

§ 1.1503(d)–8

forward to subsequent taxable years and may reduce the recapture income to the extent of consolidated taxable income generated in subsequent years. In year 3, \$25x of income was attributable to the Country X separate unit and P earns \$15x of income. Thus, the P consolidated group has \$40x of consolidated taxable income in year 3. As a result, the \$100x of recapture income can be reduced by \$40x. This is the case because if a domestic use election had not been made for the \$100x year 1 dual consolidated loss such that it was subject to the limitations of § 1.1503(d)–4(b) and (c), only \$60x of the loss would have remained subject to such limitations at the time of the foreign use triggering event. Accordingly, if S can adequately document the lesser amount, the amount of recapture income is \$60x (\$100x – \$40x). The \$60x recapture income is attributable to the Country X separate unit pursuant to § 1.1503(d)–5(c)(4)(vi).

(C) Pursuant to § 1.1503(d)–6(h)(6)(i), commencing in year 4, the \$60x recapture amount is reconstituted and treated as a net operating loss incurred by the Country X separate unit of S in a separate return limitation year, subject to the limitation under § 1.1503(d)–4(b) (and therefore subject to the restrictions of § 1.1503(d)–4(c)). The loss is only available for carryover to taxable years after year 3 (and is not available for carryback). The carryover period of the loss, for purposes of section 172(b), will start from year 1, when the dual consolidated loss that was subject to recapture was incurred. In addition, such reconstituted net operating loss is not eligible for the exceptions contained in § 1.1503(d)–6(b) through (d). Pursuant to § 1.1503(d)–6(j)(1)(iii), the domestic use agreement filed by the P consolidated group with respect to the year 1 dual consolidated loss of the Country X separate unit is terminated and has no further effect.

(iii) *Alternative facts.* The facts are the same as in paragraph (i) of this *Example 40*, except that the triggering event that occurs at the end of year 3 is a sale by S of its entire interest in DE1x to B, an unrelated domestic corporation. The sale does not qualify as a transaction described in section 381. The results are the same as in paragraph (ii) of this *Example 40*, except that pursuant to § 1.1503(d)–6(h)(6)(ii) the \$60x net operating loss is not reconstituted (with respect to either S or B). The loss is not reconstituted with respect to S because the Country X separate unit ceases to be a separate unit of S (or any other member of the consolidated group that includes S) and therefore would have been eliminated pursuant to § 1.1503(d)–4(d)(1)(ii) if no domestic use election had been made with respect to such loss. The loss is not reconstituted with respect to B because B was not the domestic owner of the combined separate unit when the dual consolidated loss that is recaptured was in-

26 CFR Ch. I (4–1–12 Edition)

curred, and B did not acquire the Country X separate unit in a section 381 transaction.

[T.D. 9315, 72 FR 12914, Mar. 19, 2007; 72 FR 20424, Apr. 25, 2007]

§ 1.1503(d)–8 Effective dates.

(a) *General rule.* Except as provided in paragraph (b) of this section, this paragraph (a) provides the dates of applicability of §§ 1.1503(d)–1 through 1.1503(d)–7. Sections 1.1503(d)–1 through 1.1503(d)–7 shall apply to dual consolidated losses incurred in taxable years beginning on or after April 18, 2007. However, a taxpayer may apply §§ 1.1503(d)–1 through 1.1503(d)–7, in their entirety, to dual consolidated losses incurred in taxable years beginning on or after January 1, 2007, by filing its return and attaching to such return the domestic use agreements, certifications, or other information in accordance with these regulations. For purposes of this section, the term *application date* means either April 18, 2007, or, if the taxpayer applies these regulations pursuant to the preceding sentence, January 1, 2007. Section 1.1503–2 applies for dual consolidated losses incurred in taxable years beginning on or after October 1, 1992, and before the application date.

(b) *Special rules—*(1) *Reduction of term of agreements filed under §§ 1.1503–2A(c)(3), 1.1503–2A(d)(3), 1.1503–2(g)(2)(i), or 1.1503–2T(g)(i).* If an agreement is filed in accordance with §§ 1.1503–2A(c)(3), 1.1503–2A(d)(3), 1.1503–2(g)(2)(i), or 1.1503–2T(g)(2)(i) with respect to a dual consolidated loss incurred in a taxable year beginning prior to the application date and an event requiring recapture with respect to the dual consolidated loss subject to the agreement has not occurred as of the application date, then such agreement will be considered by the Internal Revenue Service to apply only for any taxable year up to and including the fifth taxable year following the year in which the dual consolidated loss that is the subject of the agreement was incurred and thereafter will have no effect.

(2) *Reduction of term of agreements filed under §§ 1.1503–2(g)(2)(iv)(B)(2)(i) (1992), 1.1503–2(g)(2)(iv)(B)(3)(i), or Rev. Proc. 2000–42.* Taxpayers subject to the terms of a closing agreement entered into with the Internal Revenue Service pursuant to §§ 1.1503–2(g)(2)(iv)(B)(2)(i)

(1992), 1.1503-2(g)(2)(iv)(B)(3)(i), or Rev. Proc. 2000-42 (2000-2 CB 394), see § 601.601(d)(2)(ii)(b) of this chapter, will be deemed to have satisfied the closing agreement's fifteen-year certification period requirement if the five-year certification period specified in § 1.1503(d)-1(b)(20) has elapsed, provided such closing agreement is still in effect as of the application date, and provided the dual consolidated losses have not been recaptured. For example, if a calendar year taxpayer that has a January 1, 2007, application date entered into a closing agreement with respect to a dual consolidated loss incurred in 2003 and, as of January 1, 2007, the closing agreement is still in effect and the dual consolidated loss subject to the closing agreement has not been recaptured, then the closing agreement's fifteen-year certification period will be deemed satisfied when the five-year certification period described in § 1.1503(d)-1(b)(20) has elapsed. Thus, the dual consolidated loss will be subject to the recapture and certification provisions of the closing agreement in such a case only through December 31, 2008. Alternatively, if a calendar year taxpayer that has a January 1, 2007, application date entered into a closing agreement with respect to a dual consolidated loss incurred in 2000 and, as of January 1, 2007, the closing agreement is still in effect and the dual consolidated loss subject to the closing agreement has not been recaptured, then the certification period is deemed to be satisfied.

(3) *Relief for untimely filings.* Paragraphs (b)(3)(i) through (iii) of this section set forth the effective dates for rules that provide relief for the failure to make timely filings of an election, agreement, statement, rebuttal, computation, closing agreement, or other information, pursuant to section 1503(d) and these regulations.

(i) *General rule.* Except as provided in paragraphs (b)(3)(ii) and (iii) of this section, the reasonable cause relief standard of § 1.1503(d)-1(c) applies for all untimely filings with respect to dual consolidated losses, including with respect to dual consolidated losses incurred in taxable years beginning before the application date.

(ii) *Closing agreements.* Solely with respect to closing agreements described in § 1.1503-2(g)(2)(iv)(B)(3)(i) and Rev. Proc. 2000-42, taxpayers must request relief for untimely requests through the process provided under §§ 301.9100-1 through 301.9100-3 of this chapter. See paragraph (b)(4) of this section for rules that permit the multiple-party event exception, rather than closing agreements, for certain triggering events.

(iii) *Pending requests for relief.* Taxpayers that have letter ruling requests under §§ 301.9100-1 through 301.9100-3 of this chapter pending as of March 19, 2007 (other than requests under paragraph (b)(3)(ii) of this section) are not required to use the reasonable cause procedure under § 1.1503(d)-1(c); however, if such taxpayers have not yet received a determination of their request, they may withdraw their request consistent with the procedures contained in Rev. Proc. 2007-1 (2007-1 IRB 1), see § 601.601(d)(2)(ii)(b) of this chapter, (or any succeeding document) and use the reasonable cause procedure set forth in § 1.1503(d)-1(c). In that event, the Internal Revenue Service will refund the taxpayer's user fee.

(4) *Multiple-party event exception to triggering events.* This paragraph (b)(4) applies to events described in § 1.1503-2(g)(2)(iv)(B)(1)(i) through (iii) that occur after April 18, 2007 and that are with respect to dual consolidated losses that were incurred in taxable years beginning on or after October 1, 1992, and before the application date. The events described in the previous sentence are not eligible for the exception described in § 1.1503-2(g)(2)(iv)(B)(1), but instead are eligible for the multiple-party event exception described in § 1.1503(d)-6(f)(2)(i), as modified by this paragraph (b)(4). Thus, such events are not eligible for a closing agreement described in § 1.1503-2(g)(2)(iv)(B)(3)(i) and Rev. Proc. 2000-42. For purposes of applying § 1.1503(d)-6(f)(2)(i) to transactions covered by this paragraph, agreements described in § 1.1503-2(g)(2)(i) (rather than domestic use agreements) shall be filed, and subsequent triggering events and exceptions thereto have the meaning provided in § 1.1503-2(g)(2)(iii)(A) and (iv) (other than the exception provided under § 1.1503-2(g)(2)(iv)(B)(1)).

§ 1.1504-0

For example, if a calendar year taxpayer that has a January 1, 2007, application date filed an election under § 1.1503-2(g)(2)(i) with respect to a dual consolidated loss that was incurred in 2004, and a triggering event described in § 1.1503-2(g)(2)(iv)(B)(I)(ii) occurs with respect to such dual consolidated loss after April 18, 2007, then the event is eligible for the multiple-party event exception under § 1.1503(d)-6(f)(2)(i) (and not the exception under § 1.1503-2(g)(2)(iv)(B)(I)). However, in order to comply with § 1.1503(d)-6(f)(2)(iii)(A), the subsequent elector must file a new agreement described in § 1.1503-2(g)(2)(i) (rather than a new domestic use agreement). In addition, for purposes of determining whether there is a subsequent triggering event, and exceptions thereto, pursuant to such new agreement, § 1.1503-2(g)(2)(iii)(A) and (iv) (other than the exception provided under § 1.1503-2(g)(2)(iv)(B)(I)) shall apply. Notwithstanding the general application of this paragraph (b)(4) to events described in § 1.1503-2(g)(2)(iv)(B)(I)(i) through (iii) that occur after April 18, 2007, a taxpayer may choose to apply this paragraph (b)(4) to events described in § 1.1503-2(g)(2)(iv)(B)(I)(i) through (iii) that occur after March 19, 2007 and on or before April 18, 2007.

(5) *Basis adjustment rules.* Taxpayers may apply the basis adjustment rules of § 1.1503(d)-5(g) for all open years in which such basis is relevant, even if the basis adjustment is attributable to a dual consolidated loss incurred (or recaptured) in a closed taxable year. Taxpayers applying the provisions of § 1.1503(d)-5(g), however, must do so consistently for all open years.

[T.D. 9315, 72 FR 12914, Mar. 19, 2007; 72 FR 20424, Apr. 25, 2007]

§ 1.1504-0 Outline of provisions.

In order to facilitate the use of §§ 1.1504-1 through 1.1504-4, this section lists the captions contained in §§ 1.1504-1 through 1.1504-4.

26 CFR Ch. I (4-1-12 Edition)

§ 1.1504-1 Definitions.

§§ 1.1504-2—1.1504-3 [Reserved]

§ 1.1504-4 Treatment of warrants, options, convertible obligations, and other similar interests.

- (a) Introduction.
 - (1) General rule.
 - (2) Exceptions.
- (b) Options not treated as stock or as exercised.
 - (1) General rule.
 - (2) Options treated as exercised.
- (i) In general.
- (ii) Aggregation of options.
- (iii) Effect of treating option as exercised.
- (A) In general.
- (B) Cash settlement options, phantom stock, stock appreciation rights, or similar interests.
 - (iv) Valuation.
- (3) Example.
- (c) Definitions.
 - (1) Issuing corporation.
 - (2) Related or sequential option.
 - (3) Related persons.
 - (4) Measurement date.
- (i) General rule.
- (ii) Issuances, transfers, or adjustments not treated as measurement dates.
- (iii) Transactions increasing likelihood of exercise.
- (iv) Measurement date for options issued pursuant to a plan.
- (v) Measurement date for related or sequential options.
- (vi) Example.
- (5) In-the-money.
- (d) Options.
 - (1) Instruments treated as options.
 - (2) Instruments generally not treated as options.
- (i) Options on section 1504(a)(4) stock.
- (ii) Certain publicly traded options.
- (A) General rule.
- (B) Exception.
- (iii) Stock purchase agreements.
- (iv) Escrow, pledge, or other security agreements.
- (v) Compensatory options.
- (A) General rule.
- (B) Exceptions.
- (vi) Options granted in connection with a loan.
- (vii) Options created pursuant to a title 11 or similar case.
- (viii) Convertible preferred stock.
- (ix) Other enumerated instruments.
- (e) Elimination of federal income tax liability.
 - (f) Substantial amount of federal income tax liability.
 - (g) Reasonable certainty of exercise.
- (1) Generally.
- (i) Purchase price.
- (ii) In-the-money option.