



# TaxNewsFlash

## United States

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### **Notice 2018-30: Section 382 recognized built-in gains, losses determined without regard to section 168(k) immediate expensing**

The IRS today released an advance version of Notice 2018-30 that includes language to modify Notice 2003-65, in response to the additional first year depreciation deduction available under section 168(k)—the “immediate expensing” provision—as enacted by the new tax law (Pub. L. No. 115-97, enacted December 22, 2017).

**Notice 2018-30** [PDF 22 KB] provides:

- The hypothetical cost recovery deductions used in the section 338 approach (described in Notice 2003-65) to identify recognized built-in gain or recognized built-in loss under section 382 are determined without regard to section 168(k).
- In computing the amount of cost recovery deductions that are not attributable to an asset’s built-in loss on the change date under the section 1374 approach (also described in Notice 2003-65), the hypothetical deductions that would have been allowable had the loss corporation purchased the asset for its fair market value on the change date are determined without regard to section 168(k).

### **Background**

Released in September 2003, Notice 2003-65 provides two alternative approaches for the identification of built-in items for purposes of section 382(h):

- The section 1374 approach—which identifies built-in items by incorporating the rules of section 1374, which generally pertain to the imposition of entity-level tax on net realized built-in gains of a subchapter S corporation.
- The section 338 approach—which identifies built-in items by comparing the loss corporation’s actual items of income, gain, deduction, and loss with those

that would have resulted if a section 338 election had been made with respect to a hypothetical purchase of all outstanding stock of the loss corporation on the ownership change date.

Generally, the section 1374 approach treats items of income or deduction as attributable to the pre-change period if such items accrue for tax purposes prior to the ownership change.

Because the section 338 approach compares the actual items with items that would result from a hypothetical section 338 election, additional income resulting from foregone depreciation on a wasting asset can be treated as recognized built-in gain.

Read initial impressions of Notice 2003-65 in [TaxNewsFlash](#) [PDF 148 KB]

### **Reason for Notice 2018-30**

As explained by today's notice, the new tax law amended section 168(k) to extend and modify the additional first year depreciation deduction for qualified property that is acquired and placed in service after September 27, 2017, and before January 1, 2027. Under the new law, certain used property also may qualify for the additional first year depreciation deduction.

Notice 2018-30 notes that these changes have collateral consequences in connection with the section 338 approach—for example, the additional first year depreciation would increase recognized built-in gain and reduce recognized built-in loss in the first year of the recognition period, and in some situations, the total recognized built-in gain would increase and the total recognized built-in loss would either increase (or decrease) over the five-year recognition period. The IRS and Treasury Department determined that these changes are not appropriate, and are not mandated by the new tax law or the legislative history.

Accordingly, with today's notice, the IRS and Treasury have determined that the hypothetical cost recovery deduction using the additional first year depreciation allowed under section 168(k) does not provide a reasonable estimate of the income or expense produced by a built-in gain (or loss) asset during the recognition period. A similar concern has been found under the section 1374 approach.

### **Notice 2018-30**

Today's notice modifies the section 338 approach of Notice 2003-65, to provide that in determining the recognized built-in gain (or loss), the hypothetical cost recovery deductions that would have been allowable if an election under section 338 had been made are determined without regard to section 168(k).

Notice 2018-30 also modifies the section 1374 approach, to provide that in computing the amount of cost recovery deductions that are not attributable to an asset's built-in loss on the change date, the hypothetical cost recovery deductions that would have

been allowable had the loss corporation purchased the asset for its fair market value on the change date are determined without regard to section 168(k).

The IRS and Treasury have requested comments on the treatment of built-in items under section 382(h).

Notice 2018-30 is effective for any ownership changes that occur after May 8, 2018.

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