February 19, 2020

Hon. Charles P. Rettig
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Proposed Regulations under Section 168(k)

Dear Commissioner Rettig:

Enclosed please find comments on the Proposed Regulations under Section 168(k) of the Internal Revenue Code released on September 13, 2019. These comments are submitted on behalf of the Section of Taxation and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

The Section of Taxation would be pleased to discuss these comments with you or your staff.

Sincerely,

Tom Callahan
Chair, Section of Taxation

Hon. David Kautter, Assistant Secretary (Tax Policy), Department of the Treasury
Krishna P. Vallabhaneni, Tax Legislative Counsel, Department of the Treasury
Colin Campbell, Attorney-Advisor, Department of the Treasury
Hon. Michael J. Desmond, Chief Counsel, Internal Revenue Service
William M. Paul, Deputy Chief Counsel (Technical), Internal Revenue Service
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AMERICAN BAR ASSOCIATION
SECTION OF TAXATION

Comments on the Proposed Regulations under Section 168(k)

These comments ("Comments") are submitted on behalf of the American Bar Association Section of Taxation (the "Section") and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these comments was exercised by William Pauls, Nicole Field, Bryan P. Collins, Timothy Davis, and Sammy Evei. Significant contributions were made by William Alexander, Erik Corwin, Steve Fattman, Mark Hoffenberg, David Strong, and Thomas Wessel. These Comments have been reviewed by David Wheat, Council Director for the Corporate Tax and Affiliated & Related Corporations Committees, Eric Solomon of the Section’s Committee on Government Submissions, and Eric Sloan, Vice-Chair of Government Relations for the Section.

Although members of the Section may have clients who might be affected by the federal tax principles addressed by these Comments, no member who has been engaged by a client (or who is a member of a firm or other organization that has been engaged by a client) to make a government submission with respect to, or otherwise to influence the development or outcome of, one or more specific issues addressed by these Comments has participated in the preparation of the portion (or portions) of these Comments addressing those issues. Additionally, while the Section’s diverse membership includes government officials, no such official was involved in any part of the drafting or review of these Comments.

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Date: February 19, 2020
Executive Summary

These Comments are in response to proposed regulations released on September 13, 2019 (the “Proposed Regulations”), under section 168(k) with respect to changes made by Pub. L. No. 115-97 (the “Act”). The Act made substantial changes in the tax rules applicable to the business activities of taxpayers, generally effective as of the 2018 tax year. We commend the Department of the Treasury (“Treasury”) and the Internal Revenue Service (the “Service”) for their commitment to providing expedited guidance on these changes. We also commend Treasury and the Service for their consideration of our March 2019 comments (the “Prior Report”) on the proposed regulations under section 168(k) published on August 8, 2018 (the “August 2018 Proposed Regulations”), in connection with the publication of the final regulations under section 168(k) released on September 13, 2019 (the “Final Regulations”).

Section 168(k) provides an additional allowance for depreciation with respect to the adjusted basis of “qualified property.” Before amendment by the Act, section 168(k)(2)(A)(ii) provided that qualified property means property the original use of which commenced with the taxpayer (“Original Use Requirement”). The Act expanded the type of property subject to section 168(k); specifically, section 168(k)(2)(A)(ii), as amended by the Act, provides that “qualified property” means property meeting the Original Use Requirement or property the acquisition of which by the taxpayer meets the requirements of section 168(k)(2)(E)(ii), i.e., “used property.”

As part of this expansion of section 168(k), the Act placed restrictions on, and added requirements regarding, the acquisitions of used property that qualify for the additional allowance for depreciation under section 168(k). Section 168(k)(2)(E)(ii), as amended by the Act, provides that an acquisition of property meets these requirements if:

- Such property was not used by the taxpayer at any time prior to such acquisition (the “No Prior Use Requirement”); and

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2 Unless otherwise specified, all “section” and “§” references are to the Internal Revenue Code of 1986, as amended (the “Code”), and all “Treas. Reg. §” references are to the Treasury regulations promulgated thereunder, all as in effect (or, in the case of proposed regulations, as proposed) as of the date of this letter.


4 In particular, the Section provided the Prior Report to Treasury and the Service on March 28, 2019. The Prior Report is available on the Section’s website at: https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/032919comments.pdf


• The acquisition of such property meets the requirements of paragraphs (2)(A), (2)(B), (2)(C), and (3) of section 179(d) (the “Unrelated Purchase Requirement”).

The August 2018 Proposed Regulations addressed a number of issues raised by sections 168(k) and 179(d), which were the subject of the Prior Report. As discussed in detail below, we believe that, while the Final Regulations and the Proposed Regulations have addressed many of the issues identified in the Prior Report, further clarification and/or revision of the Proposed Regulations would meaningfully assist taxpayers in applying these provisions and avoid significant administrative issues. Specifically, we respectfully request that, in finalizing the Proposed Regulations, Treasury and the Service consider the following recommendations:

1. In order to avoid the complexities noted below in Part II.B. of the Detailed Comments, we recommend that the Deferred Sale Approach (as defined below in Part II.B. of the Detailed Comments) under the Proposed Consolidated Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(C) be revised to deem the transferor’s sale of the depreciable property to the transferee to occur on the day after the Deconsolidation Date (as defined below in Part II.A. of the Detailed Comments) pursuant to a transaction to which section 168(i)(7) does not apply for an amount equal to the transferee’s then basis in the depreciable property solely for purposes of determining whether the requirements of section 168(k) are satisfied with respect to such sale and, if satisfied, the amount, location, and timing of the transferee’s additional first-year depreciation deduction with respect to the depreciable property.

2. In keeping with the preceding recommendation, we also recommend that the Deferred Sale Approach under the Proposed Consolidated Deemed Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(D) be revised to deem old target’s sale of the depreciable property to new target to occur on the day after the Deconsolidation Date for an amount equal to new target’s then basis in the depreciable property solely for purposes of determining whether the requirements of section 168(k) are satisfied with respect to such sale and, if satisfied, the amount, location, and timing of new target’s additional first-year depreciation deduction with respect to the depreciable property.

In this regard, we noted that none of the provisions or examples from the August 2018 Proposed Regulations addressing the application of section 168(k) to consolidated groups have been included in the Final Regulations. Rather, Treasury and the Service reserved these provisions in the Final Regulations and concurrently issued the Proposed Regulations, which address the application of section 168(k) to consolidated groups.

Accordingly, (i) the transferee’s additional first-year depreciation deduction with respect to the depreciable property would be limited to the transferee’s basis in the depreciable property at the time of the deemed sale; and (ii) for all other federal income tax purposes, including the application of section 168 to depreciable property that does not qualify for the additional first-year depreciation deduction under section 168(k), the actual asset sale would be given effect as of the date that it occurs.

Accordingly, (i) new target’s additional first-year depreciation deduction with respect to the depreciable property would be limited to new target’s basis in the depreciable property at the time of the deemed sale; and (ii) for all other federal income tax purposes, including the application of section 168 to depreciable property that does not qualify for the additional first-year depreciation deduction under section 168(k), the deemed asset sale would be

(footnote continued on the next page)
3. We recommend that the 90-day Limitation (as defined below in Part III of the Detailed Comments) be removed from both the Proposed Consolidated Acquisition Rule and the Proposed Consolidated Deemed Acquisition Rule. Alternatively, if a timing limitation such as the 90-day Limitation is retained in the Consolidated Acquisition Rules, we recommend that Treasury and the Service (i) give further consideration to the commercial realities surrounding normal course business transactions; (ii) acknowledge that, in circumstances where provisions of the Code or the Treasury regulations impose a timing limitation to restrict the scope of a series of related transactions, those provisions, to a very significant degree, incorporate a much longer period of time than 90 days; and (iii) clarify the result if, in Examples 28 and 29 of the Proposed Regulations, the deconsolidation event were to occur after the pertinent timing limitation ends with respect to the relevant asset acquisition (or deemed asset acquisition).

4. We recommend that the Proposed Consolidated Deemed Acquisition Rule – or any variation of that rule adopted in the final regulations – be expanded to cover any type of qualified stock disposition for which an election under section 336(e) is made, not just those dispositions described in Treas. Reg. § 1.336-2(b)(1). 11

5. We believe that the five-year limitation set forth in Treas. Reg. § 1.168(k)-2(b)(3)(iii)(B)(1) (the “Five-Year Look-Back Period”) for purposes of ascertaining whether there was a “prior use” of acquired property by the taxpayer also should apply for purposes of the consolidated group rules set forth in Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v). Accordingly, we recommend that the final version of the consolidated group rules be clarified to explicitly incorporate the Five-Year Look-Back Period, such that this limitation also would apply (i) where one member of a consolidated group acquires property, and it is necessary to determine whether any other current or former member of the consolidated group previously used the acquired assets under the Group Prior Use Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(A); and (ii) for purposes of applying the Stock and Asset Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) and, correspondingly, the determination of whether any corporation that becomes part of the consolidated group in a series of related transactions previously used assets acquired as part of that same series of related transactions.

given effect as of the date that it is deemed to occur under the framework of section 336(e) or section 338, as appropriate.

10 As noted below in the Detailed Comments, there are a variety of situations – for example, a transaction involving an initial public offering or a public spin-off or requiring regulatory approval – where, for commercial or other business reasons, the asset sale (or deemed asset sale) will be required to occur well before the deconsolidation event.

11 That is, qualified stock dispositions (within the meaning of Treas. Reg. § 1.336-1(b)(6)) not described in section 355(d)(2) or section 355(e)(2). This recommendation is, in effect, a renewal of Recommendation 8 included in the Prior Report.
6. While the preamble to the Proposed Regulations offers a useful explanation of the Group Prior Use Rule and its application to a specific consolidated group, we recommend the addition of an example to the final regulations that confirms that the Group Prior Use Rule is inapplicable to situations where an asset is acquired by a former group member – other than the member that directly held the interest in the property – following the termination of the consolidated group as a result of either an acquisition of the group or pursuant to a reverse acquisition (within the meaning of Treas. Reg. § 1.1502-75(d)(3)(i)).

7. We recommend that Treasury and the Service reconsider the facts of Example 30 of the Proposed Regulations and clarify whether the 2018 sale of Equipment #4 by G either is or is not pursuant to the same series of related transactions as the 2019 transactions described in that example. Although we do not believe that the operation of the Stock and Asset Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) is intended to be impacted by the 2018 sale of Equipment #4 by G, we believe that clarification of Example 30 is warranted to avoid confusion concerning the operation of that rule.

8. We recommend that Treasury and the Service provide additional guidance with respect to the consequences of a purchase of an asset by one member of a consolidated group if, in an unrelated transaction, a corporation that previously had a depreciable interest in the property becomes a member of the same consolidated group. As described below in Part VII.B. of the Detailed Comments, we believe that the final regulations should confirm that the additional first-year depreciation deduction is available to a member of a consolidated group that purchases an asset if, in an unrelated transaction, a corporation that previously held a depreciable interest in that property becomes a member of the purchasing consolidated group.

9. Given the importance of the definition of the term “depreciable property” for purposes of the provisions of section 168(k), and the uncertain breadth of the reference to “depreciable property” included in Treas. Reg. § 1.168(k)-2(b)(1), we recommend an explicit definition of that term be provided in the final regulations or the use of an alternate term that is expressly limited to property the nature of which is eligible for the additional first-year depreciation deduction under section 168(k).

We appreciate all consideration given to our recommendations concerning the Proposed Regulations, and we would be pleased to discuss these Comments further if that would be helpful.

12 More broadly, we encourage Treasury and the Service to incorporate preamble statements such as this one concerning the intended operation of the Group Prior Use Rule into the portion of the regulations to which the preamble discussion relates, rather than leaving such statements as a gloss on regulations that otherwise are silent on the specific point addressed in the preamble.

13 As discussed below in Part V of the Detailed Comments, we separately recommend that Treasury and the Service incorporate the Five-Year Look-Back Period in the application of the provisions of the Proposed Regulations applying to consolidated groups and further recommend modifying Example 30 to give effect to this consideration.
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Detailed Comments

I. Background

As summarized above, pursuant to sections 168(k)(2)(A)(ii) and 168(k)(2)(E)(ii), the acquisition of used property is eligible for the additional first-year depreciation deduction only if that acquisition meets the No Prior Use Requirement and the Unrelated Purchase Requirement.\(^{14}\) Although the No Prior Use Requirement does not refer to any other Code section, the Unrelated Purchase Requirement incorporates the rules of section 179(d)(2) and section 179(d)(3), which provide additional requirements with respect to the acquisition of property. Specifically, section 179(d)(2) contains the following three requirements:

(A) The property must not be acquired from a person whose relationship to the person acquiring it would result in the disallowance of losses under sections 267 or 707(b);\(^ {15}\)

(B) The property must not be acquired by one component member of a controlled group from another component member of the same controlled group; and

(C) The basis of the property in the hands of the person acquiring it must not be determined (i) in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired (e.g., pursuant to section 351 and section 362(a)), or (ii) under section 1014(a) (relating to property acquired from a decedent).

Furthermore, section 179(d)(3) provides that the basis of such property must not be determined by reference to the basis of other property held at any time by the person acquiring such property (e.g., pursuant to section 1031). Property acquired by a “new target” as a result of an election under section 338 or section 336(e) with respect to the acquisition of the target qualifies as acquired by “purchase” under section 179(d)(2) and (3), while property acquired pursuant to a section 336(e) election in connection with a stock disposition described in section 355(d)(2) or section 355(e)(2) does not.\(^ {16}\)

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\(^{14}\) Additional criteria for property to be treated as qualified property for purposes of section 168(k) are listed in section 168(k)(2)(A)(i) and (iii). In particular, section 168(k)(2)(A)(i) provides that the term “qualified property” includes (i) property that has a recovery period of 20 years or less, (ii) computer software (as defined in section 167(f)(1)(B)) for which a deduction is allowable under section 167(a) without regard to section 168(k), (iii) water utility property, and (iv) qualified improvement property. Section 168(k)(2)(A)(iii) provides that the property must be placed in service by the taxpayer before January 1, 2027, to be qualified property.

\(^{15}\) In applying section 267(b) and (c) for purposes of section 179, paragraph (4) of section 267(c) is treated as providing that the family of an individual includes only his or her spouse, ancestors, and lineal descendants.

\(^{16}\) See Treas. Reg. § 1.179-4(c)(2) (“Property deemed to have been acquired by a new target corporation as a result of a section 338 election (relating to certain stock purchases treated as asset acquisitions) or a section 336(e) election (relating to certain stock dispositions treated as asset transfers) made for a disposition described in § 1.336-2(b)(1) will be considered acquired by purchase.”); cf. T.D. 9874, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50108, 50114 (Sept. 24, 2019) (“The final regulations clarify that the reference to section 336(e) in § 1.179-4(c)(2)”).

(footnote continued on the next page)
Special considerations are relevant to the application of these requirements where either the seller or the buyer (or both) is a corporation that is a member of a consolidated group. These considerations are discussed further below in the context of our recommendations with respect to the Proposed Regulations.

II. Proposed Modification of the Deferred Sale Approach

A. Operation of the Proposed Consolidated Acquisition Rule and the Proposed Consolidated Deemed Acquisition Rule

Proposed Consolidated Acquisition Rule. Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(C) (the “Proposed Consolidated Acquisition Rule”) would provide that, if (i) a member of a consolidated group acquires “depreciable property”17 from another member of the same consolidated group (that is, the selling group) in a taxable transaction, (ii) the transferee member would be eligible for the additional first-year depreciation deduction without regard to the Group Prior Use Rule (defined below), and (iii) the transferee member ceases to be a member of the selling group in a series of related transactions that includes the property acquisition within 90 calendar days of the date of the property acquisition, then:

- The disposition and acquisition of the depreciable property are treated as occurring one day after the date on which the transferee member ceases to be a member of the selling group (the “Deconsolidation Date”) for all federal income tax purposes; and

- The transferee member is treated as placing the depreciable property in service not earlier than one day after the Deconsolidation Date for purposes of claiming depreciation or the investment credit.

The Proposed Consolidated Acquisition Rule is intended to ensure that the used property acquisition requirements, including the No Prior Use Requirement and the Unrelated Purchase Requirement, are satisfied in cases similar to Former Example 21 of the August 2018 Proposed Regulations.18 Because the Proposed Consolidated Acquisition Rule treats the transferee member as acquiring the property after it ceases to be a member of the selling group, the transferee member is not attributed the selling group’s usage of the property under the rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(A) (the “Group Prior Use Rule”), which generally treats

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17 We note that the term “depreciable property” does not appear to be explicitly defined in the Final Regulations or the Proposed Regulations; however, the definition of “qualified property” in Treas. Reg. § 1.168(k)-2(b)(1) defines “qualified property” as “depreciable property, as defined in § 1.168(b)-1(a)(1).” Given the importance of the definition of the term “depreciable property” for purposes of these provisions, and the uncertain breadth of the reference to “depreciable property” included in Treas. Reg. § 1.168(k)-2(b)(1), we recommend an explicit definition of that term be provided in the final regulations or the use of an alternate term that is expressly limited to property the nature of which is eligible for the additional first-year depreciation deduction under section 168(k).

all members of a consolidated group as having a depreciable interest in property if any member of the group has a depreciable interest in the property while a member of the group. The requirements of section 179(d)(2)(A) and (B) – providing generally that the buyer and the seller must be unrelated – would be tested using the same analysis.

The Proposed Consolidated Acquisition Rule also provides that the transferee member is treated as placing the depreciable property in service not earlier than one day after the Deconsolidation Date for purposes of sections 167 and 168 and Treas. Reg. §§ 1.46-3(d) and 1.167(a)-11(e)(1). In so providing, it appears that Treasury and the Service were seeking to adopt an approach that prohibited the transferee member from claiming the additional first-year depreciation deduction on the selling group’s consolidated return. The rule also prevents the transferee member from claiming regular depreciation or the investment credit with respect to all of the acquired depreciable property during the period after the transferee member acquires the property but before it leaves the selling group. Example 28 in Prop. Treas. Reg. § 1.168(k)-2(b)(3)(vii)(BB), discussed further in Part III below, illustrates the application of the Proposed Consolidated Acquisition Rule.

Proposed Consolidated Deemed Acquisition Rule. Several comments on the August 2018 Proposed Regulations noted that issues similar to those in Former Example 21 also arise in the context of deemed acquisitions of property within a consolidated group resulting from an election under either section 338(h)(10) or section 336(e). In response to these comments, Treasury and the Service determined that deemed acquisitions of property should be treated the same as actual acquisitions of property and included a rule to that effect in the Proposed Regulations. Specifically, Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(D) (the “Proposed Consolidated Deemed Acquisition Rule”) sets forth a rule that applies if:

- The transferee member acquires the stock of another member of the same consolidated group that holds depreciable property (“target”) in either a “qualified stock purchase” for which a section 338 election is made or a “qualified stock

19 Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(A) provides as follows:

Solely for purposes of applying paragraph (b)(3)(iii)(A)(I) of this section, if a member of a consolidated group, as defined in § 1.1502-1(h), acquires depreciable property in which the group had a depreciable interest at any time prior to the member’s acquisition of the property, the member is treated as having a depreciable interest in the property prior to the acquisition. For purposes of this paragraph (b)(3)(v)(A), a consolidated group is treated as having a depreciable interest in property during the time any current or previous member of the group had a depreciable interest in the property while a member of the group.


21 The pertinent portion of the Prior Report addressing the issues that arise in the context of deemed acquisitions of property within a consolidated group resulting from an election under either section 338(h)(10) or section 336(e) is found at pp. 19-23 of that report.


23 See § 338(d)(3) (defining the term “qualified stock purchase”); Treas. Reg. § 1.338-2(c)(12) (same); see also Treas. Reg. § 1.338-3(b)(3) (providing rules for purposes of determining whether an acquisition of stock has been made from a related corporation).
disposition” described in Treas. Reg. § 1.336-2(b)(1) for which a section 336(e) election is made;

- Target would be eligible for the additional first-year depreciation deduction without regard to the Group Prior Use Rule; and

- The transferee member and target cease to be members of the consolidated group within 90 calendar days of the acquisition date (within the meaning of Treas. Reg. § 1.338-2(c)(1)) or disposition date (within the meaning of Treas. Reg. § 1.336-1(b)(8)) as part of the same series of related transactions that includes the acquisition.

If the Proposed Consolidated Deemed Acquisition Rule applies, (i) the acquisition date or disposition date, as applicable, is treated as the date that is one day after the date on which the transferee member and target cease to be members of the consolidated group, i.e., the Deconsolidation Date, for all federal income tax purposes, and (ii) target is treated as placing the qualified property – and any other depreciable property – in service not earlier than one day after the Deconsolidation Date for purposes of sections 167 and 168 and Treas. Reg. §§ 1.46-3(d) and 1.167(1)-11(e)(1). In sum, the Proposed Consolidated Deemed Acquisition Rule directs two principal outcomes: (i) target is eligible for the additional first-year depreciation deduction; and (ii) target will claim that deduction on a separate return (including the consolidated return of another group). Example 29 in Prop. Treas. Reg. § 1.168(k)-2(b)(3)(vii)(CC), discussed further in Part III below, illustrates the application of the Proposed Consolidated Deemed Acquisition Rule.

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24 See Treas. Reg. § 1.336-1(b)(6)(i) (defining the term “qualified stock disposition”); see also Treas. Reg. § 1.336-1(b)(5) (providing rules for purposes of determining whether a “disposition” of stock has occurred and including a cross-reference to the provisions of Treas. Reg. § 1.338-3(b)(3)).

25 See Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(D)(1) through (2). As relevant to this discussion, the term “acquisition date” means, with respect to any corporation, the first day on which there is a qualified stock purchase with respect to the stock of such corporation. See § 338(h)(2); Treas. Reg. § 1.338-2(c)(1). Further, the term “disposition date” means, with respect to any corporation, the first day on which there is a qualified stock disposition with respect to the stock of such corporation. See Treas. Reg. § 1.336-1(b)(8).

26 See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50157 (Sept. 24, 2019) (“Without the proposed rule, new target might be treated as having a depreciable interest in the assets new target is deemed to acquire by virtue of the Group Prior Use Rule because old target, a member of the same consolidated group, had a depreciable interest in those assets. If applicable, the proposed rule prevents new target from being treated as having a depreciable interest in the assets by moving the acquisition date or disposition date to the day after the Deconsolidation Date. New target is therefore a member of the acquiring group at the time it is deemed to acquire the assets.”).
B. Observations and Recommendations Concerning the Application of the Proposed Consolidated Acquisition Rule and the Proposed Consolidated Deemed Acquisition Rule

**Proposed Consolidated Acquisition Rule.** The provisions of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(C) would provide that, in the case of an actual asset acquisition (the “actual asset sale”), the transferor and transferee are treated as if the actual asset sale occurred on the day after the Deconsolidation Date for all federal income tax purposes. This treatment (the “Deferred Sale Approach”27) raises a number of complex issues, including those summarized below:

- The Deferred Sale Approach would appear to require that the income generated by, and the deductions associated with, the depreciable property during the period beginning on the date of the actual asset sale and ending on the Deconsolidation Date be reported by the transferor. How should these items of income and deduction (or any other indirect consequences relating to the actual asset sale) be reflected on the transferor’s books and records prior to the day after the Deconsolidation Date? How, if at all, should the outcome of the preceding question be impacted if the actual asset sale occurs in Year 1, but the Deconsolidation Date occurs in the following taxable year, i.e., Year 2?

- If the actual asset sale is part of a larger transaction to which section 355 applies, would the order of the steps be reversed? For example, would a situation involving an actual asset sale followed by a spin-off be treated as a spin-off followed by the actual asset sale? What if the reversal of the order of the steps disqualifies the transaction from nonrecognition treatment under section 355 because, for example, the actual asset sale involves the assets comprising the active trade or business relied upon to meet the requirements of section 355(b)?

- Would changing the timing of the actual asset sale render Treas. Reg. § 1.1502-13 inapplicable notwithstanding that the transaction is between two corporations that are members of a consolidated group immediately after the transaction?

- If the **transferor** deconsolidates from the selling group prior to the Deconsolidation Date, should the gain or loss, if any, resulting from the actual asset sale, along with any income generated by, or deductions associated with, the depreciable property following the transferor’s deconsolidation, but prior to the Deconsolidation Date, be reflected on the selling group’s consolidated return or the separate return (including the consolidated return of another group) that includes the transferor for the first taxable year ending after the transferor’s deconsolidation from the selling group? How, if at all, should the outcome of the preceding question be impacted if the actual asset sale occurs in Year 1, the Deconsolidation Date occurs in the following taxable year, i.e., Year 2?

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27 We use the term “Deferred Sale Approach” to refer to the treatment of either an actual asset sale or a deemed asset sale as occurring not on the acquisition date, but on a later date.
year, *i.e.*, Year 2, and the transferor deconsolidates from the selling group in Year 1 or Year 2, but in either instance prior to the Deconsolidation Date?

These complexities would be avoided by treating the actual asset sale as occurring on the day after the Deconsolidation Date only for purposes of the additional first-year depreciation deduction. While this approach may create some discontinuities between depreciation with respect to, and the income generated by, these assets, these discontinuities would be preferable in comparison to the open questions raised by the Deferred Sale Approach. In order to avoid the many open questions noted above, we recommend that Treasury and the Service revise the Deferred Sale Approach to deem the transferor’s sale of the depreciable property to the transferee to occur on the day after the Deconsolidation Date pursuant to a transaction to which section 168(i)(7) does not apply for an amount equal to the transferee’s then basis in the depreciable property *solely* for purposes of determining whether the requirements of section 168(k) are satisfied with respect to such sale and, if satisfied, the amount, location, and timing of the transferee’s additional first-year depreciation deduction with respect to the depreciable property.28

**Proposed Consolidated Deemed Acquisition Rule.** The provisions of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(D) would provide that, in the case of a deemed asset sale relating to a qualified stock purchase or a qualified stock disposition (a “deemed asset sale”), the qualified stock purchase or the qualified stock disposition, as appropriate, would be considered to occur on the day after the Deconsolidation Date for all federal income tax purposes. The scope of this provision would fundamentally change the federal income tax consequences of the deemed asset sale, and do so with respect to the entirety of new target’s assets, not just its depreciable property. Similar to the observations we made above with respect to the operation of the Proposed Consolidated Acquisition Rule, we have found the Deferred Sale Approach under the Proposed Consolidated Deemed Acquisition Rule raises a number of difficult issues, including those noted below:

- The Proposed Consolidated Deemed Acquisition Rule would appear to be subject to manipulation by taxpayers. For example, the introduction of a *de minimis* amount of depreciable property into the target in a scenario involving a qualified stock purchase for which an election under section 338(h)(10) is made would seem to permit the taxpayer to avail itself of the Deferred Sale Approach for purposes unrelated to the additional first-year depreciation deduction. Conversely, the Proposed Consolidated Deemed Acquisition Rule also could prove a trap for the unwary, as a taxpayer very well may not be focused on the application of section 168(k) where a target has merely a *de minimis* amount of depreciable property.

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28 Accordingly, (i) the transferee’s additional first-year depreciation deduction with respect to the depreciable property would be limited to the transferee’s basis in the depreciable property at the time of the deemed sale; and (ii) for all other federal income tax purposes, including the application of section 168 to depreciable property that does not qualify for the additional first-year depreciation deduction under section 168(k), the actual asset sale would be given effect as of the date that it occurs.
• If a section 338(h)(10) transaction is part of a larger transaction to which section 355 applies, would the order of the steps be reversed? For example, would a situation involving a section 338(h)(10) transaction followed by a spin-off be treated as a spin-off followed by section 338(h)(10) transaction? What if the reversal of the order of the steps affects whether the spin-off qualifies for nonrecognition treatment under section 355?

• If the transferor deconsolidates from the selling group prior to the Deconsolidation Date, should the gain or loss, if any, resulting from the deemed asset sale, along with any income generated by, or deductions associated with, the assets transferred in the deemed asset sale following the transferor’s deconsolidation, but prior to the Deconsolidation Date, be reflected on the selling group’s consolidated return or the separate return (including the consolidated return of another group) that includes the transferor for the first taxable year ending after the transferor’s deconsolidation from the selling group? How, if at all, should the outcome of the preceding question be impacted if the deemed asset sale occurs in Year 1, the Deconsolidation Date occurs in the following taxable year, i.e., Year 2, and the transferor deconsolidates from the selling group in Year 1 or Year 2, but in either instance prior to the Deconsolidation Date?

These difficulties would be avoided by treating the deemed asset sale as occurring on the day after the Deconsolidation Date only for purposes of the additional first-year depreciation deduction. Accordingly, we recommend that Treasury and the Service revise the Deferred Sale Approach to deem old target’s sale of the depreciable property to new target to occur on the day after the Deconsolidation Date for an amount equal to new target’s then basis in the depreciable property solely for purposes of determining whether the requirements of section 168(k) are satisfied with respect to such sale and, if satisfied, the amount, location, and timing of new target’s additional first-year depreciation deduction with respect to the depreciable property.29

III. Eliminate the 90-Day Limitation

As noted above, the Proposed Consolidated Acquisition Rule would apply if, in a series of related transactions that includes a property acquisition, the transferee member ceases to be a member of its consolidated group within 90 calendar days of the date of the property acquisition.30 Similarly, the Proposed Consolidated Deemed Acquisition Rule would apply if, as part of the series of related transactions including the property acquisition, the transferee member and target cease to be members of their consolidated group within 90 calendar days of

29 Accordingly, (i) new target’s additional first-year depreciation deduction with respect to the depreciable property would be limited to new target’s basis in the depreciable property at the time of the deemed sale; and (ii) for all other federal income tax purposes, including the application of section 168 to depreciable property that does not qualify for the additional first-year depreciation deduction under section 168(k), the deemed asset sale would be given effect as of the date that it is deemed to occur under the framework of section 336(e) or section 338, as appropriate.

the acquisition date (within the meaning of Treas. Reg. § 1.338-2(c)(1)) or disposition date (within the meaning of Treas. Reg. § 1.336-1(b)(8)).

We refer to the portions of the Proposed Consolidated Acquisition Rule and the Proposed Consolidated Deemed Acquisition Rule (collectively, the “Consolidated Acquisition Rules”) that limit their application to deconsolidation events occurring within 90 calendar days of the relevant asset acquisition (or deemed asset acquisition) as the “90-day Limitation.”

As discussed in the preamble to the Proposed Regulations, the Consolidated Acquisition Rules further the policy goals of section 168(k) by allocating the additional first-year depreciation deduction to the acquiring group that bears the economic outlay for the asset acquisition and that did not previously have a depreciable interest in the property. So stated, the intended outcome is to align the federal income tax consequences of a series of related transactions with economic reality. Treasury and the Service also have noted that, where an acquisition of property and a deconsolidation event “occur as part of the same series of related transactions . . . [and] the parties expected . . . [the purchaser of the property] to deconsolidate from the . . . [relevant] consolidated group, . . . the substance of the transaction is the same as if . . . [the purchaser of the property] first became a member of the . . . [acquiring] consolidated group and then acquired . . . [the relevant equipment].”

The substance of a series of related transactions does not differ if the deconsolidation event occurs on the 91st calendar day after a related property purchase, as opposed to the 90th calendar day. Further, there are a variety of situations – for example, a transaction involving an initial public offering or a public spin-off or requiring regulatory approval – where, for commercial or other business reasons, the asset sale (or deemed asset sale) will be required to occur well before the deconsolidation event. Thus, the 90-day Limitation threatens to impose arbitrary results upon otherwise similar series of related transactions.

In other situations in which the Proposed Regulations attempt to discern whether a sale occurs, in substance, between related parties, the Proposed Regulations look to a “series of related transactions” without regard to a specified time period. For example, for purposes of determining whether used property qualifies for the additional first-year depreciation deduction, the relationship between the parties is tested immediately after each step in the series, and

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33 Id. This statement implicitly assumes that the cost of the property acquisition will be borne by the acquiring consolidated group.

34 Although multiple discussions included in these Comments refer to a “series of related transactions,” these Comments should not be construed as offering any recommendations concerning, or otherwise offering any views regarding, the manner in which a “series of related transactions” is determined for purposes of the provisions of section 168(k) or, for that matter, any other provisions of the Code or the Treasury regulations.

35 Although the 90-day Limitation could be construed as providing certainty with respect to the determination of eligibility under the Consolidated Acquisition Rules, we nevertheless believe that any such perceived benefit is outweighed by the potential for these disparate outcomes and the further considerations we discuss below.
between the original transferor and the ultimate transferee immediately after the last transaction in the series. \(^{36}\)

More broadly, for purposes of section 338, whether a purchaser is related to another person is determined, in the case of a series of related transactions, immediately after the last transaction in the series. \(^{37}\) Consistent with this approach, the Service has issued numerous pieces of informal guidance applying section 338 to a series of related transactions involving an initial sale of target stock to an affiliated purchaser, followed by a transaction in which the purchaser becomes unrelated to the transferor. \(^{38}\) Further, it is not uncommon for provisions of the Code and the Treasury regulations to apply to transactions occurring as part of a plan or series of related transactions. \(^{39}\) Thus, relying on a “series of related transactions” to determine whether the substance of the transactions is consistent with a relevant Code provision is common throughout the tax law. Further, given that many of the rules described above likely would apply to transactions potentially subject to the Consolidated Acquisition Rules, the 90-day Limitation would appear to do little to minimize the burdens on taxpayers and the Service to determine what constitutes the relevant series.

Finally, we recognize that the Consolidated Acquisition Rules also function to address the amount, location, and timing of the additional first-year depreciation deduction between a transferor and transferee consolidated group. \(^{40}\) As discussed above in Part II, these rules

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\(^{36}\) See Prop. Treas. Reg. § 1.168(k)-2(b)(3)(iii)(C)(i) (“Solely for purposes of paragraph (b)(3)(iii) of this section, the relationship between parties under section 179(d)(2)(A) or (B) in a series of related transactions is tested immediately after each step in the series, and between the original transferor and the ultimate transferee immediately after the last transaction in the series.”).

\(^{37}\) See Treas. Reg. § 1.338-3(b)(3)(ii); see, e.g., Treas. Reg. § 1.338-3(b)(3)(iv), Ex. 1.

\(^{38}\) See, e.g., Tech. Adv. Mem. 9747001 (July 1, 1997); Priv. Ltr. Rul. 9541039 (July 20, 1995); Priv. Ltr. Rul. 9142013 (July 17, 1991). Many of these transactions in the public company context involve a series of related transactions that extend well beyond 90 days.

\(^{39}\) See, e.g., § 355(e) (providing that stock or securities in a controlled corporation are not treated as qualified property for purposes of sections 355(c)(2) and 361(c)(2) where a distribution under section 355 distribution is part of a plan or a series of related transactions) pursuant to which one or more persons acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or any controlled corporation); § 382(l)(1)(A) (ignoring capital contributions received by a loss corporation for purposes of calculating a section 382 limitation if made as part of a plan a principal purpose of which is to avoid or increase any such limitation); Treas. Reg. § 1.351-1(c)(2) (providing that, although the determination of whether a corporation is an investment company for purposes of section 351(e)(2) generally is made by reference to the circumstances in existence immediately after the transfer, where circumstances change thereafter pursuant to a plan in existence at the time of the transfer, such determination is made by reference to the later circumstances); Treas. Reg. § 1.1502-80(d) (providing that section 357(c) does not apply in the consolidated return context, unless the transferor or transferee becomes a nonmember as part of the same plan or arrangement as the intercompany transaction).

\(^{40}\) In this regard, section 1502 gives Treasury authority to prescribe such regulations, as may be deemed necessary, “in order that the tax liability of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be returned, determined, computed, assessed, collected, and adjusted, in such manner as clearly to reflect the income tax liability and the various factors necessary for the determination of such liability, and in order to prevent avoidance of such tax liability.” It is under this delegation of authority that the rules pertaining to the filing of consolidated returns have been issued. Moreover, in carrying out this delegation of authority, section 1502 provides that Treasury “may prescribe rules that

(footnote continued on the next page)
accomplish this result by deeming the property acquisition to occur one day after the Deconsolidation Date for all federal income tax purposes. Although the preamble to the Proposed Regulations identifies the Consolidated Acquisition Rules as similar to other rules disregarding certain transitory acquisitions of property in syndication transactions or involving de minimis uses of property,\textsuperscript{41} those other rules address distinct concerns and operate in an entirely different manner. The Consolidated Acquisition Rules do not involve transitory ownership and do not operate to disregard a transaction; rather, the Consolidated Acquisition Rules rely on a “series of related transactions” to evaluate how the relationship between certain parties should impact the amount, location, and timing of the additional first-year depreciation deduction, and are implemented by reordering certain steps to fulfill the policy of section 168(k).

Taking into account the foregoing discussion, as well as our proposals to narrow the application of the Consolidated Acquisition Rules,\textsuperscript{42} we recommend that the 90-day Limitation be removed from the Consolidated Acquisition Rules. Specifically, we recommend the following deletions be made to Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(C) and (D):

\begin{itemize}
  \item [(C)] Sale of depreciable property to a member that leaves the group. Except as otherwise provided in paragraph (b)(3)(v)(E) of this section, if a member of a consolidated group (transferee member) acquires from another member of the same group (transferor member) depreciable property in an acquisition meeting the requirements of paragraph (b)(3)(iii)(A) of this section without regard to section 179(d)(2)(A) or (B) or paragraph (b)(3)(v)(A) of this section, and if, as part of the same series of related transactions that includes the acquisition, the transferee member ceases to be a member of the consolidated group within 90 calendar days of the date of the acquisition, then . . .
  \item [(D)] Deemed sales of depreciable property under section 338 or 336(e) to a member that leaves the group. This paragraph (b)(3)(v)(D) applies only if a member of a consolidated group (transferee member) acquires the stock of another member of the same group that holds depreciable property (target) in
\end{itemize}

\textsuperscript{41} See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50156 (Sept. 24, 2019) (“Moreover, in circumstances similar to Former Example 21, the statute and regulations disregard a transitory acquisition of depreciable property when the property is acquired and disposed of within 90 calendar days. See section 168(k)(2)(E)(iii) and § 1.168(k)-2(b)(3)(vi) and (b)(4)(iv) (concerning syndication transactions) of the Final Regulations; see also § 1.168(k)-2(b)(3)(iii)(B)(4) of these proposed regulations (concerning de minimis uses of property).”).

\textsuperscript{42} Our first two recommendations, which are discussed above in Part II, would meaningfully limit the scope of the federal income tax determinations that are deemed to move to a later point in time under the Consolidated Acquisition Rules; specifically, the scope would be limited to whether the requirements of section 168(k) are satisfied with respect to the relevant asset acquisition (or deemed asset acquisition), and, if satisfied, the amount, location, and timing of the transferee’s additional first-year depreciation deduction with respect to the depreciable property.
either a qualified stock purchase for which a section 338 election is made or a qualified stock disposition described in § 1.336-2(b)(1) for which a section 336(e) election is made. Except as otherwise provided in paragraph (b)(3)(v)(E) of this section, if the target would be eligible for the additional first-year depreciation deduction under this section with respect to the depreciable property without regard to paragraph (b)(3)(v)(A) of this section, and if the transferee member and the target cease to be members of the group within 90 calendar days of the acquisition date, within the meaning of § 1.338-2(e)(1), or disposition date, within the meaning of § 1.336-1(b)(8), as part of the same series of related transactions that includes the acquisition, then . . .

Alternatively, if a timing limitation such as the 90-day Limitation is retained in the Consolidated Acquisition Rules, we recommend that Treasury and the Service (i) give further consideration to the commercial realities surrounding normal course business transactions; 43 (ii) acknowledge that, in circumstances where provisions of the Code or the Treasury regulations impose a timing limitation to restrict the scope of a series of related transactions, those provisions, to a very significant degree, incorporate a much longer period of time than 90 days; 44 and (iii) clarify the result if, in Examples 28 and 29 of the Proposed Regulations, the deconsolidation event were to occur after the pertinent timing limitation ends with respect to the relevant asset acquisition (or deemed asset acquisition). With respect to the last point, the facts of Example 28 are as follows:

Parent owns all of the stock of B and S, which are members of the Parent consolidated group. S has a depreciable interest in Equipment #3. No other current or previous member of the Parent consolidated group has ever had a depreciable interest in Equipment #3 while a member of the Parent consolidated group. X is the common parent of a consolidated group and is not related, within the meaning of section 179(d)(2)(A) or (B) and § 1.179-4(c), to any member of the Parent consolidated group. No member of the X consolidated group has ever had a depreciable interest in Equipment #3 while a member of the X consolidated group. On January 1, 2019, B purchases Equipment #3 from S. On February 15, 2019, as part of the same series of related transactions that includes B’s purchase of Equipment #3, Parent sells all of the stock of B to X. Thus, B leaves the Parent

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43 As noted above, there are a variety of situations – for example, a transaction involving an initial public offering or a public spin-off or requiring regulatory approval – where, for commercial or other business reasons, the asset sale (or deemed sale) will be required to occur well before the deconsolidation event.

44 See, e.g., § 355(e)(2)(B) (providing that, if one or more persons acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or any controlled corporation during the four-year period beginning on the date which is two years before the date of the distribution, such acquisition shall be treated as pursuant to a plan described in section 355(e)(2)(A)(ii) unless it is established that the distribution and the acquisition are not pursuant to a plan or series of related transactions); § 382(f)(1)(B) (providing that any capital contributions made during the two-year period ending on the change date of a loss corporation are generally treated as part of a plan a principal purpose of which is to avoid or increase any section 382 limitation); cf. Treas. Reg. § 1.1502-21(g) (providing that the separate return limitation year rules generally do not apply to net operating loss carryovers if a corporation becomes a member of a consolidated group within six months of the change date of an ownership change giving rise to a section 382 limitation with respect to such carryovers).
consolidated group at the end of the day on February 15, 2019, and joins the
X consolidated group on February 16, 2019. See § 1.1502-76(b).\(^{45}\)

Furthermore, the facts of Example 29 are the same as those in Example 28, except that:

S owns all of the stock of T (rather than a depreciable interest in Equipment #3),
which is a member of the Parent consolidated group; T has a depreciable interest
in Equipment #3; B acquires all of the stock of T (instead of a depreciable interest
in Equipment #3) on January 1, 2019; and S and B make a section 338(h)(10)
election for B’s qualified stock purchase.\(^{46}\)

The Proposed Regulations observe that each of B (in Example 28) and New T (in
Example 29) was a member of the Parent consolidated group as of the relevant asset acquisition
(or deemed asset acquisition), and that the Group Prior Use Rule of Prop. Treas. Reg. § 1.168(k)-
2(b)(3)(v)(A) generally treats each member as having a depreciable interest in property during
the time any member of the group had a depreciable interest in such property while a member of
the group. However, because the Consolidated Acquisition Rules are met in each example, the
asset acquisition is treated as occurring on the day after the relevant Deconsolidation Date.
Alternatively, if the deconsolidation event were to occur on the day after the pertinent timing
limitation ends with respect to the relevant asset acquisition (or deemed asset acquisition), the
Group Prior Use Rule apparently would prevent the asset acquisition by B and the deemed asset
acquisition by New T from qualifying for the additional first-year depreciation deduction. We
believe that clarification of this result would be helpful.

IV. Expand the Scope of the Proposed Consolidated Deemed Acquisition Rule

As an initial matter, we want to take the opportunity to commend Treasury and the
Service for including the Proposed Consolidated Deemed Acquisition Rule in the Proposed
Regulations, as the proposed rule provides helpful guidance concerning the availability of the
additional first-year depreciation deduction in the context of deemed acquisitions of property
within a consolidated group resulting from an election under either section 338(h)(10) or
section 336(e). That said, for the reasons discussed below, we recommend that the Proposed
Consolidated Deemed Acquisition Rule – or any variation of that rule adopted in the final
regulations – be expanded to cover any type of qualified stock disposition for which an election
under section 336(e) is made, not just those dispositions described in Treas. Reg. § 1.336-
2(b)(1).\(^{47}\)

The Proposed Consolidated Deemed Acquisition Rule does not apply to qualified stock
dispositions described in section 355(d)(2) or (e)(2) because “the rules applicable to such


\(^{47}\) That is, qualified stock dispositions (within the meaning of Treas. Reg. § 1.336-1(b)(6)) not described in
section 355(d)(2) or section 355(e)(2). This recommendation is, in effect, a renewal of Recommendation 8 included
in the Prior Report.
dispositions do not treat a new target corporation as acquiring assets from an unrelated person. As relevant to this conclusion, the “sale-to-self” fiction provided in Treas. Reg. § 1.336-2(b)(2) for such transactions treats “old” target as selling its assets to an unrelated party and, thereafter, purchasing those assets from an unrelated party. Although the sale-to-self fiction could be construed to violate the No Prior Use Requirement, we do not believe that construct should control eligibility for the additional first-year depreciation deduction afforded by section 168(k).

As recognized by Treasury and the Service in the preamble to the Proposed Regulations, a key rationale underlying the expansion of section 168(k) to acquisitions of used property is the desire to stimulate economic activity and promote capital investment. Assuming that the implementation of this fundamental policy in a consistent manner is a desired outcome of Treasury and the Service, and that the Proposed Consolidated Deemed Acquisition Rule falls within the ambit of that broader policy goal, we have been unable to discern a meaningful

48 Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50157 (Sept. 24, 2019). In brief, section 355(d) generally provides that a distributing corporation recognizes gain on the distribution of stock of a controlled corporation if, immediately after the distribution, a person holds 50 percent or more (by vote or value) of the distributing or controlled corporation stock that was acquired by purchase during the five-year period preceding the distribution. Furthermore, section 355(e) generally provides that the distributing corporation recognizes gain on the distribution of stock of a controlled corporation if the distribution is part of a plan that results in the acquisition of 50 percent or more (by vote or value) of the stock of either the distributing or controlled corporation.

49 See Treas. Reg. § 1.336-2(b)(2)(i)(A) (“Old target is treated as selling its assets to an unrelated person in a single transaction at the close of the disposition date in exchange for the ADADP as determined under § 1.336-3.”); Treas. Reg. § 1.336-2(b)(2)(ii)(A) (“Immediately after the deemed asset disposition described in paragraph (b)(2)(i)(A) of this section, old target is treated as acquiring all of its assets from an unrelated person in a single, separate transaction at the close of the disposition date (but before the distribution described in paragraph (b)(2)(iii)(A) of this section) in exchange for an amount equal to the AGUB as determined under § 1.336-4.”). Conversely, the fiction described in Treas. Reg. § 1.336-2(b)(1) is similar to the deemed construct afforded to transactions for which an election is made under section 338(b)(10). See Treas. Reg. § 1.336-2(b)(1)(i)(A), (ii).

50 The sale-to-self fiction otherwise satisfies the Unrelated Purchase Requirement because, pursuant to Treas. Reg. § 1.336-2(b)(2)(ii)(A), old target is treated as acquiring all of its assets from an unrelated person in a single, separate transaction at the close of the disposition date in exchange for an amount equal to the AGUB, as determined under Treas. Reg. § 1.336-4. Therefore, (i) the property is not acquired by old target from a person whose relationship to old target would result in the disallowance of losses under section 267 or section 707(b); (ii) the property is not acquired by one component member of a controlled group from another component member of the same controlled group; (iii) the basis of the property in the hands of old target is not determined in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired or under section 1014(a) (relating to property acquired from a decedent); and (iv) the cost of the property acquired by old target is not determined by reference to the basis of other property held at any time by old target.

51 See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50156 (Sept. 24, 2019) (“[T]he legislative history of section 168(k) . . . indicates that Congress intended to stimulate economic activity and promote capital investment. See H. Rept. 115-409, at 232 (2017) (‘The Committee believes that providing full expensing for certain business assets lowers the cost of capital for tangible property used in a trade or business. With lower costs of capital, the Committee believes that businesses will be encouraged to purchase equipment and other assets, which will promote capital investment and provide economic growth.’); H. Rept. 107-251, at 20 (2001) (‘The Committee believes that allowing additional first year depreciation will accelerate purchases of equipment, promote capital investment, modernization, and growth, and will help to spur an economic recovery.’”).
difference between a qualified stock disposition that is taxable at the shareholder level under section 301 and at the corporate level under section 311 versus a qualified stock disposition that is tax-free at the shareholder level under section 355(a) but taxable at the corporate level due to the application of section 355(d)(2) or (e)(2). We see no difference in these cases in the ability to stimulate economic activity and promote capital investment; yet, only in the former instance is the controlled corporation eligible for the additional first-year depreciation deduction. In our estimation, there is no sound policy rationale that supports this disparate result.

Based on the statements made in the preambles to the Proposed Regulations and the Final Regulations, it appears that Treasury and the Service believed that the mechanics of the sale-to-self fiction required the denial of the additional first-year depreciation deduction to the controlled corporation on account of a qualified stock disposition described in Treas. Reg. § 1.336-2(b)(2). However, as previously recognized by Treasury and the Service, the sale-to-self fiction was not intended to have such broad implications. Thus, the assertion that the sale-to-self fiction

52 See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50157 (Sept. 24, 2019); cf. T.D. 9874, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50108, 50114 (Sept. 24, 2019) (“The final regulations clarify that the reference to section 336(e) in § 1.179-4(c)(2) does not include dispositions described in section 355(d)(2) or (e)(2) because, under the sale-to-self model, old target will be treated as acquiring the assets in which it previously had a depreciable interest.”).

53 See, e.g., T.D. 9619, Regulations Enabling Elections for Certain Transactions Under Section 336(e), 78 Fed. Reg. 28467, 28469-28470 (May 15, 2013) (“Commenters have suggested that if the regulations retain the sale-to-self model, the regulations should address the wash sale rules of section 1091 and the anti-churning rules of section 197(f)(9). For example, old target’s deemed disposition of stock or securities and subsequent repurchase of the same stock or securities could be treated as a wash sale, which could then be subject to loss disallowance under section 1091(a) as well as the disallowed loss rule of these regulations. . . . The IRS and Treasury Department do not believe that adoption of the sale-to-self model should cause sections 197(f)(9) or 1091 to apply to a section 336(e) election with respect to a section 355(d)(2) or (e)(2) transaction. Because the deemed transactions resulting from the making of a section 336(e) election could not actually be undertaken in the context of a section 355(d)(2) or (e)(2) transaction, we do not believe that the regulations should cause a section 336(e) election in the context of a section 355(d)(2) or (e)(2) transaction to result in the application of sections 197(f)(9) or 1091 to the extent that a section 336(e) election outside the context of a section 355(d)(2) or (e)(2) transaction would not result in the application of such sections. Accordingly, the final regulations provide that for purposes of section 197(f)(9), section 1091, and any other provision designated in the Internal Revenue Bulletin by the IRS, old target, in its capacity as seller of assets in the deemed asset disposition, is treated as a separate and distinct taxpayer from, and unrelated to, old target in its capacity as acquirer of assets in the subsequent deemed purchase and for subsequent periods. For example, if one of target’s assets immediately before old target’s deemed asset disposition was stock or securities within the meaning of section 1091, old target, as seller of the stock or securities in the deemed asset disposition, is not treated for purposes of section 1091 as the same taxpayer that acquires substantially identical stock or securities in the deemed purchase of assets or that actually acquires substantially identical stock or securities in periods after the deemed asset disposition. Therefore, section 1091 will not disallow any of old target’s loss on the deemed sale of the stock or securities as a result of either old target’s deemed purchase of the same stock or securities or an actual purchase of substantially identical stock or securities within the 30-day period after the disposition date.”) (emphasis added); cf. Notice of Proposed Rulemaking, Regulations Enabling Elections for Certain Transactions Under Section 336(e), 73 Fed. Reg. 49965, 49968 (Aug. 25, 2008) (“The IRS and Treasury Department believe that, except as necessary to carry out the purposes of section 336(e), the section 355 consequences generally should continue to apply in such a transaction. For example, if the controlled corporation were treated as a new corporation, with no earnings and profits, the controlled corporation may be able to distribute its assets to its shareholders without recognizing any dividend consequences under section 301(c)(1). Therefore, to preserve the consequences of section 355 distributions, the proposed regulations provide special rules.”).
should direct the availability of the additional first-year depreciation deduction seems to us to be an unwarranted expansion of the intended impact of that fiction that does not give proper effect to Treas. Reg. § 1.336-2(b)(2)(ii)(C), which provides as follows:

(C) Application of section 197(f)(9), section 1091, and other provisions to old target.—Solely for purposes of section 197(f)(9), section 1091, and any other provision designated in the Internal Revenue Bulletin by the Internal Revenue Service (see § 601.601(d)(2)(ii) of this chapter), old target, in its capacity as seller of assets in the deemed asset disposition described in paragraph (b)(2)(i)(A) of this section, shall be treated as a separate and distinct taxpayer from, and unrelated to, old target in its capacity as acquirer of assets in the deemed purchase described in paragraph (b)(2)(ii)(A) of this section and for subsequent periods. [Emphasis added.]

Furthermore, as described above, the preamble to the Proposed Regulations observes that the approach to the treatment of a series of related transactions is to accord the same treatment that would have been available had the steps occurred in the reverse order – the separation transaction occurred first and the acquisition of the property occurred second. If that were the case in this situation, additional first-year depreciation deductions would be available in these qualified stock dispositions. Finally, if the Proposed Consolidated Deemed Acquisition Rule is not expanded to cover qualified stock dispositions described in Treas. Reg. § 1.336-2(b)(2), we believe that well-advised taxpayers simply will engage in self-help in order to achieve the desired outcome of affording the controlled corporation the ability to claim the additional first-year depreciation deduction. For example, a deemed acquisition of property within a consolidated group resulting from an election under section 338(h)(10) made incident to a stock distribution is likely to achieve the desired result. Consider the following example, which is derived from Priv. Ltr. Rul. 201702035 (Feb. 1, 2016) and Priv. Ltr. Rul. 201333007 (May 20, 2013):

Example. Parent, the widely-held common parent of a consolidated group, owns 100 percent of the stock of Target, a member of the Parent consolidated group. Target has a $15 basis in its assets, which constitute qualified property for purposes of section 168(k). Target’s assets have a fair market value of $100. Parent contributes all of its Target stock to newly-formed Sub in exchange for 100 percent of Sub’s stock, consisting of voting common stock and non-voting preferred stock (the “Target Contribution”). Sub is also a member of the Parent consolidated group. Pursuant to a prior binding commitment, Parent sells Sub’s non-voting preferred stock to an unrelated third party for cash. Two days later, and as part of the same overall plan, Parent contributes the Sub voting common stock to a newly formed Spinco and distributes the stock of Spinco to the Parent shareholders in a section 355 distribution that is subject to section 355(d)(2) (the “External Distribution”). In connection with the External Distribution, Parent and Sub make an election under section 338(h)(10) with respect to the stock of Target and the Target Contribution.

Under the Proposed Consolidated Deemed Acquisition Rule, (i) the acquisition date is treated as the date that is one day after the date on which Sub and Target cease to be members of
the Parent consolidated group, *i.e.*, the Deconsolidation Date, and (ii) Target is treated as placing the pertinent depreciable property in service not earlier than one day after the Deconsolidation Date. Accordingly, under the facts of the example, Target would be entitled to the additional first-year depreciation deduction and would claim that deduction on a separate return (including the consolidated return of another group). However, if instead of structuring into a section 338(h)(10) transaction, (i) the stock of Target simply was distributed by Parent via a section 355 distribution that is subject to section 355(d)(2), and (ii) a section 336(e) election was made for that qualified stock disposition, Target would not be eligible to claim the additional first-year depreciation deduction. As a result of causing these disparate outcomes, the distinction drawn by the Proposed Consolidated Deemed Acquisition Rule appears only to serve as a trap for the unwary, and otherwise to introduce an element of optionality into the availability of the additional first-year depreciation deduction.54 In our view, that outcome is inappropriate.

For the foregoing reasons, we recommend that the Proposed Consolidated Deemed Acquisition Rule – or any variation of that rule adopted in the final regulations – be expanded to cover *any type* of qualified stock disposition for which an election under section 336(e) is made, not just those dispositions described in Treas. Reg. § 1.336-2(b)(1).

V. Clarify Application of Five-Year Look-Back Period for Consolidated Groups

As discussed further below, we believe that the Five-Year Look-Back Period of Treas. Reg. § 1.168(k)-2(b)(3)(iii)(B)(1) also should apply for purposes of the consolidated group rules set forth in Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v).55 Accordingly, we recommend that the final version of the consolidated group rules be clarified to *explicitly incorporate* the Five-Year Look-Back Period, such that this limitation also would apply (i) where one member of a consolidated group acquires property, and it is necessary to determine whether any other current or former member of the consolidated group previously used the acquired assets under the Group Prior Use Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(A); and (ii) for purposes of applying the stock and asset acquisition rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) (the “Stock and Asset Acquisition Rule”) and, correspondingly, the determination of whether any corporation that becomes part of the consolidated group in a series of related transactions previously used assets acquired as part of that same series of related transactions.

54 In addition, a taxpayer may be precluded by non-federal tax considerations, such as regulatory prohibitions, from undertaking such a pre-distribution restructuring. Moreover, a taxpayer simply may not be sufficiently prescient to discern the post-distribution event(s) and information that ultimately result in the application of section 355(d) or (e) to a distribution otherwise qualifying for nonrecognition treatment under section 355.

55 As discussed further below, the Five-Year Look-Back Period applies to “the taxpayer or a predecessor.” In the context of a consolidated group, the “taxpayer” could be construed to be one or more of the following: (i) the consolidated group, (ii) the member acquiring the property, or (iii) the current or previous member that previously owned a depreciable interest in the property. In order to confirm the apparent intent of the operation of the Five-Year Look-Back Period in the context of a consolidated group, we recommend that the Five-Year Look-Back Period be applied by reference to the consolidated group, which, for this purpose, would be treated as a single taxpayer. In addition, as discussed further below, we recommend that the Stock and Asset Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) be clarified to provide that, for purposes of determining whether the acquired member had a depreciable interest in the acquired property, the acquiring consolidated group look backs five calendar years immediately prior to the group’s current placed-in-service year for the acquired property.
A. Operation of the Five-Year Look-Back Period

For purposes of determining whether acquired property was not used by the taxpayer or a predecessor at any time prior to the relevant acquisition, i.e., the No Prior Use Requirement, the preamble to the August 2018 Proposed Regulations requested comments as to whether a safe harbor should be provided with respect to how many taxable years a taxpayer should have to look back in determining whether the taxpayer (or its predecessor) previously held a depreciable interest in the property. In response to comments, the Five-Year Look-Back Period of Treas. Reg. § 1.168(k)-2(b)(3)(iii)(B)(1) provides that, in order to determine if the taxpayer (or a predecessor) previously held a depreciable interest in property, only the five calendar years immediately prior to the taxpayer’s current placed-in-service year of the property are taken into account. Furthermore, if the taxpayer and a predecessor have not been in existence for the entire Five-Year Look-Back Period, only the number of calendar years that the taxpayer and the predecessor have been in existence are taken into account.

With respect to the application of the No Prior Use Requirement to a consolidated group, the Group Prior Use Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(A) provides that, if a member acquires property, the member is treated as having a depreciable interest in the property before the acquisition if any current or previous member of that consolidated group had such an interest while a member of that consolidated group. The preamble to the Proposed Regulations further provides that the Group Prior Use Rule applies (i) only as long as the consolidated group remains in existence, as determined under Treas. Reg. § 1.1502-75; and (ii) only as long as the corporation remains a member of the consolidated group, but not after it deconsolidates. Thus,

58 The pertinent portion of the Prior Report addressing whether a safe harbor should be provided with respect to how many taxable years a taxpayer should have to look back in determining whether the taxpayer (or its predecessor) previously held a depreciable interest in property is found at pp. 6-8 of that report.
59 The preamble to the Final Regulations states that “five years is the appropriate number of years to reduce the potential for churning assets.” T.D. 9874, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50108, 50113 (Sept. 24, 2019). The preamble also notes that (i) most assets have a recovery period of five or seven years under section 168(c), and (ii) “this bright line test will be easy for both taxpayers and the IRS to administer.” Id.
a departing member does not continue to have a depreciable interest in property unless it actually owned the property. This clarification is illustrated by the following example:

Example. Parent, the widely held common parent of a consolidated group, owns 100 percent of the stock of each of corporation B and corporation C, which also are members of the Parent consolidated group. B owns an asset, which constitutes qualified property for purposes of section 168(k) (“Equipment #1”). Unrelated Buyer, the parent of a consolidated group that never owned an interest in Equipment #1, acquires all of the stock of C from Parent and Equipment #1 from B in a series of related transactions. C never actually owned Equipment #1.

In this example, the Group Prior Use Rule should not apply to treat C as having had a depreciable interest in Equipment #1. Stated differently, because C never directly owned Equipment #1, C is not considered to have had a depreciable interest in Equipment #1 once C departs the Parent consolidated group.

The Proposed Regulations do not include a provision explicitly coordinating the consolidated group rules of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v) with the Five-Year Look-Back Period and, further, do not provide any examples of how the Five-Year Look-Back Period applies to consolidated groups. We are concerned that, without this coordination, there would be an obligation to look back into the entire history of the consolidated group (including members that joined or departed the group) that would impose an extraordinary burden on consolidated groups and, further, would be inconsistent with the policy underlying the expansion of the additional first-year depreciation deduction to used property, i.e., the desire to stimulate economic activity and promote capital investment.

62 See id. (“Therefore, when a member deconsolidates, it does not continue to be treated under that rule as having a depreciable interest in the property. Accordingly, a departing member does not continue to have a depreciable interest in the property unless it actually owned such property.”).

63 One source of ambiguity is that the Five-Year Look-Back Period applies only to “determine if the taxpayer or a predecessor had a depreciable interest in the property at any time prior to acquisition,” while the Group Prior Use Rule looks to each “member of a consolidated group.” Similarly, the Stock and Asset Acquisition Rule (discussed below) requires a determination of whether any “corporation . . . had a depreciable interest in the property” if such corporation joins the consolidated group. See Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B). Further, the examples in the Proposed Regulations fail to acknowledge situations in which the Five-Year Look-Back Period ought to apply. In this regard, see the discussion of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(vii)(AA) and (DD), Exs. 27 and 30, below.

64 See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50156 (Sept. 24, 2019) (“[T]he legislative history of section 168(k) . . . indicates that Congress intended to stimulate economic activity and promote capital investment. See H. Rept. 115-409, at 232 (2017) (‘The Committee believes that providing full expensing for certain business assets lowers the cost of capital for tangible property used in a trade or business. With lower costs of capital, the Committee believes that businesses will be encouraged to purchase equipment and other assets, which will promote capital investment and provide economic growth.’); H. Rept. 107-251, at 20 (2001) (‘The Committee believes that allowing additional first year depreciation will accelerate purchases of equipment, promote capital investment, modernization, and growth, and will help to spur an economic recovery.’).”)
B. Recommendation

Initially, we want to take the opportunity to commend Treasury and the Service for including the Five-Year Look-Back Period in the Final Regulations, as this rule will ease the required diligence and recordkeeping associated with analyzing the No Prior Use Requirement. That said, for the reasons discussed below, we recommend that the final version of the consolidated group rules set forth in Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v) be clarified to explicitly incorporate the Five-Year Look-Back Period, such that this limitation also would apply (i) where one member of a consolidated group acquires property, and it is necessary to determine whether any other current or former member of the consolidated group previously used the acquired assets under the Group Prior Use Rule; and (ii) for purposes of applying the Stock and Asset Acquisition Rule and, correspondingly, the determination of whether any corporation that becomes part of the consolidated group in a series of related transactions previously used assets acquired as part of that same series of related transactions.

The Five-Year Look-Back Period applies to “the taxpayer or a predecessor.” In the context of a consolidated group, the “taxpayer” could be construed to be one or more of the following: (i) the consolidated group, (ii) the member acquiring the property, or (iii) the current or previous member that previously owned a depreciable interest in the property. In order to confirm the apparent intent of the operation of the Five-Year Look-Back Period in the context of a consolidated group, we recommend that the Five-Year Look-Back Period be applied by reference to the consolidated group, which, for this purpose, would be treated as a single taxpayer.

For purposes of the Group Prior Use Rule, our recommendation, if adopted, would give rise to the following outcomes:

- If any current member of a consolidated group (the “Acquiring Consolidated Group”), or any former member of the Acquiring Consolidated Group while a member of such group, held a depreciable interest in the property at issue during the five calendar years immediately prior to the current placed-in-service year for the Acquiring Consolidated Group, i.e., the Five-Year Look-Back Period, the Acquiring Consolidated Group would not satisfy the No Prior Use Requirement.

- The Acquiring Consolidated Group would not look back to any years prior to the Five-Year Look-Back Period to determine whether a current or former member held a depreciable interest in the property at issue.

In connection with this clarification to the operation of the Group Prior Use Rule, we believe that Example 27 in the Proposed Regulations should be modified. For reference, the facts of that example are excerpted below:

Parent owns all of the stock of D and E, which are members of the Parent consolidated group. D has a depreciable interest in Equipment #2. No other

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current or previous member of the Parent consolidated group has ever had a
depreciable interest in Equipment #2 while a member of the Parent consolidated

group. During 2018, D sells Equipment #2 to BA, a person not related, within the
meaning of section 179(d)(2)(A) or (B) and Treas. Reg. § 1.179-4(c), to any
member of the Parent consolidated group. In an unrelated transaction during
2019, E acquires Equipment #2 from BA or another person not related to any
member of the Parent consolidated group within the meaning of

section 179(d)(2)(A) or (B) and Treas. Reg. § 1.179-4(c).

The example concludes that E’s acquisition of Equipment #2 in 2019 is not eligible for
the additional first-year depreciation deduction, as it does not satisfy the No Prior Use
Requirement based on the Group Prior Use Rule. In order to incorporate the Five-Year Look-
Back Period, we believe that Example 27 should be modified to offer the following conclusions:

- If the acquisition of Equipment #2 by E occurs in 2024, rather than 2019, the Parent
  consolidated group satisfies the No Prior Use Requirement with respect to
  Equipment #2. Thus, E’s acquisition of Equipment #2 would be eligible for the
  additional first-year depreciation deduction, assuming all other requirements are
  satisfied. Additionally, this conclusion should note that the same outcome would be
  obtained if D, rather than E, acquired Equipment #2 in 2024.

- Alternatively, if D’s sale of Equipment #2 to BA occurred in 2013, rather than 2018,
  the Parent consolidated group satisfies the No Prior Use Requirement with respect to
  Equipment #2. Thus, E’s acquisition of Equipment #2 in 2019 would be eligible for
  the additional first-year depreciation deduction, assuming all other requirements are
  satisfied. Additionally, this conclusion should note that the same outcome would be
  obtained if D, rather than E, acquired Equipment #2 in 2019.

In addition to clarifications made with respect to the Group Prior Use Rule, the Five-Year
Look-Back Period should be coordinated with the Stock and Asset Acquisition Rule.66
Specifically, we recommend that the Stock and Asset Acquisition Rule be clarified to provide
that, for purposes of determining whether the acquired member had a depreciable interest in the
acquired property, the acquiring consolidated group looks back only five calendar years
immediately prior to the group’s current placed-in-service year for the acquired property.

In connection with this clarification to the operation of the Stock and Asset Acquisition
Rule, we believe that Example 30 in the Proposed Regulations67 should be modified. For
reference, the facts of that example are excerpted below:

66 The Stock and Asset Acquisition Rule provides that, “[s]olely for purposes of applying paragraph (b)(3)(v)(A) of
this section [i.e., the Group Prior Use Rule], if a series of related transactions includes one or more transactions in
which property is acquired by a member of a consolidated group, and one or more transactions in which a
corporation that had a depreciable interest in the property, determined without regard to the application of . . . [the
Group Prior Use Rule], becomes a member of the group, the member that acquires the property is treated as having a

G, which is not a member of a consolidated group, has a depreciable interest in Equipment #4. Parent owns all the stock of H, which is a member of the Parent consolidated group. No member of the Parent consolidated group has ever had a depreciable interest in Equipment #4 while a member of the Parent consolidated group, and neither Parent nor H is related to G within the meaning of section 179(d)(2)(A) or (B) and § 1.179-4(c). During 2018, G sells Equipment #4 to a person not related to G, Parent, or H within the meaning of section 179(d)(2)(A) or (B) and § 1.179-4(c). In a series of related transactions, during 2019, Parent acquires all of the stock of G, and H purchases Equipment #4 from an unrelated person.

The example concludes that H’s acquisition of Equipment #4 is not eligible for the additional first-year depreciation deduction, as it does not satisfy the No Prior Use Requirement by reason of the Stock and Asset Acquisition Rule. Specifically, in a series of related transactions, G became a member of the Parent consolidated group, and H, also a member of the Parent consolidated group, acquires Equipment #4. Thus, because G previously had a direct depreciable interest in Equipment #4, H is treated as having a depreciable interest in Equipment #4. In order to incorporate the Five-Year Look-Back Period, we believe that Example 30 should be modified to offer the following conclusions:

- In determining whether G previously had a direct depreciable interest in Equipment #4, the Parent consolidated group needs to determine whether G had a depreciable interest in Equipment #4 at any time during the five calendar years of the Parent consolidated group immediately prior to the group’s current placed-in-service year of Equipment #4.

- If the acquisition of Equipment #4 by H occurs in 2024, rather than 2019, the Parent consolidated group satisfies the No Prior Use Requirement with respect to Equipment #4. Thus, H’s acquisition of Equipment #4 would be eligible for the additional first-year depreciation deduction, assuming all other requirements are satisfied.

- Alternatively, if G’s sale of Equipment #4 to the unrelated person occurred in 2013, rather than 2018, the Parent consolidated group satisfies the No Prior Use Requirement with respect to Equipment #4. Thus, H’s acquisition of Equipment #4 in 2019 would be eligible for the additional first-year depreciation deduction, assuming all other requirements are satisfied.

Further, we believe that it would be helpful for the final regulations to include an example providing that an acquiring consolidated group looks back only five calendar years immediately prior to the group’s current placed-in-service year to determine whether an acquired member ever held a direct depreciable interest in the acquired property. In this regard, consider the following example:

*Example.* Parent, the widely-held common parent of a consolidated group, owns 100 percent of the stock of each of corporation B and corporation C, which also are members of the Parent consolidated group. B owns an asset, which
constitutes qualified property for purposes of section 168(k) ("Equipment #3"). Unrelated Buyer, the parent of a consolidated group that never owned an interest in Equipment #3, acquires all of the stock of C from Parent and Equipment #3 from B in a series of related transactions. C directly owned a depreciable interest in Equipment #3 six years prior to the year in which Unrelated Buyer acquired Equipment #3 from B and the stock of C from Parent, but C disposed of that interest during that prior year.

In this example, taking into account the Five-Year Look-Back Period for the Unrelated Buyer consolidated group, that group should satisfy the No Prior Use Requirement with respect to Equipment #3 because C did not own a direct interest in Equipment #3 at any time during the five calendar years of the Unrelated Buyer consolidated group immediately prior to the group’s current placed-in-service year of Equipment #3.

VI. Add Example Addressing the Application of the Group Prior Use Rule to Group Termination Transactions

While the preamble to the Proposed Regulations offers a useful explanation of the Group Prior Use Rule and its application to a specific consolidated group, we recommend the addition of an example to the final regulations that confirms that the Group Prior Use Rule is inapplicable to situations where an asset is acquired by a former group member – other than the member that directly held the interest in the property – following the termination of the consolidated group as a result of either an acquisition of the group or pursuant to a reverse acquisition (within the meaning of Treas. Reg. § 1.1502-75(d)(3)(i)). In this regard, consider the following example:

Example. P, S, and T file a consolidated return, with P as the common parent. T sells depreciable property to an unrelated person (“X”) in Year 1. Thereafter, in Year 2, P acquires all of the stock of Y, and, as a result, the P consolidated group terminates because P’s acquisition of the stock of Y qualifies as a reverse acquisition within the meaning of Treas. Reg. § 1.1502-75(d)(3)(i). During Year 3, i.e., within five years of T’s sale of the depreciable property to X, but not pursuant to the same plan or series of related transactions that includes such sale, S purchases the depreciable property from X.

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68 See Notice of Proposed Rulemaking, Additional First Year Depreciation Deduction, 84 Fed. Reg. 50152, 50155 (Sept. 24, 2019) ("The Treasury Department and the IRS did not intend the Group Prior Use Rule to continue to apply to a member of a consolidated group after the member leaves that consolidated group. By its terms, the Group Prior Use Rule applies only as long as a corporation remains a member of a consolidated group. Therefore, when a member deconsolidates, it does not continue to be treated under that rule as having a depreciable interest in the property. Accordingly, a departing member does not continue to have a depreciable interest in the property unless it actually owned such property." (emphasis added)).

69 More broadly, we encourage Treasury and the Service to incorporate preamble statements such as this one concerning the intended operation of the Group Prior Use Rule into the portion of the regulations to which the preamble discussion relates, rather than leaving such statements as a gloss on regulations that otherwise are silent on the specific point addressed in the preamble.
Under these facts, S deconsolidated from the P consolidated group as a result of the reverse acquisition in Year 2. Thus, taking into the account the discussion from the preamble to the Proposed Regulations, S’s asset purchase in Year 3 would be eligible for the additional first-year depreciation deduction because S does not continue to be treated as having a depreciable interest in the acquired property under the Group Prior Use Rule. Alternatively, if T (rather than S) purchased the depreciable property from X, we think it would be useful to clarify whether or not T would qualify for the additional first-year depreciation deduction with respect to that property. In such an instance, notwithstanding the termination of the P consolidated group, T actually held the depreciable property within the Five-Year Look-Back Period and, therefore, presumably would be ineligible for the additional first-year depreciation deduction upon reacquiring the property from X.

VII. Clarify Example 30 of the Proposed Regulations and Confirm Scope of the Stock and Asset Acquisition Rule

A. Operation of the Stock and Asset Acquisition Rule and Example 30

The Stock and Asset Acquisition Rule of Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) provides as follows:

Solely for purposes of applying paragraph (b)(3)(v)(A) of this section [i.e., the Group Prior Use Rule], if a series of related transactions includes one or more transactions in which property is acquired by a member of a consolidated group, and one or more transactions in which a corporation that had a depreciable interest in the property, determined without regard to the application of . . . [the Group Prior Use Rule], becomes a member of the group, the member that acquires the property is treated as having a depreciable interest in the property prior to the time of its acquisition.70

Example 30 of the Proposed Regulations illustrates the operation of the Stock and Asset Acquisition Rule. In Example 30, the following facts are provided:

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70 We commend Treasury and the Service for clarifying that the Stock and Asset Acquisition Rule applies with respect to the acquisition of stock of "a corporation that had a depreciable interest in the property, determined without regard to the application of . . . [the Group Prior Use Rule]," therefore resolving a significant question posed by the August 2018 Proposed Regulations. Compare Prop. Treas. Reg. § 1.168(k)-2(b)(3)(v)(B) with Former Prop. Treas. Reg. § 1.168(k)-2(b)(3)(iii)(B)(3)(i) (2018).
G, which is not a member of a consolidated group, has a depreciable interest in Equipment #4. Parent owns all the stock of H, which is a member of the Parent consolidated group. No member of the Parent consolidated group has ever had a depreciable interest in Equipment #4 while a member of the Parent consolidated group, and neither Parent nor H is related to G within the meaning of section 179(d)(2)(A) or (B) and § 1.179-4(c). **During 2018, G sells Equipment #4 to a person not related to G, Parent, or H within the meaning of section 179(d)(2)(A) or (B) and § 1.179-4(c). In a series of related transactions, during 2019, Parent acquires all of the stock of G, and H purchases Equipment #4 from an unrelated person.**

Example 30 concludes that the acquisition of Equipment #4 by H **fails** the No Prior Use Requirement because that acquisition occurred pursuant to a series of related transactions involving Parent’s purchase of the G stock, and G previously had a depreciable interest in Equipment #4.

**B. Recommendations**

We recommend that Treasury and the Service reconsider the facts of Example 30 of the Proposed Regulations and clarify whether the 2018 sale of Equipment #4 by G either is or is not pursuant to the same series of related transactions as the 2019 transactions described in that example. Although we do not believe that the operation of the Stock and Asset Acquisition Rule is intended to be impacted by the 2018 sale of Equipment #4 by G, we believe that clarification of Example 30 is warranted to avoid confusion concerning the operation of that rule.

We also recommend that Treasury and the Service provide additional guidance with respect to the consequences of a purchase of an asset by one member of a consolidated group if, in an unrelated transaction, a corporation that previously had a depreciable interest in the property becomes a member of the same consolidated group. For example, if, in a situation like the one offered by Example 30 of the Proposed Regulations, H purchased Equipment #4 in a transaction unrelated to, and prior to, Parent’s purchase of G’s stock, neither the Stock and Asset Acquisition Rule nor the Group Prior Use Rule would apply. Specifically, at the time that H purchases Equipment #4, no member of the Parent consolidated group would ever have had a depreciable interest in Equipment #4 while a member of the Parent consolidated group, and neither Parent nor H is related to G within the meaning of section 179(d)(2)(A) or (B) and Treas.

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72 As discussed above in Part V, we separately recommend that Treasury and the Service incorporate the Five-Year Look-Back Period in the application of the provisions of the Proposed Regulations applying to consolidated groups and further recommend modifying Example 30 to give effect to this consideration.

73 Alternatively, if the operation of the Stock and Asset Acquisition Rule is intended to be impacted by the 2018 sale of Equipment #4 by G, we believe that Treasury and the Service should refocus the Stock and Asset Acquisition Rule, so that it functions more appropriately as an anti-abuse provision.
Reg. § 1.179-4(c). Thus, assuming all other requirements are met, the additional first-year depreciation deduction should be available.

Conversely, if Parent purchases the G stock prior to H’s acquisition of Equipment #4, the Equipment #4 purchase would be eligible for the additional first-year depreciation deduction unless, under the Group Prior Use Rule, Equipment #4 constitutes “depreciable property in which the [Parent consolidated] group had a depreciable interest at any time prior to the member’s acquisition of the property.”74 A consolidated group is treated as having a depreciable interest in property only “during the time any current or previous member of the group had a depreciable interest in the property while a member of the group.”75 At no time while G was a member of the Parent consolidated group did G have a depreciable interest in Equipment #4. Thus, assuming all other requirements are met, the additional first-year depreciation deduction likewise should be available.

In view of these outcomes, we believe that the final regulations should confirm that the additional first-year depreciation deduction is available to a member of a consolidated group that purchases an asset if, in an unrelated transaction, a corporation that previously held a depreciable interest in that property becomes a member of the purchasing consolidated group.

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75 Id. (emphasis added).