

ALI-ABA Course of Study  
Consolidated Tax Return Regulations

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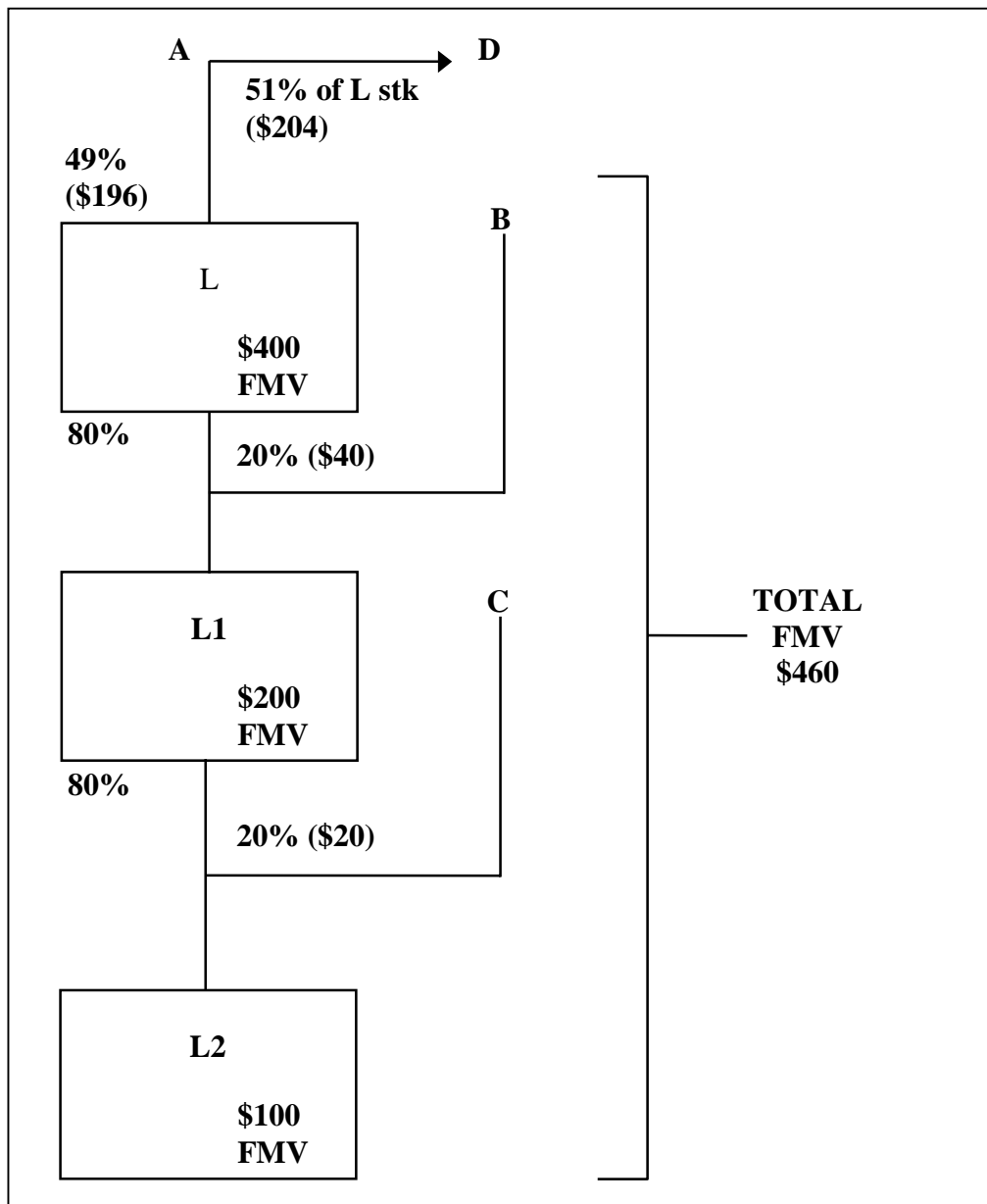
PROBLEM SET AND GLOSSARY OF TERMS  
FOR THE SECTION 382/SRLY CONSOLIDATED  
RETURN REGULATIONS

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Example 1

STATIC GROUP/NO SHIFT IN SUBSIDIARY STOCK



EXAMPLE 1

STATIC GROUP/NO SHIFT IN SUBSIDIARY STOCK

- I. A sells 51% of the L stock to D. The L group is a loss group because at least one of its members has NOLs attributable to a consolidated return year. § 1.1502-91T(c)(1).
  - A. Note that if all of the losses of L1 and L2 were SRLY losses which were not limited by section 382 in connection with the acquisition of those losses by the L consolidated group then the section 382 analysis with respect to those losses would be governed solely by § 1.382-2T. These losses are often referred to as "separately tracked" losses. See examples 4 and 5.
  - B. Where there are both non-SRLY losses and separately tracked losses, two sets of rules will simultaneously apply.
  
- II. The L loss group has an ownership change under the Parent Change rule because there has been an ownership change under § 1.1502-92T(b)(1). That means the non-separately tracked losses will be limited by the consolidated section 382 limitation. There is an ownership change with respect to the non-SRLY losses attributable to L1 and L2 even though there is less than a 50 percentage point increase in the stock ownership of each corporation (because of the minority stock interests of B and C).
  - A. If an ownership change of the common parent is anticipated but this change would not cause an ownership change to one or more subsidiaries, deconsolidation of those subsidiaries may be advantageous depending upon the income earning ability of the subsidiaries, the amount of losses attributable to them and the other effects of deconsolidation,
  - B. Thus, if prior to A's sale to D, L sells 2% of the L1 stock to B, the ownership change of L will not cause an ownership change for L1 and L2. That is, because of the prior deconsolidation, the analysis of L1 and L2 with respect to the stock sale by A to D is made on a separate entity basis with the result that D and B have jointly increased their ownership interest in L1 and L2 by only 42% and 33%, respectively. § 1.1502-95T(b)(1) (treating a corporation on a separate entity basis after ceasing to be a member of a consolidated group).
  - C. Note, the timing of the deconsolidation is crucial to avoiding an ownership change. L's sale of the 2% stock interest must occur before the ownership change occurs with respect to the L loss group. Otherwise, L1 and L2 losses are subject to a zero section 382 limitation as to their share of losses unless L elects to

apportion some portion of the L loss group's consolidated section 382 limitation to L1 and L2. § 1.1502-95T(b)(2) (pre-change consolidated attributes subject to the consolidated section 382 limitation continue to be treated as a pre-change loss with respect to the former member).

III. The consolidated section 382 limitation for the L loss group is based on the total value of the stock of the members, other than stock that is directly or indirectly owned by another member. § 1.1502-93T(b)(1).

A. Thus, the value of the stock of L1 and L2 held by L and L1, respectively, is not taken into account in determining the L loss group's consolidated section 382 limitation.

B. The total value under the facts is \$460, computed as follows:

A's and D's L stock	\$400
B's 20% of L1 stock	40 (20% of \$200)
C's 20% of L2 stock	<u>20</u> (20% of \$100)
Total Value	<u>\$460</u>

IV. Due diligence issues in anticipating a group consolidated section 382 limitation:

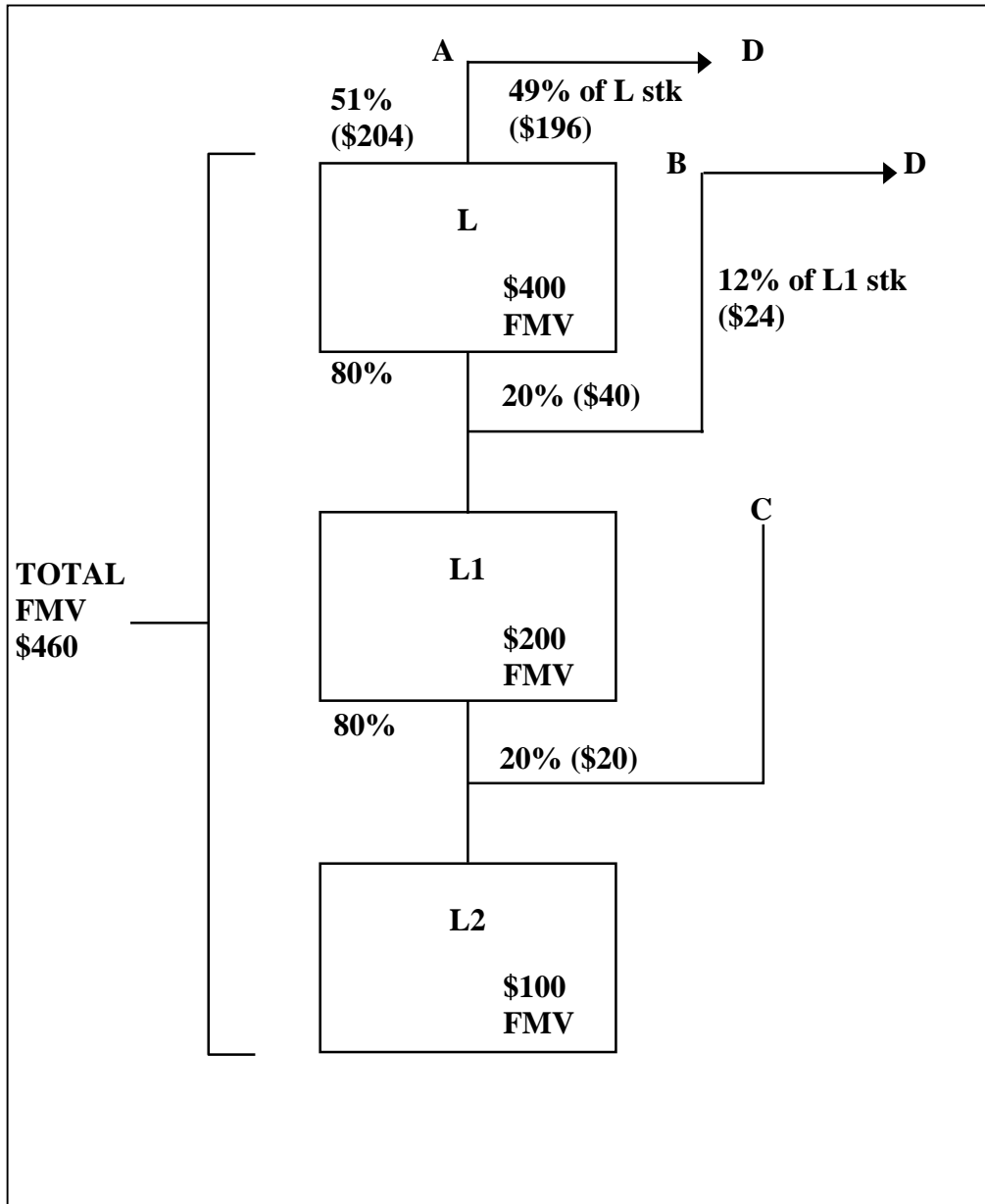
A. Capital contributions by virtue of stock issuances, including section 1504(a)(4) stock issuances by subsidiary members.

B. Obtain history relating to successive ownership changes as to group, any subgroup, or member.

C. Consider application of corporate contraction rules under section 382(e) that may apply to debt financed acquisitions to reduce value of target group, any target subgroup or target member.

D. Manipulating timing of income/loss before and after the change date to enhance loss utilization.

STATIC GROUP/SHIFT IN SUBSIDIARY STOCK



V. L1 has a 51.2% owner shift due to sales by A and B

STATIC GROUP/SHIFT IN SUBSIDIARY STOCK

- VI. A sells only 49% of the L stock to D, and B sells 12% of the L1 stock to D. Sales of subsidiary stock are generally ignored in applying, the required ownership change analysis under the consolidated return regulations. §§ 1.1502-92T(b)(1)(i) and 1.1502-92T(b)(2), Example 2.
- A. Therefore, absent the application of a special rule that supplements the parent change method, the sales of subsidiary L1 stock generally will not cause an ownership change of the L loss group or L1 even if there were a more than 50 percentage point change in L1 stock ownership as determined on a separate entity basis. § 1.1502-91T(a)(1) (making applicable §§ 1.1502-91T through 1.1502-93T to determine whether there is an ownership change with respect to pre-change consolidated attributes and pre-change subgroup attributes).
- B. Special rules that may apply in addition to the Parent Change Method include:
- Supplemental Group Change Method (also known as the "throw-up" method) which may cause an ownership change of the loss group. § 1.1502-92T(c)(1).
- Supplemental anti-abuse rules for causing an ownership change with respect to a subsidiary on a separate entity (or loss subgroup) basis even though there is not an ownership change with respect to the loss group. § 1.1502-96T(b).
- VII. The Supplemental Group Change Method of § 1.1502-92T(c) may apply in addition to the Parent Change Method (see § 1.1502-92T(c)(1) flush language) if a 5-percent shareholder of the common parent increases his interest in both a subsidiary of the loss group and the common parent and those increases occur within the 3 year testing period.
- A. If the Supplemental Group Change Method applies to these facts, the value of the L1 stock acquired by D (but no other minority stock) is treated as if it were issued by L in determining whether there is an ownership change of the L loss group. § 1.1502-92T(c)(4). L therefore would be considered as having \$424 of stock outstanding (\$400 of its own stock plus \$24 attributable to the L1 stock purchased by D (but none of the L1 stock retained by B). See § 1.382-2T(f)(18) (notwithstanding that D's interest is a minority interest, each share of stock of the same class is treated as having the same value)). Here, there would be an ownership change of the L loss group under the Supplemental Group Change Method because of a 51.89 total percentage point increase in stock ownership of L:

D46.21(from zero to \$196/\$424)

D 5.66(from zero to \$24/\$424)

51.89

- VIII. Assume that an unrelated person, E, instead of D, purchased the stock from B. The Supplemental Group Change Method of § 1.1502-92T(c) may apply in addition to the Parent Change Method (see § 1.1502-92T(c)(1) flush Language) if a 5-percent shareholder and anyone else (whether or not a 5-percent shareholder in his own right) acting pursuant to a plan or arrangement increases his ownership in the common parent and a subsidiary during a testing period.
- A. If the Supplemental Group Change Method applies to these facts, the value of the L1 stock acquired by E (but no other minority stock) is treated as if it were issued by L in determining whether there is an ownership change of the L loss group. § 1.1502-92T(c)(4)). L therefore would be considered as having \$424 of stock outstanding (\$400 of its own stock plus \$24 attributable to the L1 stock purchased by E). Here, there would be an ownership change of the L loss group under the Supplemental Group Change Method because of a 51.89 total percentage point increase in stock ownership of L:

D46.23(from zero to \$196/\$424)

E 5.66(from zero to \$24/\$424)

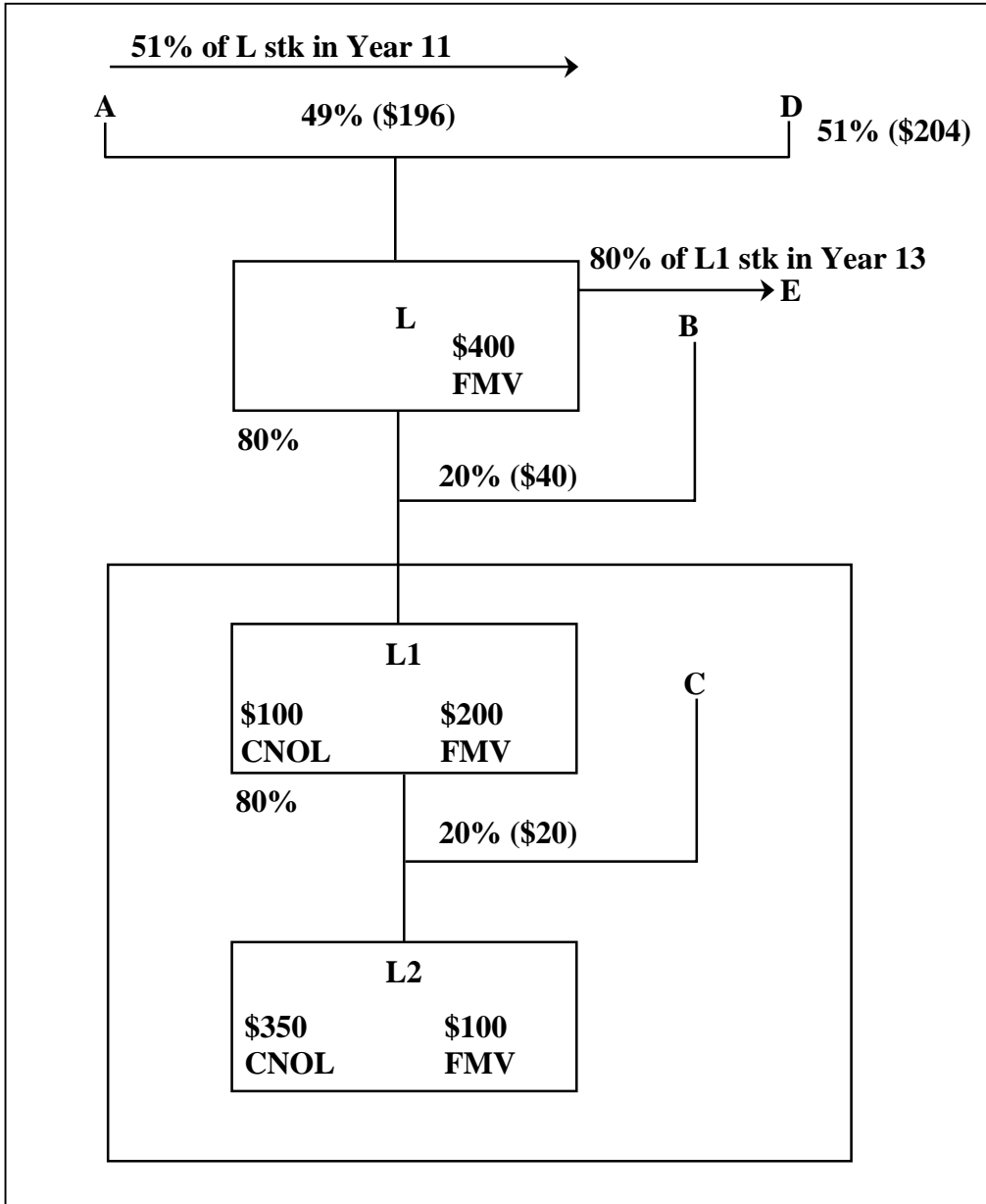
51.89

- IX. Supplemental Group Change Method rule appears to require only a very attenuated relationship between the owner shift activity at both the parent and subsidiary level.
- A. Example 2 of § 1.1502-92T(c)(5) makes clear that the alternative, additional ownership change test may apply where purchasing shareholders are acting independently of one another -- 49% stock purchase by individual B and public offering of subsidiary stock to public shareholders.
- X. Due diligence for Supplemental Group Change Method may require inquiry and representations that any offerings of subsidiary stock or other transfer of subsidiary stock were not in connection with or in anticipation of owner shifts with respect to the common parent.
- A. Beware of problem of highly leveraged common parent where subsidiary may represent a substantial portion of the total value of the consolidated group. In that case, a relatively small increase in the percentage ownership of the subsidiary can result in an ownership change for the group under the Supplemental Group Change Method.
- XI. Note that the Supplemental Group Change Method will apply even if the subsidiary whose stock is transferred has no losses.
- XII. Special Subsidiary Ownership Change Rules. Subject to only two exceptions, an ownership change with respect to the CNOLs of a subsidiary generally can occur only if

there is an ownership change with respect to the loss group of which the subsidiary is a member or if there is an ownership change with respect to the subsidiary in a transaction in which the subsidiary leaves the loss group. See § 1.1502-91T. The first exception is found in the application of the option attribution rules with respect to subsidiary stock. The second exception applies when stock of the loss subsidiary and any other subsidiary that has a direct or indirect ownership interest in such subsidiary is acquired pursuant to a plan or arrangement to shift more than 50% of the subsidiary's equity outside the group. In either of these cases, a subsidiary will be subject to section 382 on a separate entity basis even though the subsidiary has not left the loss group.

- A. 20-Percent Options. An option (other than an option with respect to the common parent's stock) held by a person, or persons acting pursuant to a "plan or arrangement," to acquire more than 20% of the subsidiary's stock is subject to the option attribution rules of section 382, and the ownership change analysis is applied on a separate entity basis. § 1.1502-96T(b)(1)(i). An exception applies for an option created under a bilateral contract to purchase stock as long as the option is exercised within one year of this date. § 1.382-4(d)(7)(i).

MEMBER/SUBGROUP DEPARTING A LOSS GROUP



### EXAMPLE 3

#### MEMBER/SUBGROUP DEPARTING A LOSS GROUP

- XIII. L-L1-L2 constitute a loss group which had an ownership change in Year 11 by virtue of A's sale to D. Its consolidated section 382 limitation is \$46, based on the group's \$460 value and a 10% long term tax-exempt rate. In Year 13, L sells 80% of the L1 stock to E, an individual, and L1 and L2 are each apportioned a portion of the L group's CNOLs under § 1.1502-21T(b)(2), and immediately form the L1-L2 loss subgroup since they file a consolidated return for their first taxable year after leaving the L group. The Year 13 tax exempt rate is 7%. Assume also that the group has no adjustments to its \$46 limitation of Year 11.
- XIV. The consolidated section 382 limitation applicable to the losses arising before the ownership change in Year 11 may be divided between L and L1-L2.
- A. L may elect to apportion to the L1-L2 loss subgroup all or any part of the L group's \$46 consolidated section 382 limitation with respect to the CNOLs arising before the first ownership change that L1 and L2 take from the group. § 1.1502-95T(c). Any such apportionment of the consolidated section 382 limitation, however, reduces the limitation retained by the L loss group.
- B. No apportionment considerations apply to the losses arising between the first ownership change for the L loss group and the second ownership change for the L1-L2 subgroup since those losses have not been subject to any limitation.
- XV. If L does not apportion any limitation to the departing L1-L2 loss subgroup, the section 382 limitation for L1 and L2 with respect to their consolidated losses arising before the change date in Year 11 (which continue to be treated as pre-change losses) will be zero. § 1.1502-95T(b)(2)(ii). Because L1 and L2 compose a loss subgroup (even though they file as a separate consolidated group after leaving the L group), L's apportionment is to a loss subgroup, rather than separately to L1 and L2, which generally will maximize the use of their pre-change losses. § 1.1502-95T(b)(3).
- XVI. Note that L can elect to apportion to the departing members even that part of the consolidated section 382 limitation that was based on the value of L's own hard assets on the change date.
- XVII. Assuming that the L1-L2 loss subgroup has an ownership change on leaving the L group, the subgroup section 382 limitation for all of the losses attributable to the period before the second ownership change in Year 13) will be \$15.40 (((\$200 FMV of the L1 stock + \$20 FMV of the L2 stock owned by C) x 7%). Therefore, any apportionment by L of more than \$15.40 of the consolidated section 382 limitation to the L1-L2 loss subgroup will be wasted since the section 382 limitation from the second ownership change will at

all times cap the utilization with respect to losses pre-dating the first ownership change. § 1.1502-96T(c); § 1.382-5T(d).

XVIII. Disposition of subsidiary requires consideration of retention of full consolidated section 382 limitation and subsidiary losses.

- A. Various additional restrictions on use of subsidiary losses (i.e., section 269, section 384 and the SRLY rules) may substantially diminish value of losses as the result of their transfer.
- B. Generate Taxable Income for Year of the Subsidiary's Cessation; For the year in which the subsidiary ceases to be a member of the consolidated group, the CNOLs attributable to the subsidiary are first carried to the consolidated return year of the subsidiary's departure, and only those amounts not absorbed by the selling group are carried to the subsidiary's first separate return year. § 1.1502-21T(b)(2)(ii). Because NOLs of the group are absorbed in the order of the taxable years in which they were sustained, utilization of a departing member's losses depends, in part, on the availability of other earlier sustained losses to the extent that a departing member's share of CNOLs is not absorbed by the selling group for the taxable year of departure, the unused CNOLs are treated as NOLs of the departing member beginning on the first day of the taxable year in which the loss arose. § 1.1502-95T(b)(1)(i).
- C. Reattribution of Losses Under the LDRs; Except to the extent the subsidiary is insolvent and only to the extent loss would be disallowed under the LDR formula set forth in § 1.1502-20(c), the selling group and the subsidiary may agree to reattribute the NOLs of the subsidiary to the common parent of the group. § 1.1502-20(g).
- D. Section 338(h)(10) Election; Absorption and/or retention of a subsidiary's NOLs also may be achieved through the sale of the subsidiary coupled with a section 338(h)(10) election. In this case, the benefit of any net unrealized loss is also retained by the selling group because the assets deemed sold result in a recognized loss which is transferred to the selling group under section 381. See § 1.338(h)(10)-1(e)(2).

XIX. Protective Apportionment; Apportionment is not relevant if the loss group or loss subgroup out of which the subsidiary is being sold has not had an ownership change. If any uncertainty exists as to whether there has been a prior ownership change, as is often the case, a protective apportionment of the limitation (although not authorized by the regulations) may be appropriate.

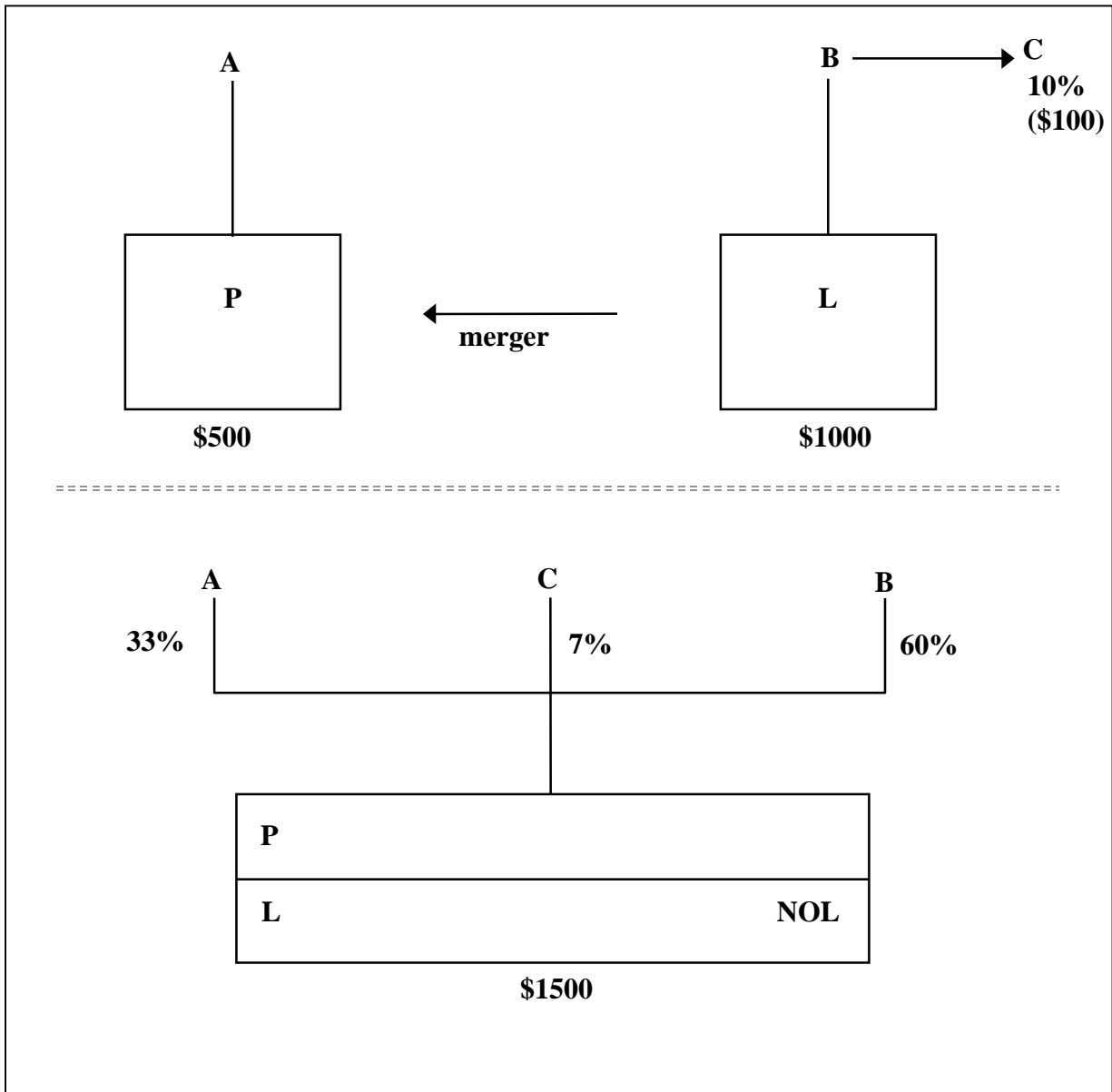
- A. When an apportionment election is made, questions will arise as to whether the apportionment can account for events occurring subsequent to the filing of the election (e.g., audit adjustments or amended returns). Although the "amount of the consolidated section 382 limitation" must be stated in the common parent's apportionment election, perhaps the IRS would permit the amount to be subject to

an accompanying formula or other adjustment to account for events following the filing of the apportionment election.

- B. Section 1.1502-95T(e) provides rules governing the form, time, and manner of an apportionment election. Once made, an apportionment election is revocable only with the consent of the IRS.

Example 4

SEPARATE TRACKING OF SRLY/PRE-REORGANIZATION LOSSES  
UNDER § 1.382-2T



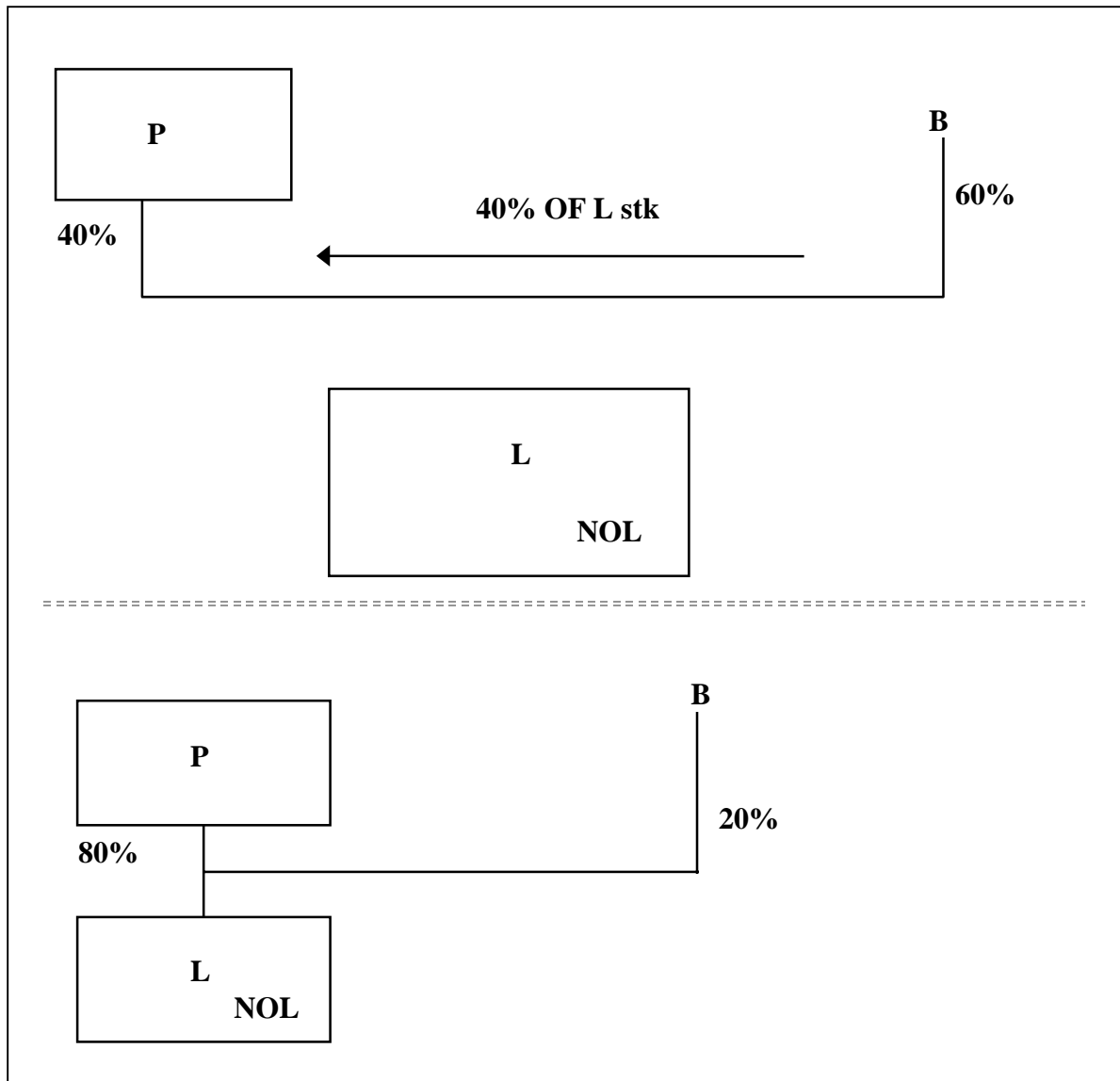
#### EXAMPLE 4

#### SEPARATE TRACKING OF SRLY/PRE-REORGANIZATION LOSSES UNDER § 1.382-2T

- XX. L is 10% on its way toward an ownership change because of B's sale of \$100 of L stock to C during the testing period. L merges into P in a section 381(a) transaction, with B and C acquiring \$900 and \$100 of P stock, respectively, in exchange for their L stock.
- XXI. Although L does not have an ownership change under § 1.382-2T(g) as the result of the merger, L is 40% on its way toward an ownership change following the merger since A and C increased their stock ownership in P (as a successor to L) by 33-1/3% and 6-2/3%, respectively, during the course of the testing period.
- XXII. Notwithstanding that L no longer exists following the merger, § 1.382-2T(f)(1)(ii) treats L as continuing in existence with respect to its pre-merger NOLs and NUBIL for purposes of testing for a future ownership change. This prevents L's losses from escaping its 40% owner shift through a change of corporate form.
- XXIII. Section 1.382-2T(f)(1)(iv) of the regulation will end the separate tracking of P (as a successor to L) following the earlier of an ownership change of P or the end of the 5 year period during which there is no ownership change of P.
- XXIV. Note that the merger of L and P may constitute a capital contribution of P's assets to L within the meaning of section 382(1)(1). See H.R. Rep. No. 426, 99th Cong., 2d Sess. 269 (1986). If L has an ownership change with respect to its separately tracked losses within 2 years after the merger, P's value as of the time immediately prior to its merger with L may be excluded in computing its section 382 limitation.

Example 5

SEPARATE TRACKING OF SRLY/PRE-REORGANIZATION LOSSES  
UNDER §1.1502-96T(a)



## Example 5

### SEPARATE TRACKING OF SRLY/PRE-REORGANIZATION LOSSES UNDER §1.1502-96T(a)

XXV. P and B have owned 40% and 60%, respectively, of L for more than 3 years. P acquires 40% of the L stock from B, and P and L commence filing consolidated returns.

XXVI. L does not have an ownership change under § 1.382-2T(g). L, however, is 40% on its way toward an ownership change following, the stock acquisition.

XXVII. Under § 1.1502-94T(a)(1), L is a new loss member because it carries over an NOL from a SRLY into the P group and is not part of a loss subgroup. Therefore, §§ 1.1502-94T and 1.382-2T apply to L.

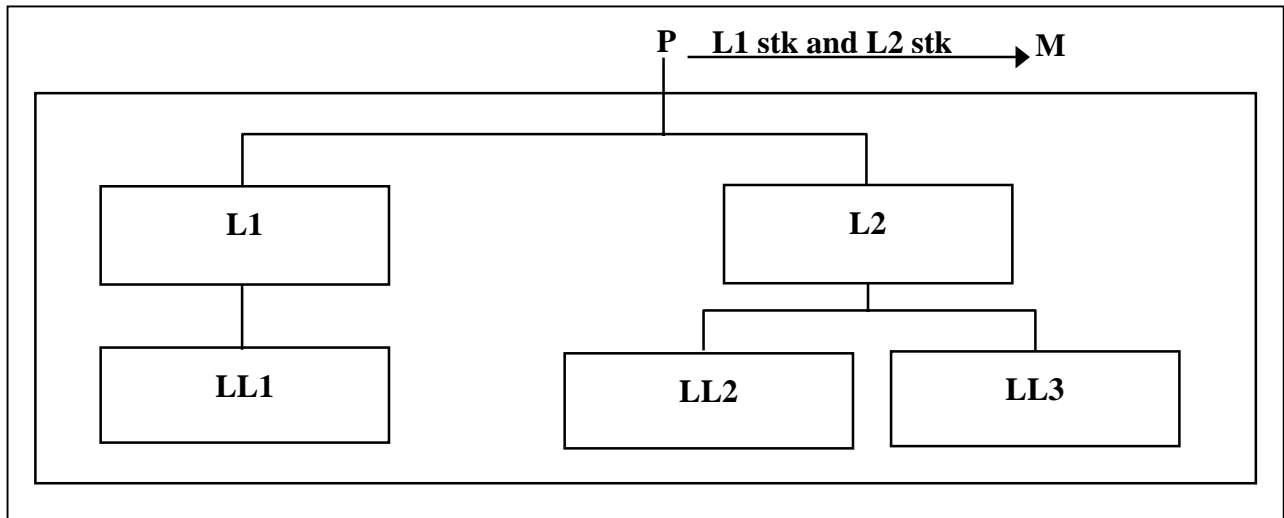
XXVIII. Section 1.1502-96T(a) will end this separate tracking of L following an ownership change of L or the end of the 5-year period during which there is no ownership change of L. For section 382 purposes, a target for which separate tracking has ended is treated as if it always had been a member of the acquiring group. This rule may have some surprising consequences. For example, the NUBIL of the target may cause an otherwise de minimis NUBIL of the acquiring group to become subject to section 382 risks.

A. Consider an acquiring group, X, with a NUBIL of \$9.8 million, which is less than the section 382(h)(3)(B)(i)(II) de minimis threshold, and which acquires a target having a \$.3 million NUBIL in a transaction causing an ownership change with respect to the target. The built-in loss of X thereafter will be increased by \$.3 million to \$10.1 million, thereby becoming subject to section 382 on an ownership change with respect to X. § 1.1502-96T(a)(2) (aggregating certain NUBILs attributable to a SRLY). For the same reasons, a net unrealized built-in gain ("NUBIG") of the acquiring group may drop below the de minimis threshold as a result of acquiring a target with a NUBIL.

XXIX. Note the abbreviated information statement under § 1.1502-94T(d) may be applicable with respect to L. Separate filing for other than the common parent is avoided if each new loss member is identified and those having an ownership change during the consolidated return year are identified. Consider the application of §§ 1.6662-3(b)(1) and -4(e)(2)(iii) (additional record keeping requirements with respect to penalties).

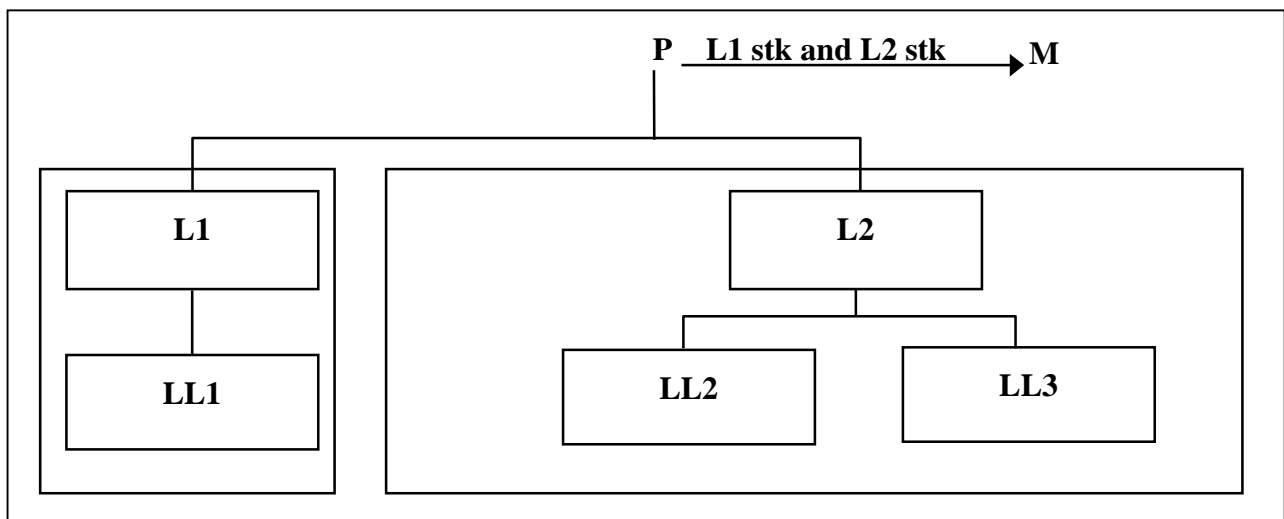
Example 6  
SUBGROUPS - DEFINITIONS

XXX. P owns all the stock of L1 and L2. L1 owns all the stock of LL1 and L2 owns all the stock of LL2 and LL3. P sells all the L1 stock and L2 stock to M, as a consequence of which the L1 and L2 chains of corporations Join the M consolidated group. No corporation has an ownership change resulting from the sale because of common ownership of P and M. All of the losses carried from the P group to the M group arose in the P group and therefore would not be characterized as SRLY losses with respect to the former P Group.



**SRLY subgroup**

**Loss subgroup**



SUBGROUPS - DEFINITIONS

- XXXI. For SRLY purposes, a separate SRLY subgroup is determined for each SRLY loss. Because all of the losses arose in the P group, and the same members simultaneously left the P group and joined the M group, all of the former P group members compose a SRLY subgroup with respect to each SRLY loss. § 1.1502-21T(c)(2). Note that even if L1 and L2 had ownership changes in connection with joining the M group, the SRLY taint is not eliminated by the special section 382 rule (described below) under § 1.1502-96T(a) for purposes of §§ 1.1502-15T and -21T(c).
- XXXII. Under the regulations, SRLY fragmentation (*i.e.*, the computation of the limitation on a member-by-member basis) generally is eliminated. Instead, the SRLY limitation is applied on a subgroup basis so that the SRLY limitation is based on the aggregate contribution to consolidated taxable income by all members included in the SRLY subgroup. § 1.1502-21T(c)(2). The anti-fragmentation rules are mandatory.
- A. NOLS; A SRLY subgroup is identified by reference to each SRLY loss and for each carryforward and carryback. With respect to both carryforwards and carrybacks, the SRLY subgroup members must be continuously affiliated with each other during the period from their affiliation in the group in which the loss arose until the beginning of the year to which the loss is carried. § 1.1502-21T(c)(2)(i), -21T(c)(2)(ii).
- B. No Required Section 1504(a)(1) Relationship; Unlike a section 382 loss subgroup, a SRLY subgroup's members do not need to maintain a section 1504(a)(1) relationship with one another. Thus, a SRLY subgroup does not need to have a subgroup common parent.
- C. Limit on Growing Subgroup Income; Once a subgroup is created, it generally is not permitted to increase its membership except through the creation of a successor. See §§ 1.1502-21T(f)(1), -21T(c)(2)(iv). However, § 1.1502-21T(f)(2) prevents a successor's taxable income from enhancing the separately computed taxable income of the SRLY subgroup unless the successor has acquired substantially all the assets and liabilities of its predecessor. In view of the cumulative computation that is made from year to year, the rule should operate to limit a successor's contribution to consolidated taxable income only on a cumulative (rather than on a year-by-year) basis.
- D. Members Inappropriately Included in a Subgroup; The inclusion of a member with a principal purpose of avoiding the application of, or increasing any limitation under, the SRLY rules will cause all members of the SRLY subgroup to be subject to fragmentation. § 1.1502-21T(c)(2)(iv). For example, this rule could apply if the acquiring group merged one of its profitable members into a newly formed shell holding company common parent of an acquired loss group.

- E. Members Inappropriately Excluded from a Subgroup; A member excluded from the SRLY subgroup with a principal purpose of avoiding the application of, or increasing any limitation under, the SRLY rules will simply be brought back into the subgroup. For example, this rule would apply if a member of the target loss group for which operating deficits are projected were excluded from the subgroup (by, for example, purchasing such member on a different date than the other members of the target loss group), thereby attempting to avoid future deflation of the subgroup's contribution to consolidated taxable income. In addition, this rule could reach the case of a post-acquisition incorporation of a loss division that is not otherwise treated as a successor. Presumably, the regulations cannot (and are not intended to) bring an excluded member back into the SRLY subgroup if the member was disaffiliated (by, for example, causing it to issue preferred stock with 21 percent of the voting power of all classes of voting stock to an unrelated third party).

XXXIII. For consolidated section 382 purposes, a separate loss subgroup is determined for all losses that arose in the same prior group, but only with respect to the members that bear a section 1504(a)(1) relationship (parent-sub) so that a loss subgroup parent can be identified. § 1.1502-91T(d).

- A. Although all of the losses arose in the P group, there are two loss subgroups because of the parent-sub relationship requirement.
- B. Section 1.1502-96T(a) will end the separate tracking of a loss subgroup's attributes following the earlier of an ownership change of the loss subgroup or the end of a 5-year period during which there is no ownership change of the loss subgroup.
- C. There would be only one loss subgroup for section 382 purposes if P contributed the L1 stock to L2 before selling, the L2 stock to M or if M contributed the L1 stock to L2 immediately after the sale. See § 1.1502-91T(d)(4).

XXXIV. Section 382 Loss Subgroup Anti-Abuse Rule; While the consolidated section 382 regulations contemplate that taxpayers may rearrange the configuration of the subsidiaries sold or acquired to qualify for the benefit of the subgroup rules, these benefits are made inapplicable if any subgroup member is "formed, acquired, or availed of" with a principal purpose of avoiding the application of, or increasing, any limitation under section 382. § 1.1502-91T(d)(4).

- A. In view of other anti-abuse rules, including section 382(l)(1) (relating to capital contributions) and § 1.1502-91T(g)(3) (relating to stuffing of built-in gain or loss assets), it is unclear when the more severe rule which fragments the subgroup applies and whether the less onerous anti-abuse rule would apply in instances where both anti-abuse rules are applicable.
- B. In creating subgroups, it may be advisable for the purpose of facilitating a later break-up to create first-tier holding companies to own the stock of two sister

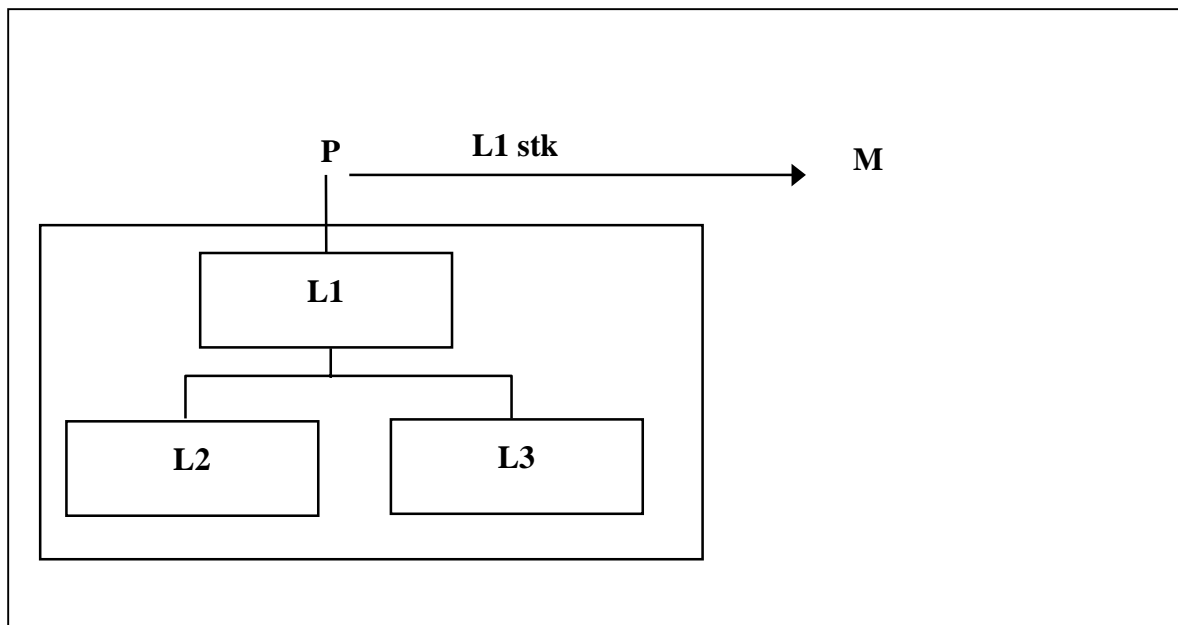
corporations. Note, however, that if the holding company is not aged for 5-years prior to the change date, it may not be treated as a member of the new loss subgroup with respect to the computation of the subgroup's NUBIL. This seems inappropriate if the two sister corporations have satisfied the 5-year requirement. §§ 1.1502-1(f)(4), -91T(j) (for the holding company to be a successor of either of the two sister corporations, it must have been a transferee/distributee of assets from one of those corporations in a nonrecognition transaction).

- C. Advantages of Avoiding the Subgroup Rules; In contrast to the SRLY anti-abuse rule designed to prevent the tax motivated exclusion of a member from a subgroup, no rule prevents a taxpayer from intentionally avoiding the section 382 subgroup rules by excluding a member from the subgroup. Cf. § 1.1502-21T(c)(2)(iv) (second sentence) (excluded member included in SRLY subgroup to prevent avoidance of SRLY rules). For example, P owns L1, which owns all the stock of L2. Both L1 and L2 have NOLS. X wants to acquire L1. L1 and L2, on a consolidated group basis, have a NUBIL of \$12 million equal to L1's separately computed NUBIL of \$21 million and L2's separately computed NUBIG of \$11 million. Depending upon the likelihood that L1 and L2 will need to dispose of or retain their respective built-in gain or loss assets during the recognition period, the amount of NOLs that would be apportioned to each corporation on ceasing to be a member of the P group, and other considerations, it may be desirable for X to first acquire L2 and thereafter L1 for the purpose of creating an \$11 million NUBIG in L2. But see § 1.1502-93T (b)(2) (controlled group principles of § 1.382-8T apply to limitation for L1's NUBIL); see also Basic, Inc. v. United States, 549 F.2d 740 (Ct. Cl. 1977) (treating purchase of parent and subsidiary stock as purchase solely of parent stock where only tax avoidance motivated separate dispositions of parent and subsidiary stock).
- D. Except for the potential manipulation of NUBIL/NUBIG amounts, the controlled group rules of § 1.382-8T largely eliminate any benefit that might otherwise be available from breaking the loss subgroup configuration. See §§ 1.382-8T(c)(5), 1.1502-93T(b)(2). For example, P owns L which owns L1. L has a value of \$200 (including the value of the L1 stock), and L1 has a value of \$150. L and L1 have losses which arose while both were members of the P group. Instead of purchasing only L for \$200, consolidated group X acquires L1 for \$150 and thereafter acquires L for \$200 (value includes the proceeds from the sale of L1 stock), L's loss is a controlled group loss and the section 382 limitation for L's loss generally must be reduced by the value of the stock of L1. § 1.382-8T(c)(5).

**COMPUTATION OF NUBIL/NUBIG  
LOSS SUBGROUP JOINING A GROUP**

XXXV. At the time the L1 loss subgroup joins the M group, the L1 loss subgroup members have the following items:

	<u>Total Net FMV</u>		<u>Asset Net FMV</u>	<u>Asset A/B</u>	<u>(h) (6) Amounts</u>	<u>Gai n/ Loss</u>
L1:	<u>\$300</u>					
		land	\$150	\$120		\$30
		L2 stk	\$120	\$80		N/A
		L3 stk	\$30	\$10		N/A
		built-in deduction			(\$20)	(\$20)
L2:	<u>\$120</u>					
		machine	\$120	\$100		\$20
L3:	<u>\$30</u>					
		built-in income			\$30	<u>\$30</u>
		<b>Total Net Unrealized Built-in Gain</b>				<b>\$60</b>



**COMPUTATION OF NUBIL/NUBIG  
LOSS SUBGROUP JOINING A GROUP**

XXXVI. The L1 loss subgroup has a NUBIG of \$60 (the sum of the built-in gain on the land, the built-in gain on the machine, and the section 382(h)(6) amounts). Note here that the built-in gain on the stock of L2 and L3 are not taken into account. Assume that this NUBIG exceeds the threshold applied on the aggregate basis. See § 1.1502-91T(g)(1).

XXXVII. Assume that L2 sells the machine outside the M group during the recognition period and recognizes a gain of \$20. The gain is a recognized built-in gain and increases the subgroup section 382 limitation for the taxable year. Section 382(h)(1)(A).

XXXVIII. Assume that L2 sells the machine to another member of the M group during the recognition period and recognizes a gain of \$20. The deferred intercompany gain may be treated as a recognized built-in gain only to the extent it is restored during the recognition period. § 1.1502-91T(h)(3).

XXXIX. Assume that L1 sells the L2 stock outside of the M group during the recognition period and recognizes a gain of \$50. Of the gain, \$40 is taken into account (notwithstanding that the gain was not taken into account in computing the loss subgroup's NUBIG) in determining the recognized built-in gain of the loss subgroup. § 1.1502-91T(h)(2). Only \$40 of the \$50 gain is treated as recognized built-in gain because \$10 of the gain was attributable to post-acquisition appreciation. Section 382(h)(2)(A)(ii). Note that this \$40 of recognized built-in gain reduces the subgroup's NUBIG from \$60 to \$20 even though L1 and L3 retain the same assets and built-in income (loss) items that gave rise to \$40 of the \$60 NUBIG. Query whether L2 departs from the loss subgroup with \$20 of NUBIG available to enhance any section 382 limitation allocated to it under § 1.1502-95T?

## Example 8

### MULTIPLE OWNERSHIP CHANGE

Assume that P acquires all of the stock of L in Year 1, causing an ownership change of L, L computes a section 382 limitation of \$40 (based on the \$500 FMV of the L stock times the tax-exempt rate of 8%). For purposes of section 382, the losses of L fold into the losses of the P group and thus are treated (for purposes of the next ownership change with respect to those losses) as if they arose in the P group. § 1.1502-96T(a)(2). The P group thereby becomes a loss group. In Year 2, M acquires all of the stock of P, causing an ownership change of the P loss group. On the later change date, the FMV of the P stock is \$800, while the FMV of the L stock owned by P is only \$300. The applicable tax-exempt rate is 7%.

- XL. The ownership change of the P loss group represents a second ownership change with respect to the L losses carried to Year 1 that are unabsorbed on the second change date. The consolidated section 382 limitation computed on the second change date is based on the \$800 FMV of the P stock (not the \$300 FMV of the L stock) times the 7% rate, or \$56. § 1.1502-96T(a)(2)(iii). However, pursuant to § 1.382-5T(d), the P loss group cannot obtain a limitation greater than \$40 with respect to pre-change losses of the first ownership change. Therefore, the consolidated section 382 limitation with respect to the pre-change losses of L without regard to any adjustments (for example, for recognized built-in gains) is \$40. The absorption of L's losses with respect to any portion of the \$40 limitation will reduce dollar-for-dollar the \$56 consolidated section 382 limitation attributable to the ownership change of the P loss group.
- XLI. Assume instead that the FMV of the P stock on the second change date is only \$350. The consolidated section 382 limitation computed based on the \$350 FMV times the 7% rate is \$24.50. Section 382 and § 1.382-5T(d) limit the section 382 limitation to the lesser limitation with respect to L's pre-change losses following a second ownership change. Therefore, the consolidated section 382 limitation with respect to all of the losses of the P loss group (including L's pre-change losses) would be \$24.50.

## Example 9

### ELIMINATIONS OF "BUT FOR" SRLY COMPUTATION

Assume that P acquires all of the stock of a previously unaffiliated corporation, T, in a transaction that does not result in an ownership change of T. T has a SRLY NOL of \$100. For T's first taxable year as a member of the P consolidated group, T has a capital gain of \$50, and P has \$100 of ordinary income and a capital loss of \$200.

	<u>Ordinary Income</u>	<u>Capital Gain (Loss)</u>
P	\$100	(200)
T	<u>-0-</u>	<u>50</u>
TOTALS	\$100	(150)

Because capital losses can only be used against capital gains, the P group's CTI (prior to the deduction of any CNOL allowed with respect to T's SRLY NOL) is \$100 (\$100 of ordinary income plus \$50 of capital gain less \$50 of allowable capital loss).

- XLII. Under the prior SRLY rules of § 1.1502-21(c), the measure of T's contribution of CTI is the difference between the P group's CTI with T's items included (\$100) and the P group's CTI without T's items included (again, \$100 in light of the fact that T's only contribution was \$50 of capital gain that was offset by P's capital loss, which capital loss cannot be used against P's ordinary income). Therefore, under the current rules, none of T's SRLY NOL would find its way into the group's CNOL because T is not treated as having made any contribution to CTI.
- XLIII. Under new § 1.1502-21T(c), the measure is T's items of income, gain, loss and deduction taken into account in determining the group's CTI, computed without regard to any other member's items of income or deduction. Thus, the new measure will be \$50 (T's \$50 of capital gain) under these facts, resulting in the allowance of \$50 of T's SRLY NOL into the computation of the group's CNOL for the year. Clearly this is the appropriate result, given that T would have used \$50 of its NOL for the year if T had filed a separate return.

Example 10

CUMULATIVE SRLY COMPUTATION

Assume that P becomes affiliated (as parent) with two previously unaffiliated corporations, T1 and T2, in transactions that do not result in ownership changes of either T1 or T2. T1 and T2 carry over SRLY NOLs of \$100 and \$40 respectively. The contribution to the P group's CTI (computed without regard to the CNOL deduction) of each member is as follows.

	Year 1	Year 2	Year 3
P	\$ (100)	\$ 80	\$ 50
T1 (\$100 NOL)	80	(25)	(15)
T2 (\$ 40 NOL)	<u>(20)</u>	<u>10</u>	<u>15</u>
	\$ (40)	\$ 65	\$ 50

XLIV. Use of the SRLY NOLs of T1 and T2 is determined under § 1.1502-21T(c)(1)(i) on a cumulative basis. Two aggregate numbers are compared: the aggregate contribution of the SRLY member to CTI (computed by taking into account only the member's items of income, gain, deduction, and loss) and the aggregate of SRLY NOLs of the member that have been included in the CNOL deduction of the group. If the SRLY member's cumulative contribution to CTI for all consolidated return years exceeds the aggregate SRLY NOLs included in the CNOL deduction, SRLY NOLs can be used to the lesser of (1) the excess or (2) the group's CTI for the year. The use of SRLY NOLs that are permitted to be absorbed under § 1.1502-21T(c) is determined in accordance with other Code provisions such as section 172

Example 10

<u>T1:</u>	Year 1	Year 2	Year 3
cumulative CTI	\$ 80	\$ 55	\$ 40
aggregate NOLs used	<u>      -</u>	<u>      0</u>	<u>      55</u>
cumulative excess	\$ 80	\$ 55	\$ 0
cumulative excess	\$ 80	\$ 55	\$ 0
P group's CTI	0	65	50
NOLs absorbed	0	55	0

<u>T2:</u>	Year 1	Year 2	Year 3
cumulative CTI	\$ (20)	\$ (10)	\$ 5
aggregate NOLs used	<u>      -</u>	<u>      0</u>	<u>      0</u>
cumulative excess	\$ 0	\$ 0	\$ 5
cumulative excess	\$ 0	\$ 0	\$ 5
P group's CTI	0	65	50
NOLs absorbed	0	0	5

XLV. Note that T1 does not recapture the benefit of \$15 of SRLY losses used in Year 2 during Year 3 when its cumulative CTI becomes \$15 less than the aggregate amount of its SRLY NOLs used in the P group.

Example 11

CUMULATIVE SRLY SUBGROUP COMPUTATION

Assume that P becomes affiliated (as parent) with two historically affiliated corporations, T1 and T2, in transactions that do not result in ownership changes of either T1 and T2, and that T1 and T2 qualify as a SRLY subgroup under § 1.1502-21T(c)(2)(i). T1 and T2 carry over SRLY NOLs of \$100 and \$40, respectively. As in Example 10, the contributions to the group's CTI (computed without regard to the CNOL deduction) of each member is as follows:

	Year 1	Year 2	Year 3
P	\$ (100)	\$ 80	\$ 50
T1 (\$100 NOL)	80	(25)	(15)
T2 (\$ 40 NOL)	<u>(20)</u>	<u>10</u>	<u>15</u>
	\$ (40)	\$ 65	\$ 50

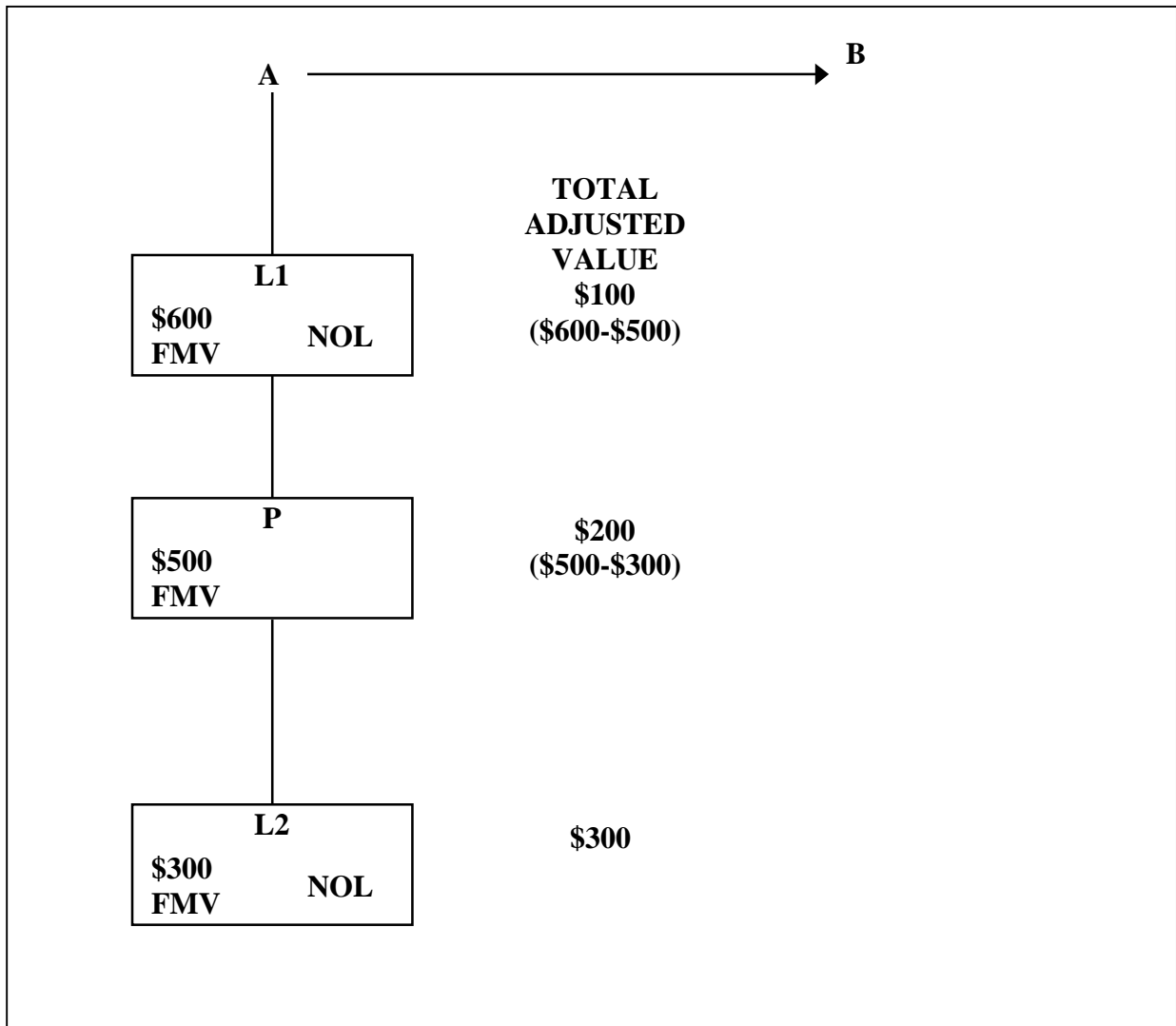
XLVI. The use of the SRLY NOLs of T1 and T2 is determined under § 1.1502-21T(c)(2) on a cumulative subgroup basis. Application of the SRLY subgroup principles is mandatory, See § 1.1502-21T(c)(2)(iv) (relating to a rule which deters manipulation of the membership of the SRLY subgroup). The computation for the amount of the allowable SRLY NOL is essentially the same for subgroups as for stand alone corporations; two aggregate numbers are compared; the cumulative contribution of the SRLY subgroup members to CTI (CTI computed by taking into account only items of income, gain, deduction, and loss of the members of the SRLY subgroup) and the aggregate of SRLY NOLs of those members that have previously been included in the CNOL deduction of the group. If the cumulative contribution to CTI exceeds the aggregate SRLY NOLs previously included in the CNOL deduction, SRLY NOLs can be used to the lesser of (1) the excess or (2) the group's CTI for the year. The use of SRLY NOLs that are permitted to be absorbed under § 1.1502-21T(c) is determined in accordance with other Code provisions such as section 172.

<u>T1- T2 subgroup:</u>	Year 1	Year 2	Year 3
cumulative CTI	\$ 60	\$ 45	\$ 45
aggregate NOLs	<u>-</u>	<u>0</u>	<u>45</u>
cumulative excess	\$ 60	\$ 45	\$ 0
cumulative excess	\$ 60	\$ 45	\$ 0
P group's CTI	0	65	50
NOLs absorbed	0	45	0

XLVII. While the former SRLY rules would have permitted a total of only \$25 of T2's NOLs to be absorbed during years 2 and 3, the new rules permit \$45 to be absorbed. However, the rules are not always favorable for taxpayers and members cannot be artificially excluded from a SRLY subgroup in order to avoid or increase the SRLY limitation. § 1.1502-21T(c)(2)(iv).

Example 12

CONTROLLED GROUPS



CONTROLLED GROUPS

Assume L1, P, and L2 compose a controlled group within the meaning of section 1563 (substituting 50% for 80%). The corporations do not file a consolidated return. A sells all of the L1 stock to B, causing an ownership change of L1 and L2. (P is not a loss corporation.)

XLVIII. Duplication of value within controlled groups is not permitted. Section 382(m)(5) and § 1.382-8T. Duplication generally arises when the same value can be matched with losses from the same period. Accordingly, the rules only apply if corporations are members of the same controlled group both in the year the NOL arises as well as in the year of the ownership change. Duplication is prevented through adjustments to value. § 1.382-8T(c). The results generally should be comparable to any limitation determined with respect to consolidated groups.

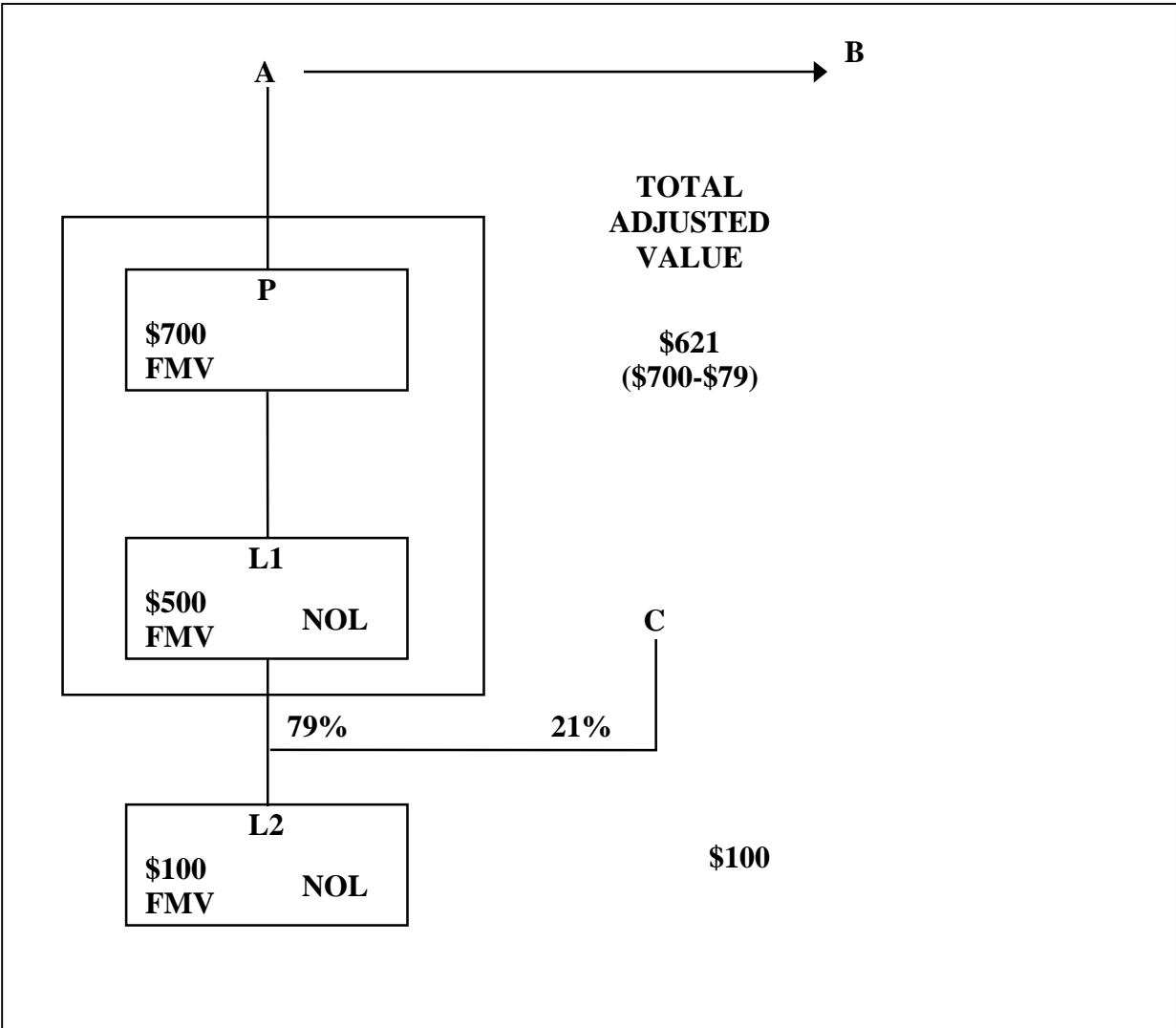
XLIX. Absent any elections to restore value (§§ 1.382-8T(c)(2) and 1.382-8T(h)), L1 and L2 compute their separate section 382 limitations based on the value of their stock, reduced by the value of any component member stock directly owned after the ownership change. L1's adjusted value is \$100; L2's adjusted value is \$300.

L. While P is not a loss corporation, the election to restore value to L1 is not automatic and must be made with L1's return for the taxable year in which the ownership change occurs. On the facts of this example, even though an election to restore at least \$200 of P's value to L1 should always be made, the restoration of value requires P's affirmative action. Hopefully, the final regulations will automatically restore value in this and other clear cases.

LI. Note that restoration is only permitted going up the chain. P and L2 may restore their individual adjusted values respectively to P and L1, but L1 and P may not assign their adjusted values respectively to P and L2. Thus, if only L2 had controlled group losses, L2 would not benefit from the adjusted values of L1 or P. However, L2 would benefit if its losses were SRY/non-SRLY losses with respect to the L1 group, and the group elects to file consolidated returns before the change date. See §§ 1.1502-91T(c)(1) (definition of loss group), -93T (computation of consolidated section 382 limitation).

Example 13

COORDINATION OF CONTROLLED GROUP RULES  
WITH CONSOLIDATED RETURN RULES



### Example 13

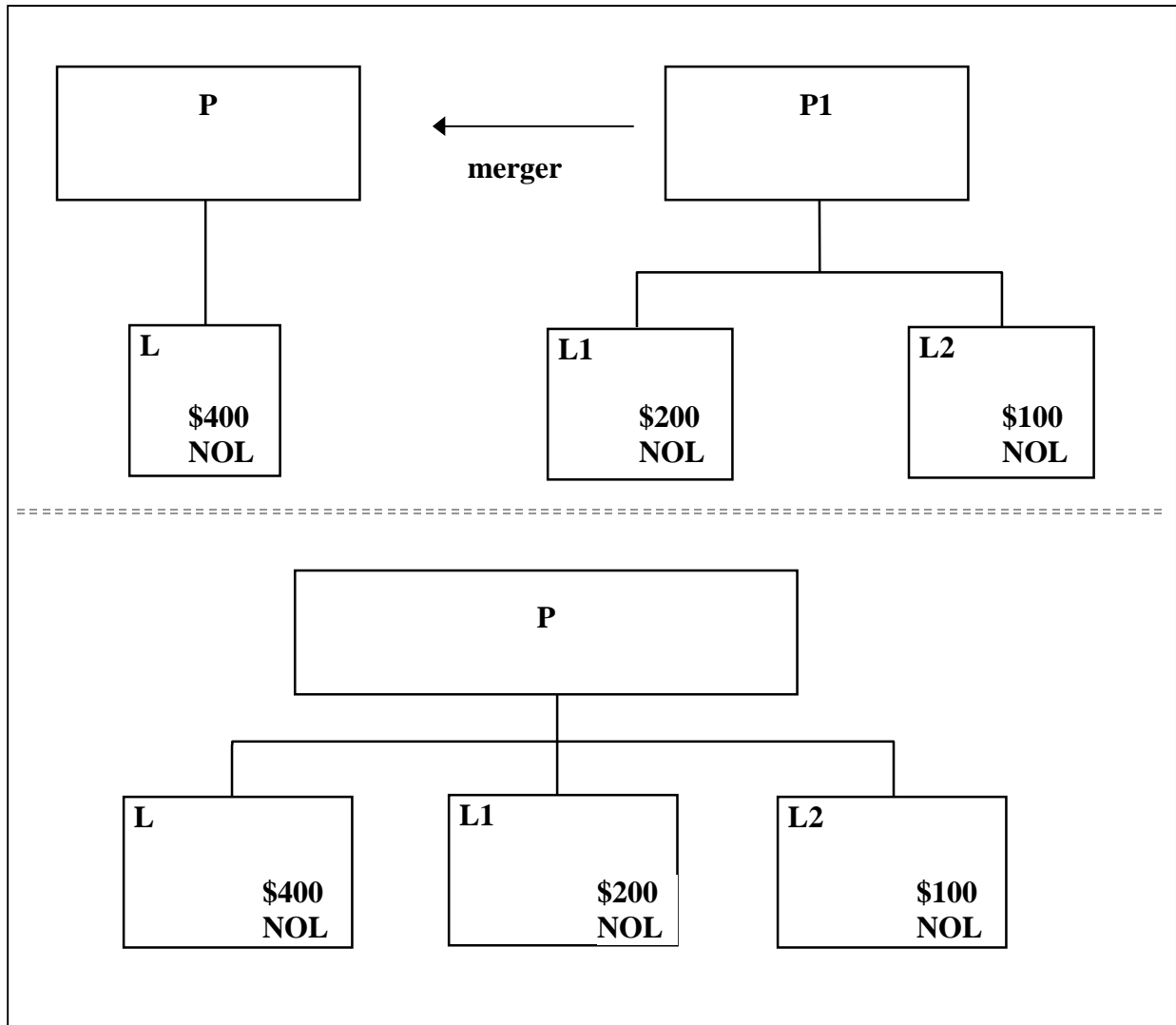
#### COORDINATION OF CONTROLLED GROUP RULES WITH CONSOLIDATED RETURN RULES

Assume P and L1 file a consolidated return and have a CNOL in 1991 that is carried over to 1998. L2 also has a NOL in 1997 that is carried over to 1998. A sells 100% of the stock of P to B on January 1, 1998. Prior to A's sale of the P stock, the ownership structure of P, L1 and L2 has been constant for all years of their existence.

- LII. The P consolidated group (P and L1 ) is a loss group within the meaning of § 1.1502-91T(c) that has an ownership change under § 1.1502-92T(b)(1)(i). L2 has an ownership change under § 1.382-2T.
- LIII. P, L1 and L2 compose a controlled group with respect to the NOL carryovers because they are component members of a controlled group within the meaning of section 1563, as modified by § 1.382-8T, for both the taxable years in which their losses arose and the taxable year in which the ownership change occurs.
- LIV. P and L1 must compute a consolidated section 382 limitation with respect to the P-L1 loss group. Where both the consolidated return and controlled group rules apply, the consolidated return regulations generally take precedence over the controlled group regulations. See § 1.382-8T(f). The consolidated section 382 limitation for the P loss group is based on the value of stock of P. § 1.1502-93T(b)(1).
- LV. For purposes of the controlled group rules, however, P and L1 are treated as a single corporation, and the P loss group must exclude the value of the L2 Stock which is directly owned by L1. §§ 1.382-8T(c)(1) and -8T(f). Accordingly, the value of the P loss group for purposes of the consolidated section 382 limitation applicable to the CNOL is \$621, which is the value of the stock of the P loss group, \$700, less the value of the L2 stock owned by the group, \$79 (\$100 x 79%). Note that this would be true even if an ownership change had not occurred with respect to L2 (e.g., A sold only 51% of the P stock to B) and even if L2 had no NOLS.
- LVI. L2's value remains at \$100 for purposes of determining its separate section 382 limitation.
- LVII. L2 could elect to restore all or a portion of such \$79 value to the P loss group. Note that L2 could not elect to restore more than \$79 in value to the P consolidated group. § 1.382-8T(c)(2).

Example 14

SECTION 382 AND SRLY LIMITATION  
SUBGROUPS AND ABSORPTION



SECTION 382 AND SRLY LIMITATIONS  
SUBGROUPS AND ABSORPTION

Assume that P1-L1-L2 group is a loss group with respect to \$300 of NOLs. At the close of business at the end of Year 1, P1 merges into P, the common parent of the P-L group, in a transaction described in section 368(a)(1)(A). The merger causes an ownership change of the P1 group. Moreover, the transaction is not described in § 1.1502-75(d), and the P1 group ceases to exist. The P1 group's consolidated section 382 limitation is \$50, based on its \$500 value and a 10% long-term tax-exempt rate. All loss carryovers are from years ending on the same date.

- LVIII. Unless P is a "successor" to P1, the P1 group ceases to exist following the merger and, for purposes of section 382, the P1 group's \$50 section 382 limitation therefore must be apportioned. § 1.1502-95T(c). However, P should be a successor to P1. §§ 1.382-2T(f)(4), -1(f)(4), -91T(j). In that case, because P, L1, and L2 bear a section 1504 relationship to each other and carry over losses from, the P1 group, they compose a loss subgroup to which the P1 group's \$50 limitation is available without the need for apportionment under § 1.1502-95T. §§ 1.1502-91T(d)(1), -95T(c)(4). In addition, because of the ownership change, § 1.1502-96T(a) (relating to the end of separate tracking) applies.
- LIX. For purposes of SRLY, P also should be a successor to P1. §§ 1.1502-1(f)(4), -21T(f). If P succeeds to P1, P-L1-L2 will compose a SRLY subgroup. § 1.1502-21T(c)(2). If P is not a successor to P1 for purposes of SRLY, only L1 and L2 will compose a SRLY subgroup, unless the anti-abuse rules apply.
- LX. Assuming that P is treated as a successor to P1 and CTI for Year 2 is \$400, consisting of P (\$200), L \$300, L1 \$300, and L2 (\$0), absorption of the NOLs of L1 and L2 is limited to the lesser of their \$100 SRLY subgroup limitation (the aggregate CTI contribution of P, L1, and L2) and \$50 section 382 limitation. Under § 1.1502-21T(b), losses from the same year are generally absorbed pro-rata with respect to losses that are available to offset CTI. Unless that ratio is altered by section 382(l)(2)(B), the P group would absorb \$356 of L's NOLs ( $(\$400/\$400 + \$50) \times (\$400)$ ), \$29 of L1's NOLs ( $(\$200/\$300) \times (\$400 - \$356)$ ), and \$15 of L2's NOLs ( $(\$100/\$300) \times (\$400 - \$356)$ ). If, however, section 382(l)(2)(B) alters the absorption, the P group would absorb \$350 of L's NOLs, \$33 of L1's NOLs, and \$17 of L2's NOLs.

## GLOSSARY OF TERMS

Listed below is a glossary of terms used in the regulations relating to the operation of section 382 in the case of consolidated groups (§§ 1.1502-90T through 1.1502-99T) and controlled groups § 1.382-8T) and to the amendments to the built-in deduction and SRLY rules (§§ 1.1502-15T and 1.1502-21T). The glossary lists the major definitions; other relevant definitions may be found in § 1.382-2T or the consolidated return regulations.

**AFFILIATED** Corporations are affiliated if they  
§ 1.1502-1(j) are members of a group with each other.

**BUILT-IN LOSS** If a corporation has a NUBIL (a "net  
§ 1.1502-15T(b) unrealized built-in loss") under  
section 382(h)(3) (as modified) when it becomes a member of a group (determined under § 1.1502-91T(g) by treating the day that it becomes a member as a change date), its deductions and losses are built-in losses under the SRLY rules to the extent they are treated as recognized built-in losses under section 382(h)(2)(B) (as modified). The same principles apply, where appropriate, on a subgroup basis.

**COMPONENT MEMBER** Component member has the same  
§ 1.382-8T(e)(3) meaning as in section 1563(b),  
determined by substituting "December 31 (or the change date, if earlier)" for "December 31" each place it appears, and without regard to section 1563(b)(2), (b)(3)(C), and (b)(4) (relating to certain members excluded or added to a controlled group).

**CONSOLIDATED NET OPERATING LOSS ("CNOL")** Any excess of a consolidated group's  
§ 1.1502-21T(b)(2)(iv) deductions over its gross income  
(without regard to any CNOL deduction).

**CNOL ATTRIBUTABLE TO A MEMBER** The amount of a CNOL that is  
attributable to a member is determined  
§ 1.1502-21T(b)(2)(iv) by a fraction the numerator of which is  
the separate NOL of the member for the year of the loss and the denominator of which is  
the sum of the separate net operating losses for that year of all members having such  
losses. For this purpose, the separate NOL of a member is determined by computing the  
CNOL by taking into account only the member's items, including the member's losses  
and deductions actually absorbed by the group in the taxable year (whether or not  
absorbed by the member).

**CONTROLLED GROUP**                      Controlled group has the same  
§ 1.382-8T(e)(2) meaning as in section 1563(a),  
determined by substituting "50 percent" for "80 percent" each place that it appears, and  
without regard to section 1563(a)(4) (relating to certain insurance companies).

**CONTROLLED GROUP LOSS**              controlled group loss is a  
pre-§ 1.382-8T(b) change loss (or a NUBIL) of a loss corporation that is attributable to a  
taxable year of the corporation with respect to which the corporation is a component  
member of a controlled group.

**CONTROLLED GROUP WITH RESPECT TO A CONTROLLED GROUP LOSS**              A controlled group with respect to  
each controlled group loss is composed  
of the loss corporation and each other  
§ 1.382-8T(b)                      corporation that is a component member  
of a controlled group that includes the loss corporation both:

- (i) With respect to the taxable year to which the controlled group loss is attributable; and
- (ii) On the date the loss corporation has an ownership change.

**REQUIRED REDETERMINATION OF OWNERSHIP CHANGE ANALYSIS**              An adjustment to a loss  
corporation's ownership change  
analysis may result from the  
fold-in rules (*i.e.*, the end of the separate tracking requirements). Rather, the loss  
corporation may assume the owner shift history of the acquiring corporation or acquiring  
group which is closer to an ownership change than the acquired corporation.

**EQUIVALENT YEARS**                      Taxable years are equivalent if they  
§ 1.1502-21T(b)(2)                      bear the same numerical relationship to  
the consolidated return year in which a CNOL arises, counting forward or backward from  
the year of the loss.

**FOLD-IN RULE**                      The rules that end separate tracking  
§ 1.382-2T(f)(1)(iv) of losses of an acquired loss  
§ 1.1502-96T(a) corporation following its ownership  
change or the completion of the 5-year period following its acquisition.

LOSS GROUP  
§ 1.1502-91T(c)

A loss group is a consolidated group  
that:

(i) Is entitled to use a net operating loss carryover to the taxable year that did not arise (and is not treated under § 1.1502-21T(c) as arising) in a SRLY;

(ii) Has a CNOL for the taxable year in which a testing date of the common parent occurs (determined by treating the common parent as a loss corporation); or

(iii) Has a NUBIL (determined under § 1.1502-91T(g) by treating the date on which the determination is made as though it were a change date).

LOSS SUBGROUP  
§ 1.1502-91T(d)

Definition For NOLS: Two or more corporations that become members of a consolidated group compose a loss subgroup if they:

(i) Were affiliated with each other in another group (whether or not the group was a consolidated group) (the former group);

(ii) Bear a relationship to each other described in section 1504(a)(1) (a parent-sub relationship) immediately after they become members of the group; and

(iii) At least one of the members carries over a NOL that did not arise (and is not treated under § 1.1502-21(c) as arising) in a SRLY with respect to the former group.

A separate loss subgroup is determined for each former group in which carryovers arose.

Definition for Built-Ins: Two or more corporations that become members of a consolidated group compose a loss subgroup if they:

(i) Have been continuously affiliated with each other for the 5 consecutive year period ending immediately before they become members of the group;

(ii) Bear a relationship to each other described in section 1504(a)(1) (a parent-sub relationship) immediately after they become members of the group; and

LOSS SUBGROUP CONTINUED (iii) Have a NUBIL (determined under § 1.1502-91T(g) by treating the day they become members of the group as though it were a change date).

LOSS SUBGROUP PARENT § 1.1502-91T(d)(3) A loss subgroup parent is the corporation that bears the same relationship to the other members of the loss subgroup as a common parent bears to the members of a group.

MEMBER § 1.1502-1(b) A member is a corporation (including the common parent) that is included in the group, or as the context may require, a corporation that is included in a subgroup,

NET UNREALIZED BUILT-IN GAIN AND LOSS ("NUBIG" AND "NUBIL") § 1.1502-91T(g) Basic Rule. A group (or loss subgroup) determines its NUBIG or NUBIL based on the aggregate amount of the separately computed NUBIG or NUBIL of each member included in the group (or loss subgroup), and taking into account the items of built-in income and deduction described in section 382(h)(6). The NUBIG or NUBIL with respect to the stock and debt of members is not taken into account in determining a member's separately computed NUBIG or NUBIL. The threshold requirement under section 382(h)(3)(B) applies on an aggregate basis and not on a member-by-member basis. If a member is not included in a group (or loss subgroup), the determination of whether the member has a NUBIG or NUBIL under section 382(h)(3) is made on a separate entity basis.

Members Included in the Group (Subgroup) Computation. The members included in the determination whether a group (or loss subgroup) has a NUBIG or NUBIL are all members other than:



(i) Any loss that makes a group a loss group and which is allocable to the period ending on or before the change date; and

(ii) Any recognized built-in loss of a loss group.

PRE-CHANGE SUBGROUP A pre-change subgroup attribute of  
ATTRIBUTE a loss subgroup is:

§ 1.1502-91T(a)

(i) Any net operating loss carryover that makes a subgroup a loss subgroup; and

(ii) Any recognized built-in loss of a loss subgroup.

PREDECESSOR The term "predecessor" means a  
§ 1.382-2T(f)(5) transferor or distributor of assets to  
§ 1.1502-1(f)(4) a member (the successor) in a  
transaction:

(1) To which section 381(a) applies;

(2) In which the SUCCESSOR's basis for the assets is determined, directly or indirectly, in whole or in part, by reference to the basis of the assets of the transferor or distributor, but only if the amount by which basis differs from value, in the aggregate, is material; or

(3) In certain transition cases.

RECOGNIZED BUILT-IN  
GAIN OR LOSS

§ 1.1502-91T(h)

§ 1.1502-15T(b)(2)(ii) (unless disallowed under § 1.1502-20 or

otherwise) in determining recognized built-in gain or loss under section 382(h)(2), even though it is not taken into account in determining a NUBIG or NUBIL of the loss group or loss subgroup.

Gain or loss recognized by a member  
on the disposition of stock or debt of  
another member is taken into account

Gain or loss that is deferred under the consolidated return regulations is treated as recognized built-in gain or loss only to the extent restored during the recognition period. See, however, Notice 90-27 which extends the recognition period for gain deferred under the installment sales rules.

For SRLY purposes only, section 382(h)(1)(B)(ii) (the cap rule) does not apply to limit the amount of recognized built-in loss to the amount of the NUBIL.

**SRLY SUBGROUP**

Definition for NOLS. Carryovers.

§ 1.1502-21T(c)(2)

In the case of a carryover, the SRLY

subgroup is composed of the member carrying over the loss (loss member) and each other member that was a member of the former group and that has been continuously affiliated with the loss member (but without a requirement of a section 1504(a)(1) relationship) since ceasing to be a member of the former group and until the beginning of the year to which the loss is carried.

Carrybacks. In the case of a carryback, the SRLY subgroup is composed of the member carrying, back the loss (loss member) and each other member that is a member of the group from which the loss is carried back and that has been continuously affiliated with the loss member (but without a requirement of a section 1504(a)(1) relationship) from the year to which the loss is carried through the year in which the loss arises.

Definition for Built-Ins. A built-in loss is treated as arising in a year that is not a SRLY with respect to each other member of the group in which the loss is recognized that has been continuously affiliated with the member recognizing the built-in loss (the loss member):

(i) From the beginning of a 60 consecutive month period ending immediately before the members became members of the group in which the loss is recognized;

(ii) Until the beginning, of the year in which the loss is recognized.

**SUCCESSOR AND**

A reference to a corporation,

**PREDECESSOR**member, common parent, loss subgroup

§ 1.1502-91T(j)parent, or subsidiary includes, as the

§ 1.1502-21T(f)(1)context may require, a reference to a

§ 1.1502-15T(e)successor or predecessor.

A successor is any corporation acquiring assets from another corporation in a section 381(a) transaction and also includes, as the context may require, a corporation which receives an asset or assets from another corporation if the corporation's basis for the asset(s) is determined, directly or indirectly, in whole or in part, by reference to the other corporation's basis and the amount by which basis differs from value is, in the aggregate, material.

**SUPPLEMENTAL GROUP CHANGE METHOD**                      The second method for determining whether a loss group (or loss subgroup) § 1.1502-92T(c) has had an ownership change generally applies if a 5-percent shareholder increases his ownership in both the common parent (or loss subgroup parent) and a subsidiary member during a testing period.