

had actually been distributed by the X corporation on December 31, 1987, only \$8,000 would have constituted a dividend under section 316 (a). The amount which could be considered as consent dividends in computing the dividends paid deduction for purposes of the accumulated earnings tax is limited to \$8,000, or \$4,000 of the \$5,000 specified in each consent. The remaining \$1,000 in each consent is disregarded for all tax purposes. (In the case of a personal holding company, see also the example in § 1.565-3(b).)

[T.D. 8244, 54 FR 10539, Mar. 14, 1989]

§ 1.565-3 Effect of consent.

(a) *General Rule.* The amount of the consent dividend that is described in paragraph (a) of § 1.565-1 shall be considered, for all purposes of the Code, as if it were distributed in money by the corporation to the shareholder on the last day of the taxable year of the corporation, received by the shareholder on such day, and immediately contributed by the shareholder as paid-in capital to the corporation on such day. Thus, the amount of the consent dividend will be treated by the shareholder as a dividend. The shareholder will be entitled to the dividends received deduction under section 243 or 245 with respect to such consent dividend. The basis of the shareholder's consent stock in a corporation will be increased by the amount thus treated in his hands as a dividend which he is considered as having contributed to the corporation as paid-in capital. The amount of the current dividend will also be treated as a dividend received from sources within the United States in the same manner as if the dividend had been paid in money to the shareholders. Among other effects of the consent dividend, the earnings and profits of the corporation will be decreased by the amount of the consent dividends. Moreover, if the shareholder is a corporation, its accumulated earnings and profits will be increased by the amount of the consent dividend with respect to which it makes a consent.

(b) *Example.* The application of section 565 (c) may be illustrated by the following example:

Example. Corporation A, a personal holding company and a calendar year taxpayer, has one shareholder, individual B, whose consent to include \$10,000 in his gross income for the

calendar year 1987 has been timely filed. A has \$8,000 of earnings and profits at the beginning of 1987. A has \$10,000 of undistributed personal holding company income (determined without regard to distributions under section 316(b)(2)) for 1987. B must include \$10,000 in his gross income as a taxable income and is treated as having immediately contributed \$10,000 to A as paid-in capital. See section 316(b)(2).

[T.D. 8244, 54 FR 10540, Mar. 14, 1989]

§ 1.565-4 Consent dividends and other distributions.

Section 565(d) provides a rule applicable where a distribution is made in part in consent dividends and in part in money or other property. With respect to such a distribution the entire amount specified in the consents and the amount of such money or other property shall be considered together. Thus, if as a part of the same distribution consents are filed by some of the shareholders and cash is distributed to other shareholders, for example, those who may be unwilling to sign consents, the total amount of the cash and the amounts specified in the consents will be viewed as a single distribution to determine the tax effects of such distribution. For example, the total of such amounts must be considered to determine whether the distribution (including the amounts specified in the consents) is preferential and whether any part of such distribution would not be dividends if the total amounts specified in the consents were distributed in cash. See paragraph (b)(2) of § 1.565-2 for examples illustrating the treatment of distributions which consist in part of consent dividends and in part of other property.

§ 1.565-5 Nonresident aliens and foreign corporations.

(a) *Withholding.* In the event that a corporation makes a consent dividend, as described in § 1.565-1 (a), to a shareholder that is subject to a withholding tax under section 1441 or 1442 on a distribution of cash or other property, the corporation must remit an amount of tax equal to the withholding tax that would be imposed under section 1441 or 1442 if an actual cash distribution equal to the consent dividend had been paid to the shareholder on the last day of the corporation's taxable year. Such

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payment must be in one of the following forms:

- (1) Cash,
- (2) United States postal money order,
- (3) Certified check drawn on a domestic bank, provided that the law of the place where the bank is located does not permit the certification to be rescinded prior to presentation,
- (4) A cashier's check of a domestic bank, or
- (5) A draft on a domestic bank or a foreign bank maintaining a United States agency or branch and payable in United States funds.

The amount of such payment shall be credited against the tax imposed on the shareholder.

[T.D. 8244, 54 FR 10540, Mar. 14, 1989]

§ 1.565-6 Definitions.

(a) *Consent stock.* (1) The term *consent stock* includes what is generally known as common stock. It also includes participating preferred stock, the participation rights of which are unlimited.

(2) The definition of consent stock may be illustrated by the following example:

Example. If in the case of the X Corporation, a personal holding company, there is only one class of stock outstanding, it would all be consent stock. If, on the other hand, there were two classes of stock, class A and class B, and class A was entitled to 6 percent before any distribution could be made on class B, but class B was entitled to everything distributed after class A had received its 6 percent, only class B stock would be consent stock. Similarly, if class A, after receiving its 6 percent, was to participate equally or in some fixed proportion with class B until it had received a second 6 percent, after which class B alone was entitled to any further distributions, only class B stock would be consent stock. The same result would follow if the order of preferences were class A 6 percent, then class B 6 percent, then class A a second 6 percent, either alone or in conjunction with class B, then class B the remainder. If, however, class A stock is entitled to ultimate participation without limit as to amount, then it, too, may be consent stock. For example, if class A is to receive 3 percent and then share equally or in some fixed proportion with class B in the remainder of the earnings or profits distributed, both class A stock and class B stock are consent stock.

(b) *Preferred dividends.* (1) The term *preferred dividends* includes all fixed

amounts (whether determined by percentage of par value, a stated return expressed in a certain number of dollars per share, or otherwise) the distribution of which on any class of stock is a condition precedent to a further distribution of earnings or profits (not including a distribution in partial or complete liquidation). A distribution, though expressed in terms of a fixed amount, is not a preferred dividend, however, unless it is preferred over a subsequent distribution within the taxable year upon some class or classes of stock other than one on which it is payable.

(2) The definition of preferred dividends may be illustrated by the following example:

Example. If, in the case of the X Corporation, there are only two classes of stock outstanding, class A and class B, and class A is entitled to a distribution of 6 percent of par, after which the balance of the earnings and profits are distributable on class B exclusively, class A's 6 percent is a preferred dividend. If the order of preferences is class A \$6 per share, class B \$6 per share, then class A and class B in fixed proportions until class A receives \$3 more per share, then class B the remainder, all of class A's \$9 per share and \$6 per share of the amount distributable on class B are preferred dividends. The amount which class B is entitled to receive in conjunction with the payment to class A of its last \$3 per share is not a preferred dividend, because the payment of such amount is preferred over no subsequent distribution except one made on class B itself. Finally, if a distribution must be \$6 on class A, \$6 on class B, then on class A and class B share and share alike, the distribution on class A of \$6 and the distribution on class B of \$6 are both preferred dividends.

[54 FR 10540, Mar. 14, 1989]

BANKING INSTITUTIONS

RULES OF GENERAL APPLICATION TO BANKING INSTITUTIONS

§ 1.581-1 Banks.

(a) In order to be a bank as defined in section 581, an institution must be a corporation for federal tax purposes. See §301.7701-2(b) of this chapter for the definition of a corporation.

(b) This section is effective as of January 1, 1997.

[T.D. 8697, 61 FR 66588, Dec. 18, 1996]