

(iii) *Consequences with an election to disaffiliate.* If, on July 1, 1996, X makes an election under § 1.597-4(g) with respect to M, the following consequences are treated as occurring immediately before M was placed in Agency receivership. M must include \$1 million (\$5 million of liabilities—\$4 million of adjusted basis) in income as of May 1, 1996. Section 1.597-4(g) (2) and (3). M is then treated as a new corporation that is not a member of the X consolidated group and that has assets (including a \$1 million account receivable for future FFA) with a basis of \$5 million and \$5 million of liabilities received from disaffiliated corporation M in a section 351 transaction. New corporation M retains the TIN of disaffiliated corporation M. Section 1.597-4(g)(4). Immediately after the disaffiliation, new corporation M is treated as transferring its assets and deposit liabilities to Bridge Bank MB. New corporation M recognizes no gain or loss from the transfer and MB succeeds to M's TIN and taxable year. Section 1.597-4(d)(1). Bridge Bank MB is treated as a single entity that includes M and has \$5 million of liabilities, an account receivable for future FFA with a basis of \$1 million, and other assets with a basis of \$4 million. Section 1.597-4(d)(1).

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§ 1.597-5 Taxable Transfers.

(a) *Taxable Transfers—(1) Defined.* The term *Taxable Transfer* means—

(i) A transaction in which an entity transfers to a transferee other than a Bridge Bank—

(A) Any deposit liability (whether or not the Institution also transfers assets), if FFA is provided in connection with the transaction; or

(B) Any asset for which Agency or a Controlled Entity has any financial obligation (e.g., pursuant to a Loss Guarantee or Agency Obligation); or

(ii) A deemed transfer of assets described in paragraph (b) of this section.

(2) *Scope.* This section provides rules governing Taxable Transfers. Rules applicable to both actual and deemed asset acquisitions are provided in paragraphs (c) and (d) of this section. Special rules applicable only to deemed asset acquisitions are provided in paragraph (e) of this section.

(b) *Deemed asset acquisitions upon stock purchase—(1) In general.* In a

deemed transfer of assets under this paragraph (b), an Institution (including a Bridge Bank or a Residual Entity) or a Consolidated Subsidiary of the Institution (the Old Entity) is treated as selling all of its assets in a single transaction and is treated as a new corporation (the New Entity) that purchases all of the Old Entity's assets at the close of the day immediately preceding the occurrence of an event described in paragraph (b)(2) of this section. However, such an event results in a deemed transfer of assets under this paragraph (b) only if it occurs—

(i) In connection with a transaction in which FFA is provided;

(ii) While the Old Entity is a Bridge Bank;

(iii) While the Old Entity has a positive balance in a deferred FFA account (see § 1.597-2(c)(4)(v) regarding the optional accelerated recapture of deferred FFA); or

(iv) With respect to a Consolidated Subsidiary, while the Institution of which it is a Consolidated Subsidiary is under Agency Control.

(2) *Events.* A deemed transfer of assets under this paragraph (b) results if the Old Entity—

(i) Becomes a non-member within the meaning of § 1.1502-32(d)(4) of its consolidated group (other than pursuant to an election under § 1.597-4(g));

(ii) Becomes a member of an affiliated group of which it was not previously a member (other than pursuant to an election under § 1.597-4(g)); or

(iii) Issues stock such that the stock that was outstanding before the imposition of Agency Control or the occurrence of any transaction in connection with the provision of FFA represents 50 percent or less of the vote or value of its outstanding stock (disregarding stock described in section 1504(a)(4) and stock owned by Agency or a Controlled Entity).

(3) *Bridge Banks and Residual Entities.* If a Bridge Bank is treated as selling all of its assets to a New Entity under this paragraph (b), each associated Residual Entity is treated as simultaneously selling its assets to a New Entity in a Taxable Transfer described in this paragraph (b).

(c) *Treatment of transferor—(1) FFA in connection with a Taxable Transfer.* A

transferor in a Taxable Transfer is treated as having directly received immediately before a Taxable Transfer any Net Worth Assistance that Agency provides to the New Entity or Acquiring in connection with the transfer. (See §1.597-2 (a) and (c) for rules regarding the inclusion of FFA in income and §1.597-2(a)(1) for related rules regarding FFA provided to shareholders.) The Net Worth Assistance is treated as an asset of the transferor that is sold to the New Entity or Acquiring in the Taxable Transfer.

(2) *Amount realized in a Taxable Transfer.* In a Taxable Transfer described in paragraph (a)(1)(i) of this section, the amount realized is determined under section 1001(b) by reference to the consideration paid for the assets. In a Taxable Transfer described in paragraph (a)(1)(ii) of this section, the amount realized is the sum of the grossed-up basis of the stock acquired in connection with the Taxable Transfer (excluding stock acquired from the Old or New Entity), plus the amount of liabilities assumed or taken subject to in the deemed transfer, plus other relevant items. The grossed-up basis of the acquired stock equals the acquirors' basis in the acquired stock divided by the percentage of the Old Entity's stock (by value) attributable to the acquired stock.

(3) *Allocation of amount realized—(i) In general.* The amount realized under paragraph (c)(2) of this section is allocated among the assets transferred in the Taxable Transfer in the same manner as amounts are allocated among assets under §1.338-6(b), (c)(1) and (2).

(ii) *Modifications to general rule.* This paragraph (c)(3)(ii) modifies certain of the allocation rules of paragraph (c)(3)(i) of this section. Agency Obligations and assets covered by Loss Guarantees in the hands of the New Entity or Acquiring are treated as Class II assets. Stock of a Consolidated Subsidiary is treated as a Class II asset to the extent the fair market value of the Consolidated Subsidiary's Class I and Class II assets exceeds the amount of its liabilities. The fair market value of an Agency Obligation is deemed to equal its adjusted issue price immediately before the Taxable Transfer. The fair market value of an asset cov-

ered by a Loss Guarantee immediately after the Taxable Transfer is deemed to be not less than the greater of the asset's highest guaranteed value or the highest price at which the asset can be put.

(d) *Treatment of a New Entity and Acquiring—(1) Purchase price.* The purchase price for assets acquired in a Taxable Transfer described in paragraph (a)(1)(i) of this section is the cost of the assets acquired. See §1.1060-1T(c)(1). The purchase price for assets acquired in a Taxable Transfer described in paragraph (a)(1)(ii) of this section is the sum of the grossed-up basis of the stock acquired in connection with the Taxable Transfer (excluding stock acquired from the Old or New Entity), plus the amount of liabilities assumed or taken subject to in the deemed transfer, plus other relevant items. The grossed-up basis of the acquired stock equals the acquirors' basis in the acquired stock divided by the percentage of the Old Entity's stock (by value) attributable to the acquired stock. FFA provided in connection with a Taxable Transfer is not included in the New Entity's or Acquiring's purchase price for the acquired assets. Any Net Worth Assistance so provided is treated as an asset of the transferor sold to the New Entity or Acquiring in the Taxable Transfer.

(2) *Allocation of basis—(i) In general.* Except as otherwise provided in this paragraph (d)(2), the purchase price determined under paragraph (d)(1) of this section is allocated among the assets transferred in the Taxable Transfer in the same manner as amounts are allocated among assets under §1.338-6(b), (c)(1) and (2).

(ii) *Modifications to general rule.* The allocation rules contained in paragraph (c)(3)(ii) of this section apply to the allocation of basis among assets acquired in a Taxable Transfer. No basis is allocable to Agency's agreement to provide Loss Guarantees, yield maintenance payments, cost to carry or cost of funds reimbursement payments, or expense reimbursement or indemnity payments. A New Entity's basis in assets it receives from its shareholders is determined under general principles of income taxation and is not governed by this paragraph (d).

(iii) *Allowance and recapture of additional basis in certain cases.* If the fair market value of the Class I and Class II assets acquired in a Taxable Transfer is greater than the New Entity's or Acquiring's purchase price for the acquired assets, the basis of the Class I and Class II assets equals their fair market value. The amount by which the fair market value of the Class I and Class II assets exceeds the purchase price is included ratably as ordinary income by the New Entity or Acquiring over a period of six taxable years beginning in the year of the Taxable Transfer. The New Entity or Acquiring must include as ordinary income the entire amount remaining to be recaptured under the preceding sentence in the taxable year in which an event occurs that would accelerate inclusion of an adjustment under section 481.

(iv) *Certain post-transfer adjustments—*
 (A) *Agency Obligations.* If an adjustment to the principal amount of an Agency Obligation or cash payment to reflect a more accurate determination of the condition of the Institution at the time of the Taxable Transfer is made before the earlier of the date the New Entity or Acquiring files its first post-transfer income tax return or the due date of that return (including extensions), the New Entity or Acquiring must adjust its basis in its acquired assets to reflect the adjustment. In making adjustments to the New Entity's or Acquiring's basis in its acquired assets, paragraph (c)(3)(ii) of this section is applied by treating an adjustment to the principal amount of an Agency Obligation pursuant to the first sentence of this paragraph (d)(2)(iv)(A) as occurring immediately before the Taxable Transfer. (See § 1.597-3(c)(3) for rules regarding other adjustments to the principal amount of an Agency Obligation.)

(B) *Assets covered by a Loss Guarantee.* If, immediately after a Taxable Transfer, an asset is not covered by a Loss Guarantee but the New Entity or Acquiring has the right to designate specific assets that will be covered by a Loss Guarantee, the New Entity or Acquiring must treat any asset so designated as having been subject to the Loss Guarantee at the time of the Taxable Transfer. The New Entity or Acquiring must adjust its basis in the

covered assets and in its other acquired assets to reflect the designation in the manner provided by paragraph (d)(2) of this section. The New Entity or Acquiring must make appropriate adjustments in subsequent taxable years if the designation is made after the New Entity or Acquiring files its first post-transfer income tax return or the due date of that return (including extensions) has passed.

(e) *Special rules applicable to Taxable Transfers that are deemed asset acquisitions—*(1) *Taxpayer identification numbers.* Except as provided in paragraph (e)(3) of this section, a New Entity succeeds to the TIN of the transferor in a deemed sale under paragraph (b) of this section.

(2) *Consolidated Subsidiaries—*(i) *In general.* A Consolidated Subsidiary that is treated as selling its assets in a Taxable Transfer under paragraph (b) of this section is treated as engaging immediately thereafter in a complete liquidation to which section 332 applies. The consolidated group of which the Consolidated Subsidiary is a member does not take into account gain or loss on the sale, exchange, or cancellation of stock of the Consolidated Subsidiary in connection with the Taxable Transfer.

(ii) *Certain minority shareholders.* Shareholders of the Consolidated Subsidiary that are not members of the consolidated group that includes the Institution do not recognize gain or loss with respect to shares of Consolidated Subsidiary stock retained by the shareholder. The shareholder's basis for that stock is not affected by the Taxable Transfer.

(3) *Bridge Banks and Residual Entities—*(i) *In general.* A Bridge Bank or Residual Entity's sale of assets to a New Entity under paragraph (b) of this section is treated as made by a single entity under § 1.597-4(e). The New Entity deemed to acquire the assets of a Residual Entity under paragraph (b) of this section is not treated as a single entity with the Bridge Bank (or with the New Entity acquiring the Bridge Bank's assets) and must obtain a new TIN.

(ii) *Treatment of consolidated groups.* At the time of a Taxable Transfer described in paragraph (a)(1)(ii) of this

section, treatment of a Bridge Bank as a subsidiary member of a consolidated group under §1.597-4(f)(1) ceases. However, the New Entity deemed to acquire the assets of a Residual Entity is a member of the selling consolidated group after the deemed sale. The group's basis or excess loss account in the stock of the New Entity that is deemed to acquire the assets of the Residual Entity is the group's basis or excess loss account in the stock of the Bridge Bank immediately before the deemed sale, as adjusted for the results of the sale.

(4) *Certain returns.* If an Old Entity without Continuing Equity is not a subsidiary of a consolidated group at the time of the Taxable Transfer, the controlling Agency must file all income tax returns for the Old Entity for periods ending on or prior to the date of the deemed sale described in paragraph (b) of this section that are not filed as of that date.

(5) *Basis limited to fair market value.* If all of the stock of the corporation is not acquired on the date of the Taxable Transfer, the Commissioner may make appropriate adjustments under paragraphs (c) and (d) of this section to the extent using a grossed-up basis of the stock of a corporation results in an aggregate amount realized for, or basis in, the assets other than the aggregate fair market value of the assets.

(f) *Examples.* The following examples illustrate the provisions of this section:

Example 1. Branch sale resulting in Taxable Transfer. (i) Institution M is a calendar year taxpayer in Agency receivership. M is not a member of a consolidated group. On January 1, 1997, M has \$200 million of liabilities (including deposit liabilities) and assets with an adjusted basis of \$100 million. M has no income or loss for 1997 and, except as described below, receives no FFA. On September 30, 1997, Agency causes M to transfer six branches (with assets having an adjusted basis of \$1 million) together with \$120 million of deposit liabilities to N. In connection with the transfer, Agency provides \$121 million in cash to N.

(ii) The transaction is a Taxable Transfer in which M receives \$121 million of Net Worth Assistance. Section 1.597-5(a)(1). (M is treated as directly receiving the \$121 million of Net Worth Assistance immediately before the Taxable Transfer. Section 1.597-5(c)(1).) M transfers branches having a basis of \$1

million and is treated as transferring \$121 million in cash (the Net Worth Assistance) to N in exchange for N's assumption of \$120 million of liabilities. Thus, M realizes a loss of \$2 million on the transfer. The amount of the FFA M must include in its income in 1997 is limited by §1.597-2(c) to \$102 million, which is the sum of the \$100 million excess of M's liabilities (\$200 million) over the total adjusted basis of its assets (\$100 million) at the beginning of 1997, plus the \$2 million excess for the taxable year, which results from the Taxable Transfer, of M's deductions (other than carryovers) over its gross income other than FFA. M must establish a deferred FFA account for the remaining \$19 million of FFA. Section 1.597-2(c)(4).

(iii) N, as Acquiring, must allocate its \$120 million purchase price for the assets acquired from M among those assets. Cash is a Class I asset. The branch assets are in Classes III and IV. N's adjusted basis in the cash is its amount, i.e., \$121 million. Section 1.597-5(d)(2). Because this amount exceeds N's purchase price for all of the acquired assets by \$1 million, N allocates no basis to the other acquired assets and, under §1.597-5(d)(2), must recapture the \$1 million excess at an annual rate of \$166,667 in the six consecutive taxable years beginning with 1997 (subject to acceleration for certain events).

Example 2. Stock issuance by Bridge Bank causing Taxable Transfer. (i) On April 1, 1996, Institution P is placed in receivership and caused to transfer assets and liabilities to Bridge Bank PB. On August 31, 1996, the assets of PB consist of \$20 million in cash, loans outstanding with an adjusted basis of \$50 million and a fair market value of \$40 million, and other non-financial assets (primarily branch assets and equipment) with an adjusted basis of \$5 million. PB has deposit liabilities of \$95 million and other liabilities of \$5 million. P, the Residual Entity, holds real estate with an adjusted basis of \$10 million and claims in litigation having a zero basis. P retains no deposit liabilities and has no other liabilities (except its liability to Agency for having caused its deposit liabilities to be satisfied).

(ii) On September 1, 1996, Agency causes PB to issue 100 percent of its common stock for \$2 million cash to X. On the same day, Agency issues a \$25 million note to PB. The note bears a fixed rate of interest in excess of the applicable federal rate in effect for September 1, 1996. Agency provides Loss Guarantees guaranteeing PB a value of \$50 million for PB's loans outstanding.

(iii) The stock issuance is a Taxable Transfer in which PB is treated as selling all of its assets to a new corporation, New PB. Section 1.597-5(b)(1). PB is treated as directly receiving \$25 million of Net Worth Assistance (the issue price of the Agency Obligation) immediately before the Taxable Transfer. Section 1.597-3(c)(2); §1.597-5(c)(1). The amount of

FFA PB must include in income is determined under § 1.597-2(a) and (c). PB in turn is deemed to transfer the note to New PB in the Taxable Transfer, together with \$20 million of cash, all its loans outstanding (with a basis of \$50 million) and its other non-financial assets (with a basis of \$5 million). The amount realized by PB from the sale is \$100 million, the amount of PB's liabilities deemed to be assumed by New PB. This amount realized equals PB's basis in its assets and thus, PB realizes no gain or loss on the transfer to New PB.

(iv) Residual Entity P also is treated as selling all its assets (consisting of real estate and claims in litigation) for \$0 (the amount of consideration received by P) to a new corporation (New P) in a Taxable Transfer. Section 1.597-5(b)(3). (P's only liability is to Agency and a liability to Agency is not treated as a debt under § 1.597-3(b).) Thus, P realizes a \$10 million loss on the transfer to New P. The combined return filed by PB and P for 1996 will reflect a total loss on the Taxable Transfer of \$10 million (\$0 for PB and \$10 million for P). Section 1.597-5(e)(3). That return also will reflect FFA income from the Net Worth Assistance, determined under § 1.597-2 (a) and (c).

(v) New PB is treated as having acquired the assets it acquired from PB for \$100 million, the amount of liabilities assumed. In allocating basis among these assets, New PB treats the Agency note and the loans outstanding (which are covered by Loss Guarantees) as Class II assets. For the purpose of allocating basis, the fair market value of the Agency note is deemed to equal its adjusted issue price immediately before the transfer, \$25 million. The fair market value of the loans is deemed not to be less than the guaranteed value of \$50 million.

(vi) New P is treated as having acquired its assets for no consideration. Thus its basis in its assets immediately after the transfer is zero. New PB and New P are not treated as a single entity. Section 1.597-5(e)(3).

Example 3. Taxable Transfer of previously disaffiliated Institution. (i) Corporation X, the common parent of a consolidated group, owns all the stock of Institution M, an insolvent Institution with no Consolidated Subsidiaries. On April 30, 1996, M has \$4 million of deposit liabilities, \$1 million of other liabilities, and assets with an adjusted basis of \$4 million and a fair market value of \$3 million. On May 1, 1996, Agency places M in receivership. X elects under § 1.597-4(g) to disaffiliate M. Accordingly, as of May 1, 1996, new corporation M is not a member of the X consolidated group. On May 1, 1996, Agency causes M to transfer all of its assets and liabilities to Bridge Bank MB. Under § 1.597-4(e), MB and M are thereafter treated as a single entity which has \$5 million of liabilities, an account receivable for future FFA with a basis of \$1 million, and other assets

with a basis of \$4 million. Section 1.597-4(g)(4).

(ii) During May 1996, MB earns \$25,000 of interest income and accrues \$20,000 of interest expense on depositor accounts and there is no net change in deposits other than the additional \$20,000 of interest expense accrued on depositor accounts. MB pays \$5,000 of wage expenses and has no other items of income or expense.

(iii) On June 1, 1996, Agency causes MB to issue 100 percent of its stock to corporation Y. In connection with the stock issuance, Agency provides an Agency Obligation for \$2 million and no other FFA.

(iv) The stock issuance results in a Taxable Transfer. Section 1.597-5(b). MB is treated as receiving the Agency Obligation immediately prior to the Taxable Transfer. Section 1.597-5(c)(1). MB has \$1 million of basis in its account receivable for FFA. This receivable is treated as satisfied, offsetting \$1 million of the \$2 million of FFA provided by Agency in connection with the Taxable Transfer. The status of the remaining \$1 million of FFA as includible income is determined as of the end of the taxable year under § 1.597-2(c). However, under § 1.597-2(b), MB obtains a \$2 million basis in the Agency Obligation received as FFA.

(v) Under § 1.597-5(c)(2), in the Taxable Transfer, Old Entity MB is treated as selling, to New Entity MB, all of Old Entity MB's assets, having a basis of \$6,020,000 (the original \$4 million of asset basis as of April 30, 1996, plus \$20,000 net cash from May 1996 activities, plus \$2 million in the Agency Obligation received as FFA), for \$5,020,000, the amount of Old Entity MB's liabilities assumed by New Entity MB pursuant to the Taxable Transfer. Therefore, Old Entity MB recognizes, in the aggregate, a loss of \$1 million from the Taxable Transfer.

(vi) Because this \$1 million loss causes Old Entity MB's deductions to exceed its gross income (determined without regard to FFA) by \$1 million, Old Entity MB must include in its income the \$1 million of FFA not offset by the FFA receivable. Section 1.597-2(c). (As of May 1, 1996, Old Entity MB's liabilities (\$5,000,000) did not exceed MB's \$5 million adjusted basis of its assets. For the taxable year, MB's deductions of \$1,025,000 (\$1,000,000 loss from the Taxable Transfer, \$20,000 interest expense and \$5,000 of wage expense) exceeded its gross income (disregarding FFA) of \$25,000 (interest income) by \$1,000,000. Thus, under § 1.597-2(c), MB includes in income the entire \$1,000,000 of FFA not offset by the FFA receivable.)

(vii) Therefore, Old Entity MB's taxable income for the taxable year ending on the date of the Taxable Transfer is \$0.

(viii) Residual Entity M is also deemed to engage in a deemed sale of its assets to New Entity M under § 1.597-5(b)(3), but there are

no tax consequences as M has no assets or liabilities at the time of the deemed sale.

(ix) Under § 1.597-5(d)(1), New Entity MB is treated as purchasing Old Entity MB's assets for \$5,020,000, the amount of New Entity MB's liabilities. Of this, \$2,000,000 is allocated to the \$2 million Agency Obligation, and \$3,020,000 is allocated to the other assets New Entity MB is treated as purchasing in the Taxable Transfer.

Example 4. Loss Sharing. Institution N acquires assets and assumes liabilities of another Institution in a Taxable Transfer. Among the assets transferred are three parcels of real estate. In the hands of the transferring Institution, these assets had book values of \$100,000 each. In connection with the Taxable Transfer, Agency agrees to reimburse Institution N for 80 percent of any loss (based on the original book value) realized on the disposition or charge-off of the three properties. This arrangement constitutes a Loss Guarantee. Thus, in allocating basis, Institution N treats the three parcels as Class II assets. By virtue of the arrangement with the Agency, Institution N is assured that the parcels will not be worth less to it than \$80,000 each, because even if the properties are worthless, Agency will reimburse 80 percent of the loss. Although Institution could obtain payments under the Loss Guarantee if the properties are worth more, it is not guaranteed that it will realize more than \$80,000. Accordingly, \$80,000 is the highest guaranteed value of the three parcels. Institution N will allocate basis to the Class II assets up to their fair market value. For this purpose, the fair market value of the three parcels is not less than \$80,000 each. Section 1.597-5(d)(2)(ii); § 1.597-5(c)(3)(ii).

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§ 1.597-6 Limitation on collection of income tax.

(a) *Limitation on collection where tax is borne by Agency.* If an Institution without Continuing Equity (or any of its Consolidated Subsidiaries) is liable for income tax that is attributable to the inclusion in income of FFA or gain from a Taxable Transfer, the tax will not be collected if it would be borne by Agency. The final determination of whether the tax would be borne by Agency is within the sole discretion of the Commissioner. In determining whether tax would be borne by Agency, the Commissioner will disregard indemnity, tax-sharing, or similar obligations of Agency, an Institution, or its Consolidated Subsidiaries. Collection of the several income tax liability

under § 1.1502-6 from members of an Institution's consolidated group other than the Institution or its Consolidated Subsidiaries is not affected by this section. Income tax will continue to be subject to collection except as specifically limited in this section. This section does not apply to taxes other than income taxes.

(b) *Amount of tax attributable to FFA or gain on a Taxable Transfer.* For purposes of paragraph (a) of this section, the amount of income tax in a taxable year attributable to the inclusion of FFA or gain from a Taxable Transfer in the income of an Institution (or a Consolidated Subsidiary) is the excess of the actual income tax liability of the Institution (or the consolidated group in which the Institution is a member) over the income tax liability of the Institution (or the consolidated group in which the Institution is a member) determined without regard to FFA or gain or loss on the Taxable Transfer.

(c) *Reporting of uncollected tax.* A taxpayer must specify on the front page of Form 1120 (U.S. Corporate Income Tax Return), to the left of the space provided for "Total Tax," the amount of income tax for the taxable year that is potentially not subject to collection under this section. If an Institution is a subsidiary member of a consolidated group, the amount specified as not subject to collection is zero.

(d) *Assessments of tax to offset refunds.* Income tax that is not collected under this section will be assessed and, thus, used to offset any claim for refund made by or on behalf of the Institution, the Consolidated Subsidiary or any other corporation with several liability for the tax.

(e) *Collection of taxes from Acquiring or a New Entity—(1) Acquiring.* No income tax liability (including the several liability for taxes under § 1.1502-6) of a transferor in a Taxable Transfer will be collected from Acquiring.

(2) *New Entity.* Income tax liability (including the several liability for taxes under § 1.1502-6) of a transferor in a Taxable Transfer will be collected from a New Entity only if stock that was outstanding in the Old Entity remains outstanding as stock in the New