

must be distributed during the taxable year to A, the sole income beneficiary. Assuming that under section 652 or 662 A must include all of such gain in his gross income, the trust is not entitled to any deduction with respect to such gain under section 1202. Assuming A had no other capital gains or losses for 1954, he would be entitled to a deduction of \$500 under section 1202. For purposes of this section, an income beneficiary shall be any beneficiary to whom an amount is required to be distributed, or is paid or credited, which is includible in his gross income.

(c) The provisions of this section may be illustrated by the following example:

*Example:* A, an individual, had the following transactions in 1954:

Long-term capital gain .....	\$6,000	
Long-term capital loss .....	4,000	
Net long-term capital gain .....		\$2,000
Short-term capital loss .....	1,800	
Short-term capital gain .....	300	
Net short-term capital loss .....		1,500
Excess of net long-term capital gain over net short-term capital loss .....		500

Since the net long-term capital gain exceeds the net short-term capital loss by \$500, 50 percent of the excess, or \$250, is allowable as a deduction under section 1202.

[T.D. 6500, 25 FR 12001, Nov. 26, 1960, as amended by T.D. 7728, 45 FR 72650, Nov. 3, 1980]

### § 1.1202-2 Qualified small business stock; effect of redemptions.

(a) *Redemptions from taxpayer or related person*—(1) *In general.* Stock acquired by a taxpayer is not qualified small business stock if, in one or more purchases during the 4-year period beginning on the date 2 years before the issuance of the stock, the issuing corporation purchases (directly or indirectly) more than a de minimis amount of its stock from the taxpayer or from a person related (within the meaning of section 267(b) or 707(b)) to the taxpayer.

(2) *De minimis amount.* For purposes of this paragraph (a), stock acquired from the taxpayer or a related person exceeds a de minimis amount only if the aggregate amount paid for the stock exceeds \$10,000 and more than 2 percent of the stock held by the taxpayer and related persons is acquired. The fol-

lowing rules apply for purposes of determining whether the 2-percent limit is exceeded. The percentage of stock acquired in any single purchase is determined by dividing the stock's value (as of the time of purchase) by the value (as of the time of purchase) of all stock held (directly or indirectly) by the taxpayer and related persons immediately before the purchase. The percentage of stock acquired in multiple purchases is the sum of the percentages determined for each separate purchase.

(b) *Significant redemptions*—(1) *In general.* Stock is not qualified small business stock if, in one or more purchases during the 2-year period beginning on the date 1 year before the issuance of the stock, the issuing corporation purchases more than a de minimis amount of its stock and the purchased stock has an aggregate value (as of the time of the respective purchases) exceeding 5 percent of the aggregate value of all of the issuing corporation's stock as of the beginning of such 2-year period.

(2) *De minimis amount.* For purposes of this paragraph (b), stock exceeds a de minimis amount only if the aggregate amount paid for the stock exceeds \$10,000 and more than 2 percent of all outstanding stock is purchased. The following rules apply for purposes of determining whether the 2-percent limit is exceeded. The percentage of the stock acquired in any single purchase is determined by dividing the stock's value (as of the time of purchase) by the value (as of the time of purchase) of all stock outstanding immediately before the purchase. The percentage of stock acquired in multiple purchases is the sum of the percentages determined for each separate purchase.

(c) *Transfers by shareholders in connection with the performance of services not treated as purchases.* A transfer of stock by a shareholder to an employee or independent contractor (or to a beneficiary of an employee or independent contractor) is not treated as a purchase of the stock by the issuing corporation for purposes of this section even if the stock is treated as having first been transferred to the corporation under § 1.83-6(d)(1) (relating to transfers by

shareholders to employees or independent contractors).

(d) *Exceptions for termination of services, death, disability or mental incompetency, or divorce.* A stock purchase is disregarded if the stock is acquired in the following circumstances:

(1) *Termination of services*—(i) *Employees and directors.* The stock was acquired by the seller in connection with the performance of services as an employee or director and the stock is purchased from the seller incident to the seller's retirement or other bona fide termination of such services;

(ii) *Independent contractors.* [Reserved]

(2) *Death.* Prior to a decedent's death, the stock (or an option to acquire the stock) was held by the decedent or the decedent's spouse (or by both), by the decedent and joint tenant, or by a trust revocable by the decedent or the decedent's spouse (or by both), and—

(i) The stock is purchased from the decedent's estate, beneficiary (whether by bequest or lifetime gift), heir, surviving joint tenant, or surviving spouse, or from a trust established by the decedent or decedent's spouse; and

(ii) The stock is purchased within 3 years and 9 months from the date of the decedent's death;

(3) *Disability or mental incompetency.* The stock is purchased incident to the disability or mental incompetency of the selling shareholder; or

(4) *Divorce.* The stock is purchased incident to the divorce (within the meaning of section 1041(c)) of the selling shareholder.

(e) *Effective date.* This section applies to stock issued after August 10, 1993.

[T.D. 8749, 62 FR 68166, Dec. 31, 1997]

TREATMENT OF CAPITAL LOSSES

**§ 1.1211-1 Limitation on capital losses.**

(a) *Corporations*—(1) *General rule.* In the case of a corporation, there shall be allowed as a deduction an amount equal to the sum of:

(i) Losses sustained during the taxable year from sales or exchanges of capital assets, plus

(ii) The aggregate of all losses sustained in other taxable years which are treated as a short-term capital loss in

such taxable year pursuant to section 1212(a)(1),

but only to the extent of gains from such sales or exchanges of capital assets in such taxable year.

(2) *Banks.* See section 582(c) for modification of the limitation under section 1211(a) in the case of a bank, as defined in section 581.

(b) *Taxpayers other than corporations*—

(1) *General rule.* In the case of a taxpayer other than a corporation, there shall be allowed as a deduction an amount equal to the sum of:

(i) Losses sustained during the taxable year from sales or exchanges of capital assets, plus

(ii) The aggregate of all losses sustained in other taxable years which are treated either as a short-term capital loss or as a long-term capital loss in such taxable year pursuant to section 1212(b), but only to the extent of gains from sales or exchanges of capital assets in such taxable year, plus (if such losses exceed such gains) the additional allowance or transitional additional allowance deductible under section 1211(b) from ordinary income for such taxable year. The additional allowance deductible under section 1211(b) shall be determined by application of subparagraph (2) of this paragraph, and the transitional additional allowance by application of subparagraph (3) of this paragraph.

(2) *Additional allowance.* Except as otherwise provided by subparagraph (3) of this paragraph, the additional allowance deductible under section 1211(b) for taxable years beginning after December 31, 1969, shall be the least of:

(i) The taxable income for the taxable year reduced, but not below zero, by the zero bracket amount (in the case of taxable years beginning before January 1, 1977, the taxable income for the taxable year);

(ii) \$3,000 (\$2,000 for taxable years beginning in 1977; \$1,000 for taxable years beginning before January 1, 1977); or

(iii) The sum of the excess of the net short-term capital loss over the net long-term capital gain, plus one-half of the excess of the net long-term capital loss over the net short-term capital gain.