$20,000 of the excess net passive income is attributable to the net capital gain ($45,000 × ($40,000 / $90,000)). Accordingly, the amount of gain taken into account under section 1374(b)(1) and the taxable income of Corporation M under section 1374(b)(2) shall be reduced by $20,000.

Example 2. Assume an S corporation with subchapter C earnings and profits has tax-exempt income of $400, its only passive income, gross receipts of $1,000 and taxable income of $250 and there are no expenses associated with the tax-exempt income. The corporation's excess net income for the taxable year would total $150 (400 × ((400 − 250 / 400)). This amount is subject to the tax imposed by section 1375, notwithstanding that such amount is otherwise tax-exempt income.

[T.D. 8104, 51 FR 34203, Sept. 26, 1986; 52 FR 9162, Mar. 23, 1987. Redesignated and amended by T.D. 8419, 57 FR 22653, May 29, 1992]

§ 1.1377–0 Table of contents.

The following table of contents is provided to facilitate the use of §§ 1.1377–1 through 1.1377–3:

[T.D. 8696, 61 FR 67455, Dec. 23, 1996, as amended by T.D. 8994, 67 FR 34401, May 14, 2002]

§ 1.1377–1 Pro rata share.

(a) *Computation of pro rata shares*—(1) *In general.* For purposes of subchapter S of chapter 1 of the Internal Revenue Code and this section, each shareholder's pro rata share of any S corporation item described in section 1366(a) for any taxable year is the sum of the amounts determined with respect to the shareholder by assigning an equal portion of the item to each day of the S corporation's taxable year, and then dividing that portion pro rata among the shares outstanding on that day. See paragraph (b) of this section for rules pertaining to the computation of each shareholder's pro rata share when an election is made under section 1377(a)(2) to treat the taxable year of an S corporation as if it consisted of two taxable years in the case of a termination of a shareholder's entire interest in the corporation. See § 1.460–4(k)(3)(iv)(D) for rules relating to the computation of the shareholders' pro rata share of S corporation's income or loss from a contract accounted for under a long-term contract method of accounting.

(2) *Special rules*—(i) *Days on which stock has not been issued.* Solely for purposes of determining a shareholder's pro rata share of an item for a taxable year under section 1377(a) and this section, the beneficial owners of the corporation are treated as the shareholders of the corporation for any day on which the corporation has not issued any stock.

(ii) *Determining shareholder for day of stock disposition.* A shareholder who disposes of stock in an S corporation is treated as the shareholder for the day of the disposition. A shareholder who dies is treated as the shareholder for the day of the shareholder's death.

(iii) Shareholder trust conversions. If, during the taxable year of an S corporation, a trust that is an eligible shareholder of the S corporation converts from a trust described in section 1361(c)(2)(A)(i), (ii), (iii), or (v) for the