

§ 5.1502-45 Limitation on losses to amount at risk.

(a) *In general*—(1) *Scope*. This section applies to a loss of any subsidiary if the common parent's stock meets the stock ownership requirement described in section 465(a)(1)(C).

(2) *Limitation on use of losses*. Except as provided in paragraph (a)(4) of this section, a loss from an activity of a subsidiary during a consolidated return year is includible in the computation of consolidated taxable income (or consolidated net operating loss) and consolidated capital gain net income (or consolidated net capital loss) only to the extent the loss does not exceed the amount that the parent is at risk in the activity at the close of that subsidiary's taxable year. In addition, the sum of a subsidiary's losses from all its activities is includible only to the extent that the parent is at risk in the subsidiary at the close of that year. Any excess may not be taken into account for the consolidated return year but will be treated as a deduction allocable to that activity of the subsidiary in the first succeeding taxable year.

(3) *Amount parent is at risk in subsidiary's activity*. The amount the parent is at risk in an activity of a subsidiary is the lesser of (i) the amount the parent is at risk in the subsidiary or (ii) the amount the subsidiary is at risk in the activity. These amounts are determined under paragraph (b) of this section and the principles of section 465. See section 465 and the regulations thereunder and the examples in paragraph (e) of this section.

(4) *Excluded activities*. The limitation on the use of losses in paragraph (a)(2) of this section does not apply to a loss attributable to an activity described in section 465(c)(3)(D).

(5) *Substance over form*. Any transaction or arrangement between members (or between a member and a person that is not a member) which does not cause the parent to be economically at risk in an activity of a subsidiary will be treated in accordance with the substance of the transaction or arrangement notwithstanding any other provision of this section.

(b) *Rules for determining amount at risk*—(1) *Excluded amounts*. The amount a parent is at risk in an activity of a

subsidiary at the close of the subsidiary's taxable year does not include any amount which would not be taken into account under section 465 were the subsidiary not a separate corporation. Thus, for example, if the amount a parent is at risk in the activity of a subsidiary is attributable to nonrecourse financing, the amount at risk is not more than the fair market value of the property (other than the subsidiary's stock or debt or assets) pledged as security.

(2) *Guarantees*. If a parent guarantees a loan by a person other than a member to a subsidiary, the loan increases the amount the parent is at risk in the activity of the subsidiary.

(c) *Application of section 465*. This section applies in a manner consistent with the provisions of section 465. Thus, for example, the recapture of losses provided in section 465(e) applies if the amount the parent is at risk in the activity of a subsidiary is reduced below zero.

(d) *Other consolidated return provisions unaffected*. This section limits only the extent to which losses of a subsidiary may be used in a consolidated return year. This section does not apply for other purposes, such as §§ 1.1502-32 and 1.1502-19, relating to investment in stock of a subsidiary and excess loss accounts, respectively. Thus, a loss which reduces a subsidiary's earnings and profits in a consolidated return year, but is disallowed as a deduction for the year by reason of this section, may nonetheless result in a negative adjustment to the basis of an owning member's stock in the subsidiary or create (or increase) an excess loss account.

(e) *Examples*. The provisions of this section may be illustrated by the examples in this paragraph (e). In each example, the stock ownership requirement of section 465(a)(1)(C) is met for the stock of the parent (P), and each affiliated group files a consolidated return on a calendar year basis and comprises only the members described.

Example (1). In 1979, P forms S with a contribution of \$200 in exchange for all of S's stock. During the year, S borrows \$400 from a commercial lender and P guarantees \$100 of the loan. S uses \$500 of its funds to acquire a motion picture film. S incurs a loss of \$120

for the year with respect to the film. At the close of 1979, the amount P is at risk in S's activity is \$300. If S has no gain or loss in 1980, and there are no contributions from or distributions to P, at the close of 1980 P's amount at risk in S's activity will be \$180.

Example. (2). P forms S-1 with a capital contribution of \$1 on January 1, 1980. On February 1, 1980, S-1 borrows \$100 with full recourse and contributes all \$101 to its newly formed subsidiary S-2. S-2 uses the proceeds to explore for natural oil and gas resources. S-2 incurs neither gain nor loss from its explorations during the taxable year. As of December 31, 1980, P is at risk in the exploration activity of S-2 only to the extent of \$1.

(f) *Effective date.* This section applies to consolidated return years ending on or after December 31, 1979.

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§5.1561-1 Taxable years of component members of controlled group of corporations that include December 31, 1978.

(a) *In general.* This section prescribes a regulation for applying sections 301 (a) and (b) (19), and 106, of the Revenue Act of 1978 (the Act) in the case of certain taxable years of component members of a controlled group of corporations (as defined in section 1563 of the Internal Revenue Code). The section applies only to taxable years that include December 31, 1978, and only if the taxable year of at least one component member ends in 1979.

(b) *Background.* Section 301(a) of the Act amends section 11 of the Code (relating to tax imposed on corporations) to provide for taxable income brackets that are subject to tax at rates less than the maximum rate of 46 percent. Section 301(b)(19) of the Act amends section 1561(a) of the Code (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) to limit the component members of a controlled group to an aggregate amount in each bracket which does not exceed the maximum amount in such bracket to which a corporation which is not a component member of a controlled group is entitled. Section 106 of the Act amends section 21 of the Code (relating to effect of changes in rate of tax) to provide that the amendments made by section 301 of the Act shall be treated as a change in

a rate of tax. Since the amendments made by section 301 of the Act are effective for taxable years beginning after December 31, 1978, under the amendment to section 21 the effective date of the change in rate of tax is January 1, 1979.

(c) *No apportionment plan in effect.* If no apportionment plan (see §1.1561-3 of the Income Tax Regulations) is in effect with respect to December 31, 1978, the single \$50,000 surtax exemption available before January 1, 1979, and the single bracket amounts available after December 31, 1978, shall be equally divided among the component members of the controlled group on December 31, 1978. In the case of a controlled group which includes component members that join in the filing of a consolidated return and other component members that do not join in the filing of such a return, each component member of the group (including each component member that joins in filing the consolidated return) shall be treated as a separate corporation for purposes of equally apportioning the \$50,000 surtax exemption in effect before January 1, 1979, and the bracket amounts in effect after December 31, 1978. In such a case, the surtax exemption and bracket amounts of the corporations filing the consolidated return shall be the sum of the amount apportioned to each component member that joins in filing the consolidated return.

(d) *Apportionment plan.* (1) If one or more component members of the controlled group have a calendar taxable year and if an apportionment plan is adopted under §1.1561-3 apportioning the entire \$50,000 surtax exemption available for 1978 to such calendar-year members, then the amount in each taxable income bracket available for fiscal-year members is zero. If only a part of the \$50,000 surtax exemption is apportioned to calendar-year members, then a proportionate part of the \$25,000 amount in each taxable income bracket is available for the fiscal-year members. For example, if \$30,000 ($\frac{3}{5}$ of \$50,000) is apportioned to calendar-year members, $\frac{3}{5}$ of the \$25,000 amount in each bracket, or \$10,000, as well as the remaining $\frac{2}{5}$ of the 1978 surtax exemption, is available to the fiscal-year members.