§ 1.1502–42 Mutual savings banks, etc.

(a) In general. This section applies to mutual savings banks and other institutions described in section 593(a).

(b) Total deposits. In computing for purposes of section 593(b)(1)(B)(ii) total deposits or withdrawable accounts at the close of the taxable year, the total deposits or withdrawable accounts of other members shall be excluded.

(c) Taxable income; taxable years for which the due date (without extensions) for filing returns is before March 15, 1983. For taxable years for which the due date (without extensions) for filing returns is before March 15, 1983, a member's taxable income for purposes of section 593(b)(2) is determined under §1.1502–27(b) (computed without regard to any deduction under section 593(b)(2)). In addition, for taxable years beginning after July 11, 1969, taxable income as computed under the preceding sentence is subject to the adjustments provided in section 593(b)(2)(E). See §1.593–6A(b)(5).

(d) Taxable income; taxable years for which the due date (without extensions) for filing returns is after March 14, 1983—

(1) In general. For a taxable year for which the due date (without extensions) for filing returns is after March 14, 1983, a thrift's taxable income for
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purposes of section 593(b)(2) is its tentative taxable income (as defined in paragraph (e)(1) of this section).

(2) Definitions. For purposes of this section:

(i) A thrift is a member described in section 593(a).

(ii) A nonthrift is a member that is not a thrift.

(e) Tentative taxable income (or loss)—

(1) Thrift. For purposes of this section, a thrift’s tentative taxable income (or loss) is its separate taxable income (determined under §1.1502–12 without paragraph (q) thereof and without any deduction under section 593(b)), subject to the following adjustments in the following order:

(i) The adjustments described in paragraph (e)(3) of this section;

(ii) The adjustments described in section 593(b)(2)(E) for those thrifts with separate taxable income greater than zero (determined after the adjustments under paragraph (e)(3) of this section); and

(iii) The adjustments described in paragraph (f) of this section.

(2) Nonthrift. For purposes of this section, a nonthrift’s tentative taxable income (or loss) is its separate taxable income (determined under §1.1502–12), adjusted for the portion of the consolidated net operating loss deduction attributable to the member, the portion of the consolidated net capital loss carryover or carryback attributable to the member, and further adjusted as described in paragraph (e)(3) of this section.

(3) Adjustments for all members. For each member, the following adjustments taken into account in the computation of consolidated taxable income are included in determining its tentative taxable income (or loss) in order to adjust separate taxable income of the member to take into account certain consolidated items:

(i) The portions of the consolidated charitable contributions deduction and the consolidated dividends received deduction attributable to the member.

(ii) The member’s capital gain net income, determined without any net capital loss carryover or carryback attributable to the member.

(iii) The member’s net capital loss and section 1231 net loss, reduced by the portion of the consolidated net capital loss attributable to the member.

(f) Adjustments for thrifts—

(1) Reductions. A thrift’s separate taxable income (as adjusted under paragraph (e)(3) of this section) is reduced (but not below zero) by losses of thrifts and to the extent attributable to functionally related activities, losses of a nonthrift. Certain operating rules for determining the amount of the reductions are provided in paragraph (f)(4) of this section. The reductions are made in the following amounts in the following order:

(i) The thrift’s allocable share (as determined under paragraph (h)(2) of this section) of another thrift’s tentative taxable loss. That tentative taxable loss is determined by including a deduction under section 593(b) (other than paragraph (2) thereof) for the year in which the loss arises.

(ii) The thrift’s allocable share (as determined under paragraph (h)(3) of this section) of the portion of the consolidated net operating loss deduction attributable to it or another thrift. That consolidated net operating loss deduction is determined by excluding losses arising in taxable years for which the due date (without extensions) for filing returns is before March 15, 1983.

(iii) The thrift’s allocable share (as determined under paragraph (h)(4) of this section) of the loss attributable to functionally related activities of a nonthrift (as determined under paragraph (g) of this section). For a rule netting that share against certain income attributable to functionally related activities of that nonthrift, see paragraph (f)(4)(iv) of this section.

(iv) The thrift’s allocable share (as determined under paragraph (h)(5) of this section) of the portion of the consolidated net operating loss deduction attributable to functionally related activities of a nonthrift (as determined under paragraph (h)(5) of this section). That consolidated net operating loss deduction is determined by excluding losses arising in taxable years for
which the due date (without extensions) for filing returns is before March 15, 1983. For a rule netting that share against certain income attributable to functionally related activities of that nonthrift, see paragraph (f)(4)(iv) of this section.

(2) Increases. (i) A thrift's separate taxable income (as adjusted under paragraphs (e)(3) and (f)(1) of this section) is increased in a subsequent consolidated return year to restore reductions made in a prior consolidated return year of a thrift's separate taxable income by reason of losses of a nonthrift. This increase is the amount of the thrift's allocable share (as determined under paragraph (h)(6) of this section) of the income attributable to functionally related activities of a nonthrift in a consolidated return year and is made only in that year. This increase is made only if both the thrift and the nonthrift were members of the group in the consolidated return years in which both the reduction and increase are made.

(ii) This subdivision (ii) limits the increases to a thrift's separate taxable income to assure that income of a particular nonthrift is used to restore reductions of a thrift only to the extent that such nonthrift's losses reduced the thrift's income. Therefore, as of the end of a consolidated return year, the cumulative increases to a thrift's tentative taxable income (by reason of income attributable to functionally related activities of a nonthrift) may not exceed the cumulative reductions to the thrift's separate taxable income made (by reason of the nonthrift's functionally related activities) during which both the thrift institution and the nonthrift institution were members of the group.

(iii) For a netting rule, see paragraph (f)(4)(iv) of this section.

(3) Special Rule. (i) If a carryback to a thrift's separate taxable income diminishes the reduction to a thrift's separate taxable income for a prior consolidated return year otherwise required by paragraph (f)(1)(iii) or (iv) of this section, then any increases to a thrift's separate taxable income under paragraph (f)(2) of this section for an intervening consolidated return year must be recomputed to take into account the effect of such carryback. Thus, if a net operating loss attributable to a thrift is carried back and completely offsets the thrift's separate taxable income (before the reductions under paragraph (f)(1)(iii) or (iv) of this section), any increase to the thrift's separate taxable income under paragraph (f)(2) of this section attributable to a reduction in the year to which the loss is carried for an intervening consolidated return year will be eliminated. The recomputation required by this subdivision (3) must be reflected on an amended return for the intervening consolidated return year for which the increase was previously reported. See example (2) in paragraph (j) of this section.

(ii) If a deficiency for an intervening consolidated return year results from the application of paragraph (f)(3)(i) of this section with respect to an item to which section 6501(h) applies, the deficiency may be assessed at any time within the period described in section 6501(h).

(iii) For purposes of chapter 67 of the Code (relating to interest), the last date prescribed for payment of any tax owed as a result of the application of paragraph (f)(3)(i) of this section is deemed to be the last day of the taxable year for which the item carried back arose.

(4) Operating rules. For purposes of paragraphs (d) through (j) of this section:

(i) The portion of a consolidated net operating loss deduction attributable to a member is determined as follows:

(A) First, determine under §§1.1502-21(b) (or §1.1502-79A(a)(3), as appropriate) the portion of each consolidated net operating loss attributable to the member for the particular year in which the loss arose.

(B) Second, apply the anti-double-counting rule in paragraph (h)(3)(iii) of this section so as not to take the same loss into account twice.

(C) Finally, apply the loss absorption limit in paragraph (f)(4)(iv) of this section to the total amount of the consolidated net operating loss deduction from a particular loss year.
(ii) Capital loss carryovers and carrybacks shall be taken into account in a manner consistent with the principles of paragraphs (d) through (j) of this section.

(iii) This subdivision (iii) prescribes a loss absorption limit. The total amount of the consolidated net operating loss deduction from a given year (loss year) taken into account as reductions under paragraph (f)(1) of this section for another year (absorption year) shall not exceed the amount of the consolidated net operating loss deduction attributable to the loss year absorbed in computing consolidated taxable income for the absorption year. For this purpose, consolidated taxable income for the absorption year shall include a deduction under section 593(b) (other than paragraph (2) thereof) for each thrift member.

(iv) This subdivision (iv) prescribes a rule for netting in certain cases income attributable to functionally related activities of a nonthrift in a consolidated return year ("income year") against losses attributable to functionally related activities of that nonthrift which arise in a consolidated return year ("loss year"). That nonthrift's income is netted against the portion of that nonthrift's loss which would otherwise be applied in a consolidated return year ("reduction year") under paragraph (f)(1) (iii) or (iv) of this section to reduce a thrift's tentative taxable income, but:
   (A) Only if the income year is not later than the loss year and the reduction year, and
   (B) Only to the extent the income had not previously been taken into account under paragraph (f)(2) of this section or this subdivision (iv) as of the close of the later of the loss year and the reduction year.

(g) Income (or loss) attributable to functionally related activities of a nonthrift—
(1) In general. For purposes of this section, the income (or loss) attributable to functionally related activities of a nonthrift is the income (or loss) of the nonthrift:
   (i) Attributable to the provision of assets or the rendition of services to a thrift (such as the leasing of office space or providing computer or financial services), or
   (ii) Derived from the assets described in section 7701(a)(19)(C) (iii) through (x), but only if such assets comprise 5 percent or more of the gross assets of the nonthrift.

(2) Amount of income (or loss). The amount of income (or loss) from such activities is the excess of (i) gross income from such activities over (ii) the deductions of the nonthrift allocable and apportionable to that gross income under the principles of §1.861-8. The loss attributable to functionally related activities of a nonthrift is the excess (if any) of such deductions over such gross income. That loss, however, may not exceed the amount of the tentative taxable loss of that nonthrift (determined by excluding losses arising in taxable years for which the due date (without extensions) for filing returns is before March 15, 1983).

(h) Allocation of income and losses—
(1) In general. Paragraphs (h)(2) through (5) of this section provides rules for allocating different losses among thrifts that have tentative taxable income greater than zero. Generally, these allocations are made in the order listed in paragraph (f)(1) of this section and are based upon the relative tentative taxable income of the thrifts to which the particular loss is allocated. For purposes of each allocation under a subdivision of such paragraph (f)(1), the tentative taxable income of the thrifts used in making this allocation is reduced by the thrift's allocable share of losses allocated to the thrift under a prior subdivision of such paragraph (f)(1). Accordingly, for purposes of this paragraph (h), tentative taxable income is determined without regard to paragraph (f) of this section, except as otherwise provided. Paragraph (h)(6) of this section provides rules for allocating income attributable to functionally related activities of a nonthrift based upon the relative reductions to thrift income made on account of that nonthrift.

(2) Allocation of tentative taxable loss of other thrifts. For purposes of paragraph (f)(1)(i) of this section, a thrift's allocable share of another thrift's tentative taxable loss is the loss multiplied by a fraction. The numerator of the fraction is the tentative taxable income (if greater than zero) of the
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thrift, and the denominator is the aggregate of such tentative taxable income of each thrift.

(3) **Allocation of portions of a consolidated net operating loss deduction.**

(i) For purposes of paragraph (f)(1)(ii) of this section, a first thrift’s allocable share of the portion of the consolidated net operating loss deduction attributable to another thrift is determined under paragraph (h)(2) of this section as if that portion were a tentative taxable loss of that other thrift and by computing tentative taxable income under such paragraph (h)(2) by taking into account paragraph (f)(1)(i) of this section. A thrift’s allocable share of the portion of the consolidated net operating loss deduction attributable to that thrift is equal to that entire portion.

(ii) For purposes of paragraph (f)(1)(iv) of this section, a thrift’s allocable share of the portion of a consolidated net operating loss deduction attributable to functionally related activities of a nonthrift (determined under paragraph (h)(5) of this section) is determined under paragraph (h)(4) of this section as if that portion were a loss attributable to functionally related activities of the nonthrift and by computing tentative taxable income under such paragraph (h)(4) by taking into account paragraph (f)(1)(i), (ii), and (iii) of this section.

(iii) This subdivision (iii) prevents the “double-counting” of losses. The reduction to the tentative taxable income of a thrift is diminished to the extent the loss that gave rise to the reduction has previously been taken into account in reducing a thrift’s tentative taxable income. Thus, any loss taken into account as a reduction to a thrift’s separate taxable income under any subdivision of paragraph (f)(1) of this section shall be reduced (but not below zero) to the extent taken into account:

(A) In a prior consolidated return year under any subdivision of such paragraph (f)(1) or

(B) In the current consolidated return year under a previous subdivision of such paragraph (f)(1).

(4) **Allocation of loss attributable to functionally related activities of a nonthrift.** For purposes of paragraph (f)(1)(iii) of this section, a thrift’s allocable share of a loss attributable to functionally related activities of a nonthrift is determined by multiplying the loss by a fraction. The numerator of the fraction is the tentative taxable income (if greater than zero) of the thrift (taking into account paragraph (f)(1) (i) and (ii) of this section) and the denominator is the aggregate of such tentative taxable income (so determined) of each thrift.

(5) **Portion of the consolidated net operating loss deduction attributable to functionally related activities of a particular nonthrift.** The portion of the consolidated net operating loss deduction attributable to functionally related activities of a particular nonthrift is the lesser of the following two amounts:

(i) The portion of the consolidated net operating loss deduction attributable to that nonthrift.

(ii) The aggregate of the losses attributable to functionally related activities of that nonthrift for the taxable years in which the consolidated net operating loss deduction arose.

(6) **Allocation of income attributable to functionally related activities of a nonthrift.** For purposes of paragraph (f)(2) of this section, a thrift institution’s allocable share of the income attributable to functionally related activities of a nonthrift is determined by multiplying that income by a fraction. The numerator of the fraction is the amount of the cumulative reductions referred to in paragraph (f)(2)(ii) of this section (minus the cumulative increases under paragraph (f)(2) of this section) made on account of that nonthrift for the thrift and the denominator is the sum of such cumulative reductions (minus such cumulative increases) made on account of that nonthrift for all thrifts.

(7) **Proper accounting** The provisions of section 482 apply in determining a thrift institution’s tentative taxable income, and in determining the gross income and deductions attributable to functionally related activities. For example, an expense such as the salary of an individual who performs services for both a thrift and a nonthrift must be allocated in a manner that fairly reflects the value of the services rendered to each.
(j) **Examples.** The provisions of this section may be illustrated by the following examples. In each example the letter "T" for a member denotes a thrift and the letters "NT" denote a non thrift. Also, in each example, a thrift loss includes a bad debt deduction under section 593(b) (other than paragraph (2) thereof) for such year and a thrift with income would have such a bad debt deduction of zero.

**Example 1.** (a) In 1983, corporations T1, T2, NT1, and NT2 are formed. These corporations constitute an affiliated group that files a consolidated return on the basis of a calendar year. For 1983, 1984, and 1985, the tentative taxable income (or loss) of each member (before the application of paragraph (f) of this section) is as follows:

<table>
<thead>
<tr>
<th></th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>NT1</td>
<td>$60</td>
<td>$(140)</td>
<td>$15</td>
</tr>
<tr>
<td>T1</td>
<td>1,000</td>
<td>500</td>
<td>750</td>
</tr>
<tr>
<td>NT2</td>
<td>(90)</td>
<td>(220)</td>
<td>150</td>
</tr>
<tr>
<td>T2</td>
<td>(300)</td>
<td>400</td>
<td>250</td>
</tr>
</tbody>
</table>

In 1983, NT1, in addition to its other business activities, acted as a collection agency for T1. Deductions attributable to those activities exceeded gross income attributable to those activities by $70, NT1’s other activities generated a $10 gain. In 1984 and 1985, NT1 acted as a collection agency for T1 as its sole activity.

(b) The tentative taxable incomes of T1 and T2 for 1983 (determined under paragraph (e) of this section) as of the close of that year are adjusted by paragraph (f) of this section, as follows:

(i) **T1’s tentative taxable income:**

T1’s tentative taxable income (before the application of paragraph (f) of this section) is $1,000.

Less:

- T2’s tentative taxable loss: $300
- NT1’s functionally related loss (limited by NT1’s overall loss): 60

T1’s tentative taxable income for 1983 is $640.

(ii) **T2’s tentative taxable income for 1983 is zero.**

(c) The tentative taxable incomes of T1 and T2 for 1984 (determined under paragraph (e) of this section as of the close of that year) are adjusted by paragraph (f) of this section as follows:

(i) **T1’s tentative taxable income:**

T1’s tentative taxable income (before the application of paragraph (f) of this section) is $500.

Less:

- T1’s allocable portion of NT1’s functionally related loss (140×500/(500+400)): 78

(ii) **T2’s tentative taxable income:**

T2’s tentative taxable income (before the application of paragraph (f) of this section) is $400.

Less:

- T2’s allocable portion of NT1’s functionally related loss (140×400/(500+400)): 62
- T2’s tentative taxable income for 1984: 338

(d) For 1985, the amount under paragraph (f)(2) of this section for both T1 and T2 is $15 (NT1’s tentative taxable income from functionally related activities for 1985).

Example 2. (a) In 1983, corporations T, NT1, and NT2 are formed. These corporations constitute an affiliated group. NT2 provides computer services to T as its sole activity. For the calendar years 1983, 1984, and 1985, the group files a consolidated return. The tentative taxable income of each member (before the application of paragraph (f) of this section) is as follows:

<table>
<thead>
<tr>
<th></th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>T</td>
<td>$100</td>
<td>$0</td>
<td>$(200)</td>
</tr>
<tr>
<td>NT1</td>
<td>200</td>
<td>0</td>
<td>100</td>
</tr>
<tr>
<td>NT2</td>
<td>(20)</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

(b) Under paragraph (f)(1) of this section, T’s tentative taxable income for 1983 (determined at the close of that year) is reduced to $80 (i.e., $100 less NT2’s $20 loss). For 1984, under paragraph (f)(2) of this section, T’s tentative taxable income is increased by $20.

Example 3. (a) T and NT are formed in 1983 and are the only members of an affiliated
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(b) At the close of 1983, T’s tentative taxable income is $100. For 1985, however, the group has a consolidated net operating loss of $40, all of which is attributable to NT’s functionally related activities and which is carried back to 1983. However, T’s tentative taxable income for 1983 is not reduced under paragraph (f)(1)(ii) of this section, since, under paragraph (f)(4)(iv) of this section, NT’s 1984 income attributable to functionally related activities of $40 is netted against that $40 carryback.

Example 4. (a) In 1983, corporations T1, T2, NT1, and NT2 are formed. For calendar years 1983, 1984, and 1985, the affiliated group consisting of T1, T2, NT1, and NT2 filed a consolidated return. NT1 provided computer services to T1 as its sole activity. The tentative taxable income of each member (before the application of paragraph (f) of this section) is as follows:

<table>
<thead>
<tr>
<th></th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>T</td>
<td>100</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>NT</td>
<td>0</td>
<td>40</td>
<td>(40)</td>
</tr>
</tbody>
</table>

(b) For 1983, the group has a consolidated net operating loss of $30, apportioned $10 each to T1, T2, and NT1 under §1.1502-79A(a)(3). For 1984, the only thrift with tentative taxable income greater than zero (before applying paragraph (f) of this section) is T1. That tentative taxable income of $100 is first reduced to $20 by T2’s $80 1984 loss under paragraph (f)(1)(i) of this section. Next, T1’s remaining tentative taxable income of $20 is reduced to $10 by the portions attributable to T1 and T2 of the 1983 consolidated net operating loss carryover to 1984 under paragraph (f)(1)(ii) of this section. The sum of those portions is limited to $10 (i.e., $5 each) by paragraph (f)(4)(iii) of this section because 1984 consolidated taxable income available for absorption after a bad debt deduction under section 593(b) (other than paragraph (2) thereof) for that year is $6 (i.e., $30 + $100 − $90 − $25). Because separate taxable income cannot be reduced below zero under paragraph (f)(1) of this section, T1’s remaining tentative taxable income of $5 is thus reduced to zero by the portions attributable to T1 and T2, respectively, of the consolidated net operating loss carryover from 1983 to 1985 under paragraph (f)(1)(i) of this section.

Example 4. (a) In 1983, corporations T1, T2, NT1, and NT2 are formed. For calendar years 1983, 1984, and 1985, the affiliated group consisting of T1, T2, NT1, and NT2 filed a consolidated return. NT1 provided computer services to T1 as its sole activity. The tentative taxable income of each member (before the application of paragraph (f) of this section) is as follows:

<table>
<thead>
<tr>
<th></th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>T1</td>
<td>(50)</td>
<td>100</td>
<td>30</td>
</tr>
<tr>
<td>T2</td>
<td>(50)</td>
<td>(80)</td>
<td>(25)</td>
</tr>
<tr>
<td>NT1</td>
<td>(50)</td>
<td>(40)</td>
<td>(99)</td>
</tr>
<tr>
<td>NT2</td>
<td>120</td>
<td>20</td>
<td>100</td>
</tr>
</tbody>
</table>

(c) For 1985, the only thrift with tentative taxable income greater than zero (before applying paragraph (f) of this section) is T1. T1’s tentative taxable income for 1983 of $30 is reduced to $5 by T2’s 1985 loss of $25 under paragraph (f)(1)(i) of this section. Next, the portions attributable to T1 and T2 of the consolidated net operating loss carryover from 1983 to 1985 for purposes of paragraph (f)(1)(i) of this section must be determined. That determination is made without applying the rules for loss absorption in computing consolidated taxable income under §1.1502-21A(b)(3). Those portions are instead determined in 3 steps under paragraph (f)(4)(i) of this section. The first of those steps is to determine each of T1’s and T2’s attributable portions of the 1983 consolidated net operating loss which under §1.1502-79A(a)(3) is $10 or $20 for both thrifts. The second of those steps is to apply the anti-double counting rule under paragraph (b)(3)(i) of this section to reduce that $20 amount by the $10 total of the two $5 portions attributable to T1 and T2 of the consolidated net operating loss carryover from 1983 to 1984 taken into account as reductions to T1’s tentative taxable income for 1984 under paragraph (f)(1)(ii) of this section. That leaves a $10 total amount available to be taken into account as reductions to T1’s remaining tentative taxable income of $5 for 1985 under paragraph (f)(1)(i) of this section. Under the third of those steps that $10 amount, however, is limited, under the loss absorption limit of paragraph (f)(4)(iii) of this section, to the $6 of the 1983 consolidated net operating loss carryover to 1985 which is absorbed in computing consolidated taxable income for 1985 since 1985 consolidated taxable income available for absorption after a bad debt deduction under section 593(b) (other than paragraph (2) thereof) for that year is $6 (i.e., $30 + $100 − $90 − $25). Because separate taxable income cannot be reduced below zero under paragraph (f)(1) of this section, T1’s remaining tentative taxable income of $5 is thus reduced to zero by the portions attributable to T1 and T2, respectively, of the consolidated net operating loss carryover from 1983 to 1985 under paragraph (f)(1)(i) of this section.

Example 4. (a) In 1983, corporations T1, T2, NT1, and NT2 are formed. For calendar years 1983, 1984, and 1985, the affiliated group consisting of T1, T2, NT1, and NT2 filed a consolidated return. NT1 provided computer services to T1 as its sole activity. The tentative taxable income of each member (before the application of paragraph (f) of this section) is as follows:

<table>
<thead>
<tr>
<th></th>
<th>1983</th>
<th>1984</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>T1</td>
<td>(50)</td>
<td>100</td>
<td>30</td>
</tr>
<tr>
<td>T2</td>
<td>(50)</td>
<td>(80)</td>
<td>(25)</td>
</tr>
<tr>
<td>NT1</td>
<td>(50)</td>
<td>(40)</td>
<td>(99)</td>
</tr>
<tr>
<td>NT2</td>
<td>120</td>
<td>20</td>
<td>100</td>
</tr>
</tbody>
</table>

(Sec. 1502, 7805, Internal Revenue Code of 1954 (88A Stat. 367 and 917; (26 U.S.C. 1502 and 7805))