

# New Section 382 proposed regulations modify and delay 2019 proposed regulations

January 16, 2020

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## In brief

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The IRS released on January 10 proposed regulations under Section 382(h) (the 2020 Proposed Regulations), which partially withdraw selected text of the 2019 proposed Section 382(h) regulations (the 2019 Proposed Regulations) primarily relating to the date the final Section 382(h) regulations would become applicable to taxpayers.

The 2019 Proposed Regulations provided a new framework for taxpayers to calculate their net unrealized built-in gains and losses and recognized built-in gains (RBIG) and losses (RBIL) under Section 382(h) that, in turn, affect their ability to use tax attributes. Under the 2019 Proposed Regulations, the final regulations under Section 382(h) would have been effective on their date of publication.

The key takeaways from the 2020 Proposed Regulations are the following:

- Final regulations under Section 382(h) generally would apply to any ownership change that occurs after the date that is 30 days after the date of publication of the Treasury Department decision adopting the proposed Section 382(h) regulations as final regulations (the Delayed Applicability Date), subject to certain exceptions discussed further below.
- Taxpayers generally may continue to rely on Notice 2003-65 either (i) up to the Delayed Applicability Date or (ii) indefinitely in situations 1 through 5 described below, even though the Notice will be obsolete on the Delayed Applicability Date.

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## In detail

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### Background

The 2019 Proposed Regulations, issued on September 10, 2019, by the Treasury Department and the IRS, provided a new framework for taxpayers to calculate their net unrealized built-in gains and losses and RBIG and RBIL under Section 382(h) that, in turn, affected their ability to use tax attributes, including

net operating losses, capital losses, disallowed business interest expense, AMT credits, general business credits, and excess foreign taxes under Section 904(c). Among other things, these regulations effectively eliminated taxpayers' use of the Section 338 Method (or wasting asset method) promulgated by the IRS in Notice 2003-65 to determine their RBIG and RBIL under Section 382(h). These regulations would have applied to an ownership change that occurred after the date the Treasury Department adopted the 2019 Proposed Regulations as final.

In order to alleviate taxpayer burden in evaluating and negotiating transactions caused by the uncertainty around the finalization date of the 2019 Proposed Regulations and the potential impact to taxpayers' ability to use their, or a target corporation's, tax attributes post-ownership change, taxpayers and practitioners requested transition relief with regard to ownership changes caused by pending or contemplated transactions.

### **Delay of applicability date**

In order to allow for a seamless transition between reliance on Notice 2003-65 and the provisions in the Section 382(h) proposed regulations, the 2020 Proposed Regulations withdraw the text of Treas. Reg. secs. 1.382-2(b)(4) and 1.382-7(g) in the 2019 Proposed Regulations and replace them with new Treas. Reg. secs. 1.382-2(b)(4) and 1.382-7(g). The new language provides that, other than the transition relief provisions and the Treas. Reg. sec. 1.382-7(d)(5) provision discussed below, the effective date of the final Section 382(h) regulations will be 30 days after the date the Treasury Department decision containing such regulations is published in the Federal Register (i.e., the Delayed Applicability Date).

### **Transition relief provisions**

Under the transition relief provisions in the 2020 Proposed Regulations, the final Section 382(h) regulations would not apply after the Delayed Applicability Date if the respective ownership change occurs immediately after an owner shift or equity structure shift that occurs:

1. Pursuant to a binding agreement in effect on or before the Delayed Applicability Date and at all times thereafter;
2. Pursuant to a specific transaction described in a public announcement made on or before the Delayed Applicability Date;
3. Pursuant to a specific transaction described in a filing with the Securities and Exchange Commission submitted on or before the Delayed Applicability Date;
4. By order of a court (or pursuant to a plan confirmed, or a sale approved, by order of a court) in a title 11 or similar case (as defined in Section 382(l)(5)(F)), provided that the taxpayer was a debtor in a case before such court on or before the Delayed Applicability Date; or
5. Pursuant to a transaction described in a private letter ruling request submitted to the IRS on or before the Delayed Applicability Date.

While taxpayers can continue to rely on Notice 2003-65 either (i) up to the Delayed Applicability Date or (ii) indefinitely with respect to any ownership change qualifying for transition relief under this provision, they instead may choose to apply the final regulations to such an ownership change.

### **Rule for business interest expense deductions disallowed under Section 163(j)**

As proposed, Treas. Reg. sec. 1.382-7(d)(5) provides that certain carryforwards of business interest expense disallowed under Section 163(j) would not be treated as RBIL under Section 382(h)(6)(B) if such amounts were allowable as deductions during the five-year recognition period set forth in Section 382(h)(7)(A). Due to the non-controversial nature of this provision, the Treasury Department and the IRS have determined that proposed Treas. Reg. sec. 1.382-7(d)(5) should be finalized before the remainder of the rules in the 2019 Proposed Regulations, and that taxpayers should be allowed to retroactively apply this rule. The Treasury Department and the IRS expect to finalize this provision as part of the Treasury Department decision that finalizes the proposed Section 163(j) regulations.

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## The takeaway

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The 2020 Proposed Regulations revise the applicability date of the initial Section 382(h) guidance released in the 2019 Proposed Regulations. In addition, the new rules allow taxpayers that undergo an ownership change the ability to continue to rely on Notice 2003-65 up to the Delayed Applicability Date for purposes of determining their RBIG and RBIL under Section 382(h), or indefinitely in situations 1 through 5 above.

Taxpayers should review and assess the impact of the 2020 Proposed Regulations and the Delayed Applicability Date in light of their current and/or future contemplated transactions that are expected to result in an ownership change under Section 382. To the extent taxpayers want to ensure continued reliance on Notice 2003-65 after the Delayed Applicability Date, consideration should be given to by the parties to plan into one of the five exceptions discussed above.

### See also:

- Tax Insight: [Proposed Regulations under Section 382 reduce tax attributes' value in M&A transactions](#)
- Tax Insight: [Treasury issues comprehensive proposed regulations under Section 382\(h\)](#)

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## Let's talk

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For a deeper discussion of how this issue might affect your business, please contact:

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