$700) is carried over to 1972 under section 1212(b). Only $1,100 of the $1,800 will be treated in 1972 as carried over from 1969 since under subparagraph (3)(iii) of this paragraph the *transitional net long-term capital loss component* of $1,800 is reduced by the amount ($700) applied to the transitional additional allowance for 1971. Assuming the same taxable income for purposes of section 1211(b) (after reduction by the zero bracket amount) and the same transactions for a taxable year beginning in 1977, the transitional additional allowance would be $2,000. A net long-term capital loss of $800 would remain to be carried over. Of this amount $100 would be treated as carried over from 1969. Assuming the original facts for a taxable year beginning in 1978, the transitional additional allowance would be $2,450. No amount would remain to be carried over to the succeeding taxable year.

[T.D. 7301, 39 FR 964, Jan. 4, 1974; 39 FR 2758, Jan. 24, 1974, as amended by T.D. 7597, 44 FR 12419, Mar. 7, 1979; T.D. 7728, 45 FR 72650, Nov. 3, 1980]

§ 1.1212–1 Capital loss carryovers and carrybacks.

(a) *Corporations; other taxpayers for taxable years beginning before January 1, 1964*—(1) *Regular net capital loss sustained for taxable years beginning before January 1, 1970*. (i) A corporation sustaining a net capital loss for any taxable year beginning before January 1, 1970, and a taxpayer other than a corporation sustaining a net capital loss for any taxable year beginning before January 1, 1964, shall carry over such net loss to each of the 5 succeeding taxable years and treat it in each of such 5 succeeding taxable years as a short-term capital loss to the extent not allowed as a deduction against any net capital gains (capital gain net income for taxable years beginning after December 31, 1976) of any taxable years intervening between the taxable year in which the net capital loss was sustained and the taxable year to which carried. The carryover is thus applied in each succeeding taxable year to offset any net capital gain in such succeeding taxable year. The amount of the capital loss carryover may not be included in computing a new net capital loss of a taxable year which can be carried over to the next 5 succeeding taxable years. For purposes of this subparagraph, a net capital gain (capital gain net income for taxable years beginning after December 31, 1976) shall be computed without regard to capital loss carryovers or carrybacks. In the case of nonresident alien individuals, see section 871 for special rules on capital loss carryovers. For the rules applicable to the portion of a net capital loss of a corporation which is attributable to a foreign expropriation capital loss sustained in taxable years beginning after December 31, 1958, see subparagraph (2) of this paragraph. For the rules applicable to a taxpayer other than a corporation in the treatment of that amount of a net capital loss which may be carried over under section 1212 and this subparagraph as a short-term capital loss to the first taxable year beginning after December 31, 1963, see paragraph (b) of this section.

(ii) The practical operation of the provisions of this subparagraph may be illustrated by the following example:

Example: (a) For the taxable years 1952 to 1956, inclusive, an individual with one exemption allowable under section 151 (or corresponding provision of prior law) is assumed to have a net short-term capital loss, net short-term capital gain, net long-term capital loss, net long-term capital gain, and taxable income (net income for 1952 and 1953) as follows:

	1952	1953	1954	1955	1956
Carryover from prior years:					
From 1952		($50,000)	($29,500)	($29,500)	
From 1954				(19,500)	($13,000)
Net short-term loss (computed without regard to the carryovers)	($30,000)	(5,000)	(10,000)		
Net short-term gain (computed without regard to the carryovers)				40,000	
Net long-term loss	(20,500)		(10,000)	(5,000)	
Net long-term gain		25,000			15,000
Net income or taxable income, computed without regard to capital gains and losses, and, after 1953, without regard to the deduction provided by section 151	500	500	500	1,000	500

	1952	1953	1954	1955	1956
Net capital gain (capital gain net income for taxable years beginning after December 31, 1976) (computed without regard to the carryovers)		20,500		36,000	
Net capital loss	(50,000)		(19,500)		
Deduction allowable under section 1202					1,000
Taxable income (after deductions allowable under sections 151 and 1202)					900

(b) *Net capital loss of 1952.* The net capital loss is $50,000. This figure is the excess of the losses from sales or exchanges of capital assets over the sum of (1) gains (in this case, none) from sales or exchanges of capital assets, and (2) net income (computed without regard to capital gains and losses) of $500. This amount may be carried forward in full as a short-term loss to 1953. However, in 1953 there was a net capital gain (capital gain net income for taxable years beginning after December 31, 1976) of $20,500, as defined by section 117(a)(10)(B) of the Internal Revenue Code of 1939, and limited by section 117(e)(1) of the 1939 Code, against which this net capital loss of $50,000 is allowed in part. The remaining portion—$29,500—may be carried forward to 1954 and 1955 since there was no net capital gain (capital gain net income for taxable years beginning after December 31, 1976) in 1954. In 1955 this $29,500 is allowed in full against net capital gain of $36,000, as defined by paragraph (d) of §1.1222–1 and limited by subdivision (i) of this subparagraph.

(c) *Net capital loss of 1954.* The net capital loss is $19,500. This figure is the excess of the losses from sales or exchanges of capital assets over the sum of (1) gains (in this case, none) from sales or exchanges of capital assets and (2) taxable income (computed without regard to capital gains and losses and the deductions provided in section 151) of $500. This amount may be carried forward in full as a short-term loss to 1955. The net capital gain (capital gain net income for taxable years beginning after December 31, 1976) in 1955, before deduction of any carryovers, is $36,000. (See sections 1222(9)(B) and 1212 of the Internal Revenue Code of 1954, as it existed prior to the enactment of the Revenue Act of 1964.) The $29,500 balance of the 1952 loss is first applied against the $36,000, leaving a balance of $6,500. Against this amount the $19,500 loss arising in 1954 is applied, leaving a loss of $13,000, which may be carried forward to 1956. Since this amount is treated as a short-term capital loss in 1956 under subdivision (i) of this subparagraph, the excess of the net long-term capital gain over the net short-term capital loss is $2,000 ($15,000 minus $13,000). Half of this excess is allowable as a deduction under section 1202. Thus, after also deducting the exemption allowed as a deduction under section 151 ($600), the taxpayer has a taxable income of $900 ($2,500 minus $1,600) for 1956.

(2) *Corporations sustaining foreign expropriation capital losses for taxable years ending after December 31, 1958*—(i) *In general.* A corporation sustaining a net capital loss for any taxable year ending after December 31, 1958, any portion of which is attributable to a foreign expropriation capital loss, shall carry over such portion of the loss to each of the ten succeeding taxable years and treat it in each of such succeeding taxable years as a short-term capital loss to the extent and consistent with the manner provided in subparagraph (1) of this paragraph. For such purposes, the portion of any net capital loss for any taxable year which is attributable to a foreign expropriation capital loss is the amount, not in excess of the net capital loss for such year, of the foreign expropriation capital loss for such year. The portion of a net capital loss for any taxable year which is attributable to a foreign expropriation capital loss shall be treated as a separate net capital loss for that year and shall be applied, after first applying the remaining portion of such net capital loss, to offset any capital gain net income (net capital gain for taxable years beginning before January 1, 1977) in a succeeding taxable year. In applying net capital losses of two or more taxable years to offset the capital gain net income (net capital gain(s) for taxable years beginning before January 1, 1977) of a subsequent taxable year, such net capital losses shall be offset against such capital gain net income (net capital gain(s) for taxable years beginning before January 1, 1977) in the order of the taxable years in which the losses were sustained, beginning with the loss for the earliest preceding taxable year, even though one or more of such net capital losses are attributable

in whole or in part to a foreign expropriation capital loss.

(ii) *Foreign expropriation capital loss defined.* For purposes of this subaparagraph the term *foreign expropriation capital loss* means, for any taxable year, the sum of the losses taken into account in computing the net capital loss for such year which are:

(*a*) Losses sustained directly by reason of the expropriation, intervention, seizure, or similar taking of property by the government of any foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing, or

(*b*) Losses (treated under section 165 (g)(1) as losses from the sale or exchange of capital assets) from securities which become worthless by reason of the expropriation, intervention, seizure, or similar taking of property by the government of any foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing.

(iii) *Illustrations.* The application of this subparagraph may be illustrated by the following examples:

Example 1. X, a domestic corporation which uses the calendar year as the taxable year, owns as a capital asset 75 percent of the outstanding stock of Y, a foreign corporation operating in a foreign country. In 1961, the foreign country seizes all of the assets of Y, rendering X's stock in Y worthless and thus causing X to sustain a $40,000 foreign expropriation capital loss for such year. In 1961, X has $30,000 of other losses from the sale or exchange of capital assets and $50,000 of gains from the sale or exchange of capital assets. X's net capital loss for 1961 is $20,000 ($70,000 − $50,000). Since the foreign expropriation capital loss exceeds this amount, the entire $20,000 is a foreign expropriation capital loss for 1961.

Example 2. Z, a domestic corporation which uses the calendar year as the taxable year, has a net capital loss of $50,000 for 1961, $30,000 of which is attributable to a foreign expropriation capital loss. Pursuant to the provisions of this paragraph, $30,000 of such net capital loss shall be carried over as a short-term capital loss to each of the 10 taxable years succeeding 1961, and the remaining $20,000 of the net capital loss shall be carried over as a short-term capital loss to each of the 5 taxable years succeeding 1961. Z has a $35,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) (determined without regard to any capital loss carryover) for 1962. In offsetting the $50,000 capital loss carryover from 1961 against the $35,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) for 1962, the $30,000 portion of such carryover which is attributable to the foreign expropriation capital loss for 1961 is applied against the 1962 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) after applying the $20,000 remaining portion of the carryover. Thus, there is a capital loss carryover of $15,000 to 1963, all of which is attributable to the foreign expropriation capital loss for 1961. Z has a net capital loss for 1963 of $10,000, no portion of which is attributable to a foreign expropriation capital loss. For 1964, Z has a net capital gain (capital gain net income for taxable years beginning after December 31, 1976) of $22,000 (determined without regard to the capital loss carryovers from 1961 and 1963). In offsetting the capital loss carryovers from 1961 and 1963 against Z's $22,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) for 1964, the $15,000 carryover from 1961 is applied against the 1964 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) before the $10,000 capital loss carryover from 1963 is applied against such gain. Thus, $3,000 of the 1963 net capital loss remains to be carried over to 1965.

(3) *Regular net capital loss sustained by a corporation for taxable years beginning after December 31, 1969*—(i) *General rule.* A corporation sustaining a net capital loss for any taxable year beginning after December 31, 1969 (hereinafter in this paragraph referred to as the *loss year*), shall:

(*a*) Carry back such net capital loss to each of the 3 taxable years preceding the loss year, but only to the extent that such net capital loss is not attributable to a foreign expropriation capital loss and the carryback of such net capital loss does not increase or produce a net operating loss (as defined in section 172(c)) for the taxable year to which it is carried back; and

(*b*) Carry over such net capital loss to each of the 5 taxable years succeeding the loss year,

and, subject to subdivision (ii) of this subparagraph, treat such net capital loss in each of such 3 preceding and 5 succeeding taxable years as a short-term capital loss.

(ii) *Amount treated as a short-term capital loss in each year.* The entire amount of the net capital loss for any loss year shall be carried to the earliest of the taxable years to which such net capital loss may be carried, and the portion of such net capital loss which shall be carried to each of the other taxable years to which such net capital loss may be carried shall be the excess, if any, of such net capital loss over the total of the capital gain net income (net capital gain for taxable years beginning before January 1, 1977) (computed without regard to the capital loss carryback from the loss year or any taxable year thereafter) for each of the prior taxable years to which such net capital loss may be carried.

(iii) *Special rules. (a)* In the case of a net capital loss which is not a foreign expropriation capital loss and which cannot be carried back in full to a preceding taxable year by reason of section 1212(a)(1)(A)(ii) and subdivision (i)(*a*) of this subparagraph because such loss would produce or increase a net operating loss in such preceding taxable year, the capital gain net income (net capital gain for taxable years beginning before January 1, 1977) for such preceding taxable year shall in no case be treated as greater than the amount of such net capital loss which can be carried back to such preceding taxable year upon the application of section 1212(a)(1)(A)(ii) and subdivision (i)(*a*) of this subparagraph.

(*b*) For the rules applicable to the portion of a net capital loss of a corporation which is attributable to a foreign expropriation capital loss sustained in a taxable year beginning after December 31, 1958, see section 1212(a)(2) and subparagraph (2) of this paragraph.

(*c*) Section 1212(a)(1)(A) and subdivision (*i*)(*a*) of this subparagraph shall not apply to (and no carryback shall be allowed with respect to) the net capital loss of a corporation for any taxable year for which such corporation is an electing small business corporation under subchapter S. See § 1.1372–1.

(*d*) A net capital loss of a corporation for a year for which it is not an electing small business corporation under subchapter S shall not be carried back under section 1212(a)(1)(A) and subdivision (i)(*a*) of this subparagraph to a taxable year for which such corporation is an electing small business corporation. See section 1212(a)(3).

(*e*) A net capital loss of a corporation shall not be carried back under section 1212(a)(1)(A) and subdivision (i)(*a*) of this subparagraph to a taxable year for which the corporation was a foreign personal holding company, a regulated investment company, or a real estate investment trust, or for which an election made by the corporation under section 1247 is applicable. See section 1212(a)(4).

(*f*) A taxable year to which a net capital loss of a corporation cannot, by reason of (*d*) or (*e*) of this subdivision, be carried back under section 1212(a)(1)(A) and subdivision (i)(*a*) of this subparagraph shall nevertheless be treated as 1 of the 3 taxable years preceding the loss year for purposes of section 1212(a)(1)(A) and such subdivision (i)(*a*); but any capital gain net income (net capital gain for taxable years beginning before January 1, 1977) for such taxable year to which such net capital loss cannot be carried back shall be disregarded for purposes of subdivision (ii) of this subparagraph.

(*g*) A regulated investment company (as defined in section 851) sustaining a net capital loss shall carry over that loss to each of the 8 taxable years succeeding the loss year. However, the 8-year period prescribed in the preceding sentence shall be reduced (but not to less than 5 years) by the sum of (*1*) the number of taxable years to which the net capital loss must be carried back pursuant to subdivision (i)(*a*) of this subparagraph (as limited by subdivision (iii)(*e*) of this subparagraph) and (*2*) the number of taxable years, of the 8 taxable year succeeding the loss year, that the corporation failed to qualify as a regulated investment company as defined in section 851. This subdivision shall not extend the carryover period prescribed in subdivision (i)(*b*) of this subparagraph to a year in which a corporation is not a regulated investment company as defined in section 851.

(iv) The application of this subparagraph may be illustrated by the following examples, in each of which it is assumed that the corporation is not, and never has been, a corporation described in subdivision (iii) (*c*) or (*d*) of this subparagraph, that the corporation files its tax returns on a calendar year basis, and that no capital loss sustained is a foreign expropriation capital loss:

Example 1. A corporation has a net capital loss for 1970 which section 1212(a)(1)(A) permits to be carried back. The entire net capital loss for 1970 may be carried back to 1967, but only to the extent that a net operating loss for 1967 would not be produced or increased. The amount of the carryback to 1968 is the excess of the net capital loss for 1970 over the net capital gain (capital gain net income for taxable years beginning after December 31, 1976) for 1967, computed without regard to a capital loss carryback from 1970 or any taxable year thereafter. The amount of the carryback to 1969 is the excess of the net capital loss for 1970 over the sum of the net capital gains (capital gain net income for taxable years beginning after December 31, 1976) for 1967 and 1968, computed without regard to a capital loss carryback from 1970 or any taxable year thereafter. The amount of the carryover to 1971 is the excess of the net capital loss for 1970 over the sum of the net capital gains (capital gain net income for taxable years beginning after December 31, 1976) for 1967, 1968, and 1969, computed without regard to a capital loss carryback from 1970 or any taxable year thereafter. Similarly, the amount of the carryover to 1972, 1973, 1974, and 1975, respectively, is the excess of the net capital loss for 1970 over the sum of the net capital gains (capital gain net income for taxable years beginning after December 31, 1976) for taxable years prior to 1972, 1973, 1974, or 1975, as the case may be, to which the net capital loss for 1970 may be carried, computed without regard to a capital loss carryback from 1970 or any year thereafter.

Example 2. For the taxable years 1967 to 1975, inclusive, a corporation is assumed to have net capital loss, net capital gain (capital gain net income for taxable years beginning after December 31, 1976), and taxable income (computed without regard to capital gains and losses) as follows:

	1967	1968	1969	1970	1971	1972	1973	1974	1975
Taxable income (computed without regard to capital gains or losses)	$25,000	$25,000	$25,000	$25,000	$25,000	$25,000	$25,000	$25,000	$25,000
Net capital loss			(1,000)	(29,500)	(16,000)	(500)			
Net capital gain (capital gain net income for taxable years beginning after December 31, 1976) (computed without regard to carrybacks or carryovers)	14,000	16,000					8,000	7,500	6,500
Carryback or carryover:									
From 1969							(1,000)		
From 1970	(14,000)	(15,500)							
From 1971		(500)					(7,000)	(7,500)	(1,000)
From 1972									(500)

The net capital loss of 1969, under the rules of subparagraph (1) of this paragraph, may not be carried back. Thus, the net capital loss for 1970 is carried back and partially absorbed by the net capital gain (capital gain net income for taxable years beginning after December 31, 1976) for 1967, and a portion of the net capital losses of both 1970 and 1971 are carried back to 1968. The net capital loss for 1969 is the oldest that may be carried to 1973, and thus, it is the first carried over and absorbed by the net capital gain for 1973. The net capital loss for 1972 (which is not carried back because of the net capital losses in the 3 years preceding 1972) may be carried over to 1973.

Example 3. For the taxable years 1967 to 1970, inclusive, a corporation which was organized on January 1, 1967, realized operating income and net capital gains (capital gain net income for taxable years beginning after December 31, 1976) and sustained operating losses and net capital losses as follows:

	Operating income or loss (exclusive of capital gain or loss)	Capital gain or loss
1967	$20,000	$24,000
1968	20,000	0
1969	20,000	0
1970	(25,000)	(20,000)

The net capital loss of $20,000 for 1970 is carried back to 1967 and applied against the $24,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) realized in that year, reducing such net capital gain (capital gain net income for taxable years beginning after December 31, 1976) to $4,000. The net operating loss of $25,000 for 1970 is then carried back to 1967 and applied first to eliminate the $20,000 of operating income for that year and then to eliminate the net capital gain (capital gain net income for taxable years beginning after December 31, 1976) for that year of $4,000 (as reduced by the 1970 capital loss carryback).

Example 4. Assume the same facts as in Example 3 but substitute the following figures:

	Operating income or loss (exclusive of capital gain or loss)	Capital gain or loss
1967	($20,000)	$24,000
1968	20,000	0
1969	20,000	0
1970	(25,000)	(20,000)

The net capital loss of $20,000 for 1970 is carried back to 1967 and applied against the $24,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) realized in that year only to the extent of $4,000, the maximum amount to which the 1970 capital loss carryback can be applied without producing a net operating loss for 1967. The unused $16,000 balance of the 1970 net long-term capital loss can be carried forward to 1971 and subsequent taxable years to the extent provided in subdivision (i)(*b*) of this subparagraph.

Example 5. Assume the same facts as in Example 3 but substitute the following figures:

	Operating income or loss (exclusive of capital gain or loss)	Capital gain or loss
1967	0	0
1968	($20,000)	0
1969	0	$24,000
1970	20,000	(24,000)

The net capital loss of $24,000 for 1970 is carried back to 1969 and applied against the $24,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) realized in that year to the extent of $24,000. The application of the capital loss carryback is not limited as it was in Example 4 because such carryback neither increases nor produces a net operating loss, as such, for 1969. The $20,000 net operating loss for 1968 is then carried forward to 1970 to eliminate the $20,000 of operating income for that year.

Example 6. Assume the same facts as in Example 3 but substitute the following figures:

	Operating income or loss (exclusive of capital gain or loss)	Capital gain or loss
1967	0	0
1968	0	0
1969	($20,000)	($24,000)
1970	20,000	20,000

The net capital loss of $24,000 for 1969 is carried forward to 1970 and applied against the $20,000 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) realized in that year. The unused $4,000 balance of the 1969 net capital loss can be carried forward to 1971 and subsequent taxable years to the extent provided in subdivision (i)(*b*) of this subparagraph.

(b) *Taxpayers other than corporations for taxable years beginning after December 31, 1963*—(1) *In general.* If a taxpayer other than a corporation sustains a net capital loss for any taxable year beginning after December 31, 1963, the portion thereof which is a short-term capital loss carryover shall be carried over to the succeeding taxable year and treated as a short-term capital loss sustained in such succeeding taxable year, and the portion thereof which constitutes a long-term capital loss carryover shall be carried over to the succeeding taxable year and treated as a long-term capital loss sustained in such succeeding taxable year. The carryovers are included in the succeeding taxable year in the determination of the amount of the short-term capital loss, the net short-term capital gain or loss, the long-term capital loss, and the net long-term capital gain or loss in such year, the net capital loss in such year, and the capital loss carryovers from such year. For purposes of this subparagraph:

(i) A short-term capital loss carryover is the excess of the net short-term capital loss for the taxable year over the net long-term capital gain for such year, and

(ii) A long-term capital loss carryover is the excess of the net long-term capital loss for the taxable year over the net short-term capital gain for such year.

(2) *Special rules for determining a net short-term capital gain or loss for purposes of carryover*—(i) *Taxable years beginning after December 31, 1963, and before January 1, 1970.* In determining a net short-term capital gain or loss of a taxable year beginning after December 31, 1963, and before January 1, 1970, for purposes of computing a short-term or long-term capital loss carryover to the succeeding taxable year, an amount equal to the additional allowance deductible under section 1211(b) for the taxable year (determined as provided

in section 1211(b), as in effect for taxable years beginning before January 1, 1970, and § 1.1211–1(b)(5)) is treated as a short-term capital gain occurring in such year.

(ii) *Taxable years beginning after December 31, 1969.* In determining a net short-term capital gain or loss of a taxable year beginning after December 31, 1969:

(*a*) For purposes of computing a short-term capital loss carryover to the succeeding taxable year, an amount equal to the additional allowance for the taxable year (determined as provided in section 1211(b) and § 1.1211–1(b)(2)) is treated as a short-term capital gain occurring in such year, and

(*b*) For purposes of computing a long-term capital loss carryover to the succeeding taxable year, an amount equal to the sum of the additional allowance for the taxable year (determined as provided in section 1211(b) and § 1.1211–1(b)(2)), plus the excess of such additional allowance over the net short-term capital loss (determined without regard to section 1212(b)(2) for such year) is treated as a short-term capital gain in such year.

The rules provided in this subdivision are for the purpose of taking into account the additional allowance deductible for the current taxable year under section 1211(b) and § 1.1211–1(b)(2) in determining the amount and character of capital loss carryovers from the current taxable year to the succeeding taxable year. Their practical application to a determination of the amount and character of capital loss carryovers from the current taxable year to the succeeding taxable year involves identification of the net long-term and net short-term capital loss components of the additional allowance deductible in the current taxable year as provided by § 1.1211–1(b)(2)(iii). To the extent that the additional allowance is composed of net short-term capital losses, such losses are treated as a short-term capital gain in the current taxable year in determining the capital loss carryovers to the succeeding year. To the extent that the additional allowance is composed of net long-term capital losses applied pursuant to the provisions of § 1.1211–1(b)(2)(iii), an amount equal to twice the amount of such component of the additional allowance is treated as a short-term capital gain in the current taxable year. See paragraph (4) of this section for transitional rules if any part of the additional allowance is composed of net long-term capital losses carried to the current taxable year from a taxable year beginning before January 1, 1970.

(3) *Transitional rule for net capital losses sustained in a taxable year beginning before January 1, 1964.* A taxpayer other than a corporation sustaining a net capital loss for any taxable year beginning before January 1, 1964, shall treat as a short-term capital loss in the first taxable year beginning after December 31, 1963, any amount which would be treated as a short-term capital loss in such year under subchapter P of chapter 1 of the Code as in effect immediately before the enactment of the Revenue Act of 1964.

(4) *Transitional rule for net long-term capital losses sustained in a taxable year beginning before January 1, 1970.* In the case of a net long-term capital loss sustained by a taxpayer other than a corporation in a taxable year beginning prior to January 1, 1970 (referred to in this section as a *pre-1970 taxable year*) which is carried over and treated as a long-term capital loss in the first taxable year beginning after December 31, 1969 (referred to in this section as a *post-1969 taxable year*), the transitional additional allowance deductible under section 1211(b) for the taxable year shall be determined by application of section 1211(b) as in effect for pre-1970 taxable years and § 1.1211–1(b)(3), and the amount of such long-term capital loss carried over and treated as a long-term capital loss in the succeeding taxable year shall be determined by application of section 1212(b)(1) as in effect for pre-1970 taxable years and subparagraph (2)(i) of this paragraph (instead of under sections 1211(b) and 1212(b)(1) as in effect for post-1969 taxable years and § 1.1211–1(b)(2) and subparagraph (2)(ii) of this paragraph, respectively) but only to the extent that such pre-1970 long-term capital loss constitutes a *transitional net long-term capital loss component* (determined as provided in § 1.1211–1(b)(3)(ii)) in the taxable year to which such pre-1970 long-term capital

loss is carried. Thus, for purposes of paragraph (2) of this section, to the extent that a component of the transitional additional allowance deductible for a post-1969 taxable year under section 1211(b) and § 1.1211–1(b)(3)(i) is a transitional net long-term capital loss component carried over to such post-1969 taxable year, such component shall be treated as a short-term capital gain in determining the amount and character of capital loss carryovers from such post-1969 taxable year to the succeeding taxable year. Such component shall be so treated as a short-term capital gain in full on a dollar-for-dollar basis and shall not be doubled for this purpose as is provided by subdivision (ii) of paragraph (2) of this section in the case of a component of the additional allowance made up of net long-term capital losses applied pursuant to the provisions of § 1.1211–1(b)(2)(iii). The transitional rule provided in this paragraph does not apply to a determination of the character of capital losses (as long-term or short-term) actually deductible for the current taxable year under section 1211(b) and § 1.1211–1(b).

(5) *Examples*. The application of this paragraph can be illustrated by the following examples:

Example 1. For the taxable year 1971, an unmarried individual has taxable income for purposes of section 1211(b) of $8,000, a long-term capital loss of $2,000, and no other capital gains or losses. $1,000 (one-half) of the net long-term capital loss is deductible in 1971 as the additional allowance deductible under section 1211(b). No amount of capital loss remains to be carried over to the succeeding taxable year.

Example 2. For the taxable year 1972, the same unmarried individual has taxable income for purposes of section 1211(b) of $8,000, a long-term capital loss of $3,000 and no other capital gains or losses. $1,500 (one-half of the excess net capital loss) is deductible in 1972, but limited to the $1,000 maximum additional allowance deductible under section 1211(b). By application of section 1212(b)(1), he will carry over to 1973 a long-term capital loss of $1,000 determined as follows:

Net long-term capital loss		($3,000)
Additional allowance deductible under section 1211(b)	$1,000	
Excess of additional allowance over net short-term capital loss (determined without regard to section 1212(b)(2)(B)(i))	1,000	
Total amount treated as short-term capital gain under 1212(b)(2)(B) for purposes of determining carryover		2,000
Long-term capital loss carryover to 1973		(1,000)

If, in 1973, he had taxable income for purposes of section 1211(b) of $8,000, but no capital gains or losses, $500 (one-half) of the net long-term capital loss carryover from 1972 would be deductible in 1973 as the additional allowance deductible under section 1211(b). No amount of capital loss would be carried over to 1974.

Example 3. For the taxable year 1971, an unmarried individual has taxable income for purposes of section 1211(b) of $9,000, a $500 short-term capital gain, a $700 short-term capital loss, a $1,000 long-term capital gain and a $1,700 long-term capital loss. He will offset $1,500 of capital losses against capital gains. The excess net capital loss of $900 is deductible in 1971 to the extent of a $550 additional allowance deductible under 1211(b) which is smaller than both $1,000 and taxable income for purposes of section 1211(b), determined as follows:

Losses allowed to the extent of gains	($1,500)
Amount allowed under section 1211(b)(1)(C):	
(i) Excess of net short-term capital loss over net long-term capital gain	(200)
(ii) One-half of the excess of net long-term capital loss over net short-term capital gain	(350)
Additional allowance deductible under section 1211(b)	550

The total amount treated as short-term capital gain under section 1212(b)(2)(B) for purposes of determining any carryover to the succeeding taxable year exceeds $900. No amount of net capital loss remains to be carried over to the succeeding taxable year.

Example 4. If in example (3) above, the long-term capital loss had been $2,800, the taxpayer would carry over $200 of long-term capital loss to 1972, determined as follows:

Losses allowed to extent of gains	($1,500)
Amount allowed under section 1211(b)(1) (B) and (C):	
(i) Excess of net short-term capital loss over net long-term capital gain	(200)
(ii) One-half the excess of net long-term capital loss over net short-term capital gain	(900)

as limited by 1211(b)(1)(B) to an additional allowance of $1,000.

Carryover under section 1212(b)(1):	
Net long-term capital loss for 1971	($1,800)
Additional allowance under section 1211(b)(1)(B)	1,000
Excess of additional allowance deductible under section 1211(b) over net short-term capital loss determined without regard to section 1212(b)(2)(B)(i) ($1,000 less $200)	800

Total amount treated as short-term capital gain under section 1212(b)(2)(B) for purposes of determining carryover	1,800
Short-term capital gain for 1971	500
Total short-term capital gain	2,300
Short-term capital loss for 1971	(700)
Net short-term capital gain	1,600
Long-term capital loss carryover ($1,800 less $1,600)	200

Example 5. For 1969, an unmarried individual has taxable income for purposes of section 1211(b) of $8,000, a long-term capital loss of $3,000, and no other capital gains or losses. He is allowed to deduct in 1969 $1,000 as the additional allowance deductible under section 1211(b) (as in effect for pre-1970 taxable years) and to carry over to 1970, a long-term capital loss of $2,000 under section 1212(b) (as in effect for pre-1970 taxable years).

If, in 1970, the same unmarried individual with taxable income for purposes of section 1211(b) of $8,000, has no capital gains or losses, he would deduct $1,000 of his pre- 1970 capital loss carryover as the transitional additional allowance deductible under section 1211(b) (as in effect for pre-1970 years) and carry over under section 1212(b)(1) (as in effect for pre-1970 taxable years) to 1971 the remaining $1,000 as a pre-1970 long-term capital loss.

If, in 1970, the same individual instead has a long-term capital gain of $2,500, and a long-term capital loss of $1,500, he would net these two items with the $2,000 carried to 1970 as a long-term capital loss. Thus, he would have a net long-term capital loss for 1970 of $1,000 which is deductible in 1970 as the transitional additional allowance deductible under section 1211(b). He would have no amount to carry over under section 1212(b)(1) to 1971.

If, in 1970, the same individual instead has a long-term capital loss of $1,200, and a long-term capital gain of $200, resulting in a net long-term capital loss of $3,000 when netted with the $2,000 carried to 1970 as a long-term capital loss, he would deduct $1,000 in respect of his pre-1970 long-term capital loss carryover as the transitional additional allowance deductible under section 1211(b) (as in effect for pre-1970 taxable years) and carry over under section 1212(b)(1) (as in effect for pre-1970 taxable years) to 1971 the remaining $1,000 of the pre-1970 component of his long-term capital loss carryover, and the $1,000 net long-term capital loss actually sustained in 1970 as the second component of his long-term capital loss carryover.

Example 6. For 1970 a married individual filing a separate return has taxable income of $8,000, a long-term capital loss of $3,500 and a short-term capital gain of $3,000. He also has a pre-1970 short-term capital loss of $2,000 which is carried to 1970. The $3,000 short-term capital gain realized in 1970 would first be reduced by the $2,000 short-term capital loss carryover, and then the remaining $1,000 balance of the short-term capital gain would be offset against the $3,500 long-term capital loss, producing a net long-term capital loss of $2,500, no part of which is a net long-term capital loss carried over from 1969. However, under the special rule of §1.1211–1(b)(7)(ii) in 1970, the taxpayer would deduct as the additional allowance deductible under section 1211(b), the $500 limitation in §1.1211–1(b)(2)(ii) in the case of a married taxpayer filing a separate return in a taxable year ending after December 31, 1969, plus the *transitional net short-term capital loss component* of $2,000 computed under §1.1211–1(b)(3)(iv), but limited to a total deduction of $1,000. The $1,000 additional allowance deductible under section 1211(b) would absorb $2,000 of the $2,500 net long-term capital loss, and he would carry the unused $500 balance of such loss to 1971 for use in that year.

Example 7. For 1970, an unmarried individual filing a separate return has taxable income for purposes of section 1211(b) of $8,000, and a long-term capital loss of $2,000. He also has a pre-1970 long-term capital loss of $2,500 which is carried to 1970. In 1970, the taxpayer would deduct as the transitional additional allowance deductible under section 1211(b) $1,000, absorbing $1,000 of the pre-1970 long-term capital loss of $2,500. He would carry to 1971 the unused $1,500 balance of his pre-1970 long-term capital loss plus the 1970 long-term capital loss of $2,000, or a total of $3,500, for use in 1971.

For 1971, the same taxpayer filing a separate return with taxable income for purposes of section 1211(b) of $8,000, has a $3,600 long-term capital gain and a $2,200 long-term capital loss. When these gains and losses are combined with the long-term capital loss carryover from 1970 of $3,500, a net long-term capital loss of $2,100 results. He would deduct $1,000 as the transitional additional allowance deductible under section 1211(b). The $1,000 additional allowance would absorb $100 of the unused pre-1970 long-term capital loss carryover of $1,500 plus $1,800 of the unused post-1969 long-term capital loss carryover of $2,100 (the amount of the 1971 net long-term capital loss necessary to make up the remaining $900 balance of the additional allowance). Although a component of the 1971 net long-term capital loss is the unused pre-1970 long-term capital loss carryover of $1,500, only $100 of this carryover is available for use in full on a dollar-for-dollar basis in computing the transitional additional allowance for 1971 since it only exceeds by that amount the $1,400 net capital gain (capital gain net income for taxable years beginning after December 31, 1976) actually realized in 1971 all of which is net long-term capital gain (long-term capital gain of $3,600 reduced by long-term capital loss of $2,200). See §1.1221–1(b)(3)(ii). The taxpayer would carry over to 1972 as a long-term capital loss the remaining $200 of the 1971 long-term capital loss.

Example 8. For 1970, an unmarried individual has taxable income for purposes of section 1211(b) of $8,000 and a short-term capital loss of $700. He also has a pre-1970 long-term capital loss carryover of $1,200. He would deduct $1,000 as the transitional additional allowance deductible under section 1211(b). The $1,000 transitional additional allowance would be composed of the 1970 short-term capital loss of $700 and $300 of the pre-1970 long-term capital loss carryover. He would carry over to 1971 the unused $900 balance of his $1,200 pre-1970 long-term capital loss carryover for use in 1971.

(c) *Husband and wife.* (1) The following rules shall be applied in computing capital loss carryovers by husband and wife:

(i) If a husband and wife making a joint return for any taxable year made separate returns for the preceding year, any capital loss carryovers of each spouse from such preceding taxable year may be carried forward to the taxable year in accordance with paragraph (a) or (b) of this section.

(ii) If a joint return was made for the preceding taxable year, any capital loss carryover from such preceding taxable year may be carried forward to the taxable year in accordance with paragraph (a) or (b) of this section.

(iii) If a husband and wife make separate returns for the first taxable year beginning after December 31, 1963, or any prior taxable year, and they made a joint return for the preceding taxable year, any capital loss carryover from such preceding taxable year shall be allocated to the spouses on the basis of their individual net capital loss which gave rise to such capital loss carryover. The capital loss carryover so allocated to each spouse may be carried forward by such spouse to the taxable year in accordance with paragraph (a) or (b) of this section.

(iv) If a husband and wife making separate returns for any taxable year following the first taxable year beginning after December 31, 1963, made a joint return for the preceding taxable year, any long-term or short-term capital loss carryovers shall be allocated to the spouses on the basis of their individual net long-term and net short-term capital losses for the preceding taxable year which gave rise to such capital loss carryovers, and the portions of the long-term or short-term capital loss carryovers so allocated to each spouse may be carried forward by such spouse to the taxable year in accordance with paragraph (b) of this section.

(v) If separate returns are made both for the taxable year and the preceding taxable year, any capital loss carryover of each spouse may be carried forward by such spouse in accordance with paragraph (a) or (b) of this section.

(2) The provisions of subparagraph (1) (i), (iii), and (iv) of this paragraph may be illustrated by the following examples:

Example 1. If H and W, husband and wife, make a joint return for 1955, having made separate returns for 1954 in which H had a net capital loss of $3,000 and W had a net capital loss of $2,000, in their joint return for 1955 they would have a short-term capital loss of $5,000 (the sum of their separate capital loss carryovers from 1954), allowable in accordance with paragraph (a) of this section. If, on the other hand, they make separate returns in 1955 following a joint return in 1954 in which their net capital loss was $5,000 allocable $3,000 to H and $2,000 to W, the carryover of H as a short-term capital loss for the purpose of his 1955 separate return would be $3,000 and that of W for her separate return would be $2,000, each allowable in accordance with paragraph (a) of this section.

Example 2. H and W, husband and wife, make separate returns for 1966 following a joint return for 1965. The capital gains and losses incurred by H and W in 1965, including those carried over by them to 1965, were as follows:

	H	W
Long-term capital gains	$8,000	$9,000
Long-term capital losses	(15,000)	(6,000)
Short-term capital gains	10,000	4,000
Short-term capital losses	(19,000)	(5,000)

Thus, in 1965 H and W had a net capital loss of $14,000 on their joint return. Of this amount, $4,000 was a long-term capital loss carryover, and $10,000 was a short-term capital loss carryover, determined in accordance paragraph (b) of this section. H's net long-term capital loss was $7,000 for 1965. This amount was offset on the joint return by W's net long-term capital gain of $3,000. Thus, H may carry over to his separate return for 1966, a long-term capital loss carryover of $4,000. H and W may carry over to their separate returns for 1966, as short-term capital loss carryovers, the amounts of their respective net short-term losses from 1965, $9,000 and $1,000.

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GENERAL RULES FOR DETERMINING CAPITAL GAINS AND LOSSES

§ 1.1221–1 Meaning of terms.

(a) The term *capital assets* includes all classes of property not specifically excluded by section 1221. In determining whether property is a *capital asset,* the period for which held is immaterial.

(b) Property used in the trade or business of a taxpayer of a character which is subject to the allowance for depreciation provided in section 167 and real property used in the trade or business of a taxpayer is excluded from the term *capital assets.* Gains and losses from the sale or exchange of such property are not treated as gains and losses from the sale or exchange of capital assets, except to the extent provided in section 1231. See §1.1231–1. Property held for the production of income, but not used in a trade or business of the taxpayer, is not excluded from the term *capital assets* even though depreciation may have been allowed with respect to such property under section 23(l) of the Internal Revenue Code of 1939 before its amendment by section 121(c) of the Revenue Act of 1942 (56 Stat. 819). However, gain or loss upon the sale or exchange of land held by a taxpayer primarily for sale to customers in the ordinary course of his business, as in the case of a dealer in real estate, is not subject to the provisions of subchapter P (section 1201 and following), chapter 1 of the Code.

(c)(1) A copyright, a literary, musical, or artistic composition, and similar property are excluded from the term *capital assets* if held by a taxpayer whose personal efforts created such property, or if held by a taxpayer in whose hands the basis of such property is determined, for purposes of determining gain from a sale or exchange, in whole or in part by reference to the basis of such property in the hands of a taxpayer whose personal efforts created such property. For purposes of this subparagraph, the phrase *similar property* includes for example, such property as a theatrical production, a radio program, a newspaper cartoon strip, or any other property eligible for copyright protection (whether under statute or common law), but does not include a patent or an invention, or a design which may be protected only under the patent law and not under the copyright law.

(2) In the case of sales and other dispositions occurring after July 25, 1969, a letter, a memorandum, or similar property is excluded from the term *capital asset* if held by (i) a taxpayer whose personal efforts created such property, (ii) a taxpayer for whom such property was prepared or produced, or (iii) a taxpayer in whose hands the basis of such property is determined, for purposes of determining gain from a sale or exchange, in whole or in part by reference to the basis of such property in the hands of a taxpayer described in subdivision (i) or (ii) of this subparagraph. In the case of a collection of letters, memorandums, or similar property held by a person who is a taxpayer described in subdivision (i), (ii), or (iii) of this subparagraph as to some of such letters, memorandums, or similar property but not as to others, this subparagraph shall apply only to those letters, memorandums, or similar property as to which such person is a taxpayer described in such subdivision. For purposes of this subparagraph, the phrase *similar property* includes, for example, such property as a draft of a speech, a manuscript, a research paper, an oral recording of any type, a transcript of an oral recording, a transcript of an oral interview or of dictation, a personal or business diary, a log or journal, a corporate archive, including a corporate charter, office correspondence, a financial record, a drawing, a photograph, or a dispatch. A letter, memorandum, or property similar to a letter or memorandum, addressed to a taxpayer shall be considered as prepared or produced for him. This subparagraph does not apply to property, such as a corporate archive, office correspondence, or a financial record, sold or disposed of as part of a going business if such property has no significant