

Section 382.—Limitations on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

26 CFR 1.382–8T: Controlled groups (temporary).

T.D. 8679

**DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1 and 602**

Regulations Under Section 382 of the Internal Revenue Code of 1986; Application of Section 382 in Short Taxable Years and With Respect to Controlled Groups

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains final and temporary regulations relating to limitations on net operating loss carryforwards and certain built-in losses following an ownership change and comply with the statutory direction under section 382(m) of the Internal Revenue Code to prescribe regulations concerning short taxable years and controlled groups. This document also contains amendments relating to the end of separate tracking of the stock ownership of loss corporations that cease to exist following a merger or similar transaction. The text of these temporary

regulations also serves as the text of the proposed regulations set forth in CO-26-96, page 31, in this issue of the Bulletin.

DATES: These regulations are effective Thursday, June 27, 1996.

For dates of application and special transition rules, see Effective Dates under SUPPLEMENTARY INFORMATION.

FOR FURTHER INFORMATION CONTACT: David B. Friedel at (202) 622-7550 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these temporary regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under the control number 1545-1434. Section 1.382-8T(h) requires a response from certain corporations that are members of controlled groups. The IRS requires this information to assure compliance with section 382(m)(5) so that the value of a loss corporation that is a member of a controlled group is not taken into account more than once in computing a section 382 limitation. Responses to this collection of information are required to obtain a benefit (relating to the restoration of value for section 382 purposes).

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden, and suggestions for reducing this burden, please refer to the preamble to CO-26-96, page 31, in this issue of the Bulletin.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background and Explanation of Provisions

On February 4, 1991, the IRS and Treasury issued three notices of proposed rulemaking, CO-132-87 (56 FR

4194), CO-077-90 (56 FR 4183), and CO-078-90 (56 FR 4228), setting forth rules regarding the application of sections 382 and 383 by consolidated groups and by controlled groups, and the carryover and carryback of losses to consolidated and separate return years.

For reasons explained in the preamble to TD 8678 (page 11 in this issue of the Bulletin), the IRS and Treasury are issuing temporary amendments concerning the limitations on net operating loss carryforwards and certain built-in losses and credits following an ownership change of a consolidated group. The temporary regulations contained in this Treasury decision complement those other temporary regulations. They assure that the members of a controlled group cannot duplicate value in computing their respective section 382 limitations, a result not permitted to members of a group filing consolidated returns. See § 1.1502-93T.

These temporary regulations are substantially identical to the rules proposed on January 29, 1991. One provision (relating to the effects of successive ownership changes) was moved from the consolidated return regulations to the section 382 regulations to clarify that it is applicable to all corporations. These temporary amendments do not address the numerous comments on the proposed regulations. Many of these comments are still under consideration.

Effective Dates

The temporary amendments are generally effective as of January 1, 1997. The final rules relating to the value of stock added to § 1.382-2(a)(3)(i) and the temporary rules in § 1.382-2T(f)(1)(ii) (relating to the end of separate tracking of certain loss corporations) are generally effective as of January 29, 1991. The temporary rules in § 1.382-5T (relating generally to short taxable years and successive ownership changes) generally apply to loss corporations that have an ownership change to which section 382(a), as amended by the Tax Reform Act of 1986, applies.

Special Analysis

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C.

chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations were sent to the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal author of the temporary regulations is David B. Friedel of the Office of Assistant Chief Counsel (Corporate), IRS. Other personnel from the IRS and Treasury participated in their development.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for Part 1 is amended by removing the entries for “1.382-2” and “1.382-2T” and adding entries in numerical order to read as follows:

Authority: 26 U.S.C. 7805

Section 1.382-2 also issued under 26 U.S.C. 382(k)(1), (l)(3), (m), and 26 U.S.C. 383.

Section 1.382-2T also issued under 26 U.S.C. 382(g)(4)(C), (i), (k)(1) and (6), (l)(3), (m), and 26 U.S.C. 383.

Section 1.382-5T also issued under 26 U.S.C. 382(m).

Section 1.382-8T also issued under 26 U.S.C. 382(m).

Par. 2. Section 1.382-1 is amended by:

- a. Adding an entry for § 1.382-2, paragraph (a)(1)(iv).
- b. Revising the entry for § 1.382-2, paragraph (a)(3)(i).
- c. Adding entries for § 1.382-2T, paragraphs (f)(1)(i) through (f)(1)(iii).
- d. Adding entries for §§ 1.382-5T and 1.382-8T.

§ 1.382-1 Table of contents.

§ 1.382-2 General rules for ownership change.

(a)

(1)

(iv) End of separate accounting for losses and credits of distributor or transferor loss corporation.

*_ *_ *_ *_ *

§ 1.382-2T Definition of ownership change under section 382, as amended by the Tax Reform Act of 1986 (temporary).

*_ *_ *_ *_ *

- (f)
- (i) In general.
- (ii) End of separate accounting for losses and credits of distributor or transferor loss corporation.
- (iii) Application to other successor corporations.

*_ *_ *_ *_ *

§ 1.382-5T Section 382 limitation (temporary).

- (a) Scope.
- (b) Computation of value.
- (c) Short taxable year.
- (d) Successive ownership changes and absorption of a section 382 limitation.
- (1) In general.
- (2) Recognized built-in gains and losses.
- (3) Effective date.
- (e) Controlled groups.
- (f) Effective date.

§ 1.382-8T Controlled groups (temporary).

- (a) Introduction.
- (b) Controlled group loss and controlled group with respect to a controlled group loss.
- (c) Computation of value.
 - (1) Reduction in value.
 - (2) Restoration of value.
 - (3) Reduction in value by the amount restored.
 - (4) Appropriate adjustments.
 - (5) Certain reductions in the value of members of a controlled group.
- (d) No double reduction.
- (e) Definitions and nomenclature.
 - (1) Definitions in Section 382 and the regulations thereunder.
 - (2) Controlled group.
 - (3) Component member.
 - (4) Predecessor and successor corporation.
- (f) Coordination between consolidated groups and controlled groups.
- (g) Examples.
- (h) Time and manner of filing election to restore.

- (1) Statement required.
- (2) Revocation of election.
- (3) Filing by component member.
- (j) [Reserved]
- (j) Effective date.
 - (1) In general.
 - (2) Transition rule.
 - (i) In general.
 - (ii) Special transition rules for controlled groups that had ownership changes before January 29, 1991.
 - (3) Amended returns.

Par. 3. Section 1.382-2 is amended as follows:

- a The first sentence of paragraph (a)(1)(iii) is amended by removing the language “Pre-change losses” and adding “Except as provided in § 1.382-2T(f)(1)(ii), pre-change losses” in its place.
- b Paragraph (a)(1)(iv) is added.
- c The text of § 1.382-2T(f)(18)(i) is redesignated as the text of § 1.382-2(a)(3)(i).

d Newly designated paragraph (a)(3)(i) is amended by adding three sentences at the end.

The additions read as follows:

§ 1.382-2 General rules for ownership change.

- (a)
 - (1) End of separate accounting for losses and credits of distributor or transferor loss corporation. For further guidance, see § 1.382-2T(f)(1)(ii).

(3) (i) Solely for purposes of determining the percentage of stock owned by a person, each share of all the outstanding shares of stock that have the same material terms is treated as having the same value. Thus, for example, a control premium or blockage discount is disregarded in determining the percentage of stock owned by any person. The previous two sentences of this paragraph (a)(3)(i) apply to any testing date occurring on or after January 29, 1991.

Par. 4. Section 1.382-2T is amended as follows:

- (a) Paragraph (e)(2)(iv) Example (1) is amended by removing the last sentence.
- (b) Paragraph (e)(2)(iv) Example (2)(ii) is amended by adding a sentence at the end.
- (c) Paragraph (e)(2)(iv) Example (2)(iii) is amended by removing the language “, but must be separately

accounted for under § 1.382-2(a)(1)(iii) of this section” from the last sentence.

(d) The text following the heading of paragraph (f)(1) is designated as paragraph (f)(1)(i) and a heading for newly designated paragraph (f)(1)(i) is added.

(e) Paragraphs (f)(1)(ii) and (f)(1)(iii) are added.

(f) Paragraph (f)(4) is amended by removing the word “loss” and by adding two sentences at the end.

(g) Paragraph (f)(5) is amended by adding two sentences at the end.

(h) A sentence is added after the heading of paragraph (f)(18)(i).

(i) Paragraph (h)(2)(i)(A) is amended by adding the language “and solely for the purposes of determining whether a loss corporation has an ownership change” immediately after “except as otherwise provided in this section.”

The additions read as follows:

§ 1.382-2T Definitions of ownership change under section 382, as amended by the Tax Reform Act of 1986 (temporary).

*_ *_ *_ *_ *

- (e)
- (2)
- (iv)

Example (2)

(ii) See paragraph (f)(1)(ii) of this section for rules that end separate accounting for L₁'s pre-change losses on any testing date occurring on or after January 29, 1991.

- (f)
- (1)

(i) In general.

(ii) End of separate accounting for losses and credits of distributor or transferor loss corporation. The separate tracking of owner shifts of the stock of an acquiring corporation required by § 1.382-2(a)(1)(iii) with respect to the net operating loss carryovers and other attributes described in § 1.382-2(a)(1)(ii) ends when a fold-in event occurs. A fold-in event is either an ownership change of the distributor or transferor corporation in connection with, or after, the transaction to which section 381(a) applies, or a period of 5 consecutive years following the section 381(a) transaction during which the distributor or transferor corporation has not had an ownership change. Starting on the day after the earlier of the change date (but not earlier than the day of the section 381(a) transaction) or the last day of the 5 consecutive year period, the losses and other attributes of the distributor or transferor corporation are

treated as losses and attributes of the acquiring corporation for purposes of determining whether an ownership change occurs with respect to such losses. Also, for purposes of determining the beginning of the acquiring corporation's testing period, such losses are considered to arise either in a taxable year that begins not earlier than the later of the day following the change date or the day of the section 381(a) transaction, or in a taxable year that begins 3 years before the end of the 5 consecutive year period. Pre-change losses of a distributor or transferor corporation that are subject to a limitation under section 382 continue to be subject to the limitation notwithstanding the occurrence of a fold-in event. Any ownership change that occurs in connection with, or subsequent to, the section 381 transaction may result in an additional, lesser limitation with respect to such pre-change losses. This paragraph (f)(1)(ii) applies to any testing date occurring on or after January 29, 1991.

(iii) *Application to other successor corporations.* Section 1.382-2(a)(1) (relating to the definition of loss corporation) and this paragraph (f)(1) also apply, as the context may require, to successor corporations other than successors in section 381(a) transactions. For example, if a corporation receives assets from the loss corporation that have basis in excess of value, the recipient corporation's basis for the assets is determined, directly or indirectly, in whole or in part, by reference to the loss corporation's basis, and the amount by which basis exceeds value is material, the recipient corporation is a successor corporation subject to § 1.382-2(a)(1) and this paragraph (f)(1). This paragraph (f)(1)(iii) applies to any testing date occurring on or after January 1, 1997.

* * * * *

(4) *Successor corporation.* * * * A successor corporation 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. The previous sentence of this paragraph (f)(4) applies to any testing date occurring on or after January 1, 1997.

(5) *Predecessor corporation.* * * * A predecessor corporation also includes, as the context may require, a corporation

which transfers an asset or assets to another corporation if the transferee's basis for the asset(s) is determined, directly or indirectly, in whole or in part, by reference to the corporation's basis and the amount by which basis differs from value is, in the aggregate, material. The previous sentence of this paragraph (f)(5) applies to any testing date occurring on or after January 1, 1997.

* * * * *

(18) * * * (i) * * * For further guidance, see § 1.382-2(a)(3)(i).

* * * * *

Par. 5. Sections 1.382-5T and 1.382-8T are added to read as follows:

§ 1.382-5T Section 382 limitation (temporary).

(a) *Scope.* Following an ownership change, the section 382 limitation for any post-change year is an amount equal to the value of the loss corporation multiplied by the long-term tax-exempt rate that applies with respect to the ownership change, and adjusted as required by section 382 and the regulations thereunder. See, for example, section 382(b)(2) (relating to the carryforward of unused section 382 limitation), section 382(b)(3)(B) (relating to the section 382 limitation for the post-change year that includes the change date), section 382(m)(2) (relating to short taxable years), and section 382(h) (relating to recognized built-in gains and section 338 gains).

(b) *Computation of value.* [Reserved]

(c) *Short taxable year.* The section 382 limitation for any post-change year that is less than 365 days is the amount that bears the same ratio to the section 382 limitation determined under section 382(b)(1) as the number of days in the post-change year bears to 365. The section 382 limitation, as so determined, is adjusted as required by section 382 and the regulations thereunder. This paragraph (c) does not apply to a 52-53 week taxable year that is less than 365 days unless a return is required under section 443 (relating to short periods) for such year.

(d) *Successive ownership changes and absorption of a section 382 limitation—(1) In general.* If a loss corporation has two (or more) ownership changes, any losses attributable to the period preceding the earlier ownership change are treated as pre-change losses with respect to both ownership changes. Thus, the later ownership change may

result in a lesser (but never in a greater) section 382 limitation with respect to such losses. In any case, the amount of taxable income for any post-change year that can be offset by pre-change losses may not exceed the section 382 limitation for such ownership change, reduced by the amount of taxable income offset by pre-change losses subject to any earlier ownership change(s).

(2) *Recognized built-in gains and losses.* [Reserved]

(3) *Effective date.* This paragraph (d) applies to taxable years of a loss corporation beginning on or after January 1, 1997.

(e) *Controlled groups.* See § 1.382-8T for rules for determining the value of a loss corporation that is a member of a controlled group.

(f) *Effective date.* Except as otherwise provided, this section applies to a loss corporation that has an ownership change to which section 382(a), as amended by the Tax Reform Act of 1986, applies.

§ 1.382-8T Controlled groups (temporary).

(a) *Introduction.* This section provides rules to adjust the value of a loss corporation that is a member of a controlled group of corporations on a change date so that the same value is not included more than once in computing the limitations under section 382 for the loss corporations that are members of the controlled group. In general, the adjustment is made under paragraph (c) of this section by reducing the value of the loss corporation by the value of the stock of each component member of the controlled group that the loss corporation owns immediately after the ownership change. The loss corporation's value may, however, be increased under paragraph (c) of this section by any amount of value that the other member elects to restore to the loss corporation.

(b) *Controlled group loss and controlled group with respect to a controlled group loss.* A controlled group loss is a pre-change loss (or a net unrealized built-in loss) 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 (as defined by paragraphs (e)(2) and (3) of this section). The controlled group with respect to each controlled group loss is composed of the loss corporation and each other corporation that is a compo-

nent member of a controlled group that includes the loss corporation both—

(1) With respect to the taxable year to which the controlled group loss is attributable; and

(2) On the date the loss corporation has an ownership change.

(c) *Computation of value.* For purposes of computing the limitation under section 382 with respect to each controlled group loss, the value of the stock of each component member of the controlled group with respect to that loss is determined immediately before the ownership change, and is adjusted by applying the following rules:

(1) *Reduction in value.* The value of the stock of each component member is reduced by the value (immediately before the ownership change and without regard to any restoration of value or other adjustment under this section) of the stock of any other component member directly owned by the component member immediately after the ownership change.

(2) *Restoration of value.* After the value of the stock of each component member is reduced pursuant to paragraph (c)(1) of this section, the value of the stock of each component member is increased by the amount of value, if any, restored to the component member by another component member (the electing member) pursuant to this paragraph (c)(2). The electing member may elect to restore value to another component member in an amount that does not exceed the lesser of—

(i) The sum of—

(A) The value, determined immediately before the ownership change, of the electing member's stock (after adjustment under paragraph (c)(1) of this section and before any restoration of value under this paragraph (c)(2)); plus

(B) Any amount of value restored to the electing member by another component member under this paragraph (c)(2); or

(ii) The value, determined immediately before the ownership change, of the electing member's stock (without regard to any adjustment under this section) that is directly owned by the other component member immediately after the ownership change.

(3) *Reduction in value by the amount restored.* The value of the stock of the electing member is reduced by any amount of value that the electing member elects to restore under paragraph (c)(2) of this section to another component member.

(4) *Appropriate adjustments.* Appropriate additional adjustments consistent with paragraphs (c)(1), (2), and (3) of this section must be made to prevent any duplication of value. Thus, for example, adjustments must be made to reflect—

(i) Any indirect ownership interest in another component member;

(ii) Any cross ownership of stock by component members of the controlled group with respect to the controlled group loss; and

(iii) Any value used to determine a limitation under section 382 with respect to controlled group losses from the same period.

(5) *Certain reductions in the value of members of a controlled group.* A loss corporation that has an ownership change is required to make adjustments consistent with this paragraph (c) with respect to its stock if the stock of another corporation in which it had a direct or indirect ownership interest was disposed of before the ownership change, and;

(i) Both corporations were component members of a controlled group—

(A) With respect to a taxable year to which a controlled group loss of the loss corporation is attributable; and

(B) At any time during the 2 year period before the ownership change; and

(ii) Both corporations are component members of a controlled group at any time during the 2 year period following the ownership change.

(d) *No double reduction.* To the extent consistent with the purposes of this section, section 382 and this section shall not be applied to duplicate a reduction in the value of a loss corporation. Thus, for example, if the value of a loss corporation is reduced under section 382(l)(1) to reflect a capital contribution of stock of a component member, it is not again reduced by such amount under paragraph (c)(1) of this section. If this paragraph (d) applies to prevent a reduction in value from being duplicated, the application of the other rules of this section, such as those relating to the restoration of value, is correspondingly limited in a manner consistent with the principles of this section.

(e) *Definitions and nomenclature—*

(1) *Definitions in section 382 and the regulations thereunder.* Except as otherwise provided, the definitions and nomenclature contained in section 382 and the regulations thereunder apply to this section.

(2) *Controlled group.* Controlled group has the same 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).

(3) *Component member.* Component member has the same 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).

(4) *Predecessor and successor corporation.* As the context may require, a reference to a corporation, or component member includes a reference to a predecessor or successor corporation.

(f) *Coordination between consolidated groups and controlled groups.* Some or all of the component members of a controlled group may also be members of a consolidated group, and a controlled group loss may be subject to a consolidated section 382 limitation or subgroup section 382 limitation determined under § 1.1502-93T. Except as otherwise provided in this paragraph (f) and §§ 1.1502-91T through 1.1502-99T, § 1.1502-93T applies instead of this section when both sections, by their terms, are otherwise applicable. This section is applicable and may require an adjustment to value if a member of a consolidated group, a loss group, or a loss subgroup (as those terms are defined in §§ 1.1502-1(h) and 1.1502-91T) is also a component member of a controlled group with respect to a controlled group loss. Solely for purposes of applying this section, a consolidated group, loss group, or loss subgroup is treated as a single corporation. Thus to determine the limitation with respect to any portion of the pre-change consolidated attributes or pre-change subgroup attributes of the loss group or loss subgroup that is a controlled group loss, the consolidated section 382 limitation or subgroup section 382 limitation is computed by treating the loss group or the loss subgroup as a single corporation, and adjusting value in accordance with paragraph (c) of this section. See paragraph (g) Example 4 of this section.

(g) *Examples.* For purposes of the examples in this section, unless otherwise stated, the nomenclature and assumptions of the examples in § 1.382-2T(b) apply, all corporations file separate income tax returns on a calendar year basis, the only 5-percent shareholder of a corporation is a public group, and the facts set forth the only owner shifts with respect to the corporations during the testing period.

Example 1. Controlled group with respect to a controlled group loss. (a) Public L owns all of the L stock, L and Public L1 own 30 percent and 70 percent, respectively, of the L1 stock, and L1 owns all of the corporation T stock. L1 has a net operating loss arising in Year 1 that is carried over to Year 4. L has a net operating loss arising in Year 2 that is carried over to Year 4. On August 1, Year 3, L acquires 30 percent of the stock of L1, thereby increasing its percentage ownership interest in L1 to 60 percent. On December 1, Year 3, L1 purchases all of the stock of corporation S from Public S. On November 1, Year 4, P acquires all of the L stock. The acquisition by P of all of the L stock on November 1, Year 4, causes ownership changes of both L and L1 under the rules of § 1.382-2T. The following is a graphic illustration of these facts.

(A) With respect to the taxable year to which L1's net operating loss carryover is attributable (i.e., Year 1); and

(B) On November 1, Year 4, L1's change date. Although L and S are component members of L1's controlled group on L1's change date, they are not component members of the controlled group with respect to the Year 1 net operating loss carryover because they were not component members with respect to the year to which the net operating loss carryover is attributable.

(2) The value of L1's stock must therefore be adjusted in accordance with paragraph (c) of this section to take into account an adjustment with respect to the T stock (but not the S stock) in computing L1's limitation under section 382 with respect to its net operating loss carryover.

(c) Although L is a member of a controlled group composed of L, L1, S, and T on November 1, Year 4, L's change date, it is not a component member of a controlled group with respect to Year 2, the taxable year to which its net operating loss carryover is attributable. Therefore, L's Year 2 net operating loss carryover is not a controlled group loss under paragraph (b) of this section and the value of L's stock is not adjusted in accordance with paragraph (c) of this section to compute L's limitation under section 382 with respect to the Year 2 net operating loss carryover.

Example 2. Adjustments to value of the controlled group members. (a) Since Year 1, A has owned all of the stock of L, L and B have owned 80 percent and 20 percent, respectively, of the stock of corporation P, and P and C have owned 75 percent and 25 percent, respectively, of the stock of L1. L and L1 each has a net operating loss for the Year 6 taxable year that is carried over to its respective Year 7 taxable year. On December 1, Year 7, A sells all of the L stock to D. The sale results in ownership changes of both L and L1. Immediately before the ownership changes, the total value of the L1 stock is \$40, the total value of the P stock (including the value of its L1 stock) is \$100, and the total value of the L stock (including the value of the P stock) is \$200. The following is a graphic illustration of these facts.

(b)(1) Under paragraph (b) of this section, the Year 1 net operating loss carryover of L1 is a controlled group loss because L1 is a component member of a controlled group with respect to Year 1, the year to which the loss is attributable. L1 and T compose a controlled group with respect to the net operating loss carryover because L1 and T are component members of a controlled group both—

(b) Under paragraph (b) of this section, the Year 6 net operating loss carryovers of each of L and L1 are controlled group losses because each of L and L1 is a component member of a controlled group with respect to Year 6, the year to which the losses are attributable. L, P, and L1 compose controlled groups with respect to both Year 6 net operating loss carryovers because L, P, and L1 are component members of a controlled group both—

(1) With respect to the taxable years to which the net operating loss carryovers are attributable (i.e., Year 6); and

(2) On December 1, Year 7, the change date.

(c) The value of the stock of L1 for purposes of determining its limitation under section 382 with respect to its net operating loss carryover from Year 6 is \$40. L1 does not elect to restore any value to P under paragraph (c)(2) of this section.

(d) The value of the stock of P (\$100) is reduced under paragraph (c)(1) of this section by the value of the stock of L1 that it directly owns, \$30 (75% x \$40). Following the adjustment, the value of the stock of P is \$70. P elects to restore this entire \$70 of value to L.

(e) The value of the stock of L, \$200, is reduced under paragraph (c)(1) of this section by the value of the stock of P it directly owns, i.e., \$80 (80% x \$100), and increased under paragraph (c)(2) of this section by the amount P elects to restore to L, i.e., \$70. Thus, the value of the L stock for purposes of determining L's limitation under section 382 with respect to its net operating loss carryover from Year 6 is \$190 (\$200 - \$80 + \$70).

Example 3. Limitation on restoration of value.

(a) The facts are the same as in *Example 2*, except that L1 elects to restore \$20 to P. For purposes of determining L1's limitation under section 382 with respect to the Year 6 net operating loss carryover, the value of the stock of L1 is \$20 (\$40 - \$20) because the value of its stock is reduced under paragraph (c)(3) of this section by the \$20 of value it elects to restore to P.

(b) The value of the stock of P (\$100) is reduced under paragraph (c)(1) of this section by the value of the L1 stock it directly owns (\$30), and is increased under paragraph (c)(2) of this section by the value that L1 elects to restore to P (\$20). Thus, the value of the P stock is \$90 (\$100 - \$30 + \$20).

(c)(1) P elects to restore to L the maximum value permitted under this section. The value of the stock of L, \$200, is reduced under paragraph (c)(1) of this section by the value of the P stock it directly owns (\$80), and is increased by the value that P elects to restore to L. P may elect to restore to L the lesser of—

(A) The sum of the value of its stock immediately after adjustment under paragraph (c)(1) of this section (i.e., \$70) plus the value restored to it by L1 (i.e., \$20) (a total of \$90); or

(B) The value of the P stock (without regard to the adjustment required by paragraphs (c)(1) and (2) of this section) that is directly owned by L immediately before the ownership change (i.e., \$80).

(2) Thus, \$80 is the maximum amount that P may elect to restore to L. Following the restoration of value by P, the value of the L stock for purposes of determining L's limitation under section 382 is \$200 (\$200 - \$80 + \$80).

Example 4. Coordination with consolidated return regulations. (a) P and its wholly owned subsidiary L file a consolidated return. L owns 79 percent of the outstanding stock of L1. P acquired the stock of L in Year 1 and L acquired the stock of L1 in Year 2. The P consolidated group has a consolidated net operating loss arising in the Year 6 consolidated return year that is carried over to Year 8. L1 has a net operating loss arising in its Year 6 taxable year that is also carried over to Year 8. On January 1, Year 8, the P consolidated group has an ownership change under § 1.1502-92T(b)(1)(i) and L1 has an ownership change under § 1.382-2T.

(b)(1) Under paragraph (b) of this section, the Year 6 net operating loss carryover of the P group is a controlled group loss because P, L, and L1 are component members of a controlled group with respect to Year 6, the year to which the loss is

attributable. P, L, and L1 compose a controlled group with respect to the Year 6 net operating loss carryover of the P loss group because they are component members of a controlled group both—

(A) With respect to the taxable years to which the net operating loss carryover is attributable (i.e., Year 6); and

(B) On January 1, Year 8, the P group's change date. (2) Because P and L compose a loss group (within the meaning of § 1.1502-91T(c)) with respect to its Year 6 net operating loss carryover, the P loss group must compute a consolidated section 382 limitation with respect to its Year 6 net operating loss carryover as a result of the ownership change.

(c) In computing the consolidated section 382 limitation under § 1.1502-93T with respect to the Year 6 net operating loss carryover, the value of the P stock immediately before the ownership change is reduced under paragraphs (c)(1) and (f) of this section by the value immediately before the ownership change of the L1 stock directly owned by L immediately after the ownership change. L1 may, however, elect to restore such value to the P consolidated group to the extent permitted under paragraph (c)(2) of this section.

Example 5. Appropriate adjustments for indirect ownership interest. (a) Individual A owns all of the stock of L, L owns an 80 percent interest in the capital and profits of partnership PS, and PS owns 75 percent of the stock of L1. Both L and L1 have net operating losses for the Year 1 taxable year that are carried over to their respective Year 2 taxable years. On December 19, Year 2, A sells all of the L stock to an unrelated individual. The sale results in an ownership change of L and L1.

(b) Under paragraph (b) of this section, the Year 1 net operating loss carryovers of each of L and L1 are controlled group losses because each of L and L1 is a component member of a controlled group with respect to Year 1, the year to which the losses are attributable. L and L1 compose controlled groups with respect to each corporation's net operating loss carryovers because L and L1 are component members of a controlled group both—

(1) With respect to the taxable years to which the net operating loss carryovers are attributable (i.e., Year 1); and

(2) On December 19, Year 2, the change date.

(c) L has an indirect ownership interest in L1 which, under paragraph (c)(4) of this section, must be taken into account in applying this section. As a result, the value of the L stock for purposes of determining its limitation under section 382 with respect to the Year 1 net operating loss carryover must be reduced by the value of L's indirect ownership interest in the L1 stock (60 percent) that it owns through PS immediately before the ownership change, and is increased by the amount (if any) that L1 elects to restore to L under paragraph (c)(2) of this section. The value of L1 is reduced under paragraph (c)(3) of this section to the extent that L1 elects to restore value to L.

(h) *Time and manner of filing election to restore*—(1) *Statement required.*

The election to restore value described in paragraph (c)(2) of this section must be in the form set forth below. It must be signed on behalf of both the electing member and the corporation to which such value is restored by persons authorized to sign their respective income tax returns. (The common parent of a consolidated group must make the election

on behalf of the group.) It must be filed by the loss corporation with its income tax return for the taxable year in which the ownership change occurs (or with an amended return for such year filed on or before the due date (including extensions) of the income tax return of any component member with respect to the taxable year in which the ownership change occurs). The statement must provide that: "THIS IS AN ELECTION UNDER § 1.382- 8T OF THE INCOME TAX REGULATIONS TO RESTORE ALL OR PART OF THE VALUE OF [insert name and E.I.N. of the electing member] TO [insert name and E.I.N. of the corporation to which value is restored]. The statement must also—

(i) Identify the change date for the loss corporation in connection with which the election is made;

(ii) State the value of the electing member's stock (without regard to any adjustment under paragraph (c) of this section) immediately before the ownership change;

(iii) State the amount of any reduction required under paragraph (c)(1) of this section with respect to stock of the electing member that is owned directly or indirectly by the corporation to which value is restored;

(iv) State the amount of value that the electing member elects to restore to the corporation; and

(v) State whether the value of either component member's stock was adjusted pursuant to paragraph (c)(4) of this section.

(2) *Revocation of election.* An election made under this section is revocable only with the consent of the Commissioner.

(3) *Filing by component member.* An electing member must attach a copy of the statement described in paragraph (h)(1) of this section to its income tax return (or amended return) for the taxable year which includes the change date in connection with which the election is made.

(i) [Reserved]

(j) *Effective date*—(1) *In general.* This section applies to a loss corporation that has an ownership change with respect to a controlled group loss on or after January 1, 1997.

(2) *Transition rule*—(i) *In general.* The members of a controlled group on January 1, 1997, that have had an ownership change with respect to a controlled group loss before January 1, 1997, must determine the limitations

under section 382 for any post-change year with respect to controlled group losses by using a reasonable method to preclude the value of stock of a component member that was owned directly or indirectly by another member immediately after an ownership change from being taken into account more than once in determining the limitations under section 382 with respect to controlled group losses. If such a reasonable method was not used for a post-change year, subject to the exception in paragraph (j)(3) of this section, the members of the controlled group described in the preceding sentence must reduce their limitations under section 382 for post-change years for which the income tax return is filed after January 1, 1997, to recapture, as quickly as possible, any limitation that members took into account in excess of the amount that would be allowable under this section.

(ii) *Special transition rule for controlled groups that had ownership changes before January 29, 1991.* For purposes of this section, in the case of an ownership change occurring before January 29, 1991, the controlled group with respect to a controlled group loss does not include a corporation that is not a component member of the controlled group on January 29, 1991. Thus, in the case of an ownership change occurring before January 29, 1991, paragraph (c) of this section does not require that a loss corporation that is a component member of a controlled group to disregard the value of stock of another corporation directly owned immediately after the ownership change in determining the value of its own stock unless the other corporation is a component member of the controlled group on January 29, 1991.

(3) *Amended returns.* A taxpayer that has had an ownership change before January 1, 1997, may file an amended return for any taxable year to modify the amount of a limitation under section 382 with respect to a controlled group loss only if—

(i) The modification complies with the rules contained in this section for computing a limitation under section 382;

(ii) Any other component member of the controlled group with respect to the controlled group loss who elects to restore value and whose taxable income is affected by the election to restore value also files amended returns that comply with such rules; and

(iii) Corresponding adjustments are made in amended returns for all taxable years ending after December 31, 1986.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. In § 602.101, paragraph (c) is amended by adding an entry in numerical order to the table to read as follows:

§ 602.101 OMB Control numbers.

* * * * *

(c)

CFR part or section where identified or described	Current OMB control No.
1.382.8T	1545-1434

Margaret Milner Richardson,
Commissioner of Internal Revenue.
Approved May 31, 1996.

Leslie Samuels,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on June 26, 1996, 8:45 a.m., and published in the issue of the Federal Register for June 27, 1996, 61 F.R. 33313)