

168, and using the rate and method the taxpayer properly applied to the uncertified portion of the facility, the adjusted basis of the certified portion on December 31, 1956, would be \$9,500, computed in the same manner as the adjusted basis of the uncertified portion. The difference between the facility's actual adjusted basis (\$15,500) and its adjusted basis determined without regard to section 168 (\$19,000), is \$3,500. Accordingly, the entire \$3,500 gain on the sale of the facility (\$19,000 sale price, less \$15,500 adjusted basis) is treated as ordinary income.

Example 2. Assume that the entire facility in example (1) had been certified under section 168(e) and that, therefore, the adjusted basis of the facility on December 31, 1956, is \$12,000. Assume further that the taxpayer adopts straight line depreciation as a proper method of depreciation for determining the adjusted basis of the facility without regard to section 168. Thus, the adjusted basis, without regard to section 168, would be \$19,000. This amount is \$7,000 more than the \$12,000 adjusted basis under section 168. Hence, the entire \$7,000 gain on the sale of the facility (\$19,000 sale price less \$12,000 adjusted basis) is treated as ordinary income.

(b) *Substituted basis.* If a taxpayer acquires other property in an exchange for an emergency facility with respect to which amortization deductions have been allowed or allowable, and if the basis in his hands of the other property is determined by reference to the basis of the emergency facility, then the basis of the other property is determined with regard to section 168, and therefore the provisions of section 1238 apply with respect to gain realized on a subsequent sale or exchange of the other property. The provisions of section 1238 also apply to gain realized on the sale or exchange of an emergency facility (or other property acquired, as described in the preceding sentence, in exchange for an emergency facility) by a taxpayer in whose hands the basis of the facility (or other property) is determined by reference to its basis in the hands of another person to whom deductions were allowable or allowed with respect to the facility under section 168.

[T.D. 6500, 25 FR 12020, Nov. 26, 1960, as amended by T.D. 6825, 30 FR 7281, June 2, 1965]

§ 1.1239-1 Gain from sale or exchange of depreciable property between certain related taxpayers after October 4, 1976.

(a) *In general.* In the case of a sale or exchange of property, directly or indirectly, between related persons after October 4, 1976 (other than a sale or exchange made under a binding contract entered into on or before that date), any gain recognized by the transferor shall be treated as ordinary income if such property is, in the hands of the transferee, subject to the allowance for depreciation provided in section 167. This rule also applies to property which would be subject to the allowance for depreciation provided in section 167 except that the purchaser has elected a different form of deduction, such as those allowed under sections 169, 188, and 191.

(b) *Related persons.* For purposes of paragraph (a) of this section, the term *related persons* means:

- (1) A husband and wife,
- (2) An individual and a corporation 80 percent or more in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual, or
- (3) Two or more corporations 80 percent or more in value of the outstanding stock of each of which is owned, directly or indirectly, by or for the same individual.

(c) *Rules of construction—(1) Husband and wife.* For purposes of paragraph (b)(1) of this section, if on the date of the sale or exchange a taxpayer is legally separated from his spouse under an interlocutory decree of divorce, the taxpayer and his spouse shall not be treated as husband and wife, provided the sale or exchange is made pursuant to the decree and the decree subsequently becomes final. Thus, if pursuant to an interlocutory decree of divorce, an individual transfers depreciable property to his spouse and, because of this section, the gain recognized on the transfer of the property is treated as ordinary income, the individual may, if the interlocutory decree becomes final after his tax return has been filed, file a claim for a refund.

(2) *Sales between commonly controlled corporations.* In general, in the case of a

sale or exchange of depreciable property between related corporations (within the meaning of paragraph (b)(3) of this section), gain which is treated as ordinary income by reason of this section shall be taxable to the transferor corporation rather than to a controlling shareholder. However, such gain shall be treated as ordinary income taxable to a controlling shareholder rather than the transferor corporation if the transferor corporation is used by a controlling shareholder as a mere conduit to make a sale to another controlled corporation, or the entity of the corporate transferor is otherwise properly disregarded for tax purposes. Sales between two or more corporations that are related within the meaning of paragraph (b)(3) of this section may also be subject to the rules of section 482 (relating to allocation of income between or among organizations, trades, or businesses which are commonly owned or controlled), and to rules requiring constructive dividend treatment to the controlling shareholder in appropriate circumstances.

(3) *Relationship determination for transfers made after January 6, 1983—taxpayer and an 80-percent owned entity.* For purposes of paragraph (b)(2) of this section with respect to transfers made after January 6, 1983—

(i) If the transferor is an entity, the transferee and such entity are related if the entity is an 80-percent owned entity with respect to such transferee either immediately before or immediately after the sale or exchange of depreciable property, and

(ii) If the transferor is not an entity, the transferee and such transferor are related if the transferee is an 80-percent owned entity with respect to such transferor immediately after the sale or exchange of depreciable property.

(4) *Relationship determination for transfers made after January 6, 1983—two 80-percent owned entities.* For purposes of paragraph (b)(3) of this section, with respect to transfers made after January 6, 1983, two entities are related if the same shareholder both owns 80 percent or more in value of the stock of the transferor before the sale or exchange of depreciable property and owns 80 percent or more in value of the stock of the transferee immediately

after the sale or exchange of depreciable property.

(5) *Ownership of stock.* For purposes of determining the ownership of stock under this section, the constructive ownership rules of section 318 shall be applied, except that section 318(a)(2)(C) (relating to attribution of stock ownership from a corporation) and section 318(a)(3)(C) (relating to attribution of stock ownership to a corporation) shall be applied without regard to the 50-percent limitation contained therein. The application of the constructive ownership rules of section 318 to section 1239 is illustrated by the following examples:

Example 1. A, an individual, owns 79 percent of the stock (by value) of Corporation X, and a trust for A's children owns the remaining 21 percent of the stock. A's children are deemed to own the stock owned for their benefit by the trust in proportion to their actuarial interests in the trust (section 318(a)(2)(B)). A, in turn, constructively owns the stock so deemed to be owned by his children (section 318(a)(1)(A)(ii)). Thus, A is treated as owning all the stock of Corporation X, and any gain A recognizes from the sale of depreciable property to Corporation X is treated under section 1239 as ordinary income.

Example 2. Y Corporation owns 100 percent in value of the stock of Z Corporation. Y Corporation sells depreciable property at a gain to Z Corporation. P and his daughter, D, own 80 percent in value of the Y Corporation stock. Under the constructive ownership rules of section 318, as applied to section 1239, P and D are each considered to own the stock in Z Corporation owned by Y Corporation. Also, P and D are each considered to own the stock in Y Corporation owned by the other. As a result, both P and D constructively own 80 percent or more in value of the stock of both Y and Z Corporations. Thus, the sale between Y and Z is governed by section 1239 and produces ordinary income to Y.

[T.D. 7569, 43 FR 51388, Nov. 3, 1978, as amended by T.D. 8106, 51 FR 42835, Nov. 26, 1986]

§ 1.1239-2 Gain from sale or exchange of depreciable property between certain related taxpayers on or before October 4, 1976.

Section 1239 provides in general that any gain from the sale or exchange of depreciable property between a husband and wife or between an individual and a controlled corporation on or before October 4, 1976 (and in the case of a sale or exchange occurring after that