

For certain definitions (including the definition of a “controlled group of corporations” and a “component member”) and special rules for purposes of part II of subchapter B, see section 1563 and the regulations thereunder.

(b) *Tax avoidance.* The provisions of part II, subchapter B, chapter 6 do not delimit or abrogate any principle of law established by judicial decision, or any existing provisions of the code, such as sections 269, 482, and 1551, which have the effect of preventing the avoidance or evasion of income taxes.

(c) *Special rules.* (1) For purposes of sections 1561 and 1563 and the regulations thereunder, the term “corporation” includes an electing small business corporation (as defined in section 1371 (b)). However, for the treatment of an electing small business corporation as an excluded member of a controlled group of corporations, see paragraph (b)(2)(ii) of § 1.1563-1.

(2) In the case of corporations electing a 52-53-week taxable year under section 441(f)(1), the provisions of sections 1561 and 1563 and the regulations thereunder shall be applied in accordance with the special rule section 441(f)(2)(A). See § 1.441-2.

[T.D. 7528, 42 FR 64694, Dec. 28, 1977, as amended by T.D. 8996, 67 FR 35012, May 17, 2002]

§ 1.1561-2 Determination of amount of tax benefits.

(a) *Surtax exemption.* (1) If a corporation is a component member of a controlled group of corporations on December 31, the surtax exemption under section 11(d) of such corporation for the taxable year which includes such December 31 shall be an amount equal to:

(i) \$50,000 divided by the number of corporations which are component members of such group on such December 31, or

(ii) If an apportionment plan is adopted under § 1.1561-3 which is effective with respect to such taxable year such portion of \$50,000 as is apportioned to such member in accordance with such plan.

(2) In the case of a controlled group of corporations which includes component members which join in the filing of a consolidated return and other com-

ponent members which do not join in the filing of such a return, and where there is no apportionment plan effective under § 1.1561-3 apportioning the \$50,000 amount among the component members filing the consolidated return and the other component members of the controlled group, each component member of the controlled group, (including each component member which joins in filing the consolidated return) shall be treated as a separate corporation for purposes of equally apportioning the \$50,000 amount under subparagraph (1)(i) of this paragraph. In such case, the surtax exemption of the corporations filing the consolidated return shall be the sum of the amounts apportioned to each component member which joins in filing the consolidated return.

(3) The provisions of section 1561 may reduce the surtax exemption of any corporation which is a component member of a controlled group or corporations and which is subject to the tax imposed by section 11, or by any other provision of subtitle A of the Code if the tax under such other provisions is computed by reference to the amount of the surtax exemption provided by section 11. Such other provisions include, for example, sections 511(a)(1), 594, 802, 831, 852, 857, 882, 1201, and 1378.

(4) This paragraph (a) shall not apply with respect to any component member of a controlled group of corporations on a December 31 if one or more component members of such controlled group has a taxable year including such December 31 which ends after December 31, 1978. Rules pertaining to the apportionment of the surtax exemption with respect to component members of controlled groups of corporations to which this paragraph does not apply are reserved.

(5) The application of this paragraph may be illustrated by the following examples:

Example (1). Corporations W, X, Y, and Z are component members of a controlled group of corporations on December 31, 1975, and each corporation files its income tax return on the basis of a calendar year. For their taxable years ending on December 31, 1975, W and X each incurs a net operating loss; Y has \$5,250 of taxable income; and Z

has \$30,000 of taxable income. If an apportionment plan is not effective for such taxable years, the surtax exemption under section 11(d) of each corporation determined under subparagraph (1)(i) of this paragraph is \$12,500 ($\$50,000 \div 4$). However, the four corporations may avoid a pro rata division of the \$50,000 amount by filing an apportionment plan in accordance with the provisions of § 1.1561-3 allocating the \$50,000 amount in any manner they deem proper.

Example (2). Corporation A files its income tax return on the basis of a calendar year; corporation B files its income tax return on the basis of a fiscal year ending March 31. On December 31, 1975, A and B are the only component members of a controlled group of corporations. Under subparagraph (1)(i) of this paragraph, the surtax exemption of A for 1975, and the surtax exemption of B for its fiscal year ending March 31, 1976, is \$25,000 ($\$50,000 \div 2$). However, if an apportionment plan is filed in accordance with the provisions of § 1.1561-3, the surtax exemption of each such corporation will be the amount apportioned to the corporation pursuant to the plan.

Example (3). Corporations R, P, and S are component members of a controlled group of corporations on December 31, 1975. P and S file a consolidated return for their fiscal years ending June 30, 1976. R files a separate return for its taxable year ending on December 31, 1975. No apportionment plan is effective with respect to R's, P's, and S's taxable years which include December 31, 1975. Therefore R, P, and S are each apportioned \$16,666.67 ($\$50,000 \div 3$) as their surtax exemption under section 11(d) for their taxable years including such date. The surtax exemption of the affiliated group filing a consolidated return (P and S) for the year ending June 30, 1976, is \$33,333.34 (i.e., the sum of the \$16,666.67 amounts apportioned to P and S). However, if an apportionment plan is filed in accordance with the provisions of § 1.1561-3, the surtax exemption of the corporations which are members of the affiliated group filing a consolidated return and of each other corporation which is a component member of the controlled group of corporations will be the amount apportioned to such affiliated group and to each such other corporations pursuant to the plan.

(b) *Allocation of amounts of taxable income subject to normal tax.* (1) In the case of a taxable year of a corporation, if:

(i) The amount of normal tax under section 11(b) is equal to the sum of 20 percent of so much of the taxable income as does not exceed \$25,000, plus 22 percent of so much of the taxable income as exceeds \$25,000 for a taxable year, and

(ii) The amount of surtax exemption of the corporation is less than \$50,000 under paragraph (a)(1) (i) or (ii) of this section,

then for purposes of applying section 11(b), the taxable income subject to taxation at the rate of 20 percent shall be (in lieu of the first \$25,000 of taxable income) one-half of the amount of the surtax exemption allocated to such corporation under paragraph (a)(1) (i) or (ii) of this section. In addition, the amount of taxable income subject to taxation at the rate of 22 percent shall be (in lieu of the amount of taxable income in excess of \$25,000) the taxable income that exceeds one-half of the amount of the surtax exemption allocated to such corporation under paragraph (a)(1) (i) or (ii) of this section for such year. In the case of an affiliated group of corporations filing a consolidated return for a taxable year, the preceding sentence shall be applied by substituting the term "affiliated group" for the term "corporation" each time it appears.

(2) The provisions of this paragraph may be illustrated by the following example:

Example. Corporations P and S are component members of a controlled group of corporations on December 31, 1975, and each corporation files a separate income tax return on the basis of a calendar year. For the taxable year ending on December 31, 1975, P incurs a net operating loss and S has \$25,000 of taxable income. If an apportionment plan is not effective for that taxable year, the surtax exemption under section 11(d) of each corporation (determined under paragraph (a)(1)(i) of this section) is \$25,000 ($\$50,000 \div 2$). For purposes of applying section 11(b) to determine S's liability for tax for 1975, the amount of taxable income subject to taxation at the rate of 20 percent is limited to \$12,500 (i.e., one-half of the amount of the surtax exemption allocated to S under paragraph (a)(1)(i) of this section), and the amount of taxable income subject to taxation at the rate of 22 percent is \$12,500 (i.e., the amount of taxable income in excess of one-half of the amount of the surtax exemption). If, on the other hand, an apportionment plan is adopted by P and S effective for such taxable years apportioning the entire \$50,000 surtax exemption to S, then, for purposes of applying section 11(b) to determine S's liability for tax for 1975, the amount of taxable income subject to taxation at the rate of 20 percent is \$25,000.

§ 1.1561-2

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

(3) If an apportionment plan is adopted under § 1.1561-3 for a December 31, and if paragraph (b)(1) of this section applies to any component member whose taxable year includes such December 31, then the plan shall specify:

- (i) The amount subject to taxation at the rate of 20 percent, and
- (ii) The amount subject to taxation at the rate of 22 percent,

as determined under paragraph (b)(1) of this section for each component member. The information required to be included in a plan by this subparagraph is in addition to the information required under § 1.1561-3(a). Where an existing apportionment plan is effective under § 1.1561-3(a)(3) for such December 31, the additional information required under this subparagraph may be provided in an amendment of the existing plan as provided in § 1.1561-3(c).

(c) *Accumulated earnings credit.* (1) Except as provided in subparagraph (2) of this paragraph, if a corporation is a component member of a controlled group on a December 31, the amount for purposes of computing the accumulated earnings credit under section 535(c) (2) and (3) of such corporation shall be an amount equal to \$150,000 divided by the number of corporations which are component members of such group on such December 31. In the case of a controlled group of corporations which includes component members which join in the filing of a consolidated return and other component members which do not join in the filing of such a return, each component member of the controlled group (including each component member which joins in filing the consolidated return) shall be treated as a separate corporation for purposes of equally apportioning the \$150,000 amount under this subparagraph. In such case, the amount for purposes of computing the accumulated earnings credit for the component members filing the consolidated return shall be the sum of the amounts apportioned to each component member which joins in filing the consolidated return.

(2) If, with respect to any component member of the controlled group, the amount determined under subparagraph (1) of this paragraph exceeds the sum of (i) such member's accumulated earnings and profits as of the close of the preceding taxable year, plus (ii) such member's earnings and profits for the taxable year which are retained (within the meaning of section 535(c)(1)), then any such excess shall be subtracted from the amount determined under subparagraph (1) of this paragraph with respect to such member and shall be divided equally among those remaining component members of the controlled group that do not have such an excess (until no such excess remains to be divided among those remaining members that have not had such an excess). The excess so divided among such remaining members shall be added to the amount determined under subparagraph (1) with respect to such members. If a controlled group of corporations includes component members which join in the filing of a consolidated return and other component members which do not join in filing such return, the component members filing the consolidated return shall be treated as a single corporation for purposes of this subparagraph.

(3) A controlled group may not adopt an apportionment plan, as provided in § 1.1561-3, with respect to the amounts computed under the provisions of this paragraph.

(4) The provisions of this paragraph may be illustrated by the following example:

Example. A controlled group is composed of four component member corporations, W, X, Y, and Z. Each corporation files a separate income tax return on the basis of a calendar year. The sum of the earnings and profits for the taxable year ending December 31, 1975, which are retained plus the sum of the accumulated earnings and profits (as of the close of the preceding taxable year) is \$15,000, \$75,000, \$37,500, and \$300,000 for W, X, Y, and Z, respectively. The amounts determined under this paragraph for W, X, Y, and Z for 1975 are \$15,000, \$48,750, \$37,500, and \$48,750, respectively, computed as follows:

	Component members			
	W	X	Y	Z
Earnings and profits	\$15,000	\$75,000	\$37,500	\$300,000

	Component members			
	W	X	Y	Z
Amount computed under subparagraph (1)	37,500	37,500	37,500	37,500
Excess	22,500	0	0	0
Allocation of excess		7,500	7,500	7,500
New excess			7,500	
Reallocation of new excess		3,750		3,750
Amount to be used for purposes of section 535(c) (2) and (3)	15,000	48,750	37,500	48,750

(d) *Small business deduction of life insurance companies.* (1) Except as provided in subparagraph (2) of this paragraph, if two or more life insurance companies which are taxable under section 802 are component members of a controlled group of corporations on a December 31, the amount for purposes of computing the limitation on the small business deduction under sections 804(a)(4) and 809(d)(10) of such corporations for their taxable years which include such December 31 shall be an amount equal to \$25,000 divided by the number of life insurance companies taxable under section 802 which are component members of such group on such December 31.

(2) If, with respect to any of the component members of the controlled group which are described in subparagraph (1) of this paragraph, the amount determined under such subparagraph exceeds 10 percent of such member's investment yield (as defined in section 304(c)), then any such excess shall be subtracted from the amount determined under subparagraph (1) of this paragraph with respect to such member and shall be divided equally among those remaining life insurance company members of the controlled group that do not have such an excess (until no such excess remains to be divided among those remaining members that have not had such an excess). The excess so divided among such remaining members shall be added to the amount determined under subparagraph (1) with respect to such members.

(3) A controlled group may not adopt an apportionment plan, as provided in § 1.1561-3, with respect to the amounts computed under the provisions of this paragraph.

(e) *Certain short taxable years.* (1) If the return of a corporation is for a

short period which does not include a December 31, and such corporation is a component member of a controlled group of corporations with respect to such short period, then for purposes of subtitle A of the Code:

(i) The surtax exemption under section 11(d) of such corporation for such short period 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 corporations which are component members of such controlled group on the last day of such short period;

(ii) The amount to be used in computing the accumulated earnings credit under section 535(c) (2) and (3) of such corporation for such short period shall be an amount equal to \$150,000 divided by the number of corporations which are members of such controlled group on the last day of such short period; and

(iii) The amount to be used in computing the limitation on the small business deduction of life insurance companies under sections 804(a)(4) and 809(d)(10) of such corporation for such short period shall not exceed an amount equal to \$25,000 divided by the number of life insurance companies taxable under section 802 which are component members of the controlled group on the last day of such short period.

For purposes of the preceding sentence, the term "short period" does not include any period if the income for such period is required to be included in a consolidated return under § 1.1502-76. The determination of whether a corporation is a component member of a controlled group of corporations on the last day of a short period is made by applying the definition of "component member" contained in section 1563(b)

§ 1.1561-3

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

and § 1.1563-1 as if the last day of such short period were a December 31 occurring after December 31, 1974.

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

Example (1). On January 2, 1975, corporation X transfers cash to newly formed corporation Y (which begins business on that date) and receives all of the stock of Y in return. X also owns all of the stock of corporation Z on each day of 1974 and 1975. X uses the calendar year as its taxable year and Z uses a fiscal year ending on March 31. Y adopts a fiscal year ending on June 30 as its annual accounting period, and, therefore, files a return for the short taxable year beginning on January 2, 1975, and ending on June 30, 1975. On June 30, 1975, Y is a component member of a parent-subsidiary controlled group of corporations of which X, Y, and Z are component members. Accordingly, the surtax exemption of Y for the short taxable year ending on June 30, 1975, is \$16,666.67 (\$50,000÷3). On December 31, 1975, X, Y, and Z are component members of a parent-subsidiary controlled group of corporations. Accordingly, the surtax exemption of each such corporation for its taxable year including December 31, 1975 (i.e., X's calendar year ending December 31, 1975, Z's fiscal year ending March 31, 1976, and Y's fiscal year ending June 30, 1976) is \$16,666.67 (\$50,000÷3), or, if an apportionment plan is filed under § 1.1561-3, the amount apportioned pursuant to such plan.

Example (2). On January 1, 1975, corporation P owns all of the stock of corporations S-1, S-2, and S-3. P, S-1, S-2, and S-3 file separate returns on a calendar year basis. On July 31, 1975, S-1 is liquidated and therefore files a return for the short taxable year beginning on January 1, 1975, and ending on July 31, 1975. On August 31, 1975, S-2 is liquidated and therefore files a return for the short taxable year beginning on January 1, 1975, and ending on August 31, 1975. On July 31, 1975, S-1 is a component member of a parent-subsidiary controlled group of corporations of which P, S-1, S-2, and S-3 are component members. Accordingly, the surtax exemption under section 11(d) of S-1 for the short taxable year ending on July 31, 1975, is \$12,500 (\$50,000÷4). On August 31, 1975, S-2 is a component member of a parent-subsidiary controlled group of corporations of which P, S-2, and S-3 are component members. Accordingly, the surtax exemption of S-2 for the short taxable year ending on August 31, 1975, is \$16,666.67 (\$50,000÷3). On December 31, 1975, P and S-3 are component members of a parent-subsidiary controlled group of corporations. Accordingly, the surtax exemption of each such corporation for the calendar year 1975 is \$25,000 (\$50,000÷2), or, if an apportionment plan is filed under § 1.1561-3,

the amount apportioned pursuant to such plan.

[T.D. 7528, 42 FR 64695, Dec. 28, 1977]

§ 1.1561-3 Apportionment of surtax exemption.

(a) *In general.* (1) In the case of corporations which are component members of a controlled group of corporations on a December 31, the single \$50,000 surtax exemption under section 11(d) may be apportioned among such members (for the taxable year of each such member which includes such December 31) if all such members consent, in the manner provided in paragraph (b) of this section, to an apportionment plan with respect to such December 31. Such plan shall provide for the apportionment of a fixed dollar amount to one or more of such members, but in no event shall the sum of the amounts so apportioned exceed \$50,000. An apportionment plan shall not be considered as adopted with respect to a particular December 31 until each component member which is required to consent to the plan under paragraph (b)(1) of this section filed the original of a statement described in such paragraph (or, the original of a statement incorporating its consent is filed on its behalf). In the case of a return filed before a plan is adopted, the surtax exemption for purposes of such return shall be equally apportioned in accordance with the rules provided in § 1.1561-2(a)(1)(i). (If a valid apportionment plan is adopted after the return is filed and within the time prescribed by subparagraph (2) of this paragraph, such return should be amended (or a claim for refund should be made) to reflect the change from equal apportionment.)

(2) A controlled group may adopt an apportionment plan with respect to a particular December 31 only if, at the time such plan is sought to be adopted, there is at least one year remaining in the statutory period (including any extensions thereof) for the assessment of a deficiency against any corporation the tax liability of which would be increased by the adoption of such plan. If there is less than one year remaining with respect to any such corporation, the director of the service center with which such corporation files its income