

(2) *Avoidance transactions.* This paragraph (1)(2) applies if a transaction is engaged in or structured on or after April 8, 1994, with a principal purpose to avoid the rules of this section (and instead to apply prior law). If this paragraph (1)(2) applies, appropriate adjustments must be made in years beginning on or after July 12, 1995, to prevent the avoidance, duplication, omission, or elimination of any item (or tax liability), or any other inconsistency with the rules of this section. For example, if S is a dealer in real property and sells land to B on March 16, 1995 with a principal purpose of converting any future appreciation in the land to capital gain, B's gain from the sale of the land on May 11, 1997 might be characterized as ordinary income under this paragraph (1)(2).

(3) *Election for certain stock elimination transactions—(i) In general.* A group may elect pursuant to this paragraph (1)(3) to apply this section (including the elections available under paragraph (f)(5)(ii) of this section) to stock elimination transactions to which prior law would otherwise apply. If an election is made, this section, and not prior law, applies to determine the timing and attributes of S's and B's gain or loss from stock with respect to all stock elimination transactions.

(ii) *Stock elimination transactions.* For purposes of this paragraph (1)(3), a stock elimination transaction is a transaction in which stock transferred from S to B—

(A) Is cancelled or redeemed on or after July 12, 1995;

(B) Is treated as cancelled in a liquidation pursuant to an election under section 338(h)(10) with respect to a qualified stock purchase with an acquisition date on or after July 12, 1995;

(C) Is distributed on or after July 12, 1995; or

(D) Is exchanged on or after July 12, 1995 for stock of a member (determined immediately after the exchange) in a transaction that would cause S's gain or loss from the transfer to be taken into account under prior law.

(iii) *Time and manner of making election.* An election under this paragraph (1)(3) is made by attaching to a timely filed original return (including extensions) for the consolidated return year

including July 12, 1995 a statement entitled “[Insert Name and Employer Identification Number of Common Parent] HEREBY ELECTS THE APPLICATION OF §1.1502-13(1)(3).” See paragraph (f)(5)(ii)(E) of this section for the manner of electing the relief provisions of paragraph (f)(5)(ii) of this section.

(4) *Prior law.* For transactions occurring in S's years beginning before July 12, 1995, see the applicable regulations issued under section 1502. See §§1.1502-13, 1.1502-13T, 1.1502-14, 1.1502-14T, 1.1502-31, and 1.1502-32 (as contained in the 26 CFR part 1 edition revised as of April 1, 1995).

(5) *Consent to adopt method of accounting.* For intercompany transactions occurring in a consolidated group's first taxable year beginning on or after July 12, 1995, the Commissioner's consent under section 446(e) is hereby granted for any changes in methods of accounting that are necessary solely by reason of the timing rules of this section. Changes in method of accounting for these transactions are to be effected on a cut-off basis.

(6) *Effective/applicability date.* (i) *In general.* Paragraph (f)(7)(i) *Example 4.* applies to transactions occurring on or after December 18, 2009.

(ii) [Reserved]

(m) *Effective/applicability date.* Paragraphs (f)(5)(ii)(E) and (f)(6)(i)(C)(2) of this section apply to any original consolidated Federal income tax return due (without extensions) after June 14, 2007. For original consolidated Federal income tax returns due (without extensions) after May 30, 2006, and on or before June 14, 2007, see §1.1502-13T as contained in 26 CFR part 1 in effect on April 1, 2007. For original consolidated Federal income tax returns due (without extensions) on or before May 30, 2006, see §1.1502-13 as contained in 26 CFR part 1 in effect on April 1, 2006.

[T.D. 8597, 60 FR 36685, July 18, 1995]

EDITORIAL NOTE: For FEDERAL REGISTER citations affecting §1.1502-13, see the List of CFR Sections Affected, which appears in the Finding Aids section of the printed volume and at www.fdsys.gov.

§ 1.1502-15 SRLY limitation on built-in losses.

(a) *SRLY limitation.* Except as provided in paragraph (f) of this section

(relating to built-in losses of the common parent) and paragraph (g) of this section (relating to an overlap with section 382), built-in losses are subject to the SRLY limitation under §§ 1.1502-21(c) and 1.1502-22(c) (including applicable subgroup principles). Built-in losses are treated as deductions or losses in the year recognized, except for the purpose of determining the amount of, and the extent to which the built-in loss is limited by, the SRLY limitation for the year in which it is recognized. Solely for such purpose, a built-in loss is treated as a hypothetical net operating loss carryover or net capital loss carryover arising in a SRLY, instead of as a deduction or loss in the year recognized. To the extent that a built-in loss is allowed as a deduction under this section in the year it is recognized, it offsets any consolidated taxable income for the year before any loss carryovers or carrybacks are allowed as a deduction. To the extent not so allowed, it is treated as a separate net operating loss or net capital loss carryover or carryback arising in the year of recognition and, under § 1.1502-21(c) or 1.1502-22(c), the year of recognition is treated as a SRLY.

(b) *Built-in losses*—(1) *Defined*. If a corporation has a net unrealized built-in loss under section 382(h)(3) (as modified by this section) on the day it becomes a member of the group (whether or not the group is a consolidated group), its deductions and losses are built-in losses under this section to the extent they are treated as recognized built-in losses under section 382(h)(2)(B) (as modified by this section). This paragraph (b) generally applies separately with respect to each member, but see paragraph (c) of this section for circumstances in which it is applied on a subgroup basis.

(2) *Operating rules*. Solely for purposes of applying paragraph (b)(1) of this section, the principles of § 1.1502-94(c) apply with appropriate adjustments, including the following:

(i) *Stock acquisition*. A corporation is treated as having an ownership change under section 382(g) on the day the corporation becomes a member of a group, and no other events (e.g., a subsequent ownership change under section 382(g)

while it is a member) are treated as causing an ownership change.

(ii) *Asset acquisition*. In the case of an asset acquisition by a group, the assets and liabilities acquired directly from the same transferor (whether corporate or non-corporate, foreign or domestic) pursuant to the same plan are treated as the assets and liabilities of a corporation that becomes a member of the group (and has an ownership change) on the date of the acquisition.

(iii) *Recognized built-in gain or loss*. A loss that is included in the determination of net unrealized built-in gain or loss and that is recognized but disallowed or deferred (e.g., under § 1.337(d)-2, § 1.1502-35, § 1.1502-36, or section 267) is not treated as a built-in loss unless and until the loss would be allowed during the recognition period without regard to the application of this section. Section 382(h)(1)(B)(ii) does not apply to the extent it limits the amount of recognized built-in loss that may be treated as a pre-change loss to the amount of the net unrealized built-in loss.

(c) *Built-in losses of subgroups*—(1) *In general*. In the case of a subgroup, the principles of paragraph (b) of this section apply to the subgroup, and not separately to its members. Thus, the net unrealized built-in loss and recognized built-in loss for purposes of paragraph (b) of this section are based on the aggregate amounts for each member of the subgroup.

(2) *Members of subgroups*. A subgroup is composed of those members that have been continuously affiliated with each other for the 60 consecutive month period ending immediately before they become members of the group in which the loss is recognized. A member remains a member of the subgroup until it ceases to be affiliated with the loss member. For this purpose, the principles of § 1.1502-21(c)(2)(iv) through (vi) apply with appropriate adjustments.

(3) *Coordination of 60 month affiliation requirement with the overlap rule*. If one or more corporations become members of a group and are included in the determination of a net unrealized built-in loss that is subject to the overlap rule described in paragraph (g)(1) of this section, then for purposes of paragraph

(c)(2) of this section, such corporations that become members of the group are treated as having been affiliated for 60 consecutive months with the common parent of the group and are also treated as having been affiliated with any other members who have been affiliated or are treated as having been affiliated with the common parent at such time. The corporations are treated as having been affiliated with such other members for the same period of time that those members have been affiliated or are treated as having been affiliated with the common parent. If two or more corporations become members of the group at the same time, but this paragraph (c)(3) does not apply to every such corporation, then immediately after the corporations become members of the group, and solely for purposes of paragraph (c)(2) of this section, the corporations to which this paragraph (c)(3) applies are treated as having not been previously affiliated with the corporations to which this paragraph (c)(3) does not apply. If the common parent has become the common parent of an existing group within the previous five year period in a transaction described in §1.1502-75(d)(2)(ii) or (3), the principles of §§1.1502-91(g)(6) and 1.1502-96(a)(2)(iii) shall apply.

(4) *Built-in amounts.* Solely for purposes of determining whether the subgroup has a net unrealized built-in loss or whether it has a recognized built-in loss, the principles of §1.1502-91(g) and (h) apply with appropriate adjustments.

(d) *Examples.* For purposes of the examples in this section, unless otherwise stated, all groups file consolidated returns, all corporations have calendar taxable years, the facts set forth the only corporate activity, value means fair market value and the adjusted basis of each asset equals its value, all transactions are with unrelated persons, and the application of any limitation or threshold under section 382 is disregarded. The principles of this section are illustrated by the following examples:

Example 1. Determination of recognized built-in loss. (i) Individual A owns all of the stock of P and T. T has two depreciable assets. Asset 1 has an unrealized loss of \$55 (basis \$75, value \$20), and asset 2 has an unrealized

gain of \$20 (basis \$30, value \$50). P acquires all the stock of T from Individual A during Year 1, and T becomes a member of the P group. P's acquisition of T is not an ownership change as defined by section 382(g). Paragraph (g) of this section does not apply because there is not an overlap of the application of the rules contained in paragraph (a) of this section and section 382.

(ii) Under paragraph (b)(2)(i) of this section, and solely for purposes of applying paragraph (b)(1) of this section, T is treated as having an ownership change under section 382(g) on becoming a member of the P group. Under paragraph (b)(1) of this section, none of T's \$55 of unrealized loss is treated as a built-in loss unless T has a net unrealized built-in loss under section 382(h)(3) on becoming a member of the P group.

(iii) Under section 382(h)(3)(A), T has a \$35 net unrealized built-in loss on becoming a member of the P group ($(\$55)+\$20=(\$35)$). Assume that this amount exceeds the threshold requirement in section 382(h)(3)(B). Under section 382(h)(2)(B), the entire amount of T's \$55 unrealized loss is treated as a built-in loss to the extent it is recognized during the 5-year recognition period described in section 382(h)(7). Under paragraph (b)(2)(iii) of this section, the restriction under section 382(h)(1)(B)(ii), which limits the amount of recognized built-in loss that is treated as pre-change loss to the amount of the net unrealized built-in loss, is inapplicable for this purpose. Consequently, the entire \$55 of unrealized loss (not just the \$35 net unrealized loss) is treated under paragraph (b)(1) of this section as a built-in loss to the extent it is recognized within 5 years of T's becoming a member of the P group. Under paragraph (a) of this section, a built-in loss is subject to the SRLY limitation under §1.1502-21(c)(1).

(iv) Under paragraph (b)(2)(ii) of this section, the built-in loss would similarly be subject to a SRLY limitation under §1.1502-21(c)(1) if T transferred all of its assets and liabilities to a subsidiary of the P group in a single transaction described in section 351. To the extent the built-in loss is recognized within 5 years of T's transfer, all of the items contributed by the acquiring subsidiary to consolidated taxable income (and not just the items attributable to the assets and liabilities transferred by T) are included for purposes of determining the SRLY limitation under §1.1502-21(c)(1).

Example 2. Actual application of section 382 not relevant. (i) Individual A owns all of the stock of P, and Individual B owns all of the stock of T. T has two depreciable assets. Asset 1 has an unrealized loss of \$25 (basis \$75, value \$50), and asset 2 has an unrealized gain of \$20 (basis \$30, value \$50). P buys 55 percent of the stock of T in January of Year 1, resulting in an ownership change of T under section 382(g). During March of Year 2,

P buys the 45 percent balance of the T stock, and T becomes a member of the P group.

(ii) Although T has an ownership change for purposes of section 382 in Year 1 and not Year 2, T's joining the P group in Year 2 is treated as an ownership change under section 382(g) solely for purposes of this section. Consequently, for purposes of this section, whether T has a net unrealized built-in loss under section 382(h)(3) is determined as if the day T joined the P group were a change date.

Example 3. Determination of a recognized built-in loss of a subgroup. (i) Individual A owns all of the stock of P, S, and M. P and M are each the common parent of a consolidated group. During Year 1, P acquires all of the stock of S from Individual A, and S becomes a member of the P group. P's acquisition of S is not an ownership change as defined by section 382(g). At the beginning of Year 7, M acquires all of the stock of P from Individual A, and P and S become members of the M group. M's acquisitions of P and S are also not ownership changes as defined by section 382(g). At the time of M's acquisition of the P stock, P has (disregarding the stock of S) a \$10 net unrealized built-in gain (two depreciable assets, asset 1 with a basis of \$35 and a value of \$55, and asset 2 with a basis of \$55 and a value of \$45), and S has a \$75 net unrealized built-in loss (two depreciable assets, asset 3 with a basis of \$95 and a value of \$10, and asset 4 with a basis of \$10 and a value of \$20).

(ii) Under paragraph (c) of this section, P and S compose a subgroup on becoming members of the M group because P and S were continuously affiliated for the 60 month period ending immediately before they became members of the M group. Consequently, paragraph (b) of this section does not apply to P and S separately. Instead, their separately computed unrealized gains and losses are aggregated for purposes of determining whether, and the extent to which, any unrealized loss is treated as built-in loss under this section and is subject to the SRLY limitation under § 1.1502-21(c).

(iii) Under paragraph (c) of this section, the P subgroup has a net unrealized built-in loss on the day P and S become members of the M group, determined by treating the day they become members as a change date. The net unrealized built-in loss is the aggregate of P's net unrealized built-in gain of \$10 and S's net unrealized built-in loss of \$75, or an aggregate net unrealized built-in loss of \$65. (The stock of S owned by P is disregarded for purposes of determining the net unrealized built-in loss. However, any loss allowed on the sale of the stock within the recognition period is taken into account in determining recognized loss.) Assume that the \$65 net unrealized built-in loss exceeds the threshold requirement under section 382(h)(3)(B).

(iv) Under paragraphs (b)(1), (b)(2)(iii), and (c) of this section, a loss recognized during

the 5-year recognition period on an asset of P or S held on the day that P and S became members of the M group is a built-in loss except to the extent the group establishes that such loss exceeds the amount by which the adjusted basis of such asset on the day the member became a member exceeded the fair market value of such asset on that same day. If P sells asset 2 for \$45 in Year 7 and recognizes a \$10 loss, the entire \$10 loss is treated as a built-in loss under paragraphs (b)(2)(iii) and (c) of this section. If S sells asset 3 for \$10 in Year 7 and recognizes an \$85 loss, the entire \$85 loss is treated as a built-in loss under paragraphs (b)(2)(iii) and (c) of this section (not just the \$55 balance of the P subgroup's \$65 net unrealized built-in loss).

(v) The determination of whether P and S constitute a SRLY subgroup for purposes of loss carryovers and carrybacks, and the extent to which built-in losses are not allowed under the SRLY limitation, is made under § 1.1502-21(c).

Example 4. Computation of SRLY limitation.

(i) Individual A owns all of the stock of P, the common parent of a consolidated group. During Year 1, Individual A forms T by contributing \$300, and T sustains a \$100 net operating loss. During Year 2, T's assets decline in value to \$100. At the beginning of Year 3, P acquires all the stock of T from Individual A, and T becomes a member of the P group with a net unrealized built-in loss of \$100. P's acquisition of T is not an ownership change as defined by section 382(g). Assume that \$100 exceeds the threshold requirements of section 382(h)(3)(B). During Year 3, T recognizes its unrealized built-in loss as a \$100 ordinary loss. The members of the P group contribute the following net income to the consolidated taxable income of the P group (disregarding T's recognized built-in loss and any consolidated net operating loss deduction under § 1.1502-21) for Years 3 and 4:

	Year 3	Year 4	Total
P group (without T)	\$100	\$100	\$200
T	60	40	100
CTI	160	140	300

(ii) Under paragraph (b) of this section, T's \$100 ordinary loss in Year 3 (not taken into account in the consolidated taxable income computations above) is a built-in loss. Under paragraph (a) of this section, the built-in loss is treated as a net operating loss carryover for purposes of determining the SRLY limitation under § 1.1502-21(c).

(iii) For Year 3, § 1.1502-21(c) limits T's \$100 built-in loss and \$100 net operating loss carryover from Year 1 to the aggregate of the P group's consolidated taxable income through Year 3, determined by reference to only T's items. For this purpose, consolidated taxable income is determined without regard to any consolidated net operating loss deductions under § 1.1502-21(a).

(iv) The P group's consolidated taxable income through Year 3 is \$60 when determined by reference to only T's items. Under §1.1502-21(c), the SRLY limitation for Year 3 is therefore \$60.

(v) Under paragraph (a) of this section, the \$100 built-in loss is treated as a current deduction for all purposes other than determination of the SRLY limitation under §1.1502-21(c). Consequently, a deduction for the built-in loss is allowed in Year 3 before T's loss carryover from Year 1 is allowed, but only to the extent of the \$60 SRLY limitation. None of T's Year 1 loss carryover is allowed because the built-in loss (\$100) exceeds the SRLY limitation for Year 3.

(vi) The \$40 balance of the built-in loss that is not allowed in Year 3 because of the SRLY limitation is treated as a \$40 net operating loss arising in Year 3 that is carried to other years in accordance with the rules of §1.1502-21(b). The \$40 net operating loss is treated under paragraph (a) of this section and §1.1502-21(c)(1)(ii) as a loss carryover or carryback from Year 3 that arises in a SRLY, and is subject to the rules of §1.1502-21 (including §1.1502-21(c)) rather than this section. See also §1.1502-21(c)(1)(iii) *Example 4*.

(vii) The facts are the same as in paragraphs (i) through (vi) of this *Example 4*, except that T has an additional built-in loss when it joins the P group which is recognized in Year 4. For purposes of determining the SRLY limitation for this additional loss in Year 4 (or any subsequent year), the \$60 of built-in loss allowed as a deduction in Year 3 is treated under paragraph (a) of this section as a deduction in Year 3 that reduces the P group's consolidated taxable income when determined by reference to only T's items.

Example 5. Built-in loss exceeding consolidated taxable income in the year recognized. (i) Individual A owns all of the stock of P and T. During Year 1, P acquires all the stock of T from Individual A, and T becomes a member of the P group. P's acquisition of T was not an ownership change as defined by section 382(g). At the time of acquisition, T has a noncapital asset with an unrealized loss of \$45 (basis \$100, value \$55), which exceeds the threshold requirements of section 382(h)(3)(B). During Year 2, T sells its asset for \$55 and recognizes the unrealized built-in loss. The P group has \$10 of consolidated taxable income in Year 2, computed by disregarding T's recognition of the \$45 built-in loss and the consolidated net operating loss deduction, while the consolidated taxable income would be \$25 if determined by reference to only T's items (other than the \$45 loss).

(ii) T's \$45 loss is recognized in Year 2 and, under paragraph (b) of this section, constitutes a built-in loss. Under paragraph (a) of this section and §1.1502-21(c)(1)(ii), the loss is treated as a net operating loss carryover

to Year 2 for purposes of applying the SRLY limitation under §1.1502-21(c).

(iii) For Year 2, T's SRLY limitation is the aggregate of the P group's consolidated taxable income through Year 2 determined by reference to only T's items. For this purpose, consolidated taxable income is determined by disregarding any built-in loss that is treated as a net operating loss carryover, and any consolidated net operating loss deductions under §1.1502-21(a). Consolidated taxable income so determined is \$25.

(iv) Under §1.1502-21(c), \$25 of the \$45 built-in loss could be deducted in Year 2. Because the P group has only \$10 of consolidated taxable income (determined without regard to the \$45), the \$25 loss creates a consolidated net operating loss of \$15. This loss is carried back or forward under the rules of §1.1502-21(b) and absorbed under the rules of §1.1502-21(a). This loss is not treated as arising in a SRLY (see §1.1502-21(c)(1)(ii)) and therefore is not subject to the SRLY limitation under §1.1502-21(c) in any consolidated return year of the group to which it is carried. The remaining \$20 is treated as a loss carryover arising in a SRLY and is subject to the limitation of §1.1502-21(c) in the year to which it is carried.

(e) *Predecessors and successors.* For purposes of this section, any reference to a corporation or member includes, as the context may require, a reference to a successor or predecessor, as defined in §1.1502-1(f)(4).

(f) *Built-in losses recognized by common parent of group—(1) General rule.* Paragraph (a) of this section does not apply to any loss recognized by the group on an asset held by the common parent on the date the group is formed. Following an acquisition described in §1.1502-75(d)(2) or (3), references to the common parent are to the corporation that was the common parent immediately before the acquisition.

(2) *Anti-avoidance rule.* If a corporation that becomes a common parent of a group acquires assets with a net unrealized built-in loss in excess of the threshold requirement of section 382(h)(3)(B) (and thereby increases its net unrealized built-in loss or decreases its net unrealized built-in gain) prior to, and in anticipation of, the formation of the group, paragraph (f)(1) of this section does not apply.

(g) *Overlap with section 382—(1) General rule.* The limitations provided in §§1.1502-21(c) and 1.1502-22(c) do not apply to recognized built-in losses or to

loss carryovers or carrybacks attributable to recognized built-in losses when the application of paragraph (a) of this section results in an overlap with the application of section 382.

(2) *Definitions*—(i) *Generally*. For purposes of this paragraph (g), the definitions and nomenclature contained in section 382, the regulations thereunder, and §§ 1.1502-90 through 1.1502-99 apply.

(ii) *Overlap*—(A) An overlap of the application of paragraph (a) of this section and the application of section 382 with respect to built-in losses occurs if a corporation becomes a member of a consolidated group (the SRLY event) within six months of the change date of an ownership change giving rise to a section 382(a) limitation that would apply with respect to the corporation's recognized built-in losses (the section 382 event). Except as provided in paragraph (g)(3) of this section, application of the overlap rule does not require that the size and composition of the corporation's net unrealized built-in loss is the same on the date of the section 382 event and the SRLY event.

(B) For special rules in the event that there is a SRLY subgroup and/or a loss subgroup as defined in § 1.1502-91(d)(2) with respect to built-in losses, see paragraph (g)(4) of this section.

(3) *Operating rules*—(i) *Section 382 event before SRLY event*. If a SRLY event occurs on the same date as a section 382 event or within the six month period beginning on the date of the section 382 event, paragraph (g)(1) of this section applies beginning with the tax year that includes the SRLY event. Paragraph (g)(1) of this section does not apply, however, if a corporation that would otherwise be subject to the overlap rule acquires assets from a person other than a member of the group with a net unrealized built-in loss in excess of the threshold requirement of section 382(h)(3)(B) (and thereby increases its net unrealized built-in loss) after the section 382 event, and before the SRLY event.

(ii) *SRLY event before section 382 event*. If a section 382 event occurs within the period beginning the day after the SRLY event and ending six months after the SRLY event, paragraph (g)(1) of this section applies starting with the first tax year that begins after the sec-

tion 382 event. However, paragraph (g)(1) of this section does not apply at any time if a corporation that otherwise would be subject to paragraph (g)(1) of this section transfers assets with an unrealized built-in loss to another member of the group after the SRLY event, but before the section 382 event, unless the corporation recognizes the built-in loss upon the transfer.

(4) *Subgroup rules*. In general, in the case of built-in losses for which there is a SRLY subgroup and the corporations joining the group at the time of the SRLY event also constitute a loss subgroup (as defined in § 1.1502-91(d)(2)), the principles of this paragraph (g) apply to the SRLY subgroup, and not separately to its members. However, paragraph (g)(1) of this section applies with respect to built-in losses only if—

(i) All members of the SRLY subgroup with respect to those built-in losses are also included in a loss subgroup (as defined in § 1.1502-91(d)(2)); and

(ii) All members of a loss subgroup (as defined in § 1.1502-91(d)(2)) are also members of a SRLY subgroup with respect to those built-in losses.

(5) *Asset acquisitions*. Notwithstanding the application of this paragraph (g), paragraph (a) of this section applies to asset acquisitions by the corporation that occurs after the latter of the SRLY event and the section 382 event. See, paragraph (b)(2)(ii) of this section.

(6) *Examples*. The principles of this paragraph (g) are illustrated by the following examples:

Example 1. Determination of subgroup. (i) Individual A owns all of the stock of P, P1, and S. In Year 1, P acquires all of the stock of P1, and they file a consolidated return. In Year 3, P acquires all of the stock of S, and S joins the P group. Individual B, unrelated to Individual A, owns all of the stock of M and K, each the common parent of a consolidated group. Individual C, unrelated to either Individual A or Individual B, owns all of the stock of T.

(ii) At the beginning of Year 7, M acquires all of the stock of P from Individual A, and, as a result, P, P1, and S become members of the M group. At the time of M's acquisition of the P stock, P has a \$15 net unrealized built-in loss (disregarding the stock of P1), P1 has a net unrealized built-in gain of \$10, and S has a net unrealized built-in gain of \$5.

(iii) During Year 8, M acquires all of the stock of T, and T joins the M group. At the time of M's acquisition of the T stock, T had an unrealized built-in loss of \$15. At the beginning of Year 9, K acquires all of the stock of M from Individual B, and the members of the M consolidated group including P, P1, S, and T become members of the K group. At the time of K's acquisition of the M stock, M has (disregarding the stock of P and T) a \$15 net unrealized built-in loss, P has a \$20 net unrealized built-in loss (disregarding the stock of P1), P1 has a net unrealized built-in gain of \$5, S has a net unrealized built-in loss of \$35, and T has a \$15 net unrealized built-in loss.

(iv) M's acquisition of P in Year 7 results in P, P1, and S becoming members of the M group (the SRLY event). Under paragraph (c) of this section, P and P1 compose a SRLY built-in loss subgroup because they have been affiliated for the 60 consecutive month period immediately preceding joining the M group. S is not a member of the subgroup because on becoming a member of the M group it had not been continuously affiliated with P and P1 for the 60 month period ending immediately before it became a member of the M group. Consequently, § 1.1502-15 applies to S separately from the P and P1 subgroup.

(v) Assuming that the \$5 net unrealized built-in loss of the P/P1 subgroup exceeds the threshold requirement under section 382(h)(3)(B), M's acquisition of P resulted in an ownership change of P and P1 within the meaning of section 382(g) that subjects P and P1 to a limitation under section 382(a) (the section 382 event). Because, with respect to P and P1, the SRLY event and the change date of the section 382 event occur on the same date and because the loss subgroup and SRLY subgroup are coextensive, there is an overlap of the application of the SRLY rules and the application of section 382.

(vi) S was not a loss corporation because it did not have a net operating loss carryover, or a net unrealized built-in loss, and therefore, M's acquisition of P did not result in an ownership change of S within the meaning of section 382(g). S, therefore, is not subject to the overlap rule of paragraph (g) of this section.

(vii) M's acquisition of T resulted in T becoming a member of the M group (the SRLY event). Assuming that T's \$15 net unrealized built-in loss exceeds the threshold requirement under section 382(h)(3)(B), M's acquisition of T also resulted in an ownership change of T within the meaning of section 382(g) that subjects T to a limitation under section 382(a) (the section 382 event). Because, with respect to T, the SRLY event and the change date of the section 382 event occur on the same date, there is an overlap of the application of the SRLY rules and the application of section 382 within the meaning of paragraph (g) of this section.

(viii) K's acquisition of M results in the members of the M consolidated group, including T, P, P1, and S, becoming members of the K group (the SRLY event). Because T, P, and P1 were each included in the determination of a net unrealized built-in loss that was subject to the overlap rule described in paragraph (g)(1) of this section when they each became members of the M group, they are deemed under paragraph (c)(3) of this section to have been continuously affiliated with M for the 60 month period ending immediately before becoming a member of the M group, notwithstanding their actual affiliation history. As a result, M, T, P, and P1 compose a SRLY built-in loss subgroup under paragraph (c)(2) of this section. K's acquisition of M is not subject to paragraph (g) of this section because it does not result in a section 382 event.

(ix) S, however, is not a member of the subgroup under paragraph (c)(2) of this section. Because S was not included in the determination of a net unrealized built-in loss that was subject to the overlap rule described in paragraph (g)(1) of this section when it joined the M group, S is treated as becoming an affiliate of M on the date it joined the M group. Furthermore, under paragraph (c)(3) of this section, S is deemed to have begun its affiliation with P and P1 on the date it joined the M group. Consequently, § 1.1502-15 applies to S separately to the extent its built-in loss is recognized within the recognition period.

Example 2. Post-overlap acquisition of assets.

(i) Individual A owns all of the stock of P, the common parent of a consolidated group. B, an individual unrelated to Individual A, owns all of the stock of T. T has two depreciable assets. Asset 1 has an unrealized built-in loss of \$25 (basis \$75, value \$50), and asset 2 has an unrealized built-in gain of \$20 (basis \$30, value \$50). During Year 3, P buys all of the stock of T from Individual B. On January 1, Year 4, P contributes \$80 cash and Individual A contributes asset 3, a depreciable asset, with a net unrealized built-in loss of \$45 (basis \$65, value \$20), in exchange for T stock in a transaction that is described in section 351.

(ii) P's acquisition of T results in T becoming a member of the P group (the SRLY event) and also results in an ownership change of T, within the meaning of section 382(g), that gives rise to a limitation under section 382(a) (the section 382 event).

(iii) Because the SRLY event and the change date of the section 382 event occur on the same date, there is an overlap of the application of the SRLY rules and the application of section 382. Consequently, under paragraph (g) of this section, the limitation under paragraph (a) of this section does not apply to T's net unrealized built-in loss when it joined the P group.

(iv) Individual A's Year 4 contribution of a depreciable asset occurred after T was a member of the P group. Assuming that the amount of the net unrealized built-in loss exceeds the threshold requirement of section 382(h)(3)(B), the sale of asset 3 within the recognition period is subject to the SRLY limitation of paragraphs (a) and (b)(2)(ii) of this section.

Example 3. Overlap rule. (i) Individual A owns all of the stock of P, the common parent of a consolidated group. B, an individual unrelated to Individual A, owns all of the stock of T. T has two depreciable assets. Asset 1 has an unrealized loss of \$55 (basis \$75, value \$20), and asset 2 has an unrealized gain of \$30 (basis \$30, value \$60). On February 28 of Year 2, P purchases 55% of T from Individual B. On June 30, of Year 2, P purchases an additional 35% of T from Individual B.

(ii) The February 28 purchase of 55% of T is a section 382 event because it results in an ownership change of T that gives rise to a section 382(a) limitation. The June 30 purchase of 35% of T results in T becoming a member of the P group and is therefore a SRLY event.

(iii) Because the SRLY event occurred within six months of the change date of the section 382 event, there is an overlap of the application of the SRLY rules and the application of section 382, and paragraph (a) of this section does not apply. Therefore, the SRLY limitation does not apply to any of the \$55 loss in asset 1 recognized by T after T joined the P group. See §1.1502-94 for rules relating to the application of section 382 with respect to T's \$25 unrealized built-in loss.

Example 4. Overlap rule-Fluctuation in value.

(i) The facts are the same as in *Example 3*, except that by June 30, of Year 2, asset 1 had declined in value by a further \$10. Thus asset 1 had an unrealized loss of \$65 (basis \$75, value \$10), and asset 2 had an unrealized gain of \$30 (basis \$30, value \$60).

(ii) Because paragraph (a) of this section does not apply, the further decrease in asset 1's value is disregarded. Consequently, the results are the same as in *Example 3*.

(h) *Effective date—(1) In general.* This section generally applies to built-in losses recognized in taxable years for which the due date (without extensions) of the consolidated return is after June 25, 1999. However—

(i) In the event that paragraphs (f)(1) and (g)(1) of this section do not apply to a particular built-in loss in the current group, then solely for purposes of applying paragraph (a) of this section to determine a limitation with respect to that built-in loss and with respect to which the SRLY register (consolidated

taxable income determined by reference to only the member's (or subgroup's) items of income, gain, deduction, or loss) began in a taxable year for which the due date of the return was on or before June 25, 1999, paragraph (c)(3) of this section shall not apply; and

(ii) For purposes of paragraph (g) of this section, only an ownership change to which section 382(a) as amended by the Tax Reform Act of 1986 applies shall constitute a section 382 event.

(2) *Prior periods.* For certain taxable years ending on or before June 25, 1999, see §1.1502-15T in effect prior to June 25, 1999, as contained in 26 CFR part 1 revised April 1, 1999, as applicable.

[T.D. 8823, 64 FR 36101, July 2, 1999; 64 FR 41784, Aug. 2, 1999, as amended by T.D. 9048, 68 FR 12290, Mar. 14, 2003; T.D. 9187, 70 FR 10326, Mar. 3, 2005; T.D. 9254, 71 FR 13018, Mar. 14, 2006; T.D. 9424, 73 FR 53986, Sept. 17, 2008]

§ 1.1502-16 Mine exploration expenditures.

(a) *Section 617—(1) In general.* If the aggregate amount of the expenditures to which section 617(a) applies, paid or incurred with respect to mines or deposits located outside the United States (as defined in section 638 and the regulations thereunder), does not exceed:

(i) \$400,000 minus

(ii) All amounts deducted or deferred during the taxable year and all preceding taxable years under section 617 or section 615 of the Internal Revenue Code of 1954 and section 23(ff) of the Internal Revenue Code of 1939 by corporations which are members of the group during the taxable year (and individuals or corporations which have transferred any mineral property to any such member within the meaning of section 617(g)(2)(B)) for taxable years ending after December 31, 1950 and prior to the taxable year, then the deduction under section 617 with respect to such foreign expenditures and paragraph (c) of §1.1502-12 for each member shall be no greater than an allocable portion of such amount hereinafter referred to as the "consolidated foreign exploration limitation." Such allocable portion shall be determined under subparagraph (2) of this paragraph. If the amount of such expenditures exceeds