

§ 1.1502-21A

26 CFR Ch. I (4-1-10 Edition)

whether a deduction or loss with respect to any asset is economically accrued in a separate return limitation year, the term “predecessor” as used in § 1.1502-1(f)(1) shall include any transferor of such asset if the basis of the asset in the hands of the transferee is determined (in whole or in part) by reference to its basis in the hands of such transferor.

(3) *Transitional rule.* If the assets which produced the built-in deductions were acquired (either directly or by acquiring a new member) by the group on or before January 4, 1973, and the separate return limitation year in which such deductions were economically accrued ended before such date, then at the option of the taxpayer, the provisions of this paragraph before amendment by T.D. 7246 shall apply, and, in addition, if such assets were acquired on or before April 17, 1968, and the separate return limitation year in which the built-in deductions were economically accrued ended on or before such date, then at the option of the taxpayer, the provisions of § 1.1502-31A(b)(9) (as contained in the 26 C.F.R. edition revised as of April 1, 1996) shall apply in lieu of this paragraph.

(4) *Exceptions.* (i) Subparagraphs (1), (2), and (3) of this paragraph shall not limit built-in deductions in a taxable year with respect to assets acquired (either directly or by acquiring a new member) by the group if:

(a) The group acquired the assets more than 10 years before the first day of such taxable year, or

(b) Immediately before the group acquired the assets, the aggregate of the adjusted basis of all assets (other than cash, marketable securities, and goodwill) acquired from the transferor or owned by the new member did not exceed the fair market value of all such assets by more than 15 percent.

(ii) For purposes of subdivision (i)(b) of this subparagraph, a security is not a marketable security if immediately before the group acquired the assets:

(a) The fair market value of the security is less than 95 percent of its adjusted basis, or

(b) The transferor or new member had held the security for at least 24 months, or

(c) The security is stock in a corporation at least 50 percent of the fair market value of the outstanding stock of which is owned by the transferor or new member.

(b) *Effective date.* This section applies to any consolidated return years to which § 1.1502-21T does not apply. See § 1.1502-21T(g) for effective dates of that section.

[T.D. 6894, 31 FR 11794, Sept. 8, 1966, as amended by T.D. 6909, 31 FR 16695, Dec. 30, 1966; T.D. 7246, 37 FR 761, Jan. 4, 1972; T.D. 7728, 45 FR 72650, Nov. 3, 1980; T.D. 8677, 61 FR 33323, June 27, 1996. Redesignated and amended by T.D. 8677, 61 FR 33326, June 27, 1996]

§ 1.1502-21A Consolidated net operating loss deduction generally applicable for consolidated return years beginning before January 1, 1997.

(a) *In general.* The consolidated net operating loss deduction shall be an amount equal to the aggregate of the consolidated net operating loss carryovers and carrybacks to the taxable year (as determined under paragraph (b) of this section).

(b) *Consolidated net operating loss carryovers and carrybacks—*(1) *In general.* The consolidated net operating loss carryovers and carrybacks to the taxable year shall consist of any consolidated net operating losses (as determined under paragraph (f) of this section) of the group, plus any net operating losses sustained by members of the group in separate return years, which may be carried over or back to the taxable year under the principles of section 172(b). However, such consolidated carryovers and carrybacks shall not include any consolidated net operating loss apportioned to a corporation for a separate return year pursuant to § 1.1502-79A(a), and shall be subject to the limitations contained in paragraphs (c), (d), and (e) of this section and to the limitation contained in § 1.1502-15A (or § 1.1502-11(c), as appropriate).

(2) *Rules for applying section 172(b)(1)—*(i) *Regulated transportation corporations.* For purposes of applying section 172(b)(1)(C) (relating to net operating losses sustained by regulated transportation corporations), in the case of a consolidated net operating loss sustained in a taxable year for which a

member of the group was a regulated transportation corporation (as defined in section 172(j)(1)), the portion, if any, of such consolidated net operating loss which is attributable to such corporation (as determined under this paragraph) shall be a carryover to the sixth taxable year following the loss year only if such corporation is a regulated transportation corporation for such sixth year, and shall be a carryover to the seventh taxable year following the loss year only if such corporation is a regulated transportation corporation for both such sixth and seventh years.

(ii) *Trade expansion losses.* In the case of a carryback of a consolidated net operating loss from a taxable year for which a member of the group has been issued a certification under section 317 of the Trade Expansion Act of 1962 and with respect to which the requirements of section 172(b)(3)(A) have been met, section 172(b)(1)(A)(ii) shall apply only to the portion of such consolidated net operating loss attributable to such member.

(iii) *Foreign expropriation losses.* An election under section 172(b)(3)(C) (relating to 10-year carryover of portion of net operating loss attributable to a foreign expropriation loss) may be made for a consolidated return year only if the sum of the foreign expropriation losses (as defined in section 172(k)) of the members of the group for such year equals or exceeds 50 percent of the consolidated net operating loss for such year. If such election is made, the amount which may be carried over under section 172(b)(1)(D) is the smaller of (a) the sum of such foreign expropriation losses, or (b) the consolidated net operating loss.

(3) *Absorption rules.* For purposes of determining the amount, if any, of a net operating loss (whether consolidated or separate) which can be carried to a taxable year (consolidated or separate), the amount of such net operating loss which is absorbed in a prior consolidated return year under section 172(b)(2) shall be determined by:

(i) Applying all net operating losses which can be carried to such prior year in the order of the taxable years in which such losses were sustained, beginning with the taxable year which ends earliest, and

(ii) Applying all such losses which can be carried to such prior year from taxable years ending on the same date on a pro rata basis, except that any portion of a net operating loss attributable to a foreign expropriation loss to which section 172(b)(1)(D) applies shall be applied last.

(c) *Limitation on net operating loss carryovers and carrybacks from separate return limitation years—(1) General rule.* In the case of a net operating loss of a member of the group arising in a separate return limitation year (as defined in paragraph (f) of § 1.1502-1) of such member (and in a separate return limitation year of any predecessor of such member), the amount which may be included under paragraph (b) of this section (computed without regard to the limitation contained in paragraph (d) of this section) in the consolidated net operating loss carryovers and carrybacks to a consolidated return year of the group shall not exceed the amount determined under subparagraph (2) of this paragraph.

(2) *Computation of limitation.* The amount referred to in subparagraph (1) of this paragraph with respect to a member of the group is the excess, if any, of:

(i) Consolidated taxable income (computed without regard to the consolidated net operating loss deduction), minus such consolidated taxable income recomputed by excluding the items of income and deduction of such member, over

(ii) The net operating losses attributable to such member which may be carried to the consolidated return year arising in taxable years ending prior to the particular separate return limitation year.

(3) *Examples.* The provisions of this paragraph and paragraphs (a) and (b) of this section may be illustrated by the following examples:

Example 1. (i) Corporation P formed corporations S and T on January 1, 1965. P, S, and T filed separate returns for the calendar year 1965, a year for which an election under section 1562 was effective. T's return for that year reflected a net operating loss of \$10,000. The group filed a consolidated return for 1966 reflecting consolidated taxable income of \$30,000 (computed without regard to the consolidated net operating loss deduction).

Among the transactions occurring during 1966 were the following:

(a) P sold goods to T deriving deferred profits of \$7,000 on such sales, \$2,000 of which was restored to consolidated taxable income on the sale of such goods to outsiders;

(b) T sold a machine to S deriving a deferred profit of \$5,000, \$1,000 of which was restored to consolidated taxable income as a result of S's depreciation deductions;

(c) T distributed a \$3,000 dividend to P; and

(d) In addition to the transactions described above, T had other taxable income of \$6,000.

(ii) The carryover of T's 1965 net operating loss to 1966 is subject to the limitation contained in this paragraph, since 1965 was a separate return limitation year (an election under section 1562 was effective for such year). Thus, only \$7,000 of T's \$10,000 net operating loss is a consolidated net operating loss carryover to 1966, since such carryover is limited to consolidated taxable income (computed without regard to the consolidated net operating loss deduction), \$30,000, minus such consolidated taxable income recomputed by excluding the items of income and deduction of T, \$23,000 (*i.e.*, consolidated taxable income computed without regard to the \$1,000 restoration of T's deferred gain and T's \$6,000 of other income). In making such recomputation, no change is made in the effect on consolidated taxable income of P's sale to T, or of the dividend from T to P.

Example 2. (i) Corporation P was formed on January 1, 1966. P filed separate returns for the calendar years 1966 and 1967 reflecting net operating losses of \$4,000 and \$12,000, respectively. P purchased corporation S on March 15, 1967. S was formed on February 1, 1966, and filed a separate return for the taxable year ending January 31, 1967. S also filed a short period return for the period from February 1 to December 31, 1967, and joined with P in filing a consolidated return for 1968. S sustained net operating losses of \$5,000 and \$6,000 for its taxable years ending January 31, 1967, and December 31, 1967, respectively. An election under section 1562 was not effective for P and S during the period involved. Consolidated taxable income for 1968 (computed without regard to the consolidated net operating loss deduction) was \$16,000; such consolidated taxable income recomputed by disregarding the items of income and deduction of S was \$9,000.

(ii) In order of time, the following losses are absorbed in 1968:

(a) P's \$4,000 net operating loss for the calendar year 1966 (such loss is not subject to the limitation contained in this paragraph since P is the common parent corporation for 1968);

(b) S's \$5,000 net operating loss for the year ended January 31, 1967. Such loss is subject to the limitation contained in this paragraph, since S was not a member of the

group on each day of such year. However, such loss can be carried over and absorbed in full since such limitation is \$7,000 (consolidated taxable income computed without regard to the consolidated net operating loss deduction, \$16,000, minus such consolidated taxable income recomputed, \$9,000); and

(c) \$6,000 of P's net operating loss and \$1,000 of S's net operating loss for the taxable years ending December 31, 1967. This is determined by applying the losses from such year which can be carried to 1968 (P's \$12,000 loss and \$2,000 of S's \$6,000 loss, since such \$6,000 loss is limited under this paragraph) on a pro rata basis against the amount of such losses which can be absorbed in that year, \$7,000 (consolidated taxable income of \$16,000 less the \$9,000 of losses absorbed from prior years). The carryover of S's loss to 1968 is subject to the limitation contained in that paragraph, since S was not a member of the group on each day of its taxable year ending December 31, 1967. Such loss is limited to \$2,000, the excess of \$7,000 (as determined under (ii)(b)) over \$5,000 (S's carryover from the year ended January 31, 1967). If a consolidated return is filed in 1969, the consolidated net operating loss carryovers will consist of P's unabsorbed loss of \$6,000 (\$12,000 minus \$6,000) from 1967 and, subject to the limitation contained in this paragraph, S's unabsorbed loss of \$5,000 (\$6,000 minus \$1,000) from its year ended December 31, 1967.

(d) *Limitation on carryovers where there has been a consolidated return change of ownership*—(1) *General rule.* If a consolidated return change of ownership (as defined in paragraph (g) of § 1.1502-1) occurs during the taxable year or an earlier taxable year, the amount which may be included under paragraph (b) of this section in the consolidated net operating loss carryovers to the taxable year with respect to the aggregate of the net operating losses attributable to old members of the group (as defined in paragraph (g)(3) of § 1.1502-1) arising in taxable years (consolidated or separate) ending on the same day and before the taxable year in which the consolidated return change of ownership occurred shall not exceed the amount determined under subparagraph (2) of this paragraph.

(2) *Computation of limitation.* The amount referred to in subparagraph (1) of this paragraph shall be the excess of:

(i) The consolidated taxable income for the taxable year (determined without regard to the consolidated net operating loss deduction) recomputed by including only the items of income and

deduction of the old members of the group, over

(ii) The sum of the net operating losses attributable to the old members of the group which may be carried to the taxable year arising in taxable years ending prior to the particular loss year or years.

(3) *Example.* The provisions of this paragraph may be illustrated by the following example:

Example. (i) Corporation P is formed on January 1, 1967, and on the same day it forms corporation S. P and S file a consolidated return for the calendar year 1967, reflecting a consolidated net operating loss of \$500,000. On January 1, 1968, individual X purchases all of the outstanding stock of P. X subsequently contributes \$1,000,000 to P and P purchases the stock of corporation T. P, S, and T file a consolidated return for 1968 reflecting consolidated taxable income of \$600,000 (computed without regard to the consolidated net operating loss deduction). Such consolidated taxable income recomputed by including only the items of income and deduction of P and S is \$350,000.

(ii) Since a consolidated return change of ownership took place in 1968 (there was more than a 50 percent change of ownership of P), the amount of the consolidated net operating loss from 1967 which can be carried over to 1968 is limited to \$350,000, the excess of \$350,000 (consolidated taxable income recomputed by including only the items of income and deduction of the old members of the group, P and S) over zero (the amount of the consolidated net operating loss carryovers attributable to the old members of the group arising in taxable years ending before 1967).

(4) *Cross-reference.* See § 1.1502-21T(d)(1) for the rule that applies the principles of this paragraph (d) in consolidated return years beginning on or after January 1, 1997, with respect to a consolidated return change of ownership occurring before January 1, 1997.

(e) *Limitations on net operating loss carryovers under section 382—(1) Section 382(a).* (i) If at the end of a taxable year (consolidated or separate) there has been an increase in ownership of the stock of the common parent of a group (within the meaning of section 382(a)(1)(A) and (B)), and any member of the group has not continued to carry on a trade or business substantially the same as that conducted before any such increase (within the meaning of section 382(a)(1)(C)), then the portion of any consolidated net operating loss

sustained in prior taxable years attributable to such member (as determined under this paragraph) shall not be allowed as a carryover to such taxable year or to any subsequent taxable year.

(ii) If the provisions of section 382(a) disallow the deduction of a net operating loss carryover from a separate return year of a member of the group to a subsequent taxable year, no amount shall be included under paragraph (b) of this section as a consolidated net operating loss carryover to such a subsequent consolidated return year with respect to such separate return year of such member.

(iii) The provisions of this subparagraph may be illustrated by the following example:

Example. P, S, and T file a consolidated return for the calendar year 1969, reflecting a consolidated net operating loss attributable in part to each member. P owns 80 percent of S's stock and S owns 80 percent of T's stock. On January 1, 1970, A purchases 50 percent of P's stock. During 1970 T's business is discontinued. Since there has been a 50 percentage point increase in ownership of P, the common parent of the group, and since T has not continued to carry on the same trade or business after such increase, the portion of the 1969 consolidated net operating loss attributable to T shall not be included in any net operating loss deduction for 1970 or for any subsequent taxable years, whether consolidated or separate.

(2) *Section 382(b).* If a net operating loss carryover from a separate return year of a predecessor of a member of the group to the taxable year is reduced under the provisions of section 382(b), the amount included under paragraph (b) of this section with respect to such predecessor shall be so reduced.

(3) *Effective date.* This paragraph (e) disallows or reduces the net operating loss carryovers of a member as a result of a transaction to which old section 382 (as defined in § 1.382-2T(f)(21)) applies. See § 1.1502-21T(d)(2) for the rule that applies the principles of this paragraph (e) in consolidated return years beginning on or after January 1, 1997, with respect to such a transaction.

(f) *Consolidated net operating loss.* The consolidated net operating loss shall be determined by taking into account the following:

(1) The separate taxable income (as determined under § 1.1502-12) of each

§ 1.1502-22A

26 CFR Ch. I (4-1-10 Edition)

member of the group, computed without regard to any deduction under section 242;

(2) Any consolidated capital gain net income (net capital gain for taxable years beginning before January 1, 1977);

(3) Any consolidated section 1231 net loss;

(4) Any consolidated charitable contributions deduction;

(5) Any consolidated dividends received deduction (determined under § 1.1502-26 without regard to paragraph (a)(2) of that section); and

(6) Any consolidated section 247 deduction (determined under § 1.1502-27 without regard to paragraph (a)(1)(ii) of that section).

(g) *Groups that include insolvent financial institutions.* For rules applicable to relinquishing the entire carryback period with respect to losses attributable to insolvent financial institutions, see § 301.6402-7 of this chapter.

(h) *Effective date.* Except as provided in § 1.1502-21T (d)(1), (d)(2), and (g)(3), this section applies to consolidated return years beginning before January 1, 1997.

[T.D. 6894, 31 FR 11794, Sept. 8, 1966, as amended by T.D. 7728, 45 FR 72650, Nov. 3, 1980; T.D. 8387, 56 FR 67489, Dec. 31, 1991; T.D. 8446, 57 FR 53034, Nov. 6, 1992; T.D. 8677, 61 FR 33323, June 27, 1996. Redesignated and amended by T.D. 8677, 61 FR 33328, June 27, 1996]

§ 1.1502-22A Consolidated net capital gain or loss generally applicable for consolidated return years beginning before January 1, 1997.

(a) *Computation*—(1) *Consolidated capital gain net income.* The consolidated capital gain net income (net capital gain for taxable years beginning before January 1, 1977) for the taxable year shall be determined by taking into account:

(i) The aggregate of the capital gains and losses (determined without regard to gains or losses to which section 1231 applies or net capital loss carryovers or carrybacks) of the members of the group for the consolidated return year,

(ii) The consolidated section 1231 net gain for such year (computed in accordance with §§ 1.1502-23A or 1.1502-23T), and

(iii) The consolidated net capital loss carryovers or carrybacks to such year

(as determined under paragraph (b) of this section).

(2) *Consolidated net capital loss.* The consolidated net capital loss shall be determined under subparagraph (1) of this paragraph but without regard to subdivision (iii) thereof.

(3) *Special rules.* For purposes of this section, capital gains and losses on intercompany transactions and transactions with respect to stock, bonds, and other obligations of a member of the group shall be reflected as provided in §§ 1.1502-13, and 1.1502-19, and capital losses shall be limited as provided in §§ 1.1502-15A and 1.1502-11(c).

(4) [Reserved]

(5) *Example.* The provisions of this paragraph may be illustrated by the following example:

Example. (i) Corporations P, S, and T file consolidated returns on a calendar year basis for 1966 and 1967. The members had the following transactions involving capital assets during 1967: P sold an asset with a \$10,000 basis to S for \$17,000 and none of the circumstances of restoration described in § 1.1502-13 occurred by the end of the consolidated return year; S sold an asset to individual A for \$7,000 which S had purchased during 1966 from P for \$10,000, and with respect to which P had deferred a gain of \$2,000; T sold an asset with a basis of \$10,000 to individual B for \$25,000. The group has a consolidated net capital loss carryover to the taxable year of \$10,000.

(ii) The consolidated net capital gain of the group is \$4,000, determined as follows: P's net capital gain of \$2,000, representing the deferred gain on the sale to S during the taxable year 1966, restored into income during taxable year 1967 (the \$7,000 gain on P's deferred intercompany transaction is not taken into account for the current year), plus T's net capital gain of \$15,000, minus S's net capital loss of \$3,000 and the consolidated net capital loss carryover of \$10,000.

(b) *Consolidated net capital loss carryovers and carrybacks*—(1) *In general.* The consolidated net capital loss carryovers and carrybacks to the taxable year shall consist of any consolidated net capital losses of the group, plus any net capital losses of members of the group arising in separate return years of such members, which may be carried to the taxable year under the principles of section 1212(a). However, such consolidated carryovers and carrybacks shall not include any consolidated net capital loss apportioned