

under this paragraph (d)(1) are determined as follows:

(A) *Sale, exchange, or distribution.* If the item is from an intercompany sale, exchange, or distribution of property, its attributes are determined under the principles of the matching rule as if B sold the property, at the time the item is taken into account under paragraph (d)(1)(i) of this section, for a cash payment equal to B's adjusted basis in the property (i.e., at no net gain or loss), to the following person:

(1) *Property leaves the group.* If the property is owned by a nonmember immediately after S's item is taken into account, B is treated as selling the property to that nonmember. If the nonmember is related for purposes of any provision of the Internal Revenue Code or regulations to any party to the intercompany transaction (or any related transaction) or to the common parent, the nonmember is treated as related to B for purposes of that provision. For example, if the nonmember is related to P within the meaning of section 1239(b), the deemed sale is treated as being described in section 1239(a). See paragraph (j)(6) of this section, under which property is not treated as being owned by a nonmember if it is owned by the common parent after the common parent becomes the only remaining member.

(2) *Property does not leave the group.* If the property is not owned by a nonmember immediately after S's item is taken into account, B is treated as selling the property to an affiliated corporation that is not a member of the group.

(B) *Other transactions.* If the item is from an intercompany transaction other than a sale, exchange, or distribution of property (e.g., income from S's services capitalized by B), its attributes are determined on a separate entity basis.

(2) *B's items—(i) Attributes.* The attributes of B's corresponding items continue to be redetermined under the principles of the matching rule, with the following adjustments:

(A) If S and B continue to join with each other in the filing of consolidated returns, the attributes of B's corresponding items (and any applicable holding periods) are determined by continuing to treat S and B as divisions of a single corporation.

(B) Once S and B no longer join with each other in the filing of consolidated returns, the attributes of B's corresponding items are determined as if the S division (but not the B division) were transferred by the single corporation to an unrelated person. Thus, S's activities (and any applicable

holding period) before the intercompany transaction continue to affect the attributes of the corresponding items (and any applicable holding period).

(ii) *Timing.* If paragraph (d)(1) of this section applies to S, B nevertheless continues to take its corresponding items into account under its accounting method. However, the redetermination of the attributes of a corresponding item under this paragraph (d)(2) might affect its timing.

(3) *Examples.* The acceleration rule of this paragraph (d) is illustrated by the following examples.

Example 1. Becoming a nonmember—timing. (a) *Facts.* S owns land with a basis of \$70. On January 1 of Year 1, S sells the land to B for \$100. On July 1 of Year 3, P sells 60% of S's stock to X for \$60 and, as a result, S becomes a nonmember.

(b) *Matching rule.* Under the matching rule, none of S's \$30 gain is taken into account in Years 1 through 3 because there is no difference between B's \$0 gain or loss taken into account and the recomputed gain or loss.

(c) *Acceleration of S's intercompany items.* Under the acceleration rule of paragraph (d) of this section, S's \$30 gain is taken into account in computing consolidated taxable income (and consolidated tax liability) immediately before the effect of treating S and B as divisions of a single corporation cannot be produced. Because the effect cannot be produced once S becomes a nonmember, S takes its \$30 gain into account in Year 3 immediately before becoming a nonmember. S's gain is reflected under § 1.1502-32 in P's basis in the S stock immediately before P's sale of the stock. Under § 1.1502-32, P's basis in the S stock is increased by \$30, and therefore P's gain is reduced (or loss is increased) by \$18 (60% of \$30). See also §§ 1.1502-33 and 1.1502-76(b). (The results would be the same if S sold the land to B in an installment sale to which section 453 would otherwise apply, because S must take its intercompany gain into account under this section.)

(d) *B's corresponding items.* Notwithstanding the acceleration of S's gain, B continues to take its corresponding items into account under its accounting method. Thus, B's items from the land are taken into account based on subsequent events (e.g., its sale of the land).

(e) *Sale of B's stock.* The facts are the same as in paragraph (a) of this *Example 1*, except that P sells 60% of B's stock (rather than S stock) to X for \$60 and, as a result, B becomes a nonmember. Because the effect of treating S and B as divisions of a single corporation cannot be produced once B becomes a nonmember, S takes its \$30 gain into account under the acceleration rule immediately before B becomes a nonmember. (The results would be the same if S sold the land to B in an installment sale to which section 453 would otherwise apply, because S must take its intercompany gain into account under this section.)

(f) *Discontinue filing consolidated returns.* The facts are the same as in paragraph (a) of this *Example 1*, except that the P group

receives permission under § 1.1502-75(c) to discontinue filing consolidated returns beginning in Year 3. Under the acceleration rule, S takes its \$30 gain into account on December 31 of Year 2.

(g) *No subgroups.* The facts are the same as in paragraph (a) of this *Example 1*, except that P simultaneously sells all of the stock of both S and B to X (rather than 60% of S's stock), and S and B become members of the X consolidated group. Because the effect of treating S and B as divisions of a single corporation in the P group cannot be produced once S and B become nonmembers, S takes its \$30 gain into account under the acceleration rule immediately before S and B become nonmembers. (Paragraph (j)(5) of this section does not apply to treat the X consolidated group as succeeding to the P group because the X group acquired only the stock of S and B.) However, so long as S and B continue to join with each other in the filing of consolidated returns, B continues to treat S and B as divisions of a single corporation for purposes of determining the attributes of B's corresponding items from the land.

Example 2. Becoming a nonmember—attributes. (a) *Facts.* S holds land for investment with a basis of \$70. On January 1 of Year 1, S sells the land to B for \$100. B holds the land for sale to customers in the ordinary course of business, and expends substantial resources over a two-year period subdividing, developing, and marketing the land. On July 1 of Year 3, before B has sold any of the land, P sells 60% of S's stock to X for \$60 and, as a result, S becomes a nonmember.

(b) *Attributes.* Under the acceleration rule, the attributes of S's gain are redetermined under the principles of the matching rule as if B sold the land to an affiliated corporation that is not a member of the group for a cash payment equal to B's adjusted basis in the land (because the land continues to be held within the group). Thus, whether S's gain is capital gain or ordinary income depends on the activities of both S and B. Because S and B no longer join with each other in the filing of consolidated returns, the attributes of B's corresponding items (e.g., from its subsequent sale of the land) are redetermined under the principles of the matching rule as if the S division (but not the B division) were transferred by the single corporation to an unrelated person at the time of P's sale of the S stock. Thus, B continues to take into account the activities of S with respect to the land before the intercompany transaction.

(c) *Depreciable property.* The facts are the same as in paragraph (a) of this *Example 2*, except that the property sold by S to B is depreciable property. Section 1239 applies to treat all of S's gain as ordinary income because it is taken into account as a result of B's deemed sale of the property to a affiliated corporation that is not a member of the group (a related person within the meaning of section 1239(b)).

Example 3. Selling member's disposition of installment note. (a) *Facts.* S owns land with a basis of \$70. On January 1 of Year 1, S sells the land to B in exchange for B's \$110 note. The note bears a market rate of interest in excess of the applicable Federal rate, and