

that date and ending on December 31, 1954. Corporation A had accumulated earnings and profits of \$50,000 immediately prior to January 1, 1943, and had earnings and profits of \$10,000 for each taxable year during the uninterrupted period from January 1, 1943, through December 31, 1954. It derived for the period from January 1, 1943, through December 31, 1953, 90 percent of its gross income from sources within the United States and in 1954 derived 95 percent of its gross income from sources within the United States. During the calendar years 1943, 1944, 1945, 1946, and 1947 Corporation A distributed in each year \$15,000; during the calendar years 1948, 1949, 1950, 1951, 1952, and 1953 it distributed in each year \$5,000; and during the year 1954, \$50,000. An analysis of the accumulated earnings and profits under the above statement of facts discloses that at December 31, 1953, the accumulation amounted to \$55,000, of which \$25,000 was accumulated prior to the "uninterrupted period" and \$30,000 was accumulated during the uninterrupted period. (See section 316(a) and paragraph (c) of this section.) For 1954 a deduction under section 245 of \$31,025 (\$8,075 on 1954 earnings of the foreign corporation, plus \$22,950 from the \$30,000 accumulation at December 31, 1953) for dividends received from a foreign corporation is allowable to Corporation B with respect to the \$50,000 received from Corporation A, computed as follows:

(i) \$8,075, which is \$8,500 (85 percent—the percent specified in section 243 for the calendar year 1954—of the \$10,000 of earnings and profits of the taxable year) multiplied by 95 percent (the portion of the gross income of Corporation A derived during the taxable year 1954 from sources within the United States), plus

(ii) \$22,950, which is \$25,500 (85 percent—the percent specified in section 243 for the calendar year 1954—of \$30,000, the part of the earnings and profits accumulated after the beginning of the uninterrupted period) multiplied by 90 percent (the portion of the gross income of Corporation A derived from sources within the United States during that portion of the uninterrupted period ending at the beginning of the taxable year 1954).

Example 2. If in *Example 1*, Corporation A for the taxable year 1954 had incurred a deficit of \$10,000 (shown to have been incurred before December 31) the amount of the earnings and profits accumulated after the beginning of the uninterrupted period would be \$20,000. If Corporation A had distributed \$50,000 on December 31, 1954, the deduction under section 245 for dividends received from a foreign corporation allowable to Corporation B for 1954 would be \$15,300, computed by multiplying \$17,000 (85 percent—the percent specified in section 243 for the calendar year 1954—of \$20,000 earnings and profits accumulated after the beginning of the uninterrupted period) by 90 percent (the portion of

the gross income of Corporation A derived from United States sources during that portion of the uninterrupted period ending at the beginning of the taxable year 1954).

Example 3. Corporation A (a foreign corporation filing its income tax returns on a calendar year basis) whose stock is 100 percent owned by corporation B (a domestic corporation filing its income tax returns on a calendar year basis) for the first time engaged in trade or business within the United States on January 1, 1960, and qualifies under section 245 for the entire period beginning on that date and ending on December 31, 1963. In 1963, A derived 75 percent of its gross income from sources within the United States. A's earnings and profits for 1963 (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year) are \$200,000. On December 31, 1963, corporation A distributes to corporation B 100 shares of corporation C stock which have an adjusted basis in A's hands of \$40,000 and a fair market value of \$100,000. For purposes of computing the deduction under section 245 for dividends received from a foreign corporation, the amount of the distribution is \$40,000. B is allowed a deduction under section 245 of \$25,500, i.e., \$34,000 (\$40,000 multiplied by 85 percent, the percent specified in section 243 for 1963), multiplied by 75 percent (the portion of the gross income of corporation A derived during 1963 from sources within the United States).

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6752, 29 FR 12701, Sept. 9, 1964, T.D. 6830; 30 FR 8046, June 23, 1965; T.D. 7293, 38 FR 32793, Nov. 28, 1973]

§ 1.246-1 Deductions not allowed for dividends from certain corporations.

The deductions provided in sections 243 (relating to dividends received by corporations), 244 (relating to dividends received on certain preferred stock), and 245 (relating to dividends received from certain foreign corporations), are not allowable with respect to any dividend received from:

(a) A corporation organized under the China Trade Act, 1922 (15 U.S.C. ch. 4) (see section 941); or

(b) A corporation which is exempt from tax under section 501 (relating to certain charitable, etc., organizations) or section 521 (relating to farmers' cooperative associations) for the taxable year of the corporation in which the distribution is made or for its next preceding taxable year; for

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(c) A corporation to which section 931 (relating to income from sources within possessions of the United States) applies for the taxable year of the corporation in which the distribution is made or for its next preceding taxable year; or

(d) A real estate investment trust which, for its taxable year in which the distribution is made, is taxable under Part II, Subchapter M, Chapter 1 of the Code. See section 243(c)(3), paragraph (c) of § 1.243-2, section 857(c), and paragraph (d) of § 1.857-6.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6598, 27 FR 4092, Apr. 28, 1962; T.D. 7767, 46 FR 11264, Feb. 6, 1981]

§ 1.246-2 Limitation on aggregate amount of deductions.

(a) *General rule.* The sum of the deductions allowed by sections 243(a)(1) (relating to dividends received by corporations), 244(a) (relating to dividends received on certain preferred stock), and 245 (relating to dividends received from certain foreign corporations), except as provided in section 246(b)(2) and in paragraph (b) of this section, is limited to 85 percent of the taxable income of the corporation. The taxable income of the corporation for this purpose is computed without regard to the net operating loss deduction allowed by section 172, the deduction for dividends paid on certain preferred stock of public utilities allowed by section 247, any capital loss carryback under section 1212(a)(1), and the deductions provided in sections 243(a)(1), 244(a), and 245. For definition of the term *taxable income*, see section 63.

(b) *Effect of net operating loss.* If the shareholder corporation has a net operating loss (as determined under sec. 172) for a taxable year, the limitation provided in section 246(b)(1) and in paragraph (a) of this section is not applicable for such taxable year. In that event, the deductions provided in sections 243(a)(1), 244(a), and 245 shall be allowable for all tax purposes to the shareholder corporation for such taxable year without regard to such limitation. If the shareholder corporation does not have a net operating loss for the taxable year, however, the limitation will be applicable for all tax purposes for such taxable year. In deter-

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mining whether the shareholder corporation has a net operating loss for a taxable year under section 172, the deductions allowed by sections 243(a)(1), 244(a), and 245 are to be computed without regard to the limitation provided in section 246(b)(1) and in paragraph (a) of this section.

[T.D. 6992, 34 FR 825, Jan. 18, 1969, as amended by T.D. 7301, 39 FR 963, Jan. 4, 1974]

§ 1.246-3 Exclusion of certain dividends.

(a) *In general.* Corporate taxpayers are denied, in certain cases, the dividends-received deduction provided by section 243 (dividends received by corporations), section 244 (dividends received on certain preferred stock), and section 245 (dividends received from certain foreign corporations). The above-mentioned dividends-received deductions are denied, under section 246(c)(1), to corporate shareholders:

(1) If the dividend is in respect of any share of stock which is sold or otherwise disposed of in any case where the taxpayer has held such share for 15 days or less; or

(2) If and to the extent that the taxpayer is under an obligation to make corresponding payments with respect to substantially identical stock or securities. It is immaterial whether the obligation has arisen pursuant to a short sale or otherwise.

(b) *Ninety-day rule for certain preference dividends.* In the case of any stock having a preference in dividends, a special rule is provided by section 246(c)(2) in lieu of the 15-day rule described in section 246(c)(1) and paragraph (a)(1) of this section. If the taxpayer receives dividends on such stock which are attributable to a period or periods aggregating in excess of 366 days, the holding period specified in section 246(c)(1)(A) shall be 90 days (in lieu of 15 days).

(c) *Definitions*—(1) “*Otherwise disposed of*”. As used in this section the term *otherwise disposed of* includes disposal by gift.

(2) “*Substantially identical stock or securities*”. The term *substantially identical stock or securities* is to be applied according to the facts and circumstances in each case. In general, the term has the same meaning as the