

[4830-01-u]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 8800]

RIN 1545-AW51

Consolidated returns--Limitation on recapture of overall foreign loss accounts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains temporary amendments to the consolidated return regulations. The temporary amendments modify the date temporary regulations apply as published in the **Federal Register** on January 12, 1998, and modified by amendments published in the **Federal Register** on March 16, 1998, relating to a consolidated group's recapture of an overall foreign loss account arising in a separate return limitation year. The regulations affect consolidated groups that claim foreign tax credits. The text of the temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section of this issue of the **Federal Register**.

DATES: Effective dates: These amendments are effective December 29, 1998.

Applicability dates: For dates of applicability of these regulations, see §1.1502-9T(b)(1)(v).

FOR FURTHER INFORMATION CONTACT: Trina Dang of the Office of Associate Chief Counsel (International), (202) 622-3850 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

### **Background**

As announced in Notice 98-40 (1998-35 I.R.B. 7), these temporary regulations permit taxpayers to elect to delay the effective date of §1.1502-9T, published in the **Federal Register** on January 12, 1998 (TD 8751, 63 FR 1740), and modified by amendments published in the **Federal Register** on March 16, 1998 (TD 8766, 63 FR 12641).

On January 12, 1998, Treasury and the IRS published in the **Federal Register** (TD 8751, 63 FR 1740) final, temporary and proposed regulations (the January 1998 regulations) relating to limitations on the use of certain tax credits and related attributes by corporations filing consolidated income tax returns. In general, the January 1998 regulations relate to the separate return limitation year (SRLY) provisions for general business credits, alternative minimum tax credits, foreign tax credits and overall foreign loss accounts. The January 1998 regulations were generally applicable to consolidated return years beginning on or after January 1, 1997.

On March 16, 1998, Treasury and the IRS published in the **Federal Register** (TD 8766, 63 FR 12641) final, temporary, and proposed regulations (the March 1998 regulations) modifying the effective date of the January 1998 regulations. The March 1998 regulations provide that the provisions of the January 1998 regulations will apply for consolidated return years for which the due date (without extensions) of the income tax return is after March 13, 1998. In lieu of applying this effective date, however, the March 1998 regulations permit a consolidated group to choose to apply the effective date provisions under the January 1998 regulations. The March 1998 regulations provide that taxpayers making this choice must apply all those effective date provisions for all relevant years. Thus, under the March 1998 regulations, taxpayers are not permitted to apply one provision of the January 1998 regulations (e.g., the general business credit effective date) without applying all the other provisions (e.g., the foreign tax credit effective date).

On May 7, 1998, a public hearing was held regarding the proposed January and March regulations. At the hearing and in written submissions, commentators expressed concern regarding the effective dates contained in the January 1998 and March 1998 regulations with respect to the overall foreign loss account provisions of §1.1502-9T. The commentators' principal concern was that these effective dates resulted in adverse tax consequences not anticipated by taxpayers with respect to

business transactions that occurred prior to the issuance of the January 1998 regulations. Treasury and the IRS now believe that certain of these consequences are inappropriate.

Accordingly, on August 14, 1998, Treasury and the Service issued Notice 98-40 (1998-35 I.R.B. 7), announcing their intent to issue regulations providing relief from the application of §1.1502-9T (the overall foreign loss account provisions) for consolidated return years beginning before January 1, 1998.

#### **Explanation of Provisions**

As announced in Notice 98-40, taxpayers are permitted to elect not to apply §1.1502-9T(b)(1)(v) to consolidated return years beginning before January 1, 1998. Section 1.1502-3T(c)(4) is amended to clarify that a taxpayer that chooses under the March 1998 regulations to apply the effective date provisions under the January 1998 regulations may also make the election referred to in Notice 98-40.

To make the election, a taxpayer must write "Election Pursuant to Notice 98-40" across the top of page 1 of an original or amended tax return for each consolidated return year subject to the election. For the first consolidated return year to which the overall foreign loss provisions of §1.1502-9T apply (i.e., the first year beginning on or after January 1, 1998), such taxpayer must write "Notice 98-40 Election in Effect in Prior Years" across the top of page 1 of the consolidated tax return for that year. For purposes of applying §1.1502-9T with respect

to such year, any member with a balance in an overall foreign loss account from a separate return limitation year on the first day of such year shall be treated as joining the group on such first day.

### **Special Analyses**

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations do not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that these regulations principally affect corporations filing consolidated federal income tax returns that have overall foreign losses from separate return limitation years. Available data indicates that many consolidated return filers are large companies (not small businesses). In addition, the data indicates that an insubstantial number of consolidated return filers that are smaller companies have overall foreign losses. Presumably, even fewer of these filers have overall foreign loss accounts that are subject to the separate return limitation year rules. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. It has also been determined that under section 553(d) of the Administrative Procedure Act (5 U.S.C. chapter 5) these regulations should be effective immediately because they involve the applicability of regulations that modify

the limitations on the use of certain tax attributes for taxable years for which a return is due after March 13, 1998. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking accompanying these regulations is being sent to the Small Business Administration for comment on its impact on small businesses.

#### **Drafting Information**

The principal author of these regulations is Trina Dang of the Office of Associate Chief Counsel (International). However, other personnel from the IRS and Treasury participated in their development.

#### **List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

#### **Adoption of Amendments to the Regulations**

Accordingly, 26 CFR part 1 is 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 \* \* \*

Par. 2. Section 1.1502-3T is amended by removing the last sentence of paragraph (c)(4) and adding two sentences in its place to read as follows:

§1.1502-3T Consolidated investment credit (temporary).

\* \* \* \* \*

(c) \* \* \*

(4) \* \* \* A consolidated group making this choice generally must apply all such paragraphs for all relevant years. However, a consolidated group making the election provided in §1.1502-9T(b)(1)(vi) (electing not to apply §1.1502-9T(b)(1)(v) to years beginning before January 1, 1998) may nevertheless choose to apply all such paragraphs other than §1.1502-9T(b)(1)(v) for all relevant years.

\* \* \* \* \*

Par. 3. In §1.1502-9, paragraph (a) is amended by revising the last two sentences to read as follows:

§1.1502-9 Application of overall foreign loss recapture rules to corporations filing consolidated returns.

(a) \* \* \* See §1.1502-9T(b)(1)(v) for the rule that ends the separate return limitation year limitation for consolidated return years for which the due date of the income tax return (without extensions) is after March 13, 1998, and §1.1502-9T(b)(1)(vi) for an election to continue the separate return limitation year limitation for consolidated return years beginning before January 1, 1998. See also §1.1502-3T(c)(4) for an optional effective date rule (generally making the rules of paragraphs (b)(1)(iii) and (iv) of this section inapplicable for a consolidated return year beginning after December 31, 1996, if the due date of the income tax return (without extensions) for such year is on or before March 13, 1998).

\* \* \* \* \*

Par. 4. Section 1.1502-9T is amended by revising paragraph (b)(1)(v) and adding paragraph (b)(1)(vi) to read as follows:

§1.1502-9T Application of overall foreign loss recapture rules to corporations filing consolidated returns (temporary).

\* \* \* \* \*

(b)(1)(v) Special effective date for SRLY limitation.

Except as provided in paragraph (b)(1)(vi) of this section, §1.1502-9(b)(1)(iii) and (iv) apply only to consolidated return years for which the due date of the income tax return (without extensions) is on or before March 13, 1998. For consolidated return years for which the due date of the income tax return (without extensions) is after March 13, 1998, the rules of §1.1502-9(b)(1)(ii) shall apply to overall foreign losses from separate return years that are separate return limitation years. For purposes of applying §1.1502-9(b)(1)(ii) in such years, the group treats a member with a balance in an overall foreign loss account from a separate return limitation year on the first day of the first consolidated return year for which the due date of the income tax return (without extensions) is after March 13, 1998, as a corporation joining the group on such first day. An overall foreign loss that is part of a net operating loss or net capital loss carryover from a separate return limitation year of a member that is absorbed in a consolidated return year for which the due date of the income tax return (without extensions) is after March 13, 1998, shall be added to the appropriate



consolidated overall foreign loss account in the year that it is absorbed. For consolidated return years for which the due date of the income tax return (without extensions) is after March 13, 1998, similar principles apply to overall foreign losses when there has been a consolidated return change of ownership (regardless of when the change of ownership occurred). See also §1.1502-3T(c)(4) for an optional effective date rule (generally making this paragraph (b)(1)(v) applicable to a consolidated return year beginning after December 31, 1996, if the due date of the income tax return (without extensions) for such year is on or before March 13, 1998).

(vi) Election to defer application of special effective date. A consolidated group may elect not to apply paragraph (b)(1)(v) of this section to consolidated return years beginning before January 1, 1998. To make this election, a consolidated group must write "Election Pursuant to Notice 98-40" across the top of page 1 of an original or amended tax return for each consolidated return year subject to the election. For the first consolidated return year to which the overall foreign loss provisions of paragraph (b)(1)(v) of this section apply (i.e., the first year beginning on or after January 1, 1998), such consolidated group must write "Notice 98-40 Election in Effect in Prior Years" across the top of page 1 of the consolidated tax return for that year. For purposes of applying §1.1502-9(b)(1)(ii) with respect to such year, any member with a balance in an overall foreign loss account from a separate return

limitation year on the first day of such year shall be treated as joining the group on such first day.

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Robert E. Wenzel

Deputy Commissioner of Internal Revenue

Approved:

Donald C. Lubick

Assistant Secretary of the Treasury