdivision such member's taxable income shall be zero.

(2)(i) The tax liability of the group shall be allocated to the several members of the group on the basis of the percentage of the total tax which the tax of such member if computed on a separate return would bear to the total amount of the taxes for all members of the group so computed.

(ii) For consolidated return years beginning after December 31, 1965, a member's portion of the tax liability of the group under the method of allocation provided by subdivision (i) of this subparagraph is an amount equal to the tax liability of the group multiplied by a fraction, the numerator of which is the separate return tax liability of such member, and the denominator of which is the sum of the separate return tax liabilities of all the members. For purposes of this subdivision the separate return tax liability of a member is its tax liability computed as if it has filed a separate return for the year except that:

(a) Gains and losses on intercompany transactions shall be taken into account as provided in § 1.1502-13 as if a consolidated return had been filed for the year;

(b) Gains and losses relating to inventory adjustments shall be taken into account as provided in § 1.1502-18 as if a consolidated return had been filed for the year;

(c) Transactions with respect to stock, bonds, or other obligations of members shall be reflected as provided in § 1.1502-13 (f) and (g) as if a consolidated return had been filed for the year;

(d) Excess losses shall be included in income as provided in §1.1502-19 as if a consolidated return had been filed for the year;

(e) In the computation of the deduction under section 167, property shall not lose its character as new property as a result of a transfer from one member to another member during the year;

(f) A dividend distributed by one member to another member during the year shall not be taken into account in computing the deductions under section 243(a)(1), 244(a), 245, or 247 (relating to deductions with respect to dividends received and dividends paid);

(g) Basis shall be determined under §§1.1502-31 and 1.1502-32, and earnings and profits shall be determined under §1.1502-33, as if a consolidated return had been filed for the year;

(h) Subparagraph (2) of §1.1502-3(f) shall apply as if a consolidated return had been filed for the year; and

(i) For purposes of Subtitle A of the Code, the surtax exemption of the member shall be an amount equal to \$25,000 (\$50,000 in the case of a taxable year ending in 1975), divided by the number of members (or such portion of \$25,000 or \$50,000 which is apportioned to the member pursuant to a schedule attached to the consolidated return for the taxable year). (However, if for the taxable year some or all of the members are component members of a controlled group of corporations (within the meaning of section 1563) and if there are other such component members which do not join in filing the consolidated return for such year, the amount to be divided among the members filing the consolidated return shall be (in lieu of \$25,000 or \$50,000) the sum of the amounts apportioned to the component members which join in filing the consolidated return (as determined for taxable years beginning after December 31, 1974 under §1.1561-2(a)(2) or §1.1561-3, whichever is applicable, and for taxable years beginning before January 1, 1975, under §1.561-2A(a)(2) or §1.1561-3A whichever is applicable).)

If the computation of the separate return tax liability of a member under this subdivision does not result in a positive tax liability, then for purposes

of this subdivision such member's separate return tax liability shall be zero.

(3)(i) The tax liability of the group (excluding the tax increases arising from the consolidation) shall be allocated on the basis of the contribution of each member of the group to the consolidated taxable income of the group. Any tax increases arising from the consolidation shall be distributed to the several members in direct proportion to the reduction in tax liability resulting to such members from the filing of the consolidated return as measured by the difference between their tax liabilities determined on a separate return basis and their tax liabilities (determined without regard to the 2-percent increase provided by section 1503(a) and paragraph (a) of §1.1502-30A (as contained in the 26 CFR edition revised as of April 1, 1996) for taxable years beginning before January 1, 1964) based on their contributions to the consolidated taxable income.

(ii) For consolidated return years beginning after December 31, 1965, a member's portion of the tax liability of the group under the method of allocation provided by subdivision (i) of this subparagraph shall be determined by:

(a) Allocating the tax liability of the group in accordance with subparagraph (1)(ii) of this paragraph, but

(b) The amount of tax liability allocated to any member shall not exceed the separate return tax liability of such member, determined in accordance with subparagraph (2)(ii) of this paragraph, and

(c) The sum of the amounts which would be allocated to the members but for (b) of this subdivision (ii) shall be apportioned among the other members in direct proportion to, but limited to, the reduction in tax liability resulting to such other members. Such reduction for any member shall be the excess, if any, of (1) its separate this paragraph.

(4) The tax liability of the group shall be allocated in accordance with any other method selected by the group with the approval of the Commissioner. No method of allocation may be approved under this subparagraph which may result in the allocation of a positive tax liability for a taxable year, among the members who are allocated a positive tax liability for

such year, in a total amount which is more or less than the tax liability of the group for such year. (However, see paragraph (d) of § 1.1502-33.)

(b) *Application of rules*—(1) *Tax liability of the group*. For purposes of section 1552 and this section, the tax liability of the group for a taxable year shall consist of the Federal income tax liability of the group for such year determined in accordance with § 1.1502-2 or § 1.1502-30A (as contained in the 26 CFR edition revised as of April 1, 1996), whichever is applicable. Thus, in the case of a carryback of a loss or credit to such year, although the earnings and profits of the members of the group may not be adjusted until the subsequent taxable year from which the loss or credit was carried back, the effect of the carryback, for purposes of this section, shall be determined by allocating the amount of the adjustment as a part of the tax liability of the group for the taxable year to which the loss or credit is carried. For example, if a consolidated net operating loss is carried back from 1969 to 1967, the allocation of the tax liability of the group for 1967 shall be recomputed in accordance with the method of allocation used for 1967, and the changes resulting from such recomputation shall, for accrual method taxpayers, be reflected in the earnings and profits of the appropriate members in 1969.

(2) *Effect of allocation*. The amount of tax liability allocated to a corporation as its share of the tax liability of the group, pursuant to this section, shall (i) result in a decrease in the earnings and profits of such corporation in such amount, and (ii) be treated as a liability of such corporation for such amount. If the full amount of such liability is not paid by such corporation, pursuant to an agreement among the members of the group or otherwise, the amount which is not paid will generally be treated as a distribution with respect to stock, a contribution to capital, or a combination thereof, as the case may be.

(c) *Method of election*. (1) The election under paragraph (a) (1), (2), or (3) of this section shall be made not later than the time prescribed by law for filing the first consolidated return of the group for a taxable year beginning

after December 31, 1953, and ending after August 16, 1954 (including extensions thereof). If the group elects to allocate its tax liability in accordance with the method prescribed in paragraph (a) (1), (2), or (3) of this section, a statement shall be attached to the return stating which method is elected. Such statement shall be made by the common parent corporation and shall be binding upon all members of the group. In the event that the group desires to allocate its tax liability in accordance with any other method pursuant to paragraph (a)(4) of this section, approval of such method by the Commissioner must be obtained within the time prescribed above. If such approval is not obtained in such time, the group shall allocate in accordance with the method prescribed in paragraph (a)(1) of this section. The request shall state fully the method which the group wishes to apply in apportioning the tax liability. Except as provided in subparagraph (2) of this paragraph, an election once made shall be irrevocable and shall be binding upon the group with respect to the year for which made and for all future years for which a consolidated return is filed or required to be filed unless the Commissioner authorizes a change to another method prior to the time prescribed by law for filing the return for the year in which such change is to be effective.

(2) Each group may make a new election to use any one of the methods prescribed in paragraph (a) (1), (2), or (3) of this section for its first consolidated return year beginning after December 31, 1965, or in conjunction with an election under paragraph (d) of § 1.1502-33, or may request the Commissioner's approval of a method under paragraph (a)(4) of this section for its first consolidated return year beginning after December 31, 1965, irrespective of its previous method of allocation under this section. If such new election is not made in conjunction with an election under paragraph (d) of § 1.1502-33, it shall be effective for the first consolidated return year beginning after December 31, 1965, and all succeeding years. (See § 1.1502-33 for the method of making such new election in conjunction with an election under paragraph (d) of § 1.1502-33.) Any other such new

election (or request for the Commissioner's approval of a method under paragraph (a)(4) of this section) shall be made within the time prescribed by law for filing the consolidated return for the first taxable year beginning after December 31, 1965 (including extensions thereof), or within 60 days after July 3, 1968, whichever is later. Such new election shall be made by attaching a statement to the consolidated return for the first taxable year beginning after December 31, 1965, or if such election is made within the time prescribed above but after such return is filed, by filing a statement with the internal revenue officer with whom such return was filed.

(d) *Failure to elect.* If a group fails to make an election in its first consolidated return, or any other election, in accordance with paragraph (c) of this section, the method prescribed under paragraph (a)(1) of this section shall be applicable and shall be binding upon the group in the same manner as if an election had been made to so allocate.

(e) *Definitions.* Except as otherwise provided in this section, the terms used in this section shall have the same meaning as provided in the regulations under section 1502.

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

Example. Corporation P is the common parent owning all of the stock of corporations S1 and S2, members of an affiliated group. A consolidated return is filed for the taxable year ending December 31, 1966, by P, S1, and S2. For 1966 such corporations had the following taxable incomes or losses computed in accordance with paragraph (a)(1)(ii) of this section:

P.....	0
S1.....	\$2,000
S2.....	(1,000)

The group has not made an election under paragraph (c) of this section or paragraph (d) of § 1.1502-33. Accordingly, the method of allocation provided by paragraph (a)(1) of this section is in effect for the group. Assuming that the consolidated taxable income is equal to the sum of the members taxable income and losses, or \$1,000, the tax liability of the group for the year (assuming a 22-percent rate) is \$220, all of which is allocated to S1. S1 accordingly reduces its earnings and profits in the amount of \$220, irrespective of who actually pays the tax liability. If S1 pays the \$220 tax liability there will be no further ef-

fect upon the income, earnings and profits, or the basis of stock of any member. If, however, P pays the \$220 tax liability (and such payment is not in fact a loan from P to S1), then P shall be treated as having made a contribution to the capital of S1 in the amount of \$220. On the other hand, if S2 pays the \$220 tax liability (and such payment is not in fact a loan from S2), then S2 shall be treated as having made a distribution with respect to its stock to P in the amount of \$220, and P shall be treated as having made a contribution to the capital of S1 in the amount of \$220.

[T.D. 6962, 33 FR 9655, July 3, 1968, as amended by T.D. 7825, 42 FR 64694, Dec. 28, 1977; T.D. 7728, 45 FR 72650, Nov. 3, 1980; T.D. 8560, 59 FR 41675, Aug. 15, 1994; T.D. 8597, 60 FR 36680, July 18, 1995; T.D. 8677, 61 FR 33325, June 27, 1996]

CERTAIN CONTROLLED CORPORATIONS

§ 1.1561-0 Effective date.

(a) *Taxable years beginning after December 31, 1974.* The provisions of §§ 1.1561-1 through 1.1561-3 apply only to taxable years beginning after December 31, 1974.

(b) *Taxable years beginning before January 1, 1975.* The provisions of §§ 1.1561-1A through 1.1561-3A apply only to taxable years beginning before January 1, 1975.

[T.D. 7528, 42 FR 64694, Dec. 28, 1977]

§ 1.1561-1 Limitations on certain multiple tax benefits in the case of certain controlled corporations.

(a) *In general.* Part II (section 1561 and following), subchapter B, chapter 6 of the Code, provides rules relating to certain controlled corporations. In general, section 1561 provides that the component members of a controlled group of corporations on a December 31, for their taxable years which include such December 31, shall be limited for purposes of subtitle A to:

- (1) One surtax exemption under section 11(d),
- (2) One \$150,000 amount for purposes of computing the accumulated earnings credit under section 535(c) (2) and (3), and
- (3) One \$25,000 amount for purposes of computing the limitation on the small business deduction of life insurance companies under sections 804(a)(4) and 809 (d)(10).