

adjustments to the shareholder member's stock of the subsidiary member that reflect income of the subsidiary member and the group's ability to use the loss recognized by another member to offset income of the subsidiary member of the group) have been enjoyed by the group.

Finally, this rule would address only cases of duplication where there have been contributions of loss property. As described above, the IRS and Treasury Department are concerned that contributions of loss property are not the only types of transactions in which a group can obtain more than one tax benefit from a single economic loss.

The IRS and Treasury Department are considering a variation of this suggested rule to address the situation where the stock loss is recognized prior to the absorption of the inside loss. This variation would allow the stock loss when recognized, but would disallow the inside losses of the subsidiary to the extent that such losses reflect losses that were duplicate losses at the time of the recognition of the stock loss. Such losses may be attributable to contributed property or losses that arose in the subsidiary member. The IRS and Treasury Department request comments regarding this variation.

Finally, the IRS and Treasury Department continue to request comments regarding any other approaches that could be implemented to address the duplication of loss within a consolidated group.

Special Analyses

In *Rite Aid Corp. v. United States*, 255 F.3d 1357 (Fed. Cir. 2001), the United States Court of Appeals for the Federal Circuit held that the duplicated loss component of § 1.1502-20 was an invalid exercise of regulatory authority. In response to the *Rite Aid* decision, the IRS and Treasury Department issued

Notice 2002-11 (2002-7 I.R.B. 526), stating that the interests of sound tax administration would not be served by the continued litigation of the validity of the duplicated loss component of § 1.1502-20. Notice 2002-11 also announced that because of the interrelationship in the operation of all of the loss disallowance factors, new rules governing loss disallowance on sales of subsidiary stock by members of consolidated groups should be implemented.

In Notice 2002-18 (2002-12 I.R.B. 644), the IRS and Treasury Department stated that regulations would be promulgated that would defer or otherwise limit the utilization of a loss on stock (or another asset that reflects the basis of stock) in transactions that facilitate the group's utilization of a single economic loss more than once. Notice 2002-18 further stated that such regulations would apply to dispositions occurring on or after March 7, 2002. These temporary regulations implement Notice 2002-18 and are necessary to provide taxpayers with immediate guidance regarding stock basis and allowable loss in connection with transfers of subsidiary member stock. Accordingly, good cause is found for dispensing with a delayed effective date pursuant to 5 U.S.C. 553(d)(3).

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations do not have a significant impact on a substantial number of small entities. This certification is based on the fact that these regulations will primarily affect affiliated groups of corporations, which tend to be larger businesses. Moreover, the number of taxpayers affected and the average burden are minimal. Therefore, a Regulatory

Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small businesses.

Drafting Information

The principle author of these regulations is Aimee K. Meacham of the Office of Chief Counsel (Corporate). 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.

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 is amended by adding entries in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *
Section 1.1502-21T(b)(1) and (b)(3)(v) also issued under 26 U.S.C. 1502. * * *
Section 1.1502-32T(a)(2), (b)(3)(iii)(C), (b)(3)(iii)(D), and (b)(4)(vi) also issued under 26 U.S.C. 1502. * * *
Section 1.1502-35T also issued under 26 U.S.C. 1502. * * *

Par. 2. In the list below, for each section indicated in the left column, remove the wording indicated in the middle column, and add the wording indicated in the right column.

Affected section	Remove	Add
§ 1.267(f)-1(k)	§§ 1.337(d)-1, §§ 1.337(d)-2, 1.1502-13(f)(6), and 1.1502-20.	§§ 1.337(d)-2T, 1.1502-13(f)(6), and 1.1502-35T.
§ 1.597-3(e)	<i>Loss disallowance.</i> For purposes of § 1.1502-20, FFA and the amount described in § 1.597-4(g)(3) are treated as an extraordinary gain disposition within the meaning of § 1.1502-20(c)(2)(i) and a Taxable Transfer is treated as an applicable asset acquisition under section 1060(c) within the meaning of § 1.1502-20(c)(2)(i)(A)(4).	[Reserved].
§ 1.597-4(g)(2)(v), second sentence.	(See §§ 1.337(d)-1 and 1.1502-20 for potential limitations on the group's worthless stock deduction).	(See §§ 1.337(d)-2T and 1.1502-35T(f) for rules applicable when a member of a consolidated group is entitled to a worthless stock deduction with respect to stock of another member of the group.)
§ 1.1502-11(b)(3)(ii) Example (c), third sentence.	See also § 1.1502-20 for rules applicable to losses from the sale of stock of subsidiaries.	See also §§ 1.337(d)-2T and 1.1502-35T for rules relating to basis adjustments and allowance of stock loss on dispositions of stock of a subsidiary member.