

INCOME TAX REGULATIONS – Section 1.318

§ 1.318-1 Constructive Ownership of Stock; Introduction.

1.318-1(a)

For the purposes of certain provisions of chapter 1 of the Code, section 318(a) provides that stock owned by a taxpayer includes stock constructively owned by such taxpayer under the rules set forth in such section. An individual is considered to own the stock owned, directly or indirectly, by or for his spouse (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance), and by or for his children, grandchildren, and parents. Under section 318(a) (2) and (3), constructive ownership rules are established for partnerships and partners, estates and beneficiaries, trusts and beneficiaries, and corporations and stockholders. If any person has an option to acquire stock, such stock is considered as owned by such person. The term “option” includes an option to acquire such an option and each of a series of such options.

1.318-1(b)

In applying section 318(a) to determine the stock ownership of any person for any one purpose

1.318-1(b)(1)

A corporation shall not be considered to own its own stock by reason of section 318(a)(3)(C);

1.318-1(b)(2)

In any case in which an amount of stock owned by any person may be included in the computation more than one time, such stock shall be included only once, in the manner in which it will impute to the person concerned the largest total stock ownership; and

1.318-1(b)(3)

In determining the 50-percent requirement of section 318(a) (2)(C) and (3)(C), all of the stock owned actually and constructively by the person concerned shall be aggregated.

§ 1.318-2 Application of General Rules.

1.318-2(a)

The application of paragraph (b) of § 1.318-1 may be illustrated by the following examples:

Example (1)

H, an individual, owns all of the stock of corporation A. Corporation A is not considered to own the stock owned by H in corporation A.

Example (2)

H, an individual, his wife, W, and his son, S, each own one-third of the stock of the Green Corporation. For purposes of determining the amount of stock owned by H, W, or S for purposes of section 318(a) (2)(C) and (3)(C), the amount of stock held by the other members of the family shall be added pursuant to paragraph (b)(3) of § 1.318-1 in applying the 50-percent requirement of such section. H, W, or S, as the case may be, is for this purpose deemed to own 100 percent of the stock of the Green Corporation.

1.318-2(b)

The application of section 318(a)(1), relating to members of a family, may be illustrated by the following example:

Example (1)

An individual, H, his wife, W, his son, S, and his grandson (S's son), G, own the 100 outstanding shares of stock of a corporation, each owning 25 shares. H, W, and S are each considered as owning 100 shares. G is considered as owning only 50 shares, that is, his own and his father's.

1.318-2(c)

The application of section 318(a) (2) and (3), relating to partnerships, trusts and corporations, may be illustrated by the following examples:

Example (1)

A, an individual, has a 50 percent interest in a partnership. The partnership owns 50 of the 100 outstanding shares of stock of a corporation, the remaining 50 shares being owned by A. The partnership is considered as owning 100 shares. A is considered as owning 75 shares.

Example (2)

A testamentary trust owns 25 of the outstanding 100 shares of stock of a corporation. A, an individual, who holds a vested remainder in the trust having a value, computed actuarially equal to 4 percent of the value of the trust property, owns the remaining 75 shares. Since the interest of A in the trust is a vested interest rather than a contingent interest (whether or not remote), the trust is considered as owning 100 shares. A is considered as owning 76 shares.

Example (3)

The facts are the same as in (2), above, except that A's interest in the trust is a contingent remainder. A is considered as owning 76 shares. However, since A's interest in the trust is a remote contingent interest, the trust is not considered as owning any of the shares owned by A.

Example (4)

A and B, unrelated individuals, own 70 percent and 30 percent, respectively, in value of the stock of Corporation M. Corporation M owns 50 of the 100 outstanding shares of stock of Corporation O, the remaining 50 shares being owned by A. Corporation M is considered as owning 100 shares of Corporation O, and A is considered as owning 85 shares.

Example (5)

A and B, unrelated individuals, own 70 percent and 30 percent, respectively, of the stock of corporation M. A, B, and corporation M all own stock of corporation O. Since B owns less than 50 percent in value of the stock of corporation M, neither B nor corporation M constructively owns the stock of corporation O owned by the other. However, for purposes of certain sections of the Code, such as sections 304 and 856(d), the 50-percent limitation of section 318(a) (2)(C) and (3)(C) is disregarded or is reduced to less than 30 percent. For such purposes, B constructively owns his proportionate share of the stock of corporation O owned directly by corporation M, and corporation M constructively owns the stock of corporation O owned by B.

§ 1.318-3 Estates, Trusts, And Options.

1.318-3(a)

For the purpose of applying section 318(a), relating to estates, property of a decedent shall be considered as owned by his estate if such property is subject to administration by the executor or administrator for the purpose of paying claims against the estate and expenses of administration notwithstanding that, under local law, legal title to such property vests in the decedent's heirs, legatees or devisees immediately upon death. The term "beneficiary" includes any person entitled to receive property of a decedent pursuant to a will or pursuant to laws of descent and distribution. A person shall no longer be considered a beneficiary of an estate when all the property to which he is entitled has been received by him, when he no longer has a claim against the estate arising out of having been a beneficiary, and when there is only a remote possibility that it will be necessary for the estate to seek the return of property or to seek payment from him by contribution or otherwise to satisfy claims against the estate or expenses of administration. When, pursuant to the preceding sentence, a person ceases to be a beneficiary, stock owned by him shall not thereafter be considered owned by the estate, and stock owned by the estate shall not thereafter be considered owned by him. The application of section 318(a) relating to estates may be illustrated by the following examples:

Example (1)

(a) A decedent's estate owns 50 of the 100 outstanding shares of stock of corporation X. The remaining shares are owned by three unrelated individuals, A, B, and C, who together own the entire interest in the estate. A owns 12 shares of stock of corporation X directly and is entitled to 50 percent of the estate. B owns 18 shares directly and has a life estate in the remaining 50 percent of the estate. C owns 20 shares directly and also owns the remainder interest after B's life estate.

(b) If section 318(a)(5)(C) applies (see paragraph (c)(3) of § 1.318-4), the stock of corporation X is considered to be owned as follows: the estate is considered as owning 80 shares, 50 shares directly, 12 shares constructively through A, and 18 shares constructively through B; A is considered as owning 37 shares, 12 shares directly, and 25 shares constructively (50 percent of the 50 shares owned directly by the estate); B is considered as owning 43 shares, 18 shares directly and 25 shares constructively (50 percent of the 50 shares owned directly by the estate); C is considered as owning 20 shares directly and no shares constructively. C is not considered a beneficiary of the estate under section 318(a) since he has no direct present interest in the property held by the estate nor in the income produced by such property.

(c) If section 318(a)(5)(C) does not apply, A is considered as owning nine additional shares (50 percent of the 18 shares owned constructively by the estate through B), and

B is considered as owning six additional shares (50 percent of the 12 shares owned constructively by the estate through A).

Example (2)

Under the will of A, Blackacre is left to B for life, remainder to C, an unrelated individual. The residue of the estate consisting of stock of a corporation is left to D. B and D are beneficiaries of the estate under section 318(a). C is not considered a beneficiary since he has no direct present interest in Blackacre nor in the income produced by such property. The stock owned by the estate is considered as owned proportionately by B and D.

1.318-3(b)

For the purpose of section 318(a)(2)(B) stock owned by a trust will be considered as being owned by its beneficiaries only to the extent of the interest of such beneficiaries in the trust. Accordingly, the interest of income beneficiaries, remainder beneficiaries, and other beneficiaries will be computed on an actuarial basis. Thus, if a trust owns 100 percent of the stock of Corporation A, and if, on an actuarial basis, W's life interest in the trust is 15 percent, Y's life interest is 25 percent, and Z's remainder interest is 60 percent, under this provision W will be considered to be the owner of 15 percent of the stock of Corporation A, Y will be considered to be the owner of 25 percent of such stock, and Z will be considered to be the owner of 60 percent of such stock. The factors and methods prescribed in § 20.2031-7 of this chapter (Estate Tax Regulations) for use in ascertaining the value of an interest in property for estate tax purposes shall be used in determining a beneficiary's actuarial interest in a trust for purposes of this section. See § 20.2031-7 of this chapter (Estate Tax Regulations) for examples illustrating the use of these factors and methods.

1.318-3(c)

The application of section 318(a) relating to options may be illustrated by the following example:

Example (1)

A and B, unrelated individuals, own all of the 100 outstanding shares of stock of a corporation, each owning 50 shares. A has an option to acquire 25 of B's shares and has an option to acquire a further option to acquire the remaining 25 of B's shares. A is considered as owning the entire 100 shares of stock of the corporation.

§ 1.318-4 Constructive Ownership As Actual Ownership; Exceptions.

1.318-4(a) In General.

Section 318(a)(5)(A) provides that, except as provided in section 318(a)(5) (B) and (C), stock constructively owned by a person by reason of the application of section 318(a) (1), (2), (3), or (4) shall be considered as actually owned by such person for purposes of applying section 318(a) (1), (2), (3), and (4). For example, if a trust owns 50 percent of the stock of corporation X, stock of corporation Y owned by corporation X which is attributed to the trust may be further attributed to the beneficiaries of the trust.

1.318-4(b) Constructive Family Ownership.

Section 318(a)(5)(B) provides that stock constructively owned by an individual by reason of ownership by a member of his family shall not be considered as owned by him for purposes of making another family member the constructive owner of such stock under section 318(a)(1). For example, if F and his two sons, A and B, each own one-third of the stock of a corporation, under section 318(a)(1), A is treated as owning constructively the stock owned by his father but is not treated as owning the stock owned by B. Section 318(a)(5)(B) prevents the attribution of the stock of one brother through the father to the other brother, an attribution beyond the scope of section 318(a)(1) directly.

1.318-4(c) Reattribution.

1.318-4(c)(1)

Section 318(a)(5)(C) provides that stock constructively owned by a partnership, estate, trust, or corporation by reason of the application of section 318(a)(3) shall not be considered as owned by it for purposes of applying section 318(a)(2) in order to make another the constructive owner of such stock. For example, if two unrelated individuals are beneficiaries of the same trust, stock held by one which is attributed to the trust under section 318(a)(3) is not reattributed from the trust to the other beneficiary. However, stock constructively owned by reason of section 318(a)(2) may be reattributed under section 318(a)(3). Thus, for example, if all the stock of corporations X and Y is owned by A, stock of corporation Z held by X is attributed to Y through A.

1.318-4(c)(2)

Section 318(a)(5)(C) does not prevent reattribution under section 318(a)(2) of stock constructively owned by an entity under section 318(a)(3) if the stock is also constructively owned by the entity under section 318(a)(4). For example, if individuals A and B are beneficiaries of a trust and the trust has an option to buy stock from A, B is considered under section 318(a)(2)(B) as owning a proportionate part of such stock.

1.318-4(c)(3)

Section 318(a)(5)(C) is effective on and after August 31, 1964, except that for purposes of sections 302 and 304 it does not apply with respect to distributions in payment for stock acquisitions or redemptions if such acquisitions or redemptions occurred before August 31, 1964.