

TAX SECTION

New York State Bar Association

Letter on Elimination of the SRLY Regulations

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TAX SECTION

New York State Bar Association

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December 10, 1996

Hon. Donald C. Lubick
 Acting Assistant Secretary (Tax Policy)
 Department of the Treasury
 1500 Pennsylvania Avenue, N.W.
 Washington, D.C. 20220

Hon. Margaret M. Richardson
 Commissioner
 Internal Revenue Service
 1111 Constitution Avenue, N.W.
 Washington, D.C. 20224

Re: Elimination of the SRLY Regulations

Dear Secretary Lubick and Commissioner Richardson:

We write to urge the Treasury Department and Internal Revenue Service to initiate a project to eliminate from the consolidated return regulations the "separate return limitation year" ("SRLY") rules.¹ The SRLY rules are among the most voluminous and complex set of regulations ever issued: in re-proposed and temporary form they number more than 300 pages.

¹ A brief history of the SRLY rules is attached as an appendix to this letter. Robert A. Jacobs and David S. Miller provided substantial assistance in the preparation of this letter.

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Because the SRLY rules are, in our experience, easily avoided and because the legislative changes made to Code section 382 in 1986 render the SRLY rules largely redundant, we urge their elimination.

We have previously recommended the SRLY rules be eliminated.² We now understand there may be renewed receptivity within the Treasury and the IRS to do just that,³ to help achieve the broader goal of tax simplification. This letter summarizes the reasons that have been advanced for retaining the SRLY rules and why we believe they, nevertheless, should be eliminated.

After a loss corporation joins a consolidated group, the SRLY rules prevent the loss corporation's pre-existing net operating losses ("NOLs") from offsetting the income produced by the old members of the consolidated group. Code section 382, which imposes an annual limitation on the ability of a corporation to use its NOLs and built-in losses following an ownership change, is generally broader in scope, but limits, rather than prohibits NOL utilization, in most cases

² See NYSBA Tax Section, Committee on Consolidated Returns, "Report on Proposed Regulations Under Sections 1.1502-15, -21 and -22" (December 13, 1991) available at 91 TNT 258-31 (December 20, 1991) (LEXIS, FEDTAX library, TNT file); NYSBA Tax Section, Committee on Net Operating Losses, "Supplemental Report on Section 382" (February 22, 1988), available at 88 TNT 42-37 (LEXIS, FEDTAX library, TNT file); NYSBA Tax Section, Committee on Net Operating Losses, "Report on the Net Operating Loss Provision of the House-Passed Version of H.R. 3838," 31 Tax Notes 1217 (June 23, 1986).

³ See 96 TNT 195-5 (Oct. 4, 1996) (LEXIS, FEDTAX library, TNT file).

where the SRLY rules would apply.⁴ As a result, when the stock of a corporation or consolidated group with NOLs is acquired in a transaction that causes an "ownership change" under Code section 382, the losses may be subject to both Code section 382 and the SRLY rules. Section 382 will allow the NOLs to be used to the extent of the annual limitation; the SRLY rules will permit the NOLs allowed to be used under Code section 382 to offset only the income of the acquired corporation or group (and not that of the acquiring corporation or group).

Three possible reasons have been suggested to justify retaining the SRLY rules. First, the legislative history accompanying the Tax Reform Act of 1986 (the "1986 Act"), which act extensively rewrote and strengthened Code section 382, contemplated the retention of the SRLY rules.⁵ However, the reference to the SRLY rules in the 1986 Act legislative history appears under the heading "Anti-abuse rules"⁶ and should be understood simply as stating that the amendments to Code section 382 did not repeal the SRLY rules.⁷ The

⁴ As amended in 1986, Code section 382 "attempts to permit the use of a loss corporation's net operating losses, following [an ownership change]... to the same extent, as to both timing and amount as would have been possible if ownership of the loss corporation had not changed...." Statement of Ronald A. Pearlman, Deputy Assistant Secretary (Tax Policy), Department of Treasury, S. Hrs. 556, 98th Cong., 1st Sess. (1983). The limited situations in which the SRLY rules apply in the absence of an ownership change under Code § 382 are addressed below

⁵ S. Rep. No. 313, 99th Cong., 2d Sess. 233 (1986) ("Senate Report").

⁶ Id.

⁷ The Senate Report states: "In addition, the committee bill retains the present law rules that are intended to limit tax-motivated acquisitions of loss corporations (e.g., section 269, relating to acquisitions to evade or avoid taxes, and the regulatory SRLY and CRCO rules)." Id

drafters did not express a belief that continuation of the SRLY rules was necessary to prevent abuse. Thus, the reference to the SRLY rules in the legislative history cannot fairly be read to reflect a Congressional mandate to retain them. Moreover, the same sentence of the Senate Report refers to the consolidated return change of ownership ("CRCO") rules, which reference did not discourage the Treasury and the IRS from repealing those rules.⁸

Second, neither the SRLY rules nor Code section 382 prohibits a loss company's NOLs and built-in losses from offsetting the income of an acquiror into which the loss company merges, although Code section 382 subjects the future use of those losses to an annual limitation. By contrast, the SRLY rules apply in addition to Code section 382 to effect an absolute prohibition against the NOLs of one corporation (or subgroup) offsetting the income of another stand alone corporation (or group). While this distinction between an asset and stock acquisition could reflect a

⁸ Id., see also S. Rep. No. 47, 99th Cong., 1st Sess. 56-57 (1985) (prior version of legislation would have directed the Secretary "to consider what changes, if any, would be necessary and appropriate to the consolidated return regulations in view of the . modification to sections 382. . ."); see also American Law Institute, ALI Federal Income Tax Project, Subchapter C Proposals at 200-301 (1980) (recommending elimination of SRLY rules).

deliberate policy judgment,⁹ we find no evidence of that intent.

The purposes underlying the SRLY rules and Code section 382 are identical: to prevent loss trafficking.¹⁰ In 1986, Congress made the policy judgment that an annual limitation on the use of losses to offset unrelated income, as opposed to disallowance of the losses entirely, is sufficient to prevent loss trafficking.¹¹ No rational policy basis compels application of the SRLY rules to impose a more stringent NOL utilization restriction for stock acquisitions by a consolidated group than Congress thought necessary for asset acquisitions. We are aware of no principled distinction between a stock acquisition by an acquiring consolidated group and an asset acquisition by a single corporate acquiror in this context. Because the SRLY rules can be avoided or minimized by merging the loss company into a profitable member of the acquiror's

⁹ Senate Report at 230 (approving of the concept of NOLs to "smooth out the distortions caused by the annual accounting system" but disapproving of the transfer of NOLs in "a way that permits a loss to offset unrelated income"). Arguably, any use of a loss corporation's NOLs by an acquiror group is the use of a loss to offset unrelated income in a manner that is not necessary to smooth out the distortions caused by the annual accounting system. But, that application completely ignores the expressed desire to achieve "neutrality" in the case of a loss corporation that sustains an ownership change.

¹⁰ See *Woolford Realty Co. v. Rose*, 286 U.S. 319 (1932).

¹¹ See Joint Committee on Taxation, "General Explanation of the Tax Reform Act of 1986, JCS 10-87 at 295-96 (1987). "The limitation on earnings approach is intended to approximate the results that would occur if a loss corporation's assets were combined with those of a profitable cooperation in a partnership." "[In general] the loss corporation's share of the partnership's income would be limited to earnings generated by the assets contributed by the loss corporation." *Id.*

group, retention of the SRLY rules discriminates only against entities that, for regulatory or other business reasons, cannot or do not merge the loss company into profitable entities.¹²

Finally, the SRLY rules arguably serve a valid purpose in situations where Code section 382 does not apply to limit the use of the pre-acquisition NOLs of a loss company that joins a consolidated group. For example, if an acquiror group's long-standing ownership of a loss company increases from 60% to 100%, Code section 382 would not apply because no "ownership change" would have occurred. Absent SRLY rules, the loss company's NOLs could offset the acquiror group's subsequent unrelated income without limitation. The 40% change in ownership falls below the threshold Congress determined appropriate to trigger the limitations on loss utilization provided by Code sections 382 and 269. No Congressionally expressed policy demands loss utilization limitation where the continuing ownership of the loss company is 50 percent or more. Second, even were the SRLY rules continued, their impact could be avoided by merging the target into a profitable member of the acquiror's group. Finally, even if the scope of the SRLY rules were restricted to situations where Code section 382 did not apply, it would be necessary to retain the entire bulk of the regulations with all of their complexities to deal with these limited cases - cases that in practice do not arise because of the

¹² We note that the merger of an acquired company into a single-member limited liability company owned by the acquiring company or an affiliate would allow continuation of a liability-limiting entity for non-tax purposes even though asset liquidation will result for federal income tax purposes. Planning opportunities such as this further erode the distinction between stock and asset acquisitions.

merger by-pass discussed in the preceding sentence. In short, we do not believe this small category of transactions warrants retaining the complex and largely ineffective SRLY rules.

Abandoning SRLY would permit considerable simplification, eliminate hundreds of pages of daunting regulations, obviate the consuming task (on the part of taxpayers and the government) of mastering and applying these rules, and avoid inevitable disputes over their application – all without jeopardizing policy or significant revenues.¹³ Eliminating the SRLY rules would advance the “single entity” theory reflected in the consolidated return regulations and would reconcile them with Code section 382, which, as discussed, is based on the analogue of combining the assets of the loss and profit corporations in a partnership. The consolidated return “single entity” model and Code section 382 analogue are frustrated by the SRLY rules because the SRLY rules retain the rigid framework of separate corporations when the loss company is acquired by the consolidated group as a subsidiary, rather than being merged into a constituent member of the group.

If the Treasury and the Service do eliminate the SRLY rules, we recommend that repeal be retroactive to the effective date of the 1986 Act (or possibly for consolidated return years ending on or after January 29, 1991, which is the effective date of the Code section 382 consolidated return regulations). We further recommend the repeal of the CRCO rules have the same

¹³ We also encourage the Treasury and the Service to consider a project to simplify the section 382 consolidated return regulations.

effective date. Otherwise, the repeal of the SRLY and CROCO rules will carry with them difficult transition and coordination issues, requiring the enforcement of rules that, after the 1986 Act, have no policy basis.

We would be pleased to assist the Treasury and the IRS in this effort. Please let me know if we can be of help.

Respectfully submitted

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APPENDIX

A Brief History of the SRLY Rules

This Appendix provides a brief history of the SRLY rules.¹ As originally promulgated, the SRLY rules acted as a limitation – not an absolute prohibition – on the use of the separate return NOLs of a new member of a consolidated group by the old members. After the enactment of new Code section 382 in 1986, the SRLY rules have become redundant, operating only in limited and frequently questionable circumstances, since Code section 382 is available to provide the appropriate tax policy result.

The 1928 Regulations.

The first version of the SRLY rules, promulgated in 1928 as Article 41 of Regulations 75, did not impose an absolute bar against a consolidated group using the carryover losses of a newly-acquired corporation to offset other group members' income, but instead limited the acquiror group's use of the target's losses to the acquiror's tax basis in the stock of the loss company.²

¹ This summary refers genetically to the rules as the "SRLY rules" even though the term "separate return limitation year" was first used in the 1966 regulations.

² The regulations provided:

A net loss sustained by a corporation prior to the date upon which its income is included in the consolidated return of an affiliated group (including any net loss sustained prior to the taxable year 1929) shall be allowed as a deduction in computing the consolidated net income of such group in the same manner to the same extent, and upon the same conditions as if the consolidated income were the income of such corporation; but in no case in which the affiliated status is created after January 1, 1929, will any such net loss be allowed as a deduction in excess of the cost or the aggregate basis of the stock of such corporation owned by the members of the group.

The rule was retained in Regulations 78, Article 41(c) (1931).

Subsequent to the promulgation of Article 41 of Regulations 75, but in a case involving a taxable year (1927) before the regulations' effective date (1929), the Supreme Court adopted a SRLY-type principle. In *Woolford Realty Co. Inc. v. Rose*,³ after the taxpayer acquired the Piedmont Savings Company in 1927, the two companies filed a consolidated return in that year. Piedmont had suffered losses in 1925 and 1926, and while Piedmont had not achieved profitability in 1927, the taxpayer did have taxable income in that year from which it attempted to deduct Piedmont's carryover losses from the prior two years. Based in part on an interpretation of the relevant statutory sections,⁴ Justice Cardozo held that the losses sustained by Piedmont during the years in which it was not a member of the taxpayer's consolidated group could not be used to offset the taxpayer's income (but would be allowable to the extent of Piedmont's income).

³ 286 U.S. 319 (1932), aff'g 53 F.2d 821 (5th Cir. 1931), aff'g 44 F.2d 856 (N.D. Ga. 1930); see also *Planters Cotton Oil Co. v. Hopkins*, 286 U.S. 332 (1932) (same as *Woolford*). *Woolford* was consistent with several lower court decisions. See *Commissioner v. Ben Ginsburg Co., Inc.*, 54 F.2d 238 (2d Cir. 1931) (same as *Woolford*), see also *Sweets Co. of America, Inc. v. Commissioner*, 40 F.2d 436 (2d Cir. 1930) (losses after affiliation ended may not be carried back to offset consolidated group income). *Contra*, *National Slag Co. v. Commissioner*, 47 F.2d 846 (3d Cir. 1931) (losses sustained in year preceding affiliation may offset income of consolidated group in subsequent year).

⁴ Section 206(b) of the Revenue Act of 1926 provided for a two-year carryover of losses to be allowed "as a deduction in computing the net income of the taxpayer." Section 234 provided that in computing the net income of corporations filing a consolidated return, deductions would be allowed for "[l]osses sustained during the taxable year." The Court interpreted section 206(b) as limiting deductions for losses sustained before a consolidated return is filed to the net income "of the taxpayer" (and not other members of the group) and interpreted section 234 as permitting the group to deduct only the "losses sustained during the taxable year" by members of the group in that year.

A different ruling would mean that a prosperous corporation could buy the shares of one that had suffered heavy losses and wipe out thereby its own liability for taxes.⁵

Under present Code section 382, the mischief envisioned by Justice Cardozo could not be perpetrated.

The Revenue Act of 1934.

In 1934, apparently in an effort to raise additional revenue, Congress abolished the privilege of filing consolidated returns, except for railroad corporations.⁶

The Second Revenue Act of 1940.

In 1940, Congress imposed consolidated returns on a mandatory basis on all corporations for excess profit tax purposes. However, only railroad (and later trolley car) companies were permitted to file consolidated returns for normal tax purposes. In addition, Congress expressly authorized regulations that would permit the Commissioner to clearly reflect excess profits tax liability "both during and after the period of affiliation."⁷

J.D. & A.B. Spreckels Company v. Commissioner (1940) and Built-in Losses.

⁵ Woolford, 286 U.S. at 329-30. Justice Cardozo noted that while Article 41 of Regulations 75 was not applicable to the taxpayer in Woolford (because it was effective for tax years beginning in 1929 and only tax year 1927 was at issue in Woolford), the tax policy behind it was identical to that applied in Woolford: "The provision in this regulation limiting the deduction to the cost or value of the stock will make it profitless hereafter to purchase stock for the purposes of gaining the benefit of deductions in excess of what is paid." Woolford, 286 U.S. at 331.

⁶ See section 141 of the Revenue Act of 1934; see generally J.S. Seidman, Seidman's Legislative History of Federal Income Tax Laws 1938-1861 376-380 (1938). The elimination of consolidated returns was perceived to be especially effective in raising revenue because the ability to carryover net losses was eliminated in the Revenue Act of 1932.

⁷ See 1940-2 C.B. 468 (statutory language) and 558-59 (legislative history).

In *J.D. & A.B. Spreckels Company v. Commissioner*,⁸ the taxpayer purchased from a related party for one dollar all the stock of a target corporation after the target had contracted to sell its plant to an unrelated purchaser at a loss. The taxpayer and the target filed a consolidated return in 1933, the year the sale closed. The taxpayer claimed the target's "built-in loss" on the sale of the plant as a deduction on the consolidated return. The Board of Tax Appeals found that the target's loss on the sale of its plant was readily ascertainable when the taxpayer acquired the target and that the acquisition "served no business purpose." Relying on *Woolford*, the court held on these facts that the target corporation would not be treated as a member of the taxpayer's consolidated group during the year the loss was sustained.

If Congress did not intend that the privilege of making a consolidated return should be enjoyed by a corporation which acquired ownership of another corporation in order to take advantage of a loss already sustained by that corporation [as the Supreme Court held in *Woolford*], it seems to follow that Congress did not intend that the privilege should be enjoyed by a corporation which acquired the ownership of another corporation in order to take advantage of a loss certain to be sustained by that corporation in the immediate future, particularly where the acquisition of the ownership of the other corporation served no business purpose.⁹

Recurrence of an abuse like that at issue in *Spreckels* would be prevented by Code section 269(a) or, if section 269(a) were for any reason inapplicable, by Code section 382(c)(1), which would permit no utilization of the loss corporation's built-in losses after the acquisition due to failure to continue the corporation's business enterprise for at least two years. The background of section 269 is discussed *infra*.

The 1941 and 1942 Regulations.

⁸ 41 B.T.A. 370 (1940).

⁹ *Spreckels*, 41 B.T.A. at 378.

In 1941, Treasury promulgated excess profits tax regulations adopting a Woolford- type SRLY rule, prohibiting any separate return losses from offsetting income of another member of the group.¹⁰ These regulations did not impose any limitation on the use of built-in losses. Amendments to the consolidated return portion of regulations 104 were made in 1942 to conform the normal tax consolidated return SRLY rules to the analogous excess profit tax rules.¹¹ The new regulations were effective for taxable years beginning after December 31, 1940.

The Revenue Act of 1942.

The 1942 Act restored the privilege of filing consolidated for normal tax purposes for all domestic affiliated corporations (and made consolidated returns optional for excess profit tax purposes).¹²

The Revenue Act of 1943 and the Predecessor to Section 269.

Responding to the Spreckels case and transactions in which corporations with large excess profits purchased corporations with "current, past, or prospective losses, deficits, or large current or unused excess-profits credits for the purpose of reducing excess profits and income taxes," Congress, in 1943, enacted the predecessor to section 269 to disallow "deductions, credits and other allowances obtained in an acquisition undertaken for the principal purpose of evading or avoiding federal income or

¹⁰ Regulations 110, section 33.31(b)(3)-(7) (1941), 1941-1 C.B. 54-57.

¹¹ T.D. 5127, 1942-1 C.B. 121, 124 (section 23.31(d)(3)-(6)).

¹² See generally, 1942-2 C.B. 603-05; J.S. Seidman, Seidman's Legislative History of Federal Income and Excess Profits Tax Laws 1953-1939 2034-37 (1954) (hereinafter, Seidman 1953-1939").

excess profits taxes."¹³ The legislative history specifically referenced transactions such as that in Spreckels as "violating in those cases the basic policies of the deduction provisions . . . and . . . the consolidated returns provisions."¹⁴

The 1944 Regulations.

Regulations 104 and 110, as amended on March 14, 1944, added a SRLY-type limitation (retroactive to March 14, 1941) applicable to four categories of built-in deductions of subsidiaries and subgroups of subsidiaries that were affiliated, but not consolidated, with the group on March 14, 1941, and of newly acquired subsidiaries.¹⁵ While the limitation was absolute in the case of existing affiliated subsidiaries and subgroups,¹⁶ in the case of newly-acquired subsidiaries, these deductions were subject to limitation only if they were "attributable to events preceding" the joining of the consolidated group. Moreover, these rules did not apply if the new subsidiary (or every member of the subgroup) was created by the consolidated group or, since March 14, 1941, 95% ownership was held in the subsidiary or each member of the subgroup "directly or indirectly by substantially the same interests."¹⁷ The Commissioner was also granted discretion to not apply the rules in appropriate cases. The built-in loss rules of Code section 382(h) are a successor to these earlier rules, and

¹³ Section 129(a) of the 1939 Code, as amended.

¹⁴ S. Rep. 627, 78th Cong., 1st Sess. (1943), reprinted in, Seidman 1953-1939 at 1971.

¹⁵ Regulations 104, section 23.3 1(d)(11), 1944 C.B. 298. These categories were (i) capital losses, (ii) involuntary conversions and section 1231-type items, (iii) worthless stock and bond deductions for 95% subsidiaries (in 1944, the consolidation threshold was 95%), and (iv) bad debts.

¹⁶ The limitation permitted the losses of members of the subgroup to offset income of other members of the subgroup, but did not permit SRLYed losses of the subgroup to offset the group's income.

¹⁷ Thus, these rules did not impose limitations where an individual had one of two old and cold wholly-owned corporations acquire the other.

obviously would remain in effect notwithstanding any repeal of the SRLY regulations.

1955 Regulations.

Regulations section 1.1502-31(b)(9) was promulgated on August 29, 1955. This section was identical in all respects to the 1944 rules, except the date January 1, 1954, replaced March 14, 1941.¹⁸ The apparent effect of this rule was to grant an amnesty from the SRLY limitation on built-in losses for all groups that began filing consolidated returns between March 15, 1941 and December 31, 1953.

1966 Regulations.

On September 8, 1966, the SRLY rules were further amended. The regulations continued the policy reflected in the 1955 regulations that, so long as loss trafficking or other tax abuse was not possible, a consolidated group should be permitted to offset its income with the prior losses of a new member. Thus, if a corporation filing separate returns for a taxable year was a member of the same "affiliated group" as the consolidated group (but did not join that group) and did not elect a multiple surtax election in that year¹⁹ then, upon joining the consolidated group, carryover losses incurred by the new member in its separate return year would be permitted to offset the group's income.

¹⁸ Regulations 129 replaced regulations 104 for taxable years ending after December 31, 1949. 1952-C.B. 161. They reflected the amalgamation of the normal income tax and the excess profits tax but in other respects were substantially similar. See also T.D. 5915, 1952-2 C.B. 148.

¹⁹ Under the law at the time, a surtax was imposed on corporations. An affiliated group was permitted one \$25,000 surtax exemption, but under certain circumstances an affiliated - but not consolidated - corporation could benefit from another surtax exemption. Multiple surtax exemptions were perceived as an abuse the SRLY limitations could discourage.

Under the 1955 regulations, the consolidated NOLs of an existing group could offset future profits of a newly-acquired member. However, since 1944 an unaffiliated loss corporation could not use its losses to offset income of a newly-acquired corporation with which it began to file consolidated returns.²⁰ The 1966 regulations introduced consistency in result by adopting the "lonely parent rule" which permits the separate losses of an unaffiliated acquiror to offset a target's income with which it consolidated.²¹ Drafters of this rule could express no policy reason for the liberalization except to note that the same result would apply in a merger of the profitable target into the loss company, and the SRLY rules should not draw a distinction between a stock and asset purchase.²² Curiously, this reasoning was not recognized as a basis to scrap the SRLY concept in its entirety.

Finally, the 1966 regulations in some respects tightened, and in other respects liberalized, the scope of the built-in loss rules. First, built-in losses were expanded to include all deductions or losses recognized for tax purposes in a consolidated return year, but which economically accrued in a SRLY.²³ However, the regulations exempted from this rule built-in losses of a corporation that had been a member of the affiliated group for 10 years prior to the date of the loss (regardless of when the loss asset was acquired) and provided a de minimis rule under which the use of a target's built-in losses would not be subject to limitation if the adjusted basis of the corporation's loss assets

²⁰ See Regulations 104, section 23.31(d)(1)(vi), 1944 C.B. 295.

²¹ This ability was limited to acquisitions that did not trigger the "consolidated return change in ownership" ("CRCO") rules that were also introduced in the 1966 regulations.

²² See Irving Salem, "How to use net operating losses effectively under the new consolidated return regulations," 26 J. Taxation 270, 272 (1967).

²³ For this purpose, if the fair market value of an asset was less than its tax basis on the date the subsidiary became a member of the consolidated group, then the difference was treated as a built-in loss upon sale of the asset, as were depreciation deductions attributable to the difference.

did not exceed their fair market value by more than 15% (excluding cash, goodwill and certain other marketable securities).²⁴

The 1972 Regulations.

The 1972 regulations²⁵ made certain technical corrections to the built-in loss rules but did not substantively change the concepts.²⁶

The Code Section 382 Revisions (1986).

In 1986, Congress substantially revised and tightened Code section 382 to prevent loss trafficking utilizing an objective standard. The amendments to Code section 382, in 1986, effectively eliminated the principal exclusions from Code section 382 application,²⁷ the continuing business exception of Code section 382(a) and the triangular acquisition permitted under Code section 382(b). The conceptual underpinnings of the new statute are discussed in greater detail in the letter to which this Appendix is attached.

1991 Regulations.

The regulations first proposed in 1991 (and now existing in temporary form) eliminated the CRCO rules and liberalized the

²⁴ Treas. Reg. §1.1502-15(a)(2) (1966).

²⁵ T.D. 7246 (December 29, 1972).

²⁶ For example, the 1972 exception to the built-in loss rules require that the group have acquired the specific assets (and not the corporation holding them) more than ten years prior to the year in which the loss was recognized. In addition, the definition of marketable security was modified.

²⁷ See discussion of "Present Law" in S. Rep. 313, 99th Cong., 2d Sess., "Tax Reform Act of 1986 to accompany H.R. 3838 at 224-230 (1986).

SRLY rules, or otherwise conformed them to Code section 382, in three major respects: first, under the SRLY rules in force at the time, SRLYed losses existing in a particular year could offset only the loss corporation's income earned that year. The 1991 regulations permitted unused SRLYed losses to be used in any year to the extent they do not exceed the loss corporation's cumulative contribution to consolidated taxable income from the date it became a group member. This rule generally reduces the SRLY taint at a faster rate, although in certain circumstances it could be disadvantageous.²⁸

Second, under the 1991 regulations, the SRLY limitation may be applied to a subgroup of corporations that joins a consolidated group, as if the subgroup were a separate entity. This rule is similar to the subgroup built-in loss rule introduced in the 1944 regulations, and tends to increase utilization of SRLYed losses.

Finally, the 1991 regulations revised the rules for built-in losses to conform them more closely to section 382. Thus, for example, the de minimis rule was conformed to the analogous Code section 382 de minimis rule and the recognized built-in loss period was reduced from ten to five years to conform to Code section 382.

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²⁸ If a loss corporation joins a profitable group and has a loss year and then a profitable year, the SRLY limitation is lower under the 1991 regulations than previously.