

Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC 20224 (Attention: CC:DOM:CORP:5) or telephone 202-622-7550 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

##### Paperwork Reduction Act

The collection of information contained in these final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3504(h)) under control number 1545-1345. The estimated annual burden per respondent varies from 0.05 to 0.2 hours depending on individual circumstances, with an estimated average of 0.1 hour.

These estimates are approximations of the average time expected to be necessary for a collection of information. They are based on such information as is available to the Internal Revenue Service. Individual respondents may require more or less time, depending on their particular circumstances.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be directed to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, TFP, Washington, DC 20224, and to the Office of Management and Budget, Attention: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

##### Background

This document contains final and temporary regulations to be added to the Income Tax Regulations (26 CFR part 1) under section 382 of the Internal Revenue Code. The final regulations provide exceptions to the rules of the temporary regulations that require the segregation of public groups after issuances of stock. Proposed regulations on this subject were set forth in a notice of proposed rulemaking published in the Federal Register on November 5, 1992 (57 FR 52738). The IRS received public comments on the proposed regulations and held a public hearing on February 2, 1993. Having considered the comments and the statements made at the hearing, the IRS and the Treasury Department adopt the proposed regulations as revised by this Treasury decision.

##### Explanation of Provisions

The final regulations adopt the exceptions to the segregation rules provided in the proposed regulations,

with the clarifications and revisions described below.

##### A. Application of Cash Issuance Exception to Issuances for Both Cash and Noncash Consideration

The proposed regulations would have excepted from the segregation rules a portion of stock issued by a loss corporation "for cash." The proposed regulations would have provided that two or more related issuances are treated as a single issuance.

Commentators requested clarification of whether the cash issuance exception applies when a loss corporation issues stock for cash and, either in the same issuance or in a separate but related issuance, also issues stock for consideration other than cash.

The final regulations clarify that the cash issuance exception applies if a loss corporation issues stock solely for cash. A share of stock is not issued solely for cash, if, as a condition of acquiring that share for cash, the acquirer is required to purchase other stock for consideration other than cash.

##### B. Stock Issued Upon the Exercise of Rights Distributed Pro Rata to Existing Shareholders

The proposed regulations would have required a loss corporation to take into account subsequent transfers of any option issued on or after November 4, 1992 (including transfers described in § 1.382-2T(h)(4)(xi)), in applying the actual knowledge exception to the segregation rules on the exercise of the options. It was intended that operation of the segregation rules on the exercise (or deemed exercise) of transferable options issued pro rata to shareholders be the same as the operation of the rules on a stock offering.

To fully effectuate this intent, the final regulations provide that, if transferable options are issued to more than one public group, § 1.382-2T(h)(2)(iii)(F) does not apply to treat options as exercised pro rata by each public group that acquired the options.

##### C. Effective Date

As proposed, the regulations would have applied to issuances of stock in taxable years ending on or after November 4, 1992, the date on which the IRS filed the proposed regulations with the Federal Register. Taxpayers would have been allowed to elect to apply the rules of the proposed regulations to prior taxable years.

Commentators questioned the mandatory application of the proposed regulations to stock issuances occurring prior to the filing of the proposed regulations. The IRS and the Treasury

Department agree that the regulations should not mandatorily apply to a transaction that occurred before the taxpayer had notice of the proposed regulations. Therefore, the final regulations generally apply to issuances of stock in taxable years beginning on or after November 4, 1992. Taxpayers may elect, however, to apply the rules of the final regulations to issuances of stock occurring in taxable years beginning prior to November 4, 1992.

The final regulations also contain a special effective date for the rule relating to stock issued on the exercise of certain options described in B. of this preamble. This rule generally applies to stock issued on the exercise of options issued on or after November 4, 1992, unless the option was issued under a transitional rule previously published in Notice 92-54, 1992-2 C.B. 384.

##### D. Application of the Regulations to Farm Credit System Institutions

A commentator suggested that the regulations should contain a provision exempting Farm Credit System institutions from the application of the segregation rules. Exemption of FCS institutions from the application of the segregation rules is beyond the scope of these regulations. The Service and the Treasury Department are studying the application of the segregation rules to FCS institutions.

##### Special Analyses

It has been determined that these regulations are not major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

##### Drafting Information

The principal author of these regulations is Roberta F. Mann, Office of the Assistant Chief Counsel (Corporate), Internal Revenue Service. However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 \* \* \* Section 1.382-3 also issued under 26 U.S.C. 382(m).

Par. 2. Section 1.382-1 is amended by revising the entries for § 1.382-3 (b) through (j), to read as follows:

§ 1.382-1 Table of contents.

§ 1.382-3 Definitions and rules relating to a 5-percent shareholder.

(b) through (i) [Reserved]

(j) Modification of the segregation rules of § 1.382-2T(j)(2)(iii) in the case of certain issuances of stock.

(1) Introduction.

(2) Small issuance exception.

(i) In general.

(ii) Small issuance defined.

(iii) Small issuance limitation.

(A) In general.

(B) Class of stock defined.

(C) Adjustments for stock splits and similar transactions.

(D) Exception.

(iv) Short taxable years.

(3) Other issuances of stock for cash.

(i) In general.

(ii) Solely for cash.

(A) In general.

(B) Related issuances.

(iii) Coordination with paragraph (j)(c) of this section.

(4) Limitation on exempted stock.

(5) Proportionate acquisition of exempted stock.

(i) In general.

(ii) Actual knowledge of greater overlapping ownership.

(6) Exception for equity structure shifts.

(7) Transitory ownership by underwriter disregarded.

(8) Certain related issuances.

(9) Application to options.

(10) Issuance of stock pursuant to the exercise of certain options.

(11) Application to first tier and higher tier entities.

(12) Certain non-stock ownership interests.

(13) Examples.

(14) Effective date.

(i) In general.

(ii) Effective date for paragraph (j)(10) of this section.

(iii) Election to apply this paragraph (j) retroactively.

(A) Election.

(B) Amended returns.

(C) Revised information statements.

Par. 3. Section 1.382-2T is amended by:

1. Adding a sentence to the end of the concluding text of paragraph (j)(2)(iii)(B)(1).

2. Adding a sentence to the end of paragraph (j)(2)(iii)(D)(1).

3. Adding a sentence to the end of paragraph (j)(2)(iii)(F)(1).

4. The additions read as follows:

§ 1.382-2T Determination of ownership change under section 382, as amended by the Tax Reform Act of 1986 (temporary).

(j) \* \* \*

(2) \* \* \*

(iii) \* \* \*

(B) \* \* \* (1) \* \* \*

\* \* \* See § 1.382-3(j) for exceptions to the segregation rules of this paragraph (j)(2)(iii)(B)(1).

(D) \* \* \* (1) \* \* \* See § 1.382-3(j)(9) for rules relating to this paragraph (j)(2)(iii)(D).

(F) \* \* \* (1) \* \* \* See § 1.382-

3(j)(10) for an exception to the application of the rule of this paragraph (j)(2)(iii)(F)(1) to stock issued on the exercise of a transferable option.

Par. 4. In § 1.382-3, paragraph (j) is added to read as follows:

§ 1.382-3 Definitions and rules relating to a 5-percent shareholder.

(j) Modification of the segregation rules of § 1.382-2T(j)(2)(iii) in the case of certain issuances of stock—(1)

Introduction. This paragraph (j) exempts, in whole or in part, certain issuances of stock by a loss corporation from the segregation rules of § 1.382-2T(j)(2)(iii)(B). Terms and nomenclature used in this paragraph (j), and not otherwise defined herein, have the same meanings as in section 382 and the regulations thereunder.

(2) Small issuance exception—(i) In general. Section 1.382-2T(j)(2)(iii)(B) does not apply to a small issuance (as defined in paragraph (j)(2)(ii) of this section), except to the extent that the total amount of stock issued in that issuance and all other small issuances previously made in the same taxable year (determined in each case on issuance) exceeds the small issuance

limitation. This paragraph (j)(2) does not apply to an issuance of stock that, by itself, exceeds the small issuance limitation.

(ii) Small issuance defined. Small issuance means an issuance (other than an issuance described in paragraph (j)(6) of this section) by the loss corporation of an amount of stock not exceeding the small issuance limitation. For purposes of this paragraph (j)(2)(ii), all stock issued in the issuance is taken into account, including stock owned immediately after the issuance by a 5-percent shareholder that is not a direct public group.

(iii) Small issuance limitation—(A) In general. For each taxable year, the loss corporation may, at its option, apply this paragraph (j)(2)—

(1) On a corporation-wide basis, in which case the small issuance limitation is 10 percent of the total value of the loss corporation's stock outstanding at the beginning of the taxable year (excluding the value of stock described in section 1504(a)(4)); or

(2) On a class-by-class basis, in which case the small issuance limitation is 10 percent of the number of shares of the class outstanding at the beginning of the taxable year.

(B) Class of stock defined. For purposes of this paragraph (j)(2)(iii), a class of stock includes all stock with the same material terms.

(C) Adjustments for stock splits and similar transactions. Appropriate adjustments to the number of shares of a class outstanding at the beginning of a taxable year must be made to take into account any stock split, reverse stock split, stock dividend to which section 305(a) applies, recapitalization, or similar transaction occurring during the taxable year.

(D) Exception. The loss corporation may not apply this paragraph (j)(2)(iii) on a class-by-class basis if, during the taxable year, more than one class of stock is issued in a single issuance (or in two or more issuances that are treated as a single issuance under paragraph (j)(8)(ii) of this section).

(iv) Short taxable years. In the case of a taxable year that is less than 365 days, the small issuance limitation is reduced by multiplying it by a fraction, the numerator of which is the number of days in the taxable year, and the denominator of which is 365.

(3) Other issuances of stock for cash—

(i) In general. If the loss corporation issues stock solely for cash, § 1.382-2T(j)(2)(iii)(B) does not apply to such stock in an amount equal (as a percentage of the total stock issued) to one-half of the aggregate percentage

ownership interest of direct public groups immediately before the issuance.

(ii) *Solely for cash*—(A) *In general.* A share of stock is not issued solely for cash if—

(1) The acquirer, as a condition of acquiring that share for cash, is required to purchase other stock for consideration other than cash; or

(2) The share is acquired upon the exercise of an option that was not issued solely for cash or was not distributed with respect to stock.

(B) *Related issuances.* Paragraph (j)(8)(i) of this section (relating to the treatment of one or more issuances as a single issuance) does not apply in determining whether stock is issued solely for cash.

(iii) *Coordination with paragraph (j)(2) of this section.* This paragraph (j)(3) does not apply to a small issuance exempted in whole from § 1.382-2T(j)(2)(iii)(B) under paragraph (j)(2) of this section. In the case of a small

issuance exempted in part from § 1.382-2T(j)(2)(iii)(E) under paragraph (j)(2) of this section, this paragraph (j)(3) applies only to the portion of the issuance not so exempted, and that portion is treated as a separate issuance for purposes of this paragraph (j)(3).

(4) *Limitation on exempted stock.* The total amount of stock that is exempted from the application of § 1.382-2T(j)(2)(iii)(B) under paragraphs (j)(2) and (j)(3) of this section cannot exceed the total amount of stock issued in the issuance less the amount of that stock owned by a 5-percent shareholder (other than a direct public group) immediately after the issuance. Except to the extent that the loss corporation has actual knowledge to the contrary, any increase in the amount of the loss corporation's stock owned by a 5-percent shareholder on the day of the issuance is considered to be attributable to an acquisition of stock in the issuance.

(5) *Proportionate acquisition of exempted stock*—(i) *In general.* Each direct public group that exists immediately before an issuance to which paragraph (j)(2) or (j)(3) of this section applies is treated as acquiring its proportionate share of the amount of stock exempted from the application of § 1.382-2T(j)(2)(iii)(B) under paragraph (j)(2) or (j)(3) of this section.

(ii) *Actual knowledge of greater overlapping ownership.* Under the last sentence of § 1.382-2T(k)(2), the loss corporation may treat direct public groups existing immediately before an issuance to which paragraph (j)(2) or (j)(3) of this section applies as acquiring in the aggregate more stock than the amount determined under paragraph (j)(5)(i) of this section, but only if the

loss corporation actually knows that the aggregate amount acquired by those groups in the issuance exceeds the amount so determined.

(6) *Exception for equity structure shifts.* This paragraph (j) does not apply to any issuance of stock in an equity structure shift, except that paragraph (j)(2) of this section applies (if its requirements are met) to the issuance of stock in a recapitalization under section 368(e)(1)(E).

(7) *Transitory ownership by underwriter disregarded.* For purposes of § 1.382-2T(g)(1) and (j), and this paragraph (j), the transitory ownership of stock by an underwriter of the issuance is disregarded.

(8) *Certain related issuances.* For purposes of this paragraph (j), two or more issuances (including issuances of stock by first tier or higher tier entities) are treated as a single issuance if—

(i) The issuances occur at approximately the same time pursuant to the same plan or arrangement; or

(ii) A principal purpose of issuing the stock in separate issuances rather than in a single issuance is to minimize or avoid an owner shift under the rules of this paragraph (j).

(9) *Application to options.* The principles of this paragraph (j) apply for purposes of applying § 1.382-2T(j)(2)(iii)(D) (relating to the deemed acquisition of stock as a result of the ownership of an option).

(10) *Issuance of stock pursuant to the exercise of certain options.* If stock is issued on the exercise of a transferable option issued by the loss corporation, § 1.382-2T(j)(2)(iii)(F) does not apply and, in applying the last sentence of § 1.382-2T(i)(2), the loss corporation must take into account any transfers of the option (including transfers described in § 1.382-2T(h)(4)(xi)). Therefore, even if transferable options are distributed pro rata to members of existing public groups, the actual knowledge exception of § 1.382-2T(k)(2) applies only to the extent that the loss corporation actually knows that the persons acquiring stock on exercise of the options are members of a pre-existing public group. Moreover, if transferable options are issued to more than one public group, § 1.382-2T(j)(2)(iii)(F) does not apply to treat the options as exercised pro rata by each such public group as the options are actually exercised.

(11) *Application to first tier and higher tier entities.* The principles of this paragraph (j) apply to issuances of stock by a first tier entity or a higher tier entity that owns 5 percent or more of the loss corporation's stock (determined

without regard to § 1.382-2T(h)(2)(i)(A)).

(12) *Certain non-stock ownership interests.* As the context may require, a non-stock ownership interest in an entity other than a corporation is treated as stock for purposes of this paragraph (j).

(13) *Examples.* The provisions of this paragraph (j) are illustrated by the following examples:

*Example 1.* (i) L corporation is a calendar year taxpayer. On January 1, 1994, L has 1,000 shares of a single class of common stock outstanding, all of which are owned by a single direct public group (Public L). On February 1, 1994, L issues to employees as compensation 60 new common shares of the same class. On May 1, 1994, L issues 50 new common shares of the same class solely for cash. Following each issuance, L's stock is owned entirely by public shareholders. No other changes in the ownership of L's stock occur prior to May 1, 1994. L chooses to determine its small issuance limitation for 1994 on a class-by-class basis under paragraph (j)(2)(iii)(A)(2) of this section.

(ii) The February issuance is a small issuance because the number of shares issued (60) does not exceed 100, the small issuance limitation (10 percent of the number of common shares outstanding on January 1, 1994). Under paragraph (j)(2) of this section, the segregation rules of § 1.382-2T(j)(2)(iii)(E) do not apply to the February issuance. Under paragraph (j)(5) of this section, Public L is treated as acquiring all 60 shares issued.

(iii) The May issuance is a small issuance because the number of shares issued (50) does not exceed 100, the small issuance limitation (10 percent of the number of common shares outstanding on January 1, 1994). However, under paragraph (j)(2) of this section, only 40 of the 50 shares issued are exempted from the segregation rules of § 1.382-2T(j)(2)(iii)(B) because the total number of shares of common stock issued in the February and May issuances exceeds 100, the small issuance limitation, by 10. Because the May issuance is solely for cash, paragraph (j)(3) of this section exempts 5 of the 10 remaining shares from the segregation rules of § 1.382-2T(j)(2)(iii)(B) (10 shares multiplied by 50 percent, one-half of Public L's 100 percent ownership interest immediately before the May issuance—1,060 shares/1,060 shares). Accordingly, under paragraph (j)(5) of this section, Public L is treated as acquiring 45 shares in the May issuance. Section 1.382-2T(j)(2)(iii)(B) applies to the remaining 5 shares issued, which are treated as acquired by a direct public group separate from Public L. Each such public group is treated as an individual who is a separate 5-percent shareholder. See § 1.382-2T(g)(1)(iv) and (j)(1)(ii).

(iv) Assume that L actually knows that at least 10 shares of the May issuance are acquired by members of Public L. The result is the same. See paragraph (j)(5)(ii) of this section.

(v) Assume instead that L actually knows that all 50 shares of the May issuance are acquired by members of Public L. Under

paragraph (j)(5)(ii) of this section, L may treat Public L as acquiring 50 shares in the May issuance.

**Example 2.** (i) L corporation is a calendar year taxpayer. On January 1, 1995, L has 1,000 shares of Class A common stock outstanding, the aggregate value of which is \$1,000. Five hundred shares are owned by one direct public group (Public 1), and 500 shares are owned by another direct public group (Public 2). On August 1, 1995, L issues 200 shares of Class B common stock for \$200 cash. A, an individual, acquires 120 Class B shares in the transaction. The remaining 80 Class B shares are acquired by public shareholders. No other changes in ownership of L's stock occur prior to August 1, 1995.

(ii) The August issuance is not a small issuance. The total value of the Class B stock issued (\$200) exceeds \$100, the small issuance limitation as calculated under paragraph (j)(2)(iii)(A)(2) of this section (10 percent of the value of L's stock on January 1, 1995). The total number of Class B shares issued (200) exceeds 0, the small issuance limitation as calculated under paragraph (j)(2)(iii)(A)(2) of this section (10 percent of the number of Class B shares outstanding on January 1, 1995). Accordingly, paragraph (j)(2) of this section does not apply to the August issuance.

(iii) Paragraph (j)(3) of this section, as limited by paragraph (j)(4) of this section, exempts 80 Class B shares from the segregation rule of § 1.382-2T(j)(2)(iii)(B). Paragraph (j)(3) of this section, without regard to paragraph (j)(4) of this section, would exempt 100 Class B shares: the product of the 200 Class B shares issued and 50 percent (one-half of the combined 100 percent pre-issuance ownership interest of Public 1 and Public 2). Paragraph (j)(4), however, limits the total number of Class B shares that may be excluded to 80 Class B shares: the difference between the 200 shares issued and the 120 shares acquired by A. Under paragraph (j)(5) of this section, Public 1 and Public 2 are treated as acquiring the 80 exempted Class B shares. Because Public 1 and Public 2 each owned 500 Class A shares prior to the issuance, Public 1 and Public 2 are considered to acquire 40 Class B shares each.

**Example 3.** (i) L has 1,000 shares of a single class of common stock outstanding, all of which are owned by a direct public group (Public L). At the same time pursuant to the same plan, L issues 500 shares of its stock to its creditors in exchange for its outstanding debt and 500 shares of its stock to the public for cash. Assume that the separate issuances of stock for debt and stock for cash do not have a principal purpose of minimizing or avoiding an owner shift. L has no individual 5-percent shareholders immediately after the issuances.

(ii) The 500 shares of stock issued by L to its former creditors were not issued solely for cash. Therefore, paragraph (j)(3) of this section does not apply to those 500 shares, which are treated as owned by a public group separate from Public L. See § 1.382-2T(j)(2)(iii)(B)(1)(iv).

(iii) Paragraph (j)(3) of this section applies to the 500 shares of stock issued by L to the public because that stock was issued solely

for cash. Because the two issuances occur at the same time pursuant to the same plan, they are generally treated as a single issuance for purposes of this paragraph (j). See paragraph (j)(8)(i) of this section. The treatment of the two issuances as a single issuance does not apply, however, for the purpose of determining whether the stock issued to the public was issued solely for cash. See paragraph (j)(3)(ii)(B) of this section.

(iv) Paragraph (j)(3) of this section applies to exempt 250 of the 500 shares issued solely for cash from the segregation rules of § 1.382-2T(j)(2)(iii)(B) (the product of the 500 shares issued for cash and 50 percent (one-half of the 100 percent pre-issuance ownership interest of Public L)). The creditors that receive stock in exchange for their debt would not be treated as acquiring any of the 250 exempted shares even if their exchange of debt for stock occurs prior to the cash issuance. Paragraph (j)(5)(i) of this section allocates exempted shares among the direct public groups that exist immediately before an issuance. Because the issuance for cash and the issuance for debt are generally treated as a single issuance, the public group comprised of the former creditors of L was not a public group that existed immediately before the issuance.

(v) Three public groups owning L stock exist immediately after the two issuances. Public L owns 1,250 shares—the 1,000 shares it owned prior to the issuances plus the 250 shares it is treated as acquiring in the cash issuance. A separate group comprised of the former creditors of L owns the 500 shares issued for debt. A third public group owns the 250 shares that are not treated as acquired by Public L in the cash issuance.

**Example 4.** (i) L has 1,000 shares of a single class of common stock outstanding, all of which are owned by a direct public group (Public L). L issues 1,000 shares pursuant to an offer under which 500 shares must be acquired in exchange for debt and the remainder may be acquired for cash. Under the terms of the offer, only persons that acquire stock for debt are eligible to acquire stock for cash. L has no 5-percent shareholders other than direct public groups immediately after the issuance.

(ii) As a condition of acquiring shares for cash, the creditors are required to purchase stock for debt. Therefore, paragraph (j)(3) of this section does not apply to any part of the issuance because it is not an issuance of stock solely for cash. The segregation rules of § 1.382-2T(j)(2)(iii)(B) apply to treat all 1,000 shares as acquired by a new public group separate from Public L.

(14) **Effective date—(i) In general.** Except as otherwise provided in this paragraph (j)(14), this paragraph (j) applies to issuances or deemed issuances of stock in taxable years beginning on or after November 4, 1992.

(ii) **Effective date for paragraph (j)(10) of this section.** Paragraph (j)(10) of this section applies to stock issued on the exercise of an option issued on or after November 4, 1992, unless the option was issued before May 4, 1993, and the

issuer, on or before November 4, 1992, filed a registration statement with the Securities and Exchange Commission (or a comparable document with a State agency regulating securities) for the specific purpose of such issuance.

(iii) **Election to apply this paragraph (j) retroactively—(A) Election.** A loss corporation may elect to apply paragraphs (j)(1) through (j)(13) of this section to all issuances or deemed issuances of stock to which § 1.382-2T(j)(2)(iii)(B) or (D) applied (or would have applied taking paragraph (j)(7) of this section into account) occurring in taxable years beginning prior to November 4, 1992. This election is made by filing with the loss corporation's first income tax return filed more than 60 days after October 4, 1993, the statement, "This is an Election to Apply § 1.382-3(j) Retroactively," accompanied by the amended return and revised information statements described in paragraphs (j)(14)(iii)(B) and (C) of this section. An election under this paragraph (j)(14)(iii) is irrevocable.

(B) **Amended returns.** If the retroactive application of the rules of this paragraph (j) affects the amount of taxable income or loss for a prior taxable year, then, except as precluded by the applicable statute of limitations, the loss corporation (or the common parent of any consolidated group of which the loss corporation was a member for the year) must file an amended return for the year that reflects the effect of the retroactive application of the rules of this paragraph (j). If the statute of limitations precludes the filing of an amended return for one or more such prior taxable years, the loss corporation (or the common parent) must make appropriate adjustments under the principles of section 382(f)(2)(A) in subsequent taxable years to reflect the difference between the losses and credits actually used in such prior taxable years and the amount that would have been used in those years applying the rules of this paragraph (j).

(C) **Revised information statements.** If the retroactive application of the rules of this paragraph (j) effects the information reported on an information statement filed for any prior taxable year pursuant to § 1.382-2T(k)(ii), then the loss corporation (or the common parent of any consolidated group of which the loss corporation was a member for the year) must file a revised information statement for the year that reflects the retroactive application of the rules of this paragraph (j).

**PART 602—OMB CONTROL NUMBERS  
UNDER THE PAPERWORK  
REDUCTION ACT**

Par. 5. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 6. Section 602.101(c) is amended by revising the entry in the table for 1.382-3 to read as follows:

§ 602.101 OMB Control numbers.

(c)

CFR part or section where identified and described	Current OMB control No.
1.382-3	1545-1345

Margaret Milner Richardson,  
*Commissioner of Internal Revenue.*

Approved:  
Samuel Y. Sessions,  
*Assistant Secretary of the Treasury (Tax Policy).*

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(B) such rate shall be properly adjusted for differences between rates on long-term taxable and tax-exempt obligations.

**Ownership change.**

For purposes of this section—

(1) **In general.** There is an ownership change if, immediately after any owner shift involving a 5-percent shareholder or any equity structure shift—

(A) the percentage of the stock of the loss corporation owned by 1 or more 5-percent shareholders has increased by more than 50 percentage points, over

(B) the lowest percentage of stock of the loss corporation (or any predecessor corporation) owned by such shareholders at any time during the testing period.

(2) **Owner shift involving 5-percent shareholder.** There is an owner shift involving a 5-percent shareholder if—

(A) there is any change in the respective ownership of stock of a corporation, and

(B) such change affects the percentage of stock of such corporation owned by any person who is a 5-percent shareholder before or after such change.

(3) **Equity structure shift defined.**

(A) **In general.** The term "equity structure shift" means any reorganization (within the meaning of section 368). Such term shall not include—

(i) any reorganization described in subparagraph (D) or (G) of section 368(a)(1) unless the requirements of section 354(b)(1) are met, and

(ii) any reorganization described in subparagraph (F) of section 368(a)(1).

(B) **Taxable reorganization-type transactions, etc.** To the extent provided in regulations, the term "equity structure shift" includes taxable reorganization-type transactions, public offerings, and similar transactions.

(4) **Special rules for application of subsection.**

(A) **Treatment of less than 5-percent shareholders.** Except as provided in subparagraphs (B)(i) and (C), in determining whether an ownership change has occurred, all stock owned by shareholders of a corporation who are not 5-percent shareholders of such corporation shall be treated as stock owned by 1 5-percent shareholder of such corporation.

(B) **Coordination with equity structure shifts.** For purposes of determining whether an equity structure shift (or subsequent transaction) is an ownership change—

(i) **Less than 5-percent shareholders.** Subparagraph (A) shall be applied separately with respect to each group of shareholders (immediately before such equity structure shift) of each corporation which was a party to the reorganization involved in such equity structure shift.

(ii) **Acquisitions of stock.** Unless a different proportion is established, acquisitions of stock after such equity structure shift shall be treated as being made proportionately from all shareholders immediately before such acquisition.

(C) **Coordination with other owner shifts.** Except as provided in regulations, rules similar to the rules of subparagraph (B) shall apply in determining whether there has been an owner shift involving a 5-percent shareholder and whether such shift (or subsequent transaction) results in an ownership change.

(D) **Treatment of worthless stock.** If any stock held by a 50-percent shareholder is treated by such shareholder as becoming worthless during any taxable year of such shareholder and such stock is held by such shareholder

as of the close of such taxable year, for purposes of determining whether an ownership change occurs after the close of such taxable year, such shareholder—

(i) shall be treated as having acquired such stock on the 1st day of his 1st succeeding taxable year, and

(ii) shall not be treated as having owned such stock during any prior period.

For purposes of the preceding sentence, the term 50-percent shareholder means any person owning 50 percent or more of the stock of the corporation at any time during the 3-year period ending on the last day of the taxable year with respect to which the stock was so treated.

(h) **Special rules for built-in gains and losses and section 338 gains.**

For purposes of this section—

(1) **In general.**

(A) **Net unrealized built-in gain.**

(i) **In general.** If the old loss corporation has a net unrealized built-in gain, the section 382 limitation for any recognition period taxable year shall be increased by the recognized built-in gains for such taxable year.

(ii) **Limitation.** The increase under clause (i) for any recognition period taxable year shall not exceed—

- (I) the net unrealized built-in gain, reduced by
- (II) recognized built-in gains for prior years ending in the recognition period.

(B) **Net unrealized built-in loss.**

(i) **In general.** If the old loss corporation has a net unrealized built-in loss, the recognized built-in loss for any recognition period taxable year shall be subject to limitation under this section in the same manner as if such loss were a pre-change loss.

(ii) **Limitation.** Clause (i) shall apply to recognized built-in losses for any recognition period taxable year only to the extent such losses do not exceed—

- (I) the net unrealized built-in loss, reduced by
- (II) recognized built-in losses for prior taxable years ending in the recognition period.

(C) **Special rules for certain section 338 gains.** If an election under section 338 is made in connection with an ownership change and the net unrealized built-in gain is zero by reason of paragraph (3)(B), then, with respect to such change, the section 382 limitation for the post-change year in which gain is recognized by reason of such election shall be increased by the lesser of—

- (i) the recognized built-in gains by reason of such election, or
- (ii) the net unrealized built-in gain (determined without regard to paragraph (3)(B)).

(2) **Recognized built-in gain and loss.**

(A) **Recognized built-in gain.** The term "recognized built-in gain" means any gain recognized during the recognition period on the disposition of any asset to the extent the new loss corporation establishes that—

- (i) such asset was held by the old loss corporation immediately before the change date, and
- (ii) such gain does not exceed the excess of—
  - (I) the fair market value of such asset on the change date, over
  - (II) the adjusted basis of such asset on such date.

(B) **Recognized built-in loss.** The term "recognized built-in loss" means any loss recognized during the recognition period on the disposition of any asset except to the extent the new loss corporation establishes that—

- (i) such asset was not held by the old loss corporation immediately before the change date, or
- (ii) such loss exceeds the excess of—
  - (I) the adjusted basis of such asset on the change date, over
  - (II) the fair market value of such asset on such date.

Such term includes any amount allowable as depreciation, amortization, or depletion for any period within the recognition period except to the extent the new loss corporation establishes that the amount so allowable is not attributable to the excess described in clause (ii).

**(3) Net unrealized built-in gain and loss defined.**

**(A) Net unrealized built-in gain and loss.**

- (i) In general. The terms "net unrealized built-in gain" and "net unrealized built-in loss" mean, with respect to any old loss corporation, the amount by which—
  - (I) the fair market value of the assets of such corporation immediately before an ownership change is more or less, respectively, than
  - (II) the aggregate adjusted basis of such assets at such time.

(ii) Special rule for redemptions or other corporate contractions. If a redemption or other corporate contraction occurs in connection with an ownership change, to the extent provided in regulations, determinations under clause (i) shall be made after taking such redemption or other corporate contraction into account.

**(B) Threshold requirement.**

- (i) In general. If the amount of the net unrealized built-in gain or net unrealized built-in loss (determined without regard to this subparagraph) of any old loss corporation is not greater than the lesser of—

- (I) 15 percent of the amount determined for purposes of subparagraph (A)(i)(I), or
- (II) \$10,000,000.

the net unrealized built-in gain or net unrealized built-in loss shall be zero.

- (ii) Cash and cash items not taken into account. In computing any net unrealized built-in gain or net unrealized built-in loss under clause (i), except as provided in regulations, there shall not be taken into account—

- (I) any cash or cash item, or
- (II) any marketable security which has a value which does not substantially differ from adjusted basis.

**(4) Disallowed loss allowed as a carryforward.** If a deduction for any portion of a recognized built-in loss is disallowed for any post-change year, such portion—

- (A) shall be carried forward to subsequent taxable years under rules similar to the rules for the carrying forward of net operating losses (or to the extent the amount so disallowed is attributable to capital losses, under rules similar to the rules for the carrying forward of net capital losses), but

(B) shall be subject to limitation under this section in the same manner as a pre-change loss.

**(5) Special rules for post-change year which includes change date.** For purposes of subsection (b)(3)—

- (A) in applying subparagraph (A) thereof, taxable income shall be computed without regard to recognized

built-in gains to the extent such gains increased the section 382 limitation for the year (or recognized built-in losses to the extent such losses are treated as change losses), and gain described in paragraph (1) for the year, and

(B) in applying subparagraph (B) thereof, the section 382 limitation shall be computed without regard to recognized built-in gains, and gain described in paragraph (1)(C), for the year.

**(6) Treatment of certain built-in items.**

(A) Income items. Any item of income which is properly taken into account during the recognition period but which is attributable to periods before the change date shall be treated as a recognized built-in gain the taxable year in which it is properly taken into account.

(B) Deduction items. Any amount which is allowable as a deduction during the recognition period (determined without regard to any carryover) but which is attributable to periods before the change date shall be treated as a recognized built-in loss for the taxable year for which it is allowable as a deduction.

(C) Adjustments. The amount of the net unrealized built-in gain or loss shall be properly adjusted for amounts which would be treated as recognized built-in gains or losses under this paragraph if such amounts were properly taken into account (or allowable as a deduction) during the recognition period.

**(7) Recognition period, etc.**

(A) Recognition period. The term "recognition period" means, with respect to any ownership change, the year period beginning on the change date.

(B) Recognition period taxable year. The term "recognition period taxable year" means any taxable year portion of which is in the recognition period.

**(8) Determination of fair market value in certain cases.**

If 80 percent or more in value of the stock of a corporation is acquired in 1 transaction (or in a series of transactions during any 12-month period), for purposes of determining the net unrealized built-in loss, the fair market value of the assets of such corporation shall not exceed the grossed up amount paid for such stock (not adjusted for indebtedness of the corporation and other event items).

(9) Tax-free exchanges or transfers. The Secretary prescribe such regulations as may be necessary to carry out the purposes of this subsection where property is transferred on the change date was acquired (or is subsequently transferred) in a transaction where gain or loss is not recognized (in whole or in part).

**(i) Testing period.**

For purposes of this section—

(1) 3-year period. Except as otherwise provided in this section, the testing period is the 3-year period ending on the day of any owner shift involving a 5-percent shareholder or equity structure shift.

(2) Shorter period where there has been recent ownership change. If there has been an ownership change under this section, the testing period for determining whether a 2nd ownership change has occurred shall begin before the 1st day following the change date of such earlier ownership change.

(3) Shorter period where all losses arise after change date. The testing period shall not begin before the earlier of the 1st day of the 1st taxable year in which there is a carryforward of a loss or of an

credit to the 1st post-change year or the taxable year in which the transaction being tested occurs. Except as provided in regulations, this paragraph shall not apply to any loss corporation which has a net unrealized built-in loss (determined after application of subsection (h)(3)(B)).

(j) Change date.

For purposes of this section, the change date is—  
 (1) in the case where the last component of an ownership change is an owner shift involving a 5-percent shareholder, the date on which such shift occurs, and  
 (2) in the case where the last component of an ownership change is an equity structure shift, the date of the reorganization.

(k) Definitions and special rules.

For purposes of this section—

(1) **Loss corporation.** The term "loss corporation" means a corporation entitled to use a net operating loss carryover or having a net operating loss for the taxable year in which the ownership change occurs. Except to the extent provided in regulations, such term includes any corporation with a net unrealized built-in loss.

(2) **Old loss corporation.** The term "old loss corporation" means any corporation—

- (A) with respect to which there is an ownership change, and
- (B) which (before the ownership change) was a loss corporation.

(3) **New loss corporation.** The term "new loss corporation" means a corporation which (after an ownership change) is a loss corporation. Nothing in this section shall be treated as implying that the same corporation may not be both the old loss corporation and the new loss corporation.

(4) **Taxable income.** Taxable income shall be computed with the modifications set forth in section 172(d).

(5) **Value.** The term "value" means fair market value.

(6) Rules relating to stock.

(A) **Preferred stock.** Except as provided in regulations and subsection (e), the term "stock" means stock other than stock described in section 1504(a)(4).

(B) **Treatment of certain rights, etc.** The Secretary shall prescribe such regulations as may be necessary—

- (i) to treat warrants, options, contracts to acquire stock, convertible debt interests, and other similar interests as stock, and
- (ii) to treat stock as not stock.

(C) **Determinations on basis of value.** Determinations of the percentage of stock of any corporation held by any person shall be made on the basis of value.

(7) **5-percent shareholder.** The term "5-percent shareholder" means any person holding 5 percent or more of the stock of the corporation at any time during the testing period.

(8) Certain additional operating rules.

For purposes of this section—

(1) **Certain capital contributions not taken into account.**

(A) In general. Any capital contribution received by an old loss corporation as part of a plan a principal purpose of which is to avoid or increase any limitation under this section shall not be taken into account for purposes of this section.

(B) **Certain contributions treated as part of plan.** For purposes of subparagraph (A), any capital contribution made during the 2-year period ending on the change

date shall, except as provided in regulations, be treated as part of a plan described in subparagraph (A).

(2) Ordering rules for application of section.

(A) **Coordination with section 172(b) carryover rules.** In the case of any pre-change loss for any taxable year (hereinafter in this subparagraph referred to as the "loss year") subject to limitation under this section, for purposes of determining under the 2nd sentence of section 172(b)(2) the amount of such loss which may be carried to any taxable year, taxable income for any taxable year shall be treated as not greater than—

- (i) the section 382 limitation for such taxable year, reduced by
- (ii) the unused pre-change losses for taxable years preceding the loss year.

Similar rules shall apply in the case of any credit or loss subject to limitation under section 383.

(B) **Ordering rule for losses carried from same taxable year.** In any case in which—

- (i) a pre-change loss of a loss corporation for any taxable year is subject to a section 382 limitation, and
- (ii) a net operating loss of such corporation from such taxable year is not subject to such limitation, taxable income shall be treated as having been offset first by the loss subject to such limitation.

(3) Operating rules relating to ownership of stock.

(A) **Constructive ownership.** Section 318 (relating to constructive ownership of stock) shall apply in determining ownership of stock, except that—

- (i) paragraphs (1) and (5)(B) of section 318(a) shall not apply and an individual and all members of his family described in paragraph (1) of section 318(a) shall be treated as 1 individual for purposes of applying this section,
- (ii) paragraph (2) of section 318(a) shall be applied—

(I) without regard to the 50-percent limitation contained in subparagraph (C) thereof, and

(II) except as provided in regulations, by treating stock attributed thereunder as no longer being held by the entity from which attributed,

(iii) paragraph (3) of section 318(a) shall be applied only to the extent provided in regulations,

(iv) except to the extent provided in regulations, an option to acquire stock shall be treated as exercised if such exercise results in an ownership change, and

(v) in attributing stock from an entity under paragraph (2) of section 318(a), there shall not be taken into account—

(I) in the case of attribution from a corporation, stock which is not treated as stock for purposes of this section, or

(II) in the case of attribution from another entity, an interest in such entity similar to stock described in subclause (I).

A rule similar to the rule of clause (iv) shall apply in the case of any contingent purchase, warrant, convertible debt, put, stock subject to a risk of forfeiture, contract to acquire stock, or similar interests.

(B) **Stock acquired by reason of death, gift, divorce, separation, etc.** If—

(i) the basis of any stock in the hands of any person is determined—

(I) under section 1014 (relating to property acquired from a decedent),



- (II) section 1015 (relating to property acquired by a gift or transfer in trust), or
  - (III) section 1041(b)(2) (relating to transfers of property between spouses or incident to divorce),
  - (ii) stock is received by any person in satisfaction of a right to receive a pecuniary bequest, or
  - (iii) stock is acquired by a person pursuant to any divorce or separation instrument (within the meaning of section 71(b)(2)).
- such person shall be treated as owning such stock during the period such stock was owned by the person from whom it was acquired.

(C) Certain changes in percentage ownership which are attributable to fluctuations in value not taken into account. Except as provided in regulations, any change in proportionate ownership which is attributable solely to fluctuations in the relative fair market values of different classes of stock shall not be taken into account.

**(4) Reduction in value where substantial nonbusiness assets.**

(A) In general. If, immediately after an ownership change, the new loss corporation has substantial nonbusiness assets, the value of the old loss corporation shall be reduced by the excess (if any) of—

- (i) the fair market value of the nonbusiness assets of the old loss corporation, over
- (ii) the nonbusiness asset share of indebtedness for which such corporation is liable.

(B) Corporation having substantial nonbusiness assets. For purposes of subparagraph (A)—

(i) In general. The old loss corporation shall be treated as having substantial nonbusiness assets if at least 1/5 of the value of the total assets of such corporation consists of nonbusiness assets.

(ii) Exception for certain investment entities. A regulated investment company to which part I of subchapter M applies, a real estate investment trust to which part II of subchapter M applies, or a REMIC to which part IV of subchapter M applies, shall not be treated as a new loss corporation having substantial nonbusiness assets.

(C) Nonbusiness assets. For purposes of this paragraph, the term "nonbusiness assets" means assets held for investment.

(D) Nonbusiness asset share. For purposes of this paragraph, the nonbusiness asset share of the indebtedness of the corporation is an amount which bears the same ratio to such indebtedness as—

- (i) the fair market value of the nonbusiness assets of the corporation, bears to
- (ii) the fair market value of all assets of such corporation.

(E) Treatment of subsidiaries. For purposes of this paragraph, stock and securities in any subsidiary corporation shall be disregarded and the parent corporation shall be deemed to own its ratable share of the subsidiary's assets. For purposes of the preceding sentence, a corporation shall be treated as a subsidiary if the parent owns 50 percent or more of the combined voting power of all classes of stock entitled to vote, and 50 percent or more of the total value of shares of all classes of stock.

**(5) Title 11 or similar case.**

(A) In general. Subsection (a) shall not apply to any ownership change if—

(i) the old loss corporation is (immediately before such ownership change) under the jurisdiction of a court in a title 11 or similar case, and

(ii) the shareholders and creditors of the old loss corporation (determined immediately before such ownership change) own (after such ownership change as a result of being shareholders or creditors immediately before such change) stock of the new loss corporation (or stock of a controlling corporation if in bankruptcy) which meets the requirements of section 1504(a)(2) (determined by substituting "50 percent" for "80 percent" each place it appears).

(B) Reduction for interest payments to creditors being shareholders. In any case to which subparagraph (A) applies, the pre-change losses and excess (within the meaning of section 383(a)(2)) which are carried to a post-change year shall be computed as deduction was allowable under this chapter for the interest paid or accrued by the old loss corporation or indebtedness which was converted into stock pursuant to title 11 or similar case during—

(i) any taxable year ending during the 3-year period preceding the taxable year in which the ownership change occurs, and

(ii) the period of the taxable year in which the ownership change occurs on or before the change date.

(C) Coordination with section 108. In applying section 108(e)(8) to any case to which subparagraph (A) applies, there shall not be taken into account any indebtedness for interest described in subparagraph (B).

(D) Section 382 limitation zero if another change within 2 years. If, during the 2-year period immediately following an ownership change to which this paragraph applies, an ownership change of the new loss corporation occurs, this paragraph shall not apply and the section 382 limitation with respect to the 2nd ownership change for any post-change year ending after change date of the 2nd ownership change shall be zero.

(E) Only certain stock taken into account. For purposes of subparagraph (A)(ii), stock transferred to a creditor shall be taken into account only to the extent such stock is transferred in satisfaction of indebtedness and on such indebtedness—

(i) was held by the creditor at least 18 months before the date of the filing of the title 11 or similar case,

(ii) arose in the ordinary course of the trade or business of the old loss corporation and is held by person who at all times held the beneficial interest in such indebtedness.

(F) Special rule for certain financial institutions.

(i) In general. In the case of any ownership change to which this subparagraph applies, this paragraph shall be applied—

(I) by substituting "1504(a)(2)(B)" for "1504(a)(2)" and "20 percent" for "50 percent" in subparagraph (A)(ii), and

(II) without regard to subparagraphs (B) and (C).

(ii) Special rule for depositors. For purposes of applying this paragraph to an ownership change to which this subparagraph applies—

(I) a depositor in the old loss corporation shall be treated as a stockholder in such loss corporation immediately before the change,

(II) deposits which, after the change, become assets of the new loss corporation shall be treated as stock of the new loss corporation, and

(III) the fair market value of the outstanding stock of the new loss corporation shall include the amount of deposits in the new loss corporation immediately after the change.

(iii) Changes to which subparagraph applies. This subparagraph shall apply to—

- (I) an equity structure shift which is a reorganization described in section 368(a)(3)(D)(ii) (as modified by section 368(a)(3)(D)(iv)), or
- (II) any other equity structure shift (or transaction to which section 351 applies) which occurs as an integral part of a transaction involving a change to which subclause (I) applies.

This subparagraph shall not apply to any equity structure shift or transaction occurring on or after May 10, 1989.

(G) Title 11 or similar case. For purposes of this paragraph, the term "title 11 or similar case" has the meaning given such term by section 368(a)(3)(A).

(H) Election not to have paragraph apply. A new loss corporation may elect, subject to such terms and conditions as the Secretary may prescribe, not to have the provisions of this paragraph apply.

(4) Special rule for insolvency transactions. If paragraph (5) does not apply to any reorganization described in subparagraph (G) of section 368(a)(1) or any exchange of debt for stock in a title 11 or similar case (as defined in section 368(a)(3)(A)), the value under subsection (c) shall reflect the increase (if any) in value of the old loss corporation resulting from any surrender or cancellation of creditors' claims in the transaction.

(5) Coordination with alternative minimum tax. The Secretary shall by regulation provide for the application of this section to the alternative tax net operating loss deduction under section 56(d).

(6) Predecessor and successor entities. Except as provided in regulations, any entity and any predecessor or successor entities of such entity shall be treated as 1 entity.

**Regulations.**

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section and section 383, including (but not limited to) regulations—

1. providing for the application of this section and section 383 where an ownership change with respect to the loss corporation is followed by an ownership change with respect to the new loss corporation, and
2. providing for the application of this section and section 383 in the case of a short taxable year,
3. providing for such adjustments to the application of this section and section 383 as is necessary to prevent the avoidance of the purposes of this section and section 383, including the avoidance of such purposes through the use of related persons, pass-thru entities, or other intermediaries,
4. providing for the application of subsection (g)(4) where there is only 1 corporation involved, and
5. providing, in the case of any group of corporations described in section 1563(a) (determined by substituting "50 percent" for "80 percent" each place it appears and determined without regard to paragraph (4) thereof), appropriate adjustments to value, built-in gain or loss, and other items so that items are not omitted or taken into account more than once.

In '93, P.L. 103-66, Sec. 13216(a)(2)(A), amended subpara. (1)(3)(C), effective for stock transferred after 12/31/94, in satisfaction of any indebtedness, except as provided in Sec. 13216(a)(3) of this Act, which read as follows:

"(B) Exception for title 11 cases. The amendments made by this subsection shall not apply to stock transferred in satisfaction of any indebtedness if such transfer is in a title 11 or similar case (as defined in section 368(a)(3)(A) of the Internal Revenue Code of 1986) which was filed on or before December 31, 1993."

Prior to amendment, subpara. (1)(3)(C) read as follows:

"(C) Reduction of tax attributes where discharge of indebtedness. (i) In general. In any case to which subparagraph (A) applies, 50 percent of the amount which, but for the application of section 106(e)(10)(B), would have been applied to reduce tax attributes under section 108(b) shall be so applied.

"(ii) Clarification with subparagraph (B). In applying clause (i), there shall not be taken into account any indebtedness for interest described in subparagraph (B)."

In '89, P.L. 101-239, Sec. 7205(a), amended clause (1)(3)(B)(i), effective for ownership changes and acquisitions after 10/2/89, in tax yrs. end. after 10/2/89, except as otherwise provided by Secs. 7205(c)(2)-(4) of this Act, which read as follows:

"(2) Binding contract.—The amendments made by this section shall not apply to any ownership change or acquisition pursuant to a written binding contract in effect on October 2, 1989, and at all times thereafter before such change or acquisition.

"(3) Bankruptcy proceedings.—In the case of a reorganization described in section 368(a)(1)(G) of the Internal Revenue Code of 1986, or an exchange of debt for stock in a title 11 or similar case (as defined in section 368(a)(3) of such Code), the amendments made by this section shall not apply to any ownership change resulting from such a reorganization or proceeding if a petition in such case was filed with the court before October 3, 1989.

"(4) Subsidiaries of bankrupt parent.—The amendments made by this section shall not apply to any built-in loss of a corporation which is a member (on October 2, 1989) of an affiliated group the common parent of which (on such date) was subject to title 11 or similar case (as defined in section 368(a)(3) of such Code). The preceding sentence shall apply only if the ownership change or acquisition is pursuant to the plan approved in such proceeding and is before the date 2 years after the date on which the petition which commenced such proceeding was filed."

Prior to amendment clause (1)(3)(B)(i) read as follows:

"(i) If the amount of the net unrealized built-in gain or net unrealized built-in loss (determined without regard to this subparagraph) of any old loss corporation is not greater than 25 percent of the amount determined for purposes of subparagraph (A)(1)(D), the net unrealized built-in gain or net unrealized built-in loss shall be zero."

—P.L. 101-239, Sec. 7304(d)(1), deleted subpara. (1)(3)(C) and redesignated subpara. (1)(3)(D) as (1)(3)(C), effective for acquisitions of employer securities after 7/12/89, except for acquisitions after 7/12/89, pursuant to a written binding contract in effect on 7/12/89, and at all times thereafter before such acquisition.

Prior to deletion, subpara. (1)(3)(C) read as follows:

"(C) Special rule for employee stock ownership plans.

"(i) In general. Except as provided in clause (ii), the acquisition of employer securities (within the meaning of section 409(1)) by—

"(I) a tax credit employee stock ownership plan or an employee stock ownership plan (within the meaning of section 4975(e)(7)), or

"(II) a participant of any such plan pursuant to the requirements of section 409(b),

shall not be taken into account in determining whether an ownership change has occurred.

"(ii) Ownership and allocation requirements. Subclause (i) of clause (i) shall not apply to any acquisition unless—

"(I) immediately after such acquisition the plan holds stock meeting the requirements of section 1042(b)(2), except that such section shall be applied by substituting "50 percent" for "30 percent",

"(II) the plan meets requirements similar to the requirements of section 409(a), and,

"(III) immediately after the acquisition the plan has a number of participants which is not less than 50 percent of the average number of employees of the loss corporation during the 3-year period ending with such acquisition.

"For purposes of subclause (II), except as provided in regulations, all members of an affiliated group which includes the loss corporation and which files a consolidated return shall be treated as 1 loss corporation."

—P.L. 101-239, Sec. 7811(c)(5)(A)(i), substituted "during the recognition period (determined without regard to any carryover)" for "during the recognition period" in subpara. (1)(3)(B)... Sec. 7811(c)(5)(A)(ii), substituted "which would be treated as recognized built-in gains or losses under this paragraph if such amounts were properly taken into account (or allowable as a deduction) during the recognition period" for "treated as recognized built-in gains

estate tax purposes. His executors were not precluded from showing his true residence.

*Est. of J. Bloch-Sulzberger*, 6 TCM 1201, Dec. 16, 1936.

## [¶ 10,340]

## RULES AND REGULATIONS

SEC. 7805 [1986 Code]. (a) AUTHORIZATION.—Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.

(b) RETROACTIVITY OF REGULATIONS OR RULINGS.—The Secretary may prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied without retroactive effect.

(c) PREPARATION AND DISTRIBUTION OF REGULATIONS, FORMS, STAMPS, AND OTHER MATTERS.—The Secretary shall prepare and distribute all the instructions, regulations, directions, forms, blanks, stamps, and other matters pertaining to the assessment and collection of internal revenue.

(d) MANNER OF MAKING ELECTIONS PRESCRIBED BY SECRETARY.—Except to the extent otherwise provided by this title, any election under this title shall be made at such time and in such manner as the Secretary shall by regulations or forms prescribe.

## (e) TEMPORARY REGULATIONS.—

(1) ISSUANCE.—Any temporary regulation issued by the Secretary shall also be issued as a proposed regulation.

(2) 3-YEAR DURATION.—Any temporary regulation shall expire within 3 years after the date of issuance of such regulation.

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