

§ 1.1382-7 Special rules applicable to cooperative associations exempt from tax before January 1, 1952.

(a) *Basis of property.* The adjustments to the cost or other basis provided in sections 1011 and 1016 and the regulations thereunder, are applicable for the entire period since the acquisition of the property. Thus, proper adjustment to basis must be made under section 1016 for depreciation, obsolescence, amortization, and depletion for all taxable years beginning prior to January 1, 1952, although the cooperative association was exempt from tax under section 521 or corresponding provisions of prior law for such years. However, no adjustment for percentage or discovery depletion is to be made for any year during which the association was exempt from tax. If a cooperative association has made a proper election in accordance with section 1020 and the regulations prescribed thereunder with respect to a taxable year beginning before 1952 in which the association was not exempt from tax, the adjustment to basis for depreciation for such years shall be limited in accordance with the provisions of section 1016(a)(2).

(b) *Amortization of bond premium.* In the case of tax exempt and partially taxable bonds purchased at a premium and subject to amortization under section 171, proper adjustment to basis must be made to reflect amortization with respect to such premium from the date of acquisition of the bond. (For principles governing the method of computation, see the example in paragraph (b) of § 1.1016-9, relating to mutual savings banks, building and loan associations, and cooperative banks.) The basis of a fully taxable bond purchased at a premium shall be adjusted from the date of the election to amortize such premium in accordance with the provisions of section 171 except that no adjustment shall be allowable for such portion of the premium attributable to the period prior to the election.

(c) *Amortization of mortgage premium.* In the case of a mortgage acquired at a premium where the principal of such mortgage is payable in installments, adjustments to the basis for the premium must be made for all taxable years (whether or not the association

was exempt from tax under section 521 during such years) in which installment payments are received. Such adjustments may be made on an individual mortgage basis or on a composite basis by reference to the average period of payments of the mortgage loans of such association. For the purpose of this adjustment, the term *premium* includes the excess of the acquisition value of the mortgage over its maturity value. The acquisition value of the mortgage is the cost including buying commissions, attorneys' fees, or brokerage fees, but such value does not include amounts paid for accrued interest.

[T.D. 6643, 28 FR 3156, Apr. 2, 1963]

§ 1.1383-1 Computation of tax where cooperative redeems nonqualified written notices of allocation.

(a) *General rule.* (1) If, during the taxable year, a cooperative organization is entitled to a deduction under section 1382 (b)(2) or (c)(2)(B) for amounts paid in redemption of nonqualified written notices of allocation, the tax imposed for the taxable year by chapter 1 of the Code shall be the lesser of:

(i) The tax for the taxable year computed under section 1383(a)(1), that is, with such deduction taken into account, or

(ii) The tax for the taxable year computed under section 1383(a)(2), that is, without taking such deduction into account, minus the decrease in tax (under chapter 1 of the Code) for any prior taxable year (or years) which would result solely from treating all such nonqualified written notices of allocation redeemed during the taxable year as qualified written notices of allocation when paid. For the purpose of this subdivision, the amount of the decrease in tax is not limited to the amount of the tax for the taxable year. See paragraph (c) of this section for rules relating to a refund of tax where the decrease in tax for the prior taxable year (or years) exceeds the tax for the taxable year.

(2) If the cooperative organization computes its tax for the taxable year under the provisions of section 1383(a)(2) and subparagraph (1)(ii) of this paragraph, then no deduction under section 1382 (b)(2) or (c)(2)(B)

shall be taken into account in computing taxable income or loss for the taxable year, including the computation of any net operating loss carryback or carryover. However, the amount of the deduction shall be taken into account in adjusting earnings and profits for the taxable year.

(3) If the tax determined under subparagraph (1)(i) of this paragraph is the same as the tax determined under subparagraph (1)(ii) of this paragraph, the tax imposed for the taxable year under chapter 1 of the Code shall be the tax determined under subparagraph (1)(l) of this paragraph, and section 1383 and this section shall not otherwise apply. The tax imposed for the taxable year shall be the tax determined under subparagraph (1)(ii) of this paragraph in any case when a credit or refund would be allowable for the taxable year under section 1383(b)(1).

(b) *Determination of decrease in tax for prior taxable years*—(1) *Prior taxable years*. The prior taxable year (or years) referred to in paragraph (a) of this section is the year (or years) within the payment period for which the nonqualified written notices of allocation were paid and, in addition, any other prior taxable year (or years) which is affected by the adjustment to income by reason of treating such nonqualified written notices of allocation as qualified written notices of allocation when paid.

(2) *Adjustment to income in prior taxable years*. The deduction for the prior taxable year (or years) in determining the decrease in tax under section 1383(a)(2)(B) and paragraph (a)(1)(ii) of this section shall be the amount paid in redemption of the nonqualified written notices of allocation which, without regard to section 1383, is allowable as a deduction under section 1382 (b)(2) or (c)(2)(B) for the current taxable year.

(3) *Computation of decrease in tax for prior taxable years*. In computing the amount of decrease in tax for a prior taxable year (or years) resulting under this section, there must first be ascertained the amount of tax previously determined for the taxpayer for such prior taxable year (or years). The tax previously determined shall be the sum of the amounts shown as such tax

by the taxpayer on his return or returns, plus any amounts which have been previously assessed (or collected without assessment) as deficiencies, reduced by the amount of any rebates which have previously been made. The amount shown as the tax by the taxpayer on his return and the amount of any rebates or deficiencies shall be determined in accordance with the provisions of section 6211 and the regulations thereunder. After the tax previously determined has been ascertained, a recomputation must then be made to determine the decrease in tax, if any, resulting under this section. In determining the decrease in tax for the prior taxable year (or years), appropriate adjustment shall be made to any item which is dependent upon the amount of gross income or taxable income (such as charitable contributions, net operating losses, the foreign tax credit, and the dividends received credit).

(c) *Refunds*. If the decrease in tax for the prior taxable year (or years) determined under section 1383(a)(2)(B) and paragraph (a)(1)(ii) of this section exceeds the tax imposed by chapter 1 of the Code for the taxable year computed without the deduction under section 1382 (b) or (c)(2)(B), the excess shall be considered to be a payment of tax for the taxable year of the deduction. Such payment is deemed to have been made on the last day prescribed by law for the payment of tax for the taxable year and shall be refunded or credited in the same manner as if it were an overpayment of tax for such taxable year. See section 6151 and the regulations thereunder, for rules relating to time and place for paying tax shown on returns.

(d) *Example*. The application of section 1383 may be illustrated by the following example:

Example: The X Cooperative (which reports its income on a calendar year basis) pays patronage dividends of \$100,000 in nonqualified written notices of allocation on February 1, 1964, with respect to patronage occurring in 1963. Since the patronage dividends of \$100,000 were paid in nonqualified written notices of allocation the X Cooperative is not allowed a deduction for that amount for 1963. On December 1, 1966, the X Cooperative redeems these nonqualified written notices of allocation for \$50,000. Under section 1382(b)(2), a deduction of \$50,000 is allowable

in computing its taxable income for 1966. However, the X Cooperative has a loss for 1966 determined without regard to this deduction. The X Cooperative, therefore, makes the computation under the alternative method provided in section 1383(a)(2). Under this alternative method, it will claim a credit or refund (as an overpayment of tax for 1966) of the decrease in tax for 1963 and for such other years prior to 1966 as are affected which results from recomputing its tax for 1963 and such other years affected) as if patronage dividends of \$50,000 had been paid on February 1, 1964, in qualified written notices of allocation. In addition, under this alternative method the X Cooperative cannot use the \$50,000 as a deduction for 1966 so as to increase its net operating loss for such year for purposes of computing a net operating loss carryback or carryover. If the X Cooperative also redeems on December 1, 1966, nonqualified written notices of allocation which were paid as patronage dividends on February 1, 1965, with respect to patronage occurring in 1964, it will claim a credit or refund (as an overpayment of tax for 1966) of the decrease in tax for 1964 and for such other years prior to 1966 as are affected. It shall not, however, apply one method for computing the tax with respect to the redemptions in 1966 of the nonqualified written notices of allocation paid in 1964 and the other method with respect to the redemption in 1966 of the nonqualified written notices of allocation paid in 1965.

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TAX TREATMENT BY PATRONS OF
PATRONAGE DIVIDENDS

§ 1.1385-1 Amounts includible in patron's gross income.

(a) *General rules.* Section 1385(a) requires every person to include in gross income the following amounts received by him during the taxable year, to the extent paid by the organization in money, a qualified written notice of allocation, or other property (other than a nonqualified written notice of allocation):

(1) The amount of any patronage dividend received from an organization subject to the provisions of part I, subchapter T, chapter 1 of the Code, unless such amount is excludable from gross income under the provisions of section 1385(b) and paragraph (c) of this section, and

(2) The amount of any distribution received from a farmers', fruit growers', or like association, organized and operated in compliance with the re-

quirements of section 521 and § 1.521-1, which is paid on a patronage basis with respect to earnings derived by such association either from business done with or for the United States or any of its agencies or from sources other than patronage.

The amounts described in subparagraphs (1) and (2) of this paragraph are includible in gross income for the taxable year in which they are received even though the cooperative organization was allowed a deduction for such amounts for its preceding taxable year because they were paid during the payment period for such preceding taxable year. Similarly, such amounts are includible in gross income even though the cooperative organization is not permitted any deduction for such amounts under the provisions of section 1382 because such amounts were not paid within the time prescribed by such section.

(b) *Treatment of certain nonqualified written notices of allocation.* (1) Except as provided in paragraph (c) of this section, any gain on the redemption, sale, or other disposition of a nonqualified written notice of allocation described in subparagraph (2) of this paragraph shall, to the extent that the stated dollar amount of such written notice of allocation exceeds its basis, be considered as gain from the sale or exchange of property which is not a capital asset, whether such gain is realized by the patron who received the nonqualified written notice of allocation initially or by any subsequent holder. Any amount realized on the redemption, sale, or other disposition of such a nonqualified written notice of allocation in excess of its stated dollar amount will be treated under the applicable provisions of the Code. For example, amounts received in redemption of a nonqualified written notice of allocation which are in excess of the stated dollar amount of such written notice of allocation and which, in effect, constitute interest shall be treated by the recipient as interest.

(2) The nonqualified written notices of allocation to which subparagraph (1) of this paragraph applies are the following: