

[4830-01-u]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-116567-99]

RIN 1545-AX67

Definition of Hyperinflationary Currency for Purposes of Section 988

AGENCY: Internal Revenue Service (IRS), Treasury

ACTION: Notice of proposed rulemaking and notice of public hearing

SUMMARY: This document contains proposed regulations concerning when a currency will be considered hyperinflationary for purposes of section 988. These regulations are intended to prevent distortions associated with the computation of income and expense arising from section 988 transactions denominated in hyperinflationary currencies. This document also provides notice of a public hearing on these regulations.

DATES: Written and electronic comments must be received by April 20, 2000. Requests to speak (with outlines of oral comments) at the public hearing scheduled for May 17, 2000 at 10 a.m. must be submitted by April 20, 2000.

ADDRESSES: Send submissions to CC:DOM:CORP:R (REG-116567-99), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC. 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (REG-116567-99), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by

submitting comments directly to the IRS site at <http://www.irs.ustreas.gov/tax-regs/regslst.html>. The public hearing is in room 2615, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Roger M. Brown at (202) 622-3830; concerning submissions of comments, the hearing, and/or requests to be placed on the building access list to attend the hearing, contact Guy R. Traynor at (202)-622-7180 (not toll-free numbers) .

SUPPLEMENTARY INFORMATION:

Background

This document contains a proposed amendment to the Income Tax Regulations (26 CFR part 1) under section 988 of the Internal Revenue Code (Code). On March 17, 1992, the IRS and Treasury published final regulations in the **Federal Register** at 57 FR 9172 relating to the taxation of section 988 transactions, including, *inter alia*, transactions denominated in hyperinflationary currencies. Also on March 17, 1992, proposed regulations were published in the **Federal Register** at 57 FR 9217 (INTL-15-91) relating to the treatment of certain financial instruments denominated in hyperinflationary currencies. The proposed regulations did not separately define hyperinflationary currency. Rather, they simply made reference to the definition in the final regulations, §1.988-1(f).

Further, elsewhere in this issue of the **Federal Register**, TD 8860 finalized the proposed regulations issued in 1992. This notice of proposed rulemaking is intended to accompany the publication of these final regulations and propose a change in the period of years that are considered in determining whether a currency is hyperinflationary for purposes of section 988.

Explanation of Provisions

For purposes of section 988, the term hyperinflationary currency is defined in §1.988-1(f), which utilizes the definition in §1.985-1(b)(2)(ii)(D). This definition was developed in the context of the Dollar Approximate Separate Transactions Method (DASTM) regulations, §1.985-3, and generally considers the cumulative effects of inflation over the base period in determining whether a currency is hyperinflationary. The base period consists of the thirty-six calendar month period immediately preceding the first day of the current calendar year. Use of this base period is generally appropriate in the context of DASTM because a qualified business unit needs to know in advance if it is subject to §1.985-3 calculations. In part, this is because of the translation period requirements of §1.985-3(c)(7).

However, failure to take the current year's inflation into account for purposes of computing foreign currency gain or loss under section 988 may lead to distortions in income and expense arising from certain items whose cash flows reflect hyperinflationary conditions because inflation may rise dramatically in single year. Accordingly, the IRS and Treasury believe that for purposes of section 988, it is more appropriate to consider the cumulative inflation rate over the thirty-six month period ending on the last day of the taxpayer's (or the qualified business unit's) current taxable year. See also §1.905-3T(d)(4)(i) (including current year inflation in determining whether a currency is hyperinflationary for purposes of section 905). The change in the base period in this notice of proposed rulemaking, however, applies only for the purposes of section 988 and not for the purpose of determining whether a taxpayer (or QBU) is subject to the provisions of §1.985-3. However, other Code provisions may be affected by this change, due to the relationship of their substantive rule to section 988. See, e.g., §1.267(f)-1(e) (relating to the

application of the loss disallowance rule of section 267(a)(1) as applied to related party, nonfunctional currency loans).

Proposed Effective Date

These regulations are proposed to apply to transactions entered into after February 14, 2000. Until these proposed regulations are finalized, the existing final regulations under §1.988-1(f) shall remain in effect.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because these regulations do not impose a collection of information on small entities, the provisions of the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Small Business Administration for comment on its impact on small businesses.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any electronic and written comments (a signed original and eight (8) copies, if written) that are submitted timely to the IRS. In particular, the IRS and Treasury are interested in comments relating to the change in the measurement of the base period, and suggesting other standards that may be applied in determining whether a currency should be considered hyperinflationary for purposes of section 988. Examples of the latter category of comments

would be suggestions of alternative time periods (base periods) and hyperinflationary thresholds (e.g., different from the current 100% cumulative inflation rate) which may be used in determining whether a currency is hyperinflationary. All comments will be available for public inspection and copying.

A public hearing has been scheduled for May 17, 2000, beginning at 10 a.m. in room 2615, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance, located 1111 Constitution Avenue. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 15 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the FOR FURTHER INFORMATION CONTACT section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons who wish to present oral comments at the hearing must submit written comments by April 20, 2000, and submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by April 20, 2000. A period of ten (10) minutes will be allotted to each person for making comments. An agenda showing the scheduling of speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Roger M. Brown of the Office of the Associate Chief Counsel (International). However, other personnel from the IRS and Treasury Department

also participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1 -- INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. In §1.988-1 paragraph (f) is revised to read as follows:

§1.988-1 Certain definitions and special rules.

* * * * *

(f) Hyperinflationary currency--(1) Definition. For purposes of section 988, a hyperinflationary currency means a currency described in §1.985-1(b)(2)(ii)(D). However, the base period means the thirty-six calendar month period ending on the last day of the taxpayer's (or qualified business unit's) current taxable year. Thus, for example, if for 1996, 1997, and 1998, a country's annual inflation rates are 6 percent, 11 percent, and 90 percent, respectively, the cumulative inflation rate for the three-year base period is 124% $[(1.06 \times 1.11 \times 1.90) - 1.0 = 1.24] \times 100 = 124\%$. Accordingly, assuming the QBU has a calendar year as its taxable year, the currency of the country is hyperinflationary for the 1998 taxable year.

(2) Effective date. Paragraph (f)(1) shall apply to transactions entered into after February 14, 2000.

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Robert E. Wenzel
Deputy Commissioner of Internal Revenue