

# Internal Revenue bulletin

Bulletin No. 2000-40  
October 2, 2000

## HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

### INCOME TAX

#### **T.D. 8895, page 304.**

Final regulations implement section 6071(b) of the Code and extend the due date for filing information returns from February 28 or the last day of February to March 31 if the information returns are filed electronically by payors required to file after December 31, 1999. Final regulations under sections 6651(a)(2) and 6651(a)(3) of the Code provide that the failure to pay penalties will be reduced from 0.5 percent per month to 0.25 percent per month during the period an installment agreement under section 6159 of the Code is in effect. The penalty reduction applies to installment agreements beginning after December 31, 1999.

#### **REG-112502-00, page 316.**

Proposed regulations provide guidance on the treatment under subpart F of income earned by a controlled foreign corporation (CFC) through a partnership. A public hearing is scheduled for December 5, 2000.

#### **Rev. Proc. 2000-37, page 308.**

**Like-kind exchanges; replacement property; “parking” arrangements.** This procedure provides a safe harbor under which the Service will not challenge (a) the qualification of property as either “replacement property” or “relinquished property” for purposes of section 1031 of the Code or (b) the treat-

ment of the “exchange accommodation titleholder” as the beneficial owner of such property for federal income tax purposes, if the property is held in a “qualified exchange accommodation arrangement” (QEAA).

### ADMINISTRATIVE

#### **Rev. Proc. 2000-38, page 310.**

**Distributor commissions.** This revenue procedure provides three permissible methods of accounting for distributor commissions. It also provides instructions for a taxpayer to obtain consent from the Commissioner of Internal Revenue to change to any of the three permissible methods of accounting, including rules relating to the limitations, terms, and conditions the Commissioner deems necessary to make the change. Rev. Proc. 99-49 modified and amplified.

#### **Announcement 2000-80, page 320.**

This announcement informs the public of the new toll-free number for contacting an Appeals Officer (Customer Service/Outreach).

Finding Lists begin on page ii.  
Index for July through September begins on page iv.



Department of the Treasury  
Internal Revenue Service

# The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities

and by applying the tax law with integrity and fairness to all.

## Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and proce-

dures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

### **Part I.—1986 Code.**

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

### **Part II.—Treaties and Tax Legislation.**

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

### **Part III.—Administrative, Procedural, and Miscellaneous.**

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

### **Part IV.—Items of General Interest.**

This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The first Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the first Bulletin of the succeeding semiannual period, respectively.

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# Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

## Section 6071.—Time for Filing Returns and Other Documents

26 CFR 31.6071(b): Electronically filed information returns.

T.D.8895

### DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Parts 1, 31, and 301

#### Extension of Due Date for Electronically Filed Information Returns; Limitation of Failure to Pay Penalty for Individuals During Period of Installment Agreement

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

**SUMMARY:** This document contains final regulations implementing section 6071(b) relating to the extension of the due date for certain electronically filed information returns. The final regulations also provide rules under section 6651(h) relating to a penalty reduction for certain individuals who have agreed with the IRS to make installment payments in satisfaction of their tax liability. The regulations relating to extension of filing dates affect payors required to file information returns after December 31, 1999. The regulations relating to penalty reduction affect individual taxpayers with installment agreements in effect during months beginning after December 31, 1999.

**DATES:** *Effective Date:* These regulations are effective August 18, 2000.

*Applicability Date:* The provisions of these regulations under section 6071(b) apply for returns required to be filed after December 31, 1999. The provisions of these regulations under section 6651(h) apply for determining the addition to tax for months beginning after December 31, 1999.

**FOR FURTHER INFORMATION CONTACT:** Marilyn E. Brookens, (202) 622-4920 (for information relating to the extension of due dates under section 6071(b)); or Robert B. Taylor, (202) 622-4940 (for information relating to the reduction in the penalty under section 6651(h)) (not toll-free numbers).

## SUPPLEMENTARY INFORMATION:

### Background and Explanation of Provisions

This document contains amendments to the Income Tax Regulations, Employment Tax Regulations, and Procedure and Administration Regulations (26 CFR Parts 1, 31, and 301), and implements sections 6071(b) and 6651(h), which were added to the Internal Revenue Code (Code) by the Internal Revenue Service Restructuring and Reform Act of 1998, Public Law 105-206 (112 Stat. 685, 724 (1998 Act)). Section 6071(b) was added to the Code by section 2002 of the 1998 Act and extends the due date for information returns required by chapter 61, subchapter A, part III, subparts B and C (sections 6041 through 6053) that are filed electronically. The information returns affected include the Form W-2 series, Form W-2G, the Form 1098 series, the Form 1099 series, and Form 8027. Under section 6071(b) such information returns are due on or before March 31 of the year following the calendar year to which the returns relate. Section 6071(b) applies to information returns required to be filed with the IRS or the Social Security Administration after December 31, 1999.

Section 6651(h) was added to the Code by section 3303 of the 1998 Act and provides that, for individuals, the failure to pay penalty is reduced from 0.5 percent per month to 0.25 percent per month during the period an installment agreement under section 6159 is in effect with regard to a timely filed return. Section 6651(h) applies to any Federal tax liability of an individual (including a liability under subtitle C) and is effective for determining the addition to tax for months beginning after December 31, 1999.

On January 27, 2000, a notice of proposed rulemaking (REG-105279-99, 2000-8 I.R.B. 707) under sections 6071(b) and 6651(h) was published in the **Federal Register** (65 F.R. 4396). Although written or electronic comments and requests for a public hearing were solicited, no comments were received and no public hearing was requested or held. The proposed regulations under sections 6071(b) and 6651(h) are adopted by this Treasury decision.

## Special Analyses

It has been determined that this Treasury decision 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 the regulations do not impose a collection of information on small entities, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking that preceded these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

## Drafting Information

The principal author of the regulations relating to the extension of due dates under section 6071(b) is Marilyn E. Brookens, Office of Associate Chief Counsel (Income Tax & Accounting). The principal author of the regulations relating to the reduction in the penalty under section 6651(h) is Robert B. Taylor, Office of Assistant Chief Counsel (Administrative Provisions and Judicial Practice). However, other personnel from the IRS and Treasury Department participated in their development.

\* \* \* \* \*

## Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1, 31, and 301 are 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 § 1.6041-2, paragraph (a)(3)(ii) is revised to read as follows:

*§ 1.6041-2 Return of information as to payments to employees.*

(a) \* \* \*

(3) \* \* \*

(ii) *Exception.* In a case where an employer is not required to file Forms W-3 and W-2 under §31.6011(a)-4 or §31.6011(a)-5 of this chapter, returns on Forms W-3 and W-2 required under this paragraph (a) for any calendar year shall be filed on or before February 28 (March 31 if filed electronically) of the following year.

\* \* \* \* \*

Par. 3. In §1.6041-6, the first sentence is revised to read as follows:

*§1.6041-6 Returns made on Forms 1096 and 1099 under section 6041; contents and time and place for filing.*

Returns made under section 6041 on Forms 1096 and 1099 for any calendar year shall be filed on or before February 28 (March 31 if filed electronically) of the following year with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for such forms. \* \* \*

Par. 4. In §1.6042-2, the first sentence of paragraph (c) is revised to read as follows:

*§1.6042-2 Returns of information as to dividends paid in calendar years after 1962.*

\* \* \* \* \*

(c) *Time and place for filing.* The returns required under this section for any calendar year shall be filed after September 30 of such year, but not before the payer's final payment for the year, and on or before February 28 (March 31 if filed electronically) of the following year with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for Form 1096. \* \* \*

\* \* \* \* \*

Par. 5. In §1.6043-2, paragraph (a) is revised to read as follows:

*§1.6043-2 Return of information respecting distributions in liquidation.*

(a) Unless the distribution is one in respect of which information is required to be filed pursuant to §1.332-6(b), 1.368-3(a), or 1.1081-11, every corporation making any distribution of \$600 or more during a calendar year to any shareholder in liquidation of the whole or any part of its capital stock shall file a return of information on Forms 1096 and 1099,

giving all the information required by such form and by the regulations in this part. A separate Form 1099 must be prepared for each shareholder to whom such distribution was made, showing the name and address of such shareholder, the number and class of shares owned by him in liquidation of which such distribution was made, and the total amount distributed to him on each class of stock. If the amount distributed to such shareholder on any class of stock consisted in whole or in part of property other than money, the return on such form shall in addition show the amount of money distributed, if any, and shall list separately each class of property other than money distributed, giving a description of the property in each such class and a statement of its fair market value at the time of the distribution. Such forms, accompanied by transmittal Form 1096 showing the number of Forms 1099 filed therewith, shall be filed on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which such distribution was made with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for Form 1096.

\* \* \* \* \*

Par. 6. In §1.6044-2, the first sentence of paragraph (d) is revised to read as follows:

*§1.6044-2 Returns of information as to payments of patronage dividends with respect to patronage occurring in taxable years beginning after 1962.*

\* \* \* \* \*

(d) *Time and place for filing.* The return required under this section on Forms 1096 and 1099 for any calendar year shall be filed after September 30 of such year, but not before the payer's final payment for the year, and on or before February 28 (March 31 if filed electronically) of the following year, with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for such forms. \* \* \*

\* \* \* \* \*

Par. 7. Section §1.6045-1 is amended by adding paragraph (r) to read as follows:

*§1.6045-1 Returns of information of brokers and barter exchanges.*

\* \* \* \* \*

(r) *Electronic filing.* Notwithstanding the time prescribed for filing in paragraph (j) of this section, Forms 1096 and 1099 required under this section for reporting periods ending during a calendar year shall, if filed electronically, be filed after the last calendar day of the reporting period elected by the broker or barter exchange and on or before March 31 of the following calendar year.

Par. 8. In §1.6045-2, paragraph (g)(3) is revised to read as follows:

*§1.6045-2 Furnishing statement required with respect to certain substitute payments.*

\* \* \* \* \*

(g) \* \* \*

(3) *Time and place of filing.* The returns required under this paragraph (g) for any calendar year shall be filed after September 30 of such year, but not before the final substitute payment for the year is received by the broker, and on or before February 28 (March 31 if filed electronically) of the following year with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for Form 1096.

\* \* \* \* \*

Par. 9. In §1.6045-4, the first sentence of paragraph (j) is revised to read as follows:

*§1.6045-4 Information reporting on real estate transactions with dates of closing on or after January 1, 1991.*

\* \* \* \* \*

(j) *Time and place for filing.* A reporting person shall file the information returns required by this section with respect to a real estate transaction after December 31 of the calendar year that includes the date of closing (as determined under paragraph (h)(2)(ii) of this section) and on or before February 28 (March 31 if filed electronically) of the following calendar year. \* \* \*

\* \* \* \* \*

Par. 10. In §1.6047-1, the first sentence of paragraph (a)(6) is revised to read as follows:

*§1.6047-1 Information to be furnished with regard to employee retirement plan covering an owner-employee.*

(a) \* \* \*

(6) *Time and place for filing.* The return required under this section for any calendar year shall be filed after the close of that year and on or before February 28 (March 31 if filed electronically) of the following year with any of the Internal Revenue Service Centers, the addresses of which are listed in the instructions for Form 1096. \* \* \*

Par. 11. Section 1.6049-4 is amended by:

1. Revising the first sentence of paragraph (g)(1).

2. Revising the first sentence of paragraph (g)(2).

The revisions read as follows:

*§1.6049-4 Return of information as to interest paid and original issue discount includible in gross income after December 31, 1982.*

\* \* \* \* \*

(g) \* \* \* (1) *Annual return.* Except as provided in paragraph (g)(2) of this section, the returns required under this section for any calendar year for the payment of interest shall be filed after September 30 of such year, but not before the payor's final payment to the payee for the year, and on or before February 28 (March 31 if filed electronically) of the following year. \* \* \*

(2) *Transactional return.* In the case of a return under paragraph (e) of this section, relating to returns on a transactional basis, such return shall be filed at any time but in no event later than February 28 (March 31 if filed electronically) of the year following the calendar year in which the interest was paid. \* \* \*

\* \* \* \* \*

Par. 12. In §1.6049-7, the first sentence of paragraph (b)(2)(iv) is revised to read as follows:

*§1.6049-7 Returns of information with respect to REMIC regular interests and collateralized debt obligations.*

\* \* \* \* \*

(b) \* \* \*

(2) \* \* \*

(iv) *Time and place for filing a return with respect to amounts includible as interest.* The returns required under this paragraph (b)(2) for any calendar year

must be filed after September 30 of that year, but not before the payor's final payment to the payee for the year, and on or before February 28 (March 31 if filed electronically) of the following year. \* \* \*

\* \* \* \* \*

Par. 13. In §1.6050A-1, paragraph (b) is revised to read as follows:

*§1.6050A-1 Reporting requirements of certain fishing boat operators.*

\* \* \* \* \*

(b) *Time and place for filing.* Returns required to be made under this section on Form 1099-MISC shall be filed with the Internal Revenue Service Center, designated in the instructions for Form 1099-MISC, on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the relevant services were performed. \* \* \*

\* \* \* \* \*

Par. 14. In §1.6050D-1, paragraph (b) is revised to read as follows:

*§1.6050D-1 Information returns relating to energy grants and financing.*

\* \* \* \* \*

(b) *Time and place for filing.* Returns required to be made under this section shall be filed with the Internal Revenue Service Center designated in the instructions for Form 6497 or 1099-G on or before the last day of February (March 31 if filed electronically) of the year following the calendar year for which the return is made.

Par. 15. In §1.6050E-1, the first sentence of paragraph (h) is revised to read as follows:

*§1.6050E-1 Reporting of State and local income tax refunds.*

\* \* \* \* \*

(h) *Time and place for filing.* The returns required under this section for any calendar year shall be filed after September 30 of that calendar year, but not before the refund officer's final payment (or allowance of credit or offset) for the year, and on or before February 28 (March 31 if filed electronically) of the following year. \* \* \*

\* \* \* \* \*

Par. 16. In §1.6050H-2, the first and second sentences of paragraph (a)(4) are revised to read as follows:

*§1.6050H-2 Time, form, and manner of reporting interest received on qualified mortgage.*

(a) \* \* \*

(4) *Time and place for filing return.* An interest recipient must file a return required by this paragraph (a) on or before February 28 (March 31 if filed electronically) of the year following the calendar year for which it receives the mortgage interest. If no interest is required to be reported for the calendar year, but a reimbursement of interest on a qualified mortgage is required to be reported for the calendar year, then a return required by this paragraph (a) must be filed on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the reimbursement was made. \* \* \*

\* \* \* \* \*

Par. 17. In §1.6050J-1T, A-33 is revised to read as follows:

*§1.6050J-1T Questions and answers concerning information returns relating to foreclosures and abandonments of security (temporary).*

\* \* \* \* \*

A-33: The return or returns must be filed on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the acquisition of an interest in the property occurs or in which the lender knows or has reason to know of the abandonment of the property. \* \* \*

\* \* \* \* \*

Par. 18. In §1.6050P-1, paragraph (a)(4)(i) is revised to read as follows:

*§1.6050P-1 Information reporting for discharges of indebtedness by certain financial entities.*

(a) \* \* \*

(4) \* \* \* (i) *In general.* Except as provided in paragraph (a)(4)(ii) of this section, returns required by this section must be filed with the Internal Revenue Service office designated in the instructions for Form 1099-C on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the identifiable event occurs. \* \* \*

\* \* \* \* \*

Par. 19. In §1.6052-1, paragraph (b)(1)(ii) is revised to read as follows:

*§1.6052-1 Information returns regarding payment of wages in the form of group-term life insurance.*

\* \* \* \* \*

(b) \* \* \* (1) \* \* \*

(ii) *Exception.* In a case where an employer is not required to file Forms W-3 and W-2 under §31.6011(a)-4 or §31.6011(a)-5 of this chapter, returns on Forms W-3 and W-2 required under paragraph (a) of this section for any calendar year shall be filed on or before February 28 (March 31 if filed electronically) of the following year.

\* \* \* \* \*

**PART 31—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT THE SOURCE**

Par. 20. The authority citation for part 31 continues to read in part as follows:

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

Par. 21. In §31.3402(q)-1, the first sentence of paragraph (f)(1) is revised to read as follows:

*§31.3402(q)-1 Extension of withholding to certain gambling winnings.*

\* \* \* \* \*

(f)(1) *In general.* Every person making payment of winnings for which a statement is required under paragraph (e) of this section shall file a return on Form W-2G with the Internal Revenue Service Center serving the district in which is located the principal place of business of the person making the return on or before February 28 (March 31 if filed electronically) of the calendar year following the calendar year in which the payment of winnings is made. \* \* \*

\* \* \* \* \*

Par. 22. In §31.6053-3, the first sentence of paragraph (a)(4) is revised to read as follows:

*§31.6053-3 Reporting by certain large food or beverage establishments with respect to tips.*

(a) \* \* \*

(4) *Time and place for filing.* The information return required by this paragraph (a) shall be filed on or before the last day of February (March 31 if filed

electronically) of the year following the calendar year for which the return is made with the Internal Revenue Service Center specified by the Form 8027 or its instructions. \* \* \*

\* \* \* \* \*

Par. 23. In §31.6071(a)-1, paragraph (a)(3)(i) is revised to read as follows:

*§31.6071(a)-1 Time for filing returns and other documents.*

(a) \* \* \*

(3) \* \* \* (i) *General rule.* Each information return in respect of wages as defined in the Federal Insurance Contributions Act or of income tax withheld from wages which is required to be made under §31.6051-2 shall be filed on or before the last day of February (March 31 if filed electronically) of the year following the calendar year for which it is made, except that, if a tax return under §31.6011(a)-5(a) is filed as a final return for a period ending prior to December 31, the information statement shall be filed on or before the last day of the second calendar month following the period for which the tax return is filed.

\* \* \* \* \*

**PART 301—PROCEDURE AND ADMINISTRATION**

Par. 24. The authority citation for part 301 continues to read in part as follows:

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

Par. 25. Section 301.6651-1 is amended by:

1. Revising the last sentence in paragraph (a)(2).

2. Revising the second sentence in paragraph (a)(3).

3. Adding paragraph (a)(4).

The revisions and additions read as follows:

*§301.6651-1 Failure to file tax return or to pay tax.*

(a) \* \* \*

(2) \* \* \* Except as provided in paragraph (a)(4) of this section, the amount to be added to the tax is 0.5 percent of the amount of tax shown on the return if the failure is for not more than 1 month, with an additional 0.5 percent for each additional month or fraction thereof during

which the failure continues, but not to exceed 25 percent in the aggregate.

(3) \* \* \* Except as provided in paragraph (a)(4) of this section, the amount to be added to the tax is 0.5 percent of the amount stated in the notice and demand if the failure is for not more than 1 month, with an additional 0.5 percent for each additional month or fraction thereof during which the failure continues, but not to exceed 25 percent in the aggregate. \* \* \*

(4) *Reduction of failure to pay penalty during the period an installment agreement is in effect—(i) In general.* In the case of a return filed by an individual on or before the due date for the return (including extensions)—

(A) The amount added to tax for a month or fraction thereof is determined by using 0.25 percent instead of 0.5 percent under paragraph (a)(2) of this section if at any time during the month an installment agreement under section 6159 is in effect for the payment of such tax; and

(B) The amount added to tax for a month or fraction thereof is determined by using 0.25 percent instead of 0.5 percent under paragraph (a)(3) of this section if at any time during the month an installment agreement under section 6159 is in effect for the payment of such tax.

(ii) *Effective date.* This paragraph (a)(4) applies for purposes of determining additions to tax for months beginning after December 31, 1999.

\* \* \* \* \*

Robert E. Wenzel,  
*Deputy Commissioner  
of Internal Revenue.*

Approved August 1, 2000.

Jonathan Talisman,  
*Acting Assistant Secretary  
of the Treasury.*

(Filed by the Office of the Federal Register on August 17, 2000, 8:45 a.m., and published in the issue of the Federal Register for August 18, 2000, 65 F.R. 50405)

## Part III. Administrative, Procedural, and Miscellaneous

26 CFR 1.1031(a)-1: Property held for productive use in trade or business or for investment;  
1.1031(k)-1: Treatment of deferred exchanges.

### Rev. Proc. 2000-37

#### SECTION 1. PURPOSE

This revenue procedure provides a safe harbor under which the Internal Revenue Service will not challenge (a) the qualification of property as either “replacement property” or “relinquished property” (as defined in § 1.1031(k)-1(a) of the Income Tax Regulations) for purposes of § 1031 of the Internal Revenue Code and the regulations thereunder or (b) the treatment of the “exchange accommodation titleholder” as the beneficial owner of such property for federal income tax purposes, if the property is held in a “qualified exchange accommodation arrangement” (QEAA), as defined in section 4.02 of this revenue procedure.

#### SECTION 2. BACKGROUND

.01 Section 1031(a)(1) provides that no gain or loss is recognized on the exchange of property held for productive use in a trade or business or for investment if the property is exchanged solely for property of like kind that is to be held either for productive use in a trade or business or for investment.

.02 Section 1031(a)(3) provides that property received by the taxpayer is not treated as like-kind property if it: (a) is not identified as property to be received in the exchange on or before the day that is 45 days after the date on which the taxpayer transfers the relinquished property; or (b) is received after the earlier of the date that is 180 days after the date on which the taxpayer transfers the relinquished property, or the due date (determined with regard to extension) for the transferor’s federal income tax return for the year in which the transfer of the relinquished property occurs.

.03 Determining the owner of property for federal income tax purposes requires an analysis of all of the facts and circumstances. As a general rule, the party that bears the economic burdens and benefits of ownership will be considered the owner of property for federal income tax purposes. See Rev. Rul. 82-144, 1982-2 C.B. 34.

.04 On April 25, 1991, the Treasury Department and the Service promulgated final regulations under § 1.1031(k)-1 providing rules for deferred like-kind exchanges under § 1031(a)(3). The preamble to the final regulations states that the deferred exchange rules under § 1031(a)(3) do not apply to reverse-*Starker* exchanges (*i.e.*, exchanges where the replacement property is acquired before the relinquished property is transferred) and consequently that the final regulations do not apply to such exchanges. T.D. 8346, 1991-1 C.B. 150, 151; see *Starker v. United States*, 602 F.2d 1341 (9<sup>th</sup> Cir. 1979). However, the preamble indicates that Treasury and the Service will continue to study the applicability of the general rule of § 1031(a)(1) to these transactions. T.D. 8346, 1991-1 C.B. 150, 151.

.05 Since the promulgation of the final regulations under § 1.1031(k)-1, taxpayers have engaged in a wide variety of transactions, including so-called “parking” transactions, to facilitate reverse like-kind exchanges. Parking transactions typically are designed to “park” the desired replacement property with an accommodation party until such time as the taxpayer arranges for the transfer of the relinquished property to the ultimate transferee in a simultaneous or deferred exchange. Once such a transfer is arranged, the taxpayer transfers the relinquished property to the accommodation party in exchange for the replacement property, and the accommodation party then transfers the relinquished property to the ultimate transferee. In other situations, an accommodation party may acquire the desired replacement property on behalf of the taxpayer and immediately exchange such property with the taxpayer for the relinquished property, thereafter holding the relinquished property until the taxpayer arranges for a transfer of such property to the ultimate transferee. In the parking arrangements, taxpayers attempt to arrange the transaction so that the accommodation party has enough of the benefits and burdens relating to the property so that the accommodation party will be treated as the owner for federal income tax purposes.

.06 Treasury and the Service have determined that it is in the best interest of sound tax administration to provide tax-

payers with a workable means of qualifying their transactions under § 1031 in situations where the taxpayer has a genuine intent to accomplish a like-kind exchange at the time that it arranges for the acquisition of the replacement property and actually accomplishes the exchange within a short time thereafter. Accordingly, this revenue procedure provides a safe harbor that allows a taxpayer to treat the accommodation party as the owner of the property for federal income tax purposes, thereby enabling the taxpayer to accomplish a qualifying like-kind exchange.

#### SECTION 3. SCOPE

.01 *Exclusivity.* This revenue procedure provides a safe harbor for the qualification under § 1031 of certain arrangements between taxpayers and exchange accommodation titleholders and provides for the treatment of the exchange accommodation titleholder as the beneficial owner of the property for federal income tax purposes. These provisions apply only in the limited context described in this revenue procedure. The principles set forth in this revenue procedure have no application to any federal income tax determinations other than determinations that involve arrangements qualifying for the safe harbor.

.02 *No inference.* No inference is intended with respect to the federal income tax treatment of arrangements similar to those described in this revenue procedure that were entered into prior to the effective date of this revenue procedure. Further, the Service recognizes that “parking” transactions can be accomplished outside of the safe harbor provided in this revenue procedure. Accordingly, no inference is intended with respect to the federal income tax treatment of “parking” transactions that do not satisfy the terms of the safe harbor provided in this revenue procedure, whether entered into prior to or after the effective date of this revenue procedure.

.03 *Other issues.* Services for the taxpayer in connection with a person’s role as the exchange accommodation titleholder in a QEAA shall not be taken into account in determining whether that person or a related person is a disqualified

person (as defined in § 1.1031(k)-1(k)). Even though property will not fail to be treated as being held in a QEAA as a result of one or more arrangements described in section 4.03 of this revenue procedure, the Service still may recast an amount paid pursuant to such an arrangement as a fee paid to the exchange accommodation titleholder for acting as an exchange accommodation titleholder to the extent necessary to reflect the true economic substance of the arrangement. Other federal income tax issues implicated, but not addressed, in this revenue procedure include the treatment, for federal income tax purposes, of payments described in section 4.03(7) and whether an exchange accommodation titleholder may be precluded from claiming depreciation deductions (e.g., as a dealer) with respect to the relinquished property or the replacement property.

.04 *Effect of Noncompliance.* If the requirements of this revenue procedure are not satisfied (for example, the property subject to a QEAA is not transferred within the time period provided), then this revenue procedure does not apply. Accordingly, the determination of whether the taxpayer or the exchange accommodation titleholder is the owner of the property for federal income tax purposes, and the proper treatment of any transactions entered into by or between the parties, will be made without regard to the provisions of this revenue procedure.

#### SECTION 4. QUALIFIED EXCHANGE ACCOMMODATION ARRANGEMENTS

.01 *Generally.* The Service will not challenge the qualification of property as either “replacement property” or “relinquished property” (as defined in § 1.1031(k)-1(a)) for purposes of § 1031 and the regulations thereunder, or the treatment of the exchange accommodation titleholder as the beneficial owner of such property for federal income tax purposes, if the property is held in a QEAA.

.02 *Qualified Exchange Accommodation Arrangements.* For purposes of this revenue procedure, property is held in a QEAA if all of the following requirements are met:

(1) Qualified indicia of ownership of the property is held by a person (the “exchange accommodation titleholder”) who

is not the taxpayer or a disqualified person and either such person is subject to federal income tax or, if such person is treated as a partnership or S corporation for federal income tax purposes, more than 90 percent of its interests or stock are owned by partners or shareholders who are subject to federal income tax. Such qualified indicia of ownership must be held by the exchange accommodation titleholder at all times from the date of acquisition by the exchange accommodation titleholder until the property is transferred as described in section 4.02(5) of this revenue procedure. For this purpose, “qualified indicia of ownership” means legal title to the property, other indicia of ownership of the property that are treated as beneficial ownership of the property under applicable principles of commercial law (e.g., a contract for deed), or interests in an entity that is disregarded as an entity separate from its owner for federal income tax purposes (e.g., a single member limited liability company) and that holds either legal title to the property or such other indicia of ownership;

(2) At the time the qualified indicia of ownership of the property is transferred to the exchange accommodation titleholder, it is the taxpayer’s bona fide intent that the property held by the exchange accommodation titleholder represent either replacement property or relinquished property in an exchange that is intended to qualify for nonrecognition of gain (in whole or in part) or loss under § 1031;

(3) No later than five business days after the transfer of qualified indicia of ownership of the property to the exchange accommodation titleholder, the taxpayer and the exchange accommodation titleholder enter into a written agreement (the “qualified exchange accommodation agreement”) that provides that the exchange accommodation titleholder is holding the property for the benefit of the taxpayer in order to facilitate an exchange under § 1031 and this revenue procedure and that the taxpayer and the exchange accommodation titleholder agree to report the acquisition, holding, and disposition of the property as provided in this revenue procedure. The agreement must specify that the exchange accommodation titleholder will be treated as the beneficial owner of the property for all federal income tax purposes. Both parties must report the federal in-

come tax attributes of the property on their federal income tax returns in a manner consistent with this agreement;

(4) No later than 45 days after the transfer of qualified indicia of ownership of the replacement property to the exchange accommodation titleholder, the relinquished property is properly identified. Identification must be made in a manner consistent with the principles described in § 1.1031(k)-1(c). For purposes of this section, the taxpayer may properly identify alternative and multiple properties, as described in § 1.1031(k)-1(c)(4);

(5) No later than 180 days after the transfer of qualified indicia of ownership of the property to the exchange accommodation titleholder, (a) the property is transferred (either directly or indirectly through a qualified intermediary (as defined in § 1.1031(k)-1(g)(4))) to the taxpayer as replacement property; or (b) the property is transferred to a person who is not the taxpayer or a disqualified person as relinquished property; and

(6) The combined time period that the relinquished property and the replacement property are held in a QEAA does not exceed 180 days.

.03 *Permissible Agreements.* Property will not fail to be treated as being held in a QEAA as a result of any one or more of the following legal or contractual arrangements, regardless of whether such arrangements contain terms that typically would result from arm’s length bargaining between unrelated parties with respect to such arrangements:

(1) An exchange accommodation titleholder that satisfies the requirements of the qualified intermediary safe harbor set forth in § 1.1031(k)-1(g)(4) may enter into an exchange agreement with the taxpayer to serve as the qualified intermediary in a simultaneous or deferred exchange of the property under § 1031;

(2) The taxpayer or a disqualified person guarantees some or all of the obligations of the exchange accommodation titleholder, including secured or unsecured debt incurred to acquire the property, or indemnifies the exchange accommodation titleholder against costs and expenses;

(3) The taxpayer or a disqualified person loans or advances funds to the exchange accommodation titleholder or guarantees a loan or advance to the exchange accommodation titleholder;

(4) The property is leased by the exchange accommodation titleholder to the taxpayer or a disqualified person;

(5) The taxpayer or a disqualified person manages the property, supervises improvement of the property, acts as a contractor, or otherwise provides services to the exchange accommodation titleholder with respect to the property;

(6) The taxpayer and the exchange accommodation titleholder enter into agreements or arrangements relating to the purchase or sale of the property, including puts and calls at fixed or formula prices, effective for a period not in excess of 185 days from the date the property is acquired by the exchange accommodation titleholder; and

(7) The taxpayer and the exchange accommodation titleholder enter into agreements or arrangements providing that any variation in the value of a relinquished property from the estimated value on the date of the exchange accommodation titleholder's receipt of the property be taken into account upon the exchange accommodation titleholder's disposition of the relinquished property through the taxpayer's advance of funds to, or receipt of funds from, the exchange accommodation titleholder.

*.04 Permissible Treatment.* Property will not fail to be treated as being held in a QEAA merely because the accounting, regulatory, or state, local, or foreign tax treatment of the arrangement between the taxpayer and the exchange accommodation titleholder is different from the treatment required by section 4.02(3) of this revenue procedure.

## SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for QEAAs entered into with respect to an exchange accommodation titleholder that acquires qualified indicia of ownership of property on or after September 15, 2000.

## SECTION 6. PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1701. An agency may not conduct or sponsor, and a person is not required to

respond to, a collection of information unless the collection of information displays a valid control number.

The collections of information are contained in section 4.02 of this revenue procedure, which requires taxpayers and exchange accommodation titleholders to enter into a written agreement that the exchange accommodation titleholder will be treated as the beneficial owner of the property for all federal income tax purposes. This information is required to ensure that both parties to a QEAA treat the transaction consistently for federal tax purposes. The likely respondents are businesses and other for-profit institutions, and individuals.

The estimated average annual burden to prepare the agreement and certification is two hours. The estimated number of respondents is 1,600, and the estimated total annual reporting burden is 3,200 hours.

The estimated annual frequency of responses is on occasion.

Books and records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

## DRAFTING INFORMATION

The principal author of this revenue procedure is J. Peter Baumgarten of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue procedure, contact Mr. Baumgarten at (202) 622-4950 (not a toll-free call).

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*26 CFR 601.204: Changes in accounting periods and in methods of accounting.  
(Also Part I, §§ 446, 481; 1.446-1, 1.481-1.)*

## Rev. Proc. 2000-38

### SECTION 1. PURPOSE

This revenue procedure provides three permissible methods of accounting for distributor commissions (as defined in § 2 below). A taxpayer may change to or adopt any of the three methods. This revenue procedure provides procedures for a taxpayer to obtain consent from the Commissioner of Internal Revenue to change to any of the three methods of accounting

for distributor commissions, including rules relating to the limitations, terms, and conditions the Commissioner deems necessary to make the change.

## SECTION 2. DEFINITIONS

Under Rule 12b-1 (17 C.F.R. § 270.12b-1), an open-end regulated investment company ("mutual fund") may adopt, for one or more classes of its shares, a plan that permits it to use fund assets to pay a fee to cover distribution costs of fund shares ("distribution fee"). For purposes of this revenue procedure, the term "distributor commissions" means commissions paid or incurred by a distributor of a mutual fund on the sale of mutual fund shares for which the distributor is to receive a distribution fee from the mutual fund and, in some cases, a contingent deferred sales charge from the investor in future taxable year(s) (typically referred to in the mutual fund industry as "B shares"). Distributor commissions do not include commissions paid or incurred on the sale of mutual fund shares for which the distributor is to receive a distribution fee and, in some cases, a contingent deferred sales charge in future taxable years and will make commission payments to the selling broker in an amount equal to the amount it receives each year that the shares remain outstanding (typically referred to in the mutual fund industry as "C shares").

## SECTION 3. BACKGROUND

.01 Mutual funds generally distribute new shares to the public through a distributor. If an investor purchases mutual fund shares through a broker, either the investor or the distributor pays the brokerage commissions. If the distributor pays the brokerage commissions (i.e., distributor commissions), the distributor typically recovers this cost by collecting from the mutual fund a distribution fee in accordance with Rule 12b-1 and, in some cases, by receiving a sales charge from the investor if the shares are redeemed within a specified period of time.

.02 Under § 446, the Commissioner has broad authority to determine whether a method of accounting clearly reflects income. Under § 446(b), if a taxpayer's method of accounting does not clearly reflect income, the computation of taxable income must be made under a method

that, in the opinion of the Secretary, does clearly reflect income. See *Thor Power Tool Co. v. Commissioner*, 439 U.S. 522 (1979), 1979-1 C.B. 167; *Commissioner v. Hansen*, 360 U.S. 446 (1959), 1959-2 C.B. 460; § 1.446-1(c)(2)(ii) of the Income Tax Regulations.

.03 To minimize disputes regarding the accounting for distributor commissions and to provide appropriate methods for matching those commissions with the related distribution fees and sales charges so as to clearly reflect income, the Internal Revenue Service will permit a taxpayer that complies with the requirements of this revenue procedure to account for distributor commissions using any of the three permissible methods of accounting described in § 5 of this revenue procedure. A taxpayer may use any of these three methods to account for the distributor commissions related to each class of shares within each mutual fund for which it acts as a distributor.

.04 A change in a taxpayer's treatment of distributor commissions to any of the three permissible methods described in § 5 of this revenue procedure is a change in method of accounting to which §§ 446 and 481 apply. Sections 446(e) and 1.446-1(e) provide that, except as otherwise provided, a taxpayer must secure the consent of the Commissioner before changing a method of accounting for federal income tax purposes. Section 1.446-1(e)(3)(ii) authorizes the Commissioner to prescribe administrative procedures setting forth the limitations, terms, and conditions deemed necessary to permit a taxpayer to obtain consent to change a method of accounting.

#### SECTION 4. SCOPE

This revenue procedure applies to a taxpayer that chooses to account for distributor commissions under any of the three permissible methods of accounting for distributor commissions provided in § 5 of this revenue procedure. This revenue procedure does not apply to amortizable section 197 intangibles.

#### SECTION 5. PERMISSIBLE METHODS OF ACCOUNTING

##### .01 DISTRIBUTION FEE PERIOD METHOD.

(1) *Description of Method.* The treatment of distributor commissions in accor-

dance with the distribution fee period method is a permissible method of accounting. Under the distribution fee period method, a taxpayer must capitalize distributor commissions paid or incurred during the taxable year on the sale of shares in a mutual fund and amortize those amounts ratably over a specific recovery period determined by the number of years for which the 12b-1 plan provides the taxpayer is to receive a distribution fee from the mutual fund as a result of the sale of those shares (distribution fee period). Amortization for a short taxable year is based on the number of months in the short taxable year (taking into account the half-year convention if § 5.01(2)(b) applies).

##### (2) *Pooling Allowed.*

(a) For purposes of accounting for distributor commissions under the distribution fee period method, a taxpayer may establish one or more pools of commissions. A pool may be established with respect to distributor commissions related to a class of shares of a mutual fund sold in a single taxable year. A pool of distributor commissions may contain commissions related to a class of mutual fund shares sold in a single taxable year from one or more mutual funds, provided the distributor commissions for each class of mutual fund shares is accounted for under the distribution fee method. However, a pool may only include distributor commissions related to a class of mutual fund shares sold in a single taxable year with the same distribution fee period and the same compensation structure.

(b) A taxpayer that establishes annual pools for purposes of using the distribution fee period method must compute the amount of the amortization deduction using a half-year convention.

(c) Distribution fees have the same compensation structure if they are calculated on the basis of the same percentage of the mutual fund's average net assets.

##### (3) *Termination of Right to Distribution Fees.*

(a) Basis recovery allowed. A taxpayer that uses the distribution fee period method described in this § 5.01 may account for the termination of its right to receive a distribution fee for a particular share in a mutual fund by claiming in the year of termination a loss or, for a sale of the distributor's right to all, or an undi-

vided interest in a part, of its future distribution fees for the share, an offset against sales proceeds. A taxpayer that uses pools in connection with the distribution fee period method described in this § 5.01 determines its unrecovered basis in its right to receive distribution fees for particular shares in a prior year pool that are terminated by multiplying its unrecovered basis in the applicable pool of distributor commissions as of the beginning of the year by a fraction, the numerator of which is the number of terminated shares for which commissions were in the pool as of the beginning of the year and the denominator of which is the number of shares for which commissions were in the pool as of the beginning of the year. To determine the unrecovered basis for its right to receive distribution fees for a particular share in a current year pool that is terminated in the initial year (i.e., the year the share giving rise to the right to receive distribution fees is sold), the taxpayer must multiply the unrecovered basis in the applicable pool as of the end of the year by a fraction, the numerator of which is the number of shares terminated during the year for which commissions in the pool were paid or incurred during the year and the denominator of which is the number of shares sold during the year for which commissions in that pool were paid or incurred during the year. The unrecovered basis in the applicable pool of distributor commissions must be reduced by the basis allocable to the terminated shares, as determined in the preceding two sentences, before calculating the amortization deduction for the year. If a taxpayer does not have sufficient information to relate a termination event to a specific pool, the taxpayer must treat the termination event as relating to the earliest remaining pool in accordance with the principles of § 1.1012-1(c)(1).

(b) Termination events. For purposes of § 5.01(3)(a) of this revenue procedure, a taxpayer's right to a distribution fee for a particular share terminates when the taxpayer is no longer entitled to receive a distribution fee related to that share in subsequent years. Termination may occur as a result of (i) a sale of the distributor's right to all future distribution fees for the share, (ii) the redemption of the share by the shareholder, or (iii) the conversion of the share into another class of shares for

which the taxpayer is not entitled to receive a distribution fee. If a taxpayer sells an undivided interest in its right to all present and future distribution fees associated with a share or a portion of a pool, termination occurs in proportion to the interest sold.

#### .02 5-YEAR METHOD.

(1) *Description of Method.* The treatment of distributor commissions in accordance with the 5-year method is a permissible method of accounting. Under the 5-year method, a taxpayer must capitalize distributor commissions paid or incurred during the taxable year and amortize those amounts ratably over a 5-year period. Amortization for a short taxable year is based on the number of months in the short taxable year (taking into account the half-year convention).

##### (2) *Pooling Required.*

(a) For purposes of accounting for distributor commissions under the 5-year method, a taxpayer must establish one or more pools of commissions. All commissions related to a class of shares of a mutual fund sold in a single taxable year must be in the same pool. A pool of distributor commissions may contain commissions related to classes of mutual fund shares from one or more mutual funds, provided the distributor commissions for each of the classes of mutual fund shares are accounted for using the 5-year method.

(b) A taxpayer that uses the 5-year method must compute the amount of the amortization deduction using a half-year convention.

(3) *Termination of Right to Distribution Fees.* A taxpayer that uses the 5-year method described in this § 5.02 may not claim a loss or an offset against sales proceeds for the unamortized portion of a distributor commission as a result of a termination event for a particular share, as described in § 5.01(3)(b) of this revenue procedure. However, if the taxpayer experiences a termination event with respect to the distribution fees related to all the shares in a pool, the taxpayer may claim a loss or an offset against sales proceeds for the unamortized portion of the distributor commissions in that pool. In addition, if a taxpayer sells an undivided interest in its right to all present and future distribution fees for all the shares in a pool, the tax-

payer experiences a termination event with respect to the pool, but only in proportion to the interest sold, and may claim the corresponding loss or offset against sales proceeds.

#### .03 USEFUL LIFE METHOD

(1) *Description of Method.* The treatment of distributor commissions in accordance with the useful life method is a permissible method of accounting. Under the useful life method, a taxpayer must capitalize distributor commissions paid or incurred during the taxable year and recover those amounts over their estimated useful life. See § 1.167(a)–1(b).

(2) *Determination of Useful Life.* The recovery method and useful life of distributor commissions must be established by taking into account all the facts and circumstances including, for example, (i) the period during which the taxpayer is to receive distribution fees from a mutual fund under the 12b–1 plan with respect to particular shares, and (ii) the experience of the taxpayer regarding how long a typical share burdened with a given distribution fee remains outstanding after purchase. See § 1.167(a)–1(b).

(3) *Pooling Allowed.* For purposes of accounting for distributor commissions under the useful life method, a taxpayer may establish one or more pools of commissions. A taxpayer that establishes annual pools under the useful life method must compute the amount of the amortization deduction using a half-year convention.

(4) *Retirement of Right to Distribution Fees.* The determination of whether or not a taxpayer using the useful life method may claim a loss is governed by § 1.167(a)–8. For example, if the useful life of the distributor commissions under the useful life method does not reflect any retirements, including a termination of a right to a distribution fee, the taxpayer may claim a loss for the unamortized portion of a distributor commission as a result of a retirement. If the useful life of the distributor commissions under the useful life method is an average useful life that reflects retirements, the taxpayer may not claim a loss for the unamortized portion of a distributor commission as a result of a retirement, regardless of whether the distributor commission is accounted for as a single asset or in a pool,

unless distributor commissions related to all the shares in the pool are retired.

## SECTION 6. CHANGE IN METHOD OF ACCOUNTING

.01 *Change to the Distribution Fee Period Method, the 5-year Method, or the Useful Life Method.* A taxpayer that wants to change its method of accounting for distributor commissions for the taxable year that includes January 1, 2001, to any of the three methods described in this revenue procedure must follow the automatic change in method of accounting provisions in Rev. Proc. 99–49, 1999–52 I.R.B. 725, (or its successor) with the following modifications:

(1) A taxpayer that files a copy of the Form 3115, Application for Change in Accounting Method, to change its method of accounting for distributor commissions with the national office of the Internal Revenue Service on or before April 2, 2001, is not subject to the scope limitations in § 4.02 of Rev. Proc. 99–49, unless the taxpayer's method of accounting for distributor commissions is an issue under consideration before a federal court within the meaning of § 3.09(3) of Rev. Proc. 99–49. If the taxpayer is under examination, before an appeals office, or before a federal court at the time that a copy of the Form 3115 is filed with the national office, the taxpayer must provide a duplicate copy of the Form 3115 to the examining agent, appeals officer, or counsel for the government, as appropriate, at the time the copy of the Form 3115 is filed. The Form 3115 must contain the name(s) and telephone number(s) of the examining agent, appeals officer, or counsel for the government, as appropriate. If the taxpayer's method of accounting for distributor commissions is an issue pending within the meaning of § 6.01(6) of this revenue procedure at the time that a Form 3115 is filed with the national office, the taxpayer also must provide to the examining agent or appeals officer, as appropriate, an executed closing agreement substantially in the form set forth in APPENDIX A of this revenue procedure.

(2) The change must be made using a cut-off method and applies only to distributor commissions paid or incurred on or after January 1, 2001. Because no items are duplicated or omitted from income when a cut-off method is used, a § 481(a)

adjustment described in § 5.03 of Rev. Proc. 99-49 is not necessary. See § 2.06 of Rev. Proc. 99-49.

(3) The year of change is the taxable year that includes January 1, 2001.

(4) Section 6.02(2)(a) of Rev. Proc. 99-49 is modified to allow the required copy of the Form 3115 to be filed with the national office before the first day of the year of change if the taxpayer properly files a Form 3115 under this revenue procedure.

(5) In order to assist the Internal Revenue Service in processing changes in method of accounting under this revenue procedure, and to ensure proper handling, § 6.02(3)(a) of Rev. Proc. 99-49 is modified to require that a Form 3115 filed under this revenue procedure include the statement: "Automatic Change Filed Under [*insert section number*] of Rev. Proc. 2000-38." This statement must be legibly printed or typed at the top of any Form 3115 filed under this revenue procedure.

(6) For purposes of this revenue procedure, the taxpayer's method of accounting for distributor commissions is an issue pending if the Service has given the taxpayer written notification indicating an adjustment is being made or will be proposed with respect to the taxpayer's method of accounting for distributor commissions. This will normally occur after the Service has gathered information suf-

ficient to determine that a proposed adjustment is appropriate and justified, although the exact amount of the adjustment may not yet be determined.

*.02 Audit Protection.* If a taxpayer complies with the requirements of this revenue procedure for changing its method of accounting for distributor commissions to any of the three methods of accounting described in this revenue procedure, the treatment of distributor commissions will not be raised as an issue in any taxable year before the year of change and, if the treatment of distributor commissions has already been raised as an issue in a taxable year before the year of change, the treatment of distributor commissions will not be further pursued.

*.03 Changes Not Made under this Revenue Procedure.* A taxpayer that wants to change from a method of currently deducting distributor commissions to a method of capitalizing and amortizing distributor commissions under any of the three methods described in this revenue procedure for any taxable year other than the taxable year that includes January 1, 2001, must follow the automatic change in method of accounting provisions in Rev. Proc. 99-49. However, this change must be made on a cut-off basis as described in § 2.06 of Rev. Proc. 99-49. A change from one method of amortizing described in this revenue procedure to another method of amortizing described in

this revenue procedure, and a change from pooling to single asset, or vice versa, under the distribution fee period method or the useful life method, must be made in accordance with the automatic change in method of accounting provisions in § 2.02 of the APPENDIX of Rev. Proc. 99-49. A change in the useful life of distributor commissions under the distribution fee period method or the useful life method is not a change in method of accounting. See § 1.446-1(e)(2)(ii)(b).

#### SECTION 7. EFFECTIVE DATE

This revenue procedure is effective October 2, 2000.

#### SECTION 8. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 99-49 is modified and amplified to include this accounting method change in the APPENDIX.

#### DRAFTING INFORMATION

The principal author of this revenue procedure is John Moriarty of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information about this revenue procedure, contact John Moriarty at (202) 622-4950 (not a toll-free call).

## APPENDIX A

Department of the Treasury—Internal Revenue Service

# Closing Agreement on Final Determination Covering Specific Matters

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Under § 7121 of the Internal Revenue Code of 1986,

[Taxpayer's name, address, telephone number, and identifying number]

("the taxpayer") and the Commissioner of Internal Revenue make the following closing agreement:

WHEREAS, the taxpayer is a distributor of open-end regulated investment companies ("mutual funds").

WHEREAS, the taxpayer is an accrual basis taxpayer.

WHEREAS, the taxpayer incurs commissions on the sale of shares in the mutual funds for which the taxpayer is to receive a distribution fee under Rule 12b-1 (17 C.F.R. § 270.12b-1). For purposes of this closing agreement, the term "distributor commissions" has the meaning ascribed to it in Rev. Proc. 2000-38.

WHEREAS, the taxpayer seeks to account for distributor commissions under one of the methods described in Rev. Proc. 2000-38 and has filed a Form 3115 requesting permission to change its method of accounting for distributor commissions in accordance with Rev. Proc. 2000-38 and the Commissioner is relying on that Form 3115 in proceeding with this closing agreement.

NOW IT IS HEREBY DETERMINED AND AGREED for federal income tax purposes:

1. That the taxpayer changes its present method of accounting for distributor commissions for purposes of filing federal tax returns to the [Insert name of method] method described in Rev. Proc. 2000-38 effective for the taxable year which includes January 1, 2001 ("year of change"). The Commissioner consents to that change in method of accounting.

2. That the execution of this agreement does not signify the Commissioner's agreement with the useful life or recovery method selected by the taxpayer. In accordance with § 601.204(c) of the Statement of Procedural Rules, in examining returns involving the adoption of either the useful life method or the distribution fee period method the Commissioner will ascertain whether the representations on which the change in method of accounting is based, including representations related to the useful life of the distributor commissions, reflect an accurate statement of the material facts.

3. That the taxpayer's change in accounting method for distributor commissions must be made using a cut-off method without an adjustment under § 481(a).

4. That the Commissioner accepts the taxpayer's reported method of accounting for distributor commissions for all taxable years prior to the year of change.

5. That this agreement does not preclude the taxpayer from requesting, nor the Service from requiring, a change in the taxpayer's method of accounting for distributor commissions for years after the year of change.

This agreement is final and conclusive except:

(1) The matter it relates to may be reopened in the event of fraud, malfeasance or misrepresentation of a material fact;

(2) It is subject to the Internal Revenue Code Sections that expressly provide that effect be given to their provisions (including any stated exception for I.R.C. § 7122) notwithstanding any law or rule of law; and

(3) If it relates to a tax period ending after the date of this agreement, it is subject to any law enacted after the agreement date, that applies to the tax period.

By Signing, the parties certify that they have read and agreed to the terms of this document.

Taxpayer (other than individual): \_\_\_\_\_

By: \_\_\_\_\_ Date: \_\_\_\_\_

Title: \_\_\_\_\_

Commissioner of Internal Revenue

By: \_\_\_\_\_ Date: \_\_\_\_\_

Title: \_\_\_\_\_

#### Instructions

This agreement must be signed and filed in triplicate. (All copies must have original signatures.) The original and copies of the agreement must be identical. The name of the taxpayer must be stated accurately. The agreement may relate to one or more years.

If an attorney or agent signs the agreement for the taxpayer, the power of attorney (or a copy) authorizing that person to sign must be attached to the agreement. If the agreement is made for a year when a joint income tax return was filed by a husband and wife, it should be signed by or for both spouses. One spouse may sign as agent for the other if the document (or a copy) specifically authorizing that spouse to sign is attached to the agreement.

If the fiduciary signs the agreement for a decedent or an estate, an attested copy of the letters testamentary or the court order authorizing the fiduciary to sign, and a certificate of recent date that the authority remains in full force and effect must be attached to the agreement. If a trustee signs, a certified copy of the trust instrument or a certified copy of extracts from that instrument must be attached showing:

- (1) the date of the instrument;
- (2) that it is or is not of record in any court;
- (3) the names of the beneficiaries;
- (4) the appointment of the trustee, the authority granted, and other information necessary to show that the authority extends to Federal tax matters; and
- (5) that the trust has not been terminated, and that the trustee appointed is still acting. If a fiduciary is a party, Form 56, Notice Concerning Fiduciary Relationship, is ordinarily required.

If the taxpayer is a corporation, the agreement must be dated and signed with the name of the corporation, the signature and title of an authorized officer or officers, or the signature of an authorized attorney or agent. It is not necessary that a copy of an enabling corporate resolution be attached.

Use additional pages if necessary, and identify them as part of this agreement.

Please see Revenue Procedure 68-16, C. B. 1968 1, page 770, for a detailed description of practices and procedures applicable to most closing agreements.

I have examined the specific matters involved and recommend the acceptance of the proposed agreement

\_\_\_\_\_  
(Receiving Officer)                      (Date)

\_\_\_\_\_  
(Title)

I have examined the specific matters involved and recommend the acceptance of the proposed agreement

\_\_\_\_\_  
(Reveiwng Officer)                      (Date)

\_\_\_\_\_  
(Title)

## Part IV. Items of General Interest

### Notice of Proposed Rulemaking and Notice of Public Hearing

#### Guidance Under Subpart F Relating to Partnerships

##### REG-112502-00

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: A notice of proposed rulemaking and notice of proposed rulemaking by cross-reference to temporary regulations published in the **Federal Register** on March 26, 1998, providing guidance under subpart F relating to partnerships and branches, were withdrawn by a notice of proposed rulemaking published in the **Federal Register** on July 13, 1999. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments and outlines of oral comments to be discussed at the public hearing scheduled for December 5, 2000, must be received by November 14, 2000.

ADDRESSES: Send submissions to: CC:M&SP:RU (REG-112502-00), 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:M&SP:RU (REG-112502-00), 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 Internet site at [http://www.irs.ustreas.gov/tax\\_regs/comments.html](http://www.irs.ustreas.gov/tax_regs/comments.html). The public hearing will be held in room 4718, Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC 20224.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Valerie Mark, (202) 622-3840; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Treena Garrett, (202) 622-7180 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

##### Background

On March 26, 1998 (63 F.R. 14613), the IRS issued proposed regulations (REG-104537-97, 1998-1 C.B. 892) which contained two sets of provisions, one relating to the treatment under subpart F of a controlled foreign corporation's (CFC's) distributive share of partnership income (including a clarification of the manufacturing exception under the foreign base company sales income rules) and the other relating to hybrid branch transactions. The provisions relating to hybrid branch transactions were also issued as temporary regulations (T.D. 8767, 1998-1 C.B. 875). Congress and taxpayers raised concerns about the proposed and temporary regulations relating to hybrid branch transactions. To respond to these concerns, on July 6, 1998, Treasury and the IRS issued Notice 98-35 (1998-2 C.B. 34), which announced that they would withdraw the proposed regulations and remove the temporary regulations. Notice 98-35 also announced that Treasury and the IRS would issue two new separate sets of proposed regulations. One proposed regulation would contain hybrid branch rules. The other proposed regulation would contain rules pertaining to the treatment under subpart F of a CFC's distributive share of partnership income. On July 13, 1999, in furtherance of Notice 98-35, Treasury and the IRS published REG-113909-98 (1999-30 I.R.B. 125 [64 F.R. 37727]), which withdrew the proposed regulations and issued new proposed regulations containing the hybrid branch provisions with new dates of applicability to give Congress and the Treasury more time to evaluate the issues raised by these provisions. On the same date, T.D. 8827 (1999-30 I.R.B. 120 [64 F.R. 37677]) removed the temporary regulations relating to hybrid branch transactions. Treasury and the IRS are now proposing the regulations relating to the subpart F treatment of a CFC's distributive share of partnership income.

This document substantially restates the former proposed regulations relating to the treatment of a CFC's distributive share of partnership income under subpart

F. These new proposed regulations, however, do not contain the provisions of the former proposed regulations that clarified the manufacturing exception under subpart F. Regulations clarifying the manufacturing exception will be proposed at a later date.

##### Explanation of Provisions

These proposed regulations clarify the appropriate treatment under subpart F of certain partnership items that had been the subject of *Brown Group, Inc. v. Commissioner*, 77 F.3d 217 (8th Cir. 1996), vacating and remanding 104 T.C. 105 (1995). In *Brown Group*, a Cayman Islands partnership with a Cayman Islands CFC partner earned commission income from purchasing footwear in Brazil on behalf of the CFC's U.S. parent. This commission income would have been subpart F income, specifically foreign base company sales income under section 954(d), to the CFC if it had earned this commission income directly and under the same circumstances in which the partnership earned this income. The Tax Court applied an aggregate theory of partnerships and held that the CFC's distributive share of this commission income was foreign base company sales income. The Eighth Circuit, vacating and remanding the Tax Court's decision, applied an entity theory of partnerships and held that the CFC's distributive share of this commission income was not foreign base company sales income.

In response to the Eighth Circuit's opinion, the IRS announced that it intended to issue regulations under subpart F to clarify its position that whether a CFC partner's distributive share of partnership income is subpart F income generally is determined at the CFC partner level. See Notice 96-39 (1996-2 C.B. 209).

The proposed regulations would provide guidance for the treatment under subpart F of a CFC partner's distributive share of subpart F income. The regulations would provide general rules to determine whether a CFC partner's distributive share of partnership income falls within, not only foreign base company sales income, the category of income at

issue in *Brown Group*, but any category of subpart F income. These regulations also would provide guidance about the treatment of a CFC partner's distributive share of foreign personal holding company income, foreign base company sales income, foreign base company services income, and earnings invested in United States property under certain specific provisions of subpart F.

The proposed regulations are based on the authority of subchapter K and subpart F and the policies underlying those provisions. The legislative history of subchapter K provides that a partnership distributive share should be characterized by using the approach that best serves the Internal Revenue Code or regulations section at issue.

To allow a CFC to avoid subpart F treatment for items of income through the simple expedient of receiving them as distributive shares of partnership income, rather than directly, is contrary to the intent of subpart F. Subpart F was intended to limit deferral of U.S. income tax on passive income received by CFCs, as well as on certain other kinds of easily transferrable income.

Under these proposed regulations, gross income would be characterized at the partnership level, as, for example, sales income. If any part of the partnership's gross income would be subpart F income if received directly by partners that are CFCs, it must be separately taken into account by each partner, under section 702. Thus, to the extent the separately stated income is subpart F income at the CFC partner level, it will be taken into account in determining the CFC's total subpart F income for the taxable year and U.S. shareholders of the CFC will currently include their pro rata share of this income in gross income to the extent provided under the rules of subpart F.

The regulations under section 702 would be clarified to expressly provide that an item must be separately taken into account when, if separately taken into account by any partner, the item would result in an income tax liability for that partner, or any other person, different from that which would result if the partner did not take the item into account separately. This clarification incorporates into the regulations Rev. Rul. 86-138 (1986-2 C.B. 84), which holds that a subsidiary

partnership in a multi-tiered arrangement must separately state items which, if separately taken into account by any partner of any partnership in the multi-tiered arrangement, would affect the income tax liability of that partner.

The regulations under section 952 also would be clarified to expressly include within the definition of subpart F income a CFC's distributive share of any item of gross income of a partnership to the extent the income would have been subpart F income if received by the CFC partner directly. Comments are requested as to whether this rule should apply for ownership interests that fall below certain thresholds.

The proposed regulations would provide further that, generally, in determining whether a distributive share of partnership income is subpart F income, whether an entity is a related person and whether an activity takes place in or outside the CFC's country of incorporation is determined with respect to the CFC partner and not the partnership. Applying these rules to the *Brown Group* facts, the income would be characterized at the partnership level as commission income from the purchase of shoes in Brazil on behalf of the U.S. parent for sale in the U.S. Each partner would be required to separately take into account its distributive share of this commission income. It would then be determined at the CFC partner level that the shoes were manufactured and sold for use outside of the CFC's country of incorporation (Cayman Islands), and that the U.S. parent was a related person with respect to the CFC. Thus, the CFC's distributive share of commission income would be foreign base company sales income.

The proposed regulations also would address whether a CFC's distributive share of partnership income can qualify for the exceptions from foreign personal holding company income treatment that are based on the activities performed by the CFC in connection with the property through which it earns the income. The proposed regulations would provide that an exception requiring activity would generally apply if the exception would have applied to the income if the CFC itself had directly earned the income taking into account only the property and activities of the partnership. This requirement

is not met if the partnership can qualify for the exception only by taking into account the separate activities of its partners. Thus, for example, if the partnership earns rental income from leasing real property that it owns and with respect to which it performs active and substantial management functions, the CFC partner's distributive share of the rental income can be excluded from subpart F income under the active rents exception of section 954(c)(2)(A) if the rental income is earned from a person that is not a related person with respect to the CFC partner. However, if the partnership owns the real property but the CFC contracts to perform the management functions, the rental income is not excludible under this exception.

These proposed regulations would clarify how the manufacturing exception of §1.954-3(a)(4) applies in the context of the distributive share rules. The proposed regulations would provide that the manufacturing activities of a partnership may be taken into account under the distributive share rules when the partnership sells the property that it manufactures. As previously noted, the general rules would provide that income that could be foreign base company sales income at the CFC partner level is separately stated and that determinations as to relatedness and the relevant country are made at the partner level. Consistent with the general rules outlined above, these regulations would allow a CFC's distributive share of sales income to be excluded, under the manufacturing exception of §1.954-3(a)(4), when the partnership manufactures the property that it sells (without regard to the activities of the CFC partner or any other person).

The general rule, described above, would determine whether a CFC partner's distributive share of partnership income is foreign base company services income when the income is earned from performing services for or on behalf of a person that is a related person with respect to the CFC partner. These proposed regulations also would describe how the substantial assistance rule of §1.954-4(b)(1)(iv) applies when the CFC earns services income through a partnership. When the partnership is performing services for a person unrelated to the CFC partner but the CFC partner, or a related person, provides sub-

stantial assistance to the partnership contributing to the performance of those services, the CFC partner and the partnership would be regarded as separate entities and the substantial assistance provided to the partnership by the CFC partner, or a related person, would cause the CFC's partner's distributive share of the services income to be treated as foreign base company services income. Treasury and the IRS are considering applying similar principles to branches of CFCs. Comments are requested on this issue.

Finally, consistent with Rev. Rul. 90-112 (1990-2 C.B. 186), the regulations would provide that, for purposes of section 956, a CFC partner's investment in U.S. property includes the U.S. property held by a partnership to the extent of the CFC's interest in the partnership. Comments are requested as to whether, for purposes of section 956, a CFC partner's interest in a partnership should be based on the CFC's capital interest in the partnership, the CFC's interest in partnership profits, or another standard, such as the facts and circumstances relating to the CFC's interest in the partnership.

Treasury is currently conducting a study to review the provisions of subpart F. The study may examine the foreign base company rules, contract manufacturing, and the use of hybrid partnerships under subpart F. Although comments will be sought separately on the study, comments received on these regulations will be reviewed in connection with the study.

### Proposed Effective Date

These regulations are proposed to apply for taxable years of a controlled foreign corporation beginning on or after the date the final regulations are published in the **Federal Register**. For prior periods, the IRS will rely on principles and authorities under subpart F and subchapter K to apply an aggregate approach, (including §1.701-2(e) and (f) of the regulations for periods for which it is applicable).

### 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 Procedures Act (5

U.S.C. chapter 5) does not apply to these regulations, and, because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

### Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (preferably a signed original and eight (8) copies) that are timely submitted to the IRS. All comments will be available for public inspection and copying. The IRS and Treasury specifically request comments on the clarity of these proposed regulations and how they may be made easier to understand.

A public hearing has been scheduled for December 5, 2000, at 10 a.m., in room 4718, Internal Revenue Building, 1111 Constitution Avenue NW., Washington DC. Due to building security procedures, visitors must enter at the 10th Street entrance, located between Constitution and Pennsylvania Avenues, NW. 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 that wish to present oral comments at the hearing must submit written comments and an outline of topics to be discussed and time to be devoted to each topic (signed original and eight (8) copies) by November 14, 2000.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the 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 Valerie Mark of the Office of the Associate Chief Counsel (International), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

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### 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 26 CFR part 1 continues to read in part as follows:

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

Par. 2 Section §1.702-1 is amended as follows:

1. Paragraph (a)(8)(ii) is revised.
2. Paragraph (c)(1)(iii) is amended by removing the word "and".
3. Paragraph (c)(1)(iv) is amended by removing the period at the end and adding "; and" in its place.
4. Paragraph (c)(1)(v) is added.

The addition and revision read as follows:

#### *§1.702-1 Income and credits of partner.*

(a) \* \* \*

(8) \* \* \*

(ii) Each partner must also take into account separately the partner's distributive share of any partnership item which, if separately taken into account by any partner, would result in an income tax liability for that partner, or for any other person, different from that which would result if that partner did not take the item into account separately. Thus, if any partner is a controlled foreign corporation, as defined in section 957, items of income that would be gross subpart F income if separately taken into account by the controlled foreign corporation must be separately stated for all partners. Under section 911(a), if any partner is a bona fide resident of a foreign country who may exclude from gross income the part of the partner's distributive share which qualifies as earned income, as defined in section 911(b), the earned income of the partnership for all partners must be separately stated. Similarly, all relevant items of in-

come or deduction of the partnership must be separately stated for all partners in determining the applicability of section 183 (relating to activities not engaged in for profit) and the recomputation of tax thereunder for any partner. This paragraph (a)(8)(ii) applies to taxable years beginning on or after the date final regulations are published in the Federal Register.

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(c) \*\*\*

(1) \*\*\*

(v) In determining whether the *de minimis* or full inclusion rules of section 954(b)(3) apply.

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Par. 3. In §1.952-1, paragraph (g) is added to read as follows:

*§1.952-1 Subpart F income defined.*

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(g) *Treatment of distributive share of partnership income—(1) In general.* A controlled foreign corporation's distributive share of any item of income of a partnership is income that falls within a category of subpart F income described in section 952(a) to the extent the item of income would have been income in such category if received by the controlled foreign corporation directly. For specific rules regarding the treatment of a distributive share of partnership income under certain provisions of subpart F, see §§1.954-1(g), 1.954-2(a)(5), 1.954-3(a)(6), and 1.954-4(b)(2)(iii).

(2) *Example.* The application of this paragraph (g) may be illustrated by the following example:

*Example.* CFC, a controlled foreign corporation, is an 80-percent partner in PRS, a foreign partnership. PRS earns \$100 of interest income that is not export financing interest, as defined in section 954(c)(2)(B), from a person unrelated to CFC. This interest income would have been foreign personal holding company income to CFC, under section 954(c), if it had received this income directly. Accordingly, CFC's distributive share of this interest income, \$80, is foreign personal holding company income.

(3) *Effective date.* This paragraph (g) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the Federal Register.

Par. 4. In §1.954-1, paragraph (g) is added to read as follows:

*§1.954-1 Foreign base company income.*

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(g) *Distributive share of partnership income—(1) Application of related per-*

*son and country of organization tests.* Unless otherwise provided, to determine the extent to which a controlled foreign corporation's distributive share of any item of gross income of a partnership would have been subpart F income if received by it directly, under §1.952-1(g), if a provision of subpart F requires a determination of whether an entity is a related person, within the meaning of section 954(d)(3), or whether an activity occurred within or outside the country under the laws of which the controlled foreign corporation is created or organized, this determination shall be made by reference to such controlled foreign corporation and not by reference to the partnership.

(2) *Examples.* The application of paragraph (g)(1) of this section is illustrated by the following examples:

*Example 1.* CFC, a controlled foreign corporation organized in Country A, is an 80-percent partner in Partnership, a partnership organized in Country A. All of the stock of CFC is owned by USP, a U.S. corporation. Partnership earns commission income from purchasing Product O on behalf of USP, from unrelated manufacturers in Country B, for sale in the United States. To determine whether CFC's distributive share of Partnership's commission income is foreign base company sales income under section 954(d), CFC is treated as if it purchased Product O on behalf of USP. Under section 954(d)(3), USP is a related person with respect to CFC. Thus, with respect to CFC, the sales income is deemed to be derived from the purchase of personal property on behalf of a related person. Because the property purchased is both manufactured and sold for use outside of Country A, CFC's country of organization, CFC's distributive share of the sales income is foreign base company sales income.

*Example 2.* (i) CFC1, a controlled foreign corporation organized in Country A, is an 80-percent partner in Partnership, a partnership organized in Country B. CFC2, a controlled foreign corporation organized in Country B, owns the remaining 20 percent interest in Partnership. CFC1 and CFC2 are owned by a common U.S. parent, USP. CFC2 manufactures Product A in Country B. Partnership earns sales income from purchasing Product A from CFC2 and selling it to third parties located in Country B that are not related persons with respect to CFC1 or CFC2. To determine whether CFC1's distributive share of Partnership's sales income is foreign base company sales income under section 954(d), CFC1 is treated as if it purchased Product A from CFC2 and sold it to third parties in Country B. Under section 954(d)(3), CFC2 is a related person with respect to CFC1. Thus, with respect to CFC1, the sales income is deemed to be derived from the purchase of personal property from a related person. Because the property purchased is both manufactured and sold for use outside of Country A, CFC1's country of organization, CFC1's distributive share of the sales income is foreign base company sales income.

(ii) To determine whether CFC2's distributive share of Partnership's sales income is foreign base company sales income, CFC2 is treated as if it directly sold Product A to third parties within Country B. Because Product A is both manufactured and sold for use within CFC2's country of organization, CFC2's distributive share of Partnership's sales income is not foreign base company sales income.

(3) *Effective date.* This paragraph (g) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the Federal Register.

Par. 5. In §1.954-2, paragraph (a)(5) is added to read as follows:

*§1.954-2 Foreign personal holding company income.*

(a) \*\*\*

(5) *Special rules applicable to distributive share of partnership income.* (i) [Reserved]

(ii) *Certain other exceptions applicable to foreign personal holding company income.* To determine the extent to which a controlled foreign corporation's distributive share of an item of income of a partnership is foreign personal holding company income, the exceptions contained in section 954(c) that are based on whether the controlled foreign corporation is engaged in the active conduct of a trade or business, including section 954(c)(2), (h) and (i), and paragraphs (b)(2) and (6), (e)(1)(ii) and (3)(ii), (iii) and (iv), (f)(1)(ii), (g)(2)(ii), and (h)(3)(ii) of this section, shall apply only if any such exception would have applied to exclude the income from foreign personal holding company income if the controlled foreign corporation had earned the income directly, determined by taking into account only the activities of, and property owned by, the partnership and not the separate activities or property of the controlled foreign corporation or any other person.

(iii) [Reserved]

(iv) *Effective date.* This paragraph (a)(5) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the Federal Register.

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Par. 6. In §1.954-3, paragraph (a)(6) is added to read as follows: §1.954-3 Foreign base company sales income.

(a) \*\*\*

(6) *Special rule applicable to distributive share of partnership income—(i) In general.* To determine the extent to which a controlled foreign corporation's distribu-

tive share of any item of gross income of a partnership would have been foreign base company sales income if received by it directly, under §1.952-1(g), the property sold will be considered to be manufactured, produced or constructed by the controlled foreign corporation, within the meaning of paragraph (a)(4) of this section, only if the manufacturing exception of paragraph (a)(4) of this section would have applied to exclude the income from foreign base company sales income if the controlled foreign corporation had earned the income directly, determined by taking into account only the activities of, and property owned by, the partnership and not the separate activities or property of the controlled foreign corporation or any other person.

(ii) Example. The application of paragraph (a)(6)(i) of this section is illustrated by the following example:

*Example.* CFC, a controlled foreign corporation organized under the laws of Country A, is an 80-percent partner in Partnership X, a partnership organized under the laws of Country B. Partnership X performs activities in Country B that would constitute the manufacture of Product O, within the meaning of paragraph (a)(4) of this section, if performed directly by CFC. Partnership X, through its sales offices in Country B, then sells Product O to Corp D, a corporation that is a related person with respect to CFC, within the meaning of section 954(d)(3), for use within Country B. CFC's distributive share of Partnership X's sales income is not foreign base company sales income because the manufacturing exception of paragraph (a)(4) of this section would have applied to exclude the income from foreign base company sales income if CFC had earned the income directly. (The branch rule of paragraph (b) of this section does not apply to these facts).

(iii) *Effective date.* This paragraph (a)(6) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the **Federal Register**.

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Par. 7. In §1.954-4, paragraph (b)(2)(iii) is added to read as follows:

*§1.954-4 Foreign base company services income.*

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(b) \*\*\*

(2) \*\*\*

(iii) *Special rule applicable to distributive share of partnership income.* A controlled foreign corporation's distributive share of a partnership's services income will be deemed to be derived from services performed for or on behalf of a related person, within the meaning of

section 954(e)(1)(A), if the partnership is a related person with respect to the controlled foreign corporation, under section 954(d)(3), and, in connection with the services performed by the partnership, the controlled foreign corporation, or a person that is a related person with respect to the controlled foreign corporation, provided assistance that would have constituted substantial assistance contributing to the performance of such services, under paragraph (b)(2)(ii) of this section, if furnished to the controlled foreign corporation by a related person. This paragraph (b)(2)(iii) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the **Federal Register**.

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Par. 8. In §1.956-2, paragraph (a)(3) is added to read as follows:

*§1.956-2 Definition of United States property.*

(a) \*\*\*

(3) *Property owned through partnership.* For purposes of section 956, if a controlled foreign corporation is a partner in a partnership that owns property that would be United States property, within the meaning of paragraph (a)(1) of this section, if owned directly by the controlled foreign corporation, the controlled foreign corporation will be treated as holding an interest in the property equal to its interest in the partnership and such interest will be treated as an interest in United States property. This paragraph (a)(3) applies to taxable years of a controlled foreign corporation beginning on or after the date final regulations are published in the **Federal Register**.

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Robert E. Wenzel,  
Deputy Commissioner  
of Internal Revenue.

(Filed by the Office of the Federal Register on September 19, 2000, 8:45 a.m., and published in the issue of the Federal Register for September 20, 2000, 65 F.R. 56836)

**TOLL-FREE NUMBER FOR THE  
APPEALS OFFICER (CUSTOMER  
SERVICE/OUTREACH) PROGRAM  
Announcement 2000-80**

This document informs the public of the new Appeals Officer (Customer Service/Outreach) program. Appeals now has a toll-free number for contacting an Appeals Officer (Customer Service/Outreach) who will provide assistance with an Appeals tax matter. Previously, Announcement 99-98, 1999-42 I.R.B. 520, listed telephone numbers which were not toll-free.

The toll-free number for contacting an Appeals Officer (Customer Service/Outreach) is **1-877-457-5055**. The new toll-free system will automatically send the call to the nearest Appeals Officer (Customer Service/Outreach). This new service emphasizes Appeal's commitment to advancing its customer service program under the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685, Appeals Policy Statement P-8-1, and Treasury Directive 63-01.

Appeals presently has an Appeals Officer (Customer Service/Outreach) in each of the thirty-three Appeals Offices nationwide. A list of the office locations appears at the end of this announcement.

The duties of the Appeals Officer (Customer Service/Outreach) include:

- 1) Serving as proponents of the Appeals process;
- 2) Providing assistance to taxpayers during their administrative appeal;
- 3) Handling taxpayers' complaints regarding Appeals;
- 4) Participating in National Problem Solving Days;
- 5) Coordinating with Taxpayer Advocate Service representatives on Appeals matters;
- 6) Performing Appeals education and outreach with the public, as well as other IRS functions;
- 7) Ensuring that taxpayer rights are not abridged; and
- 8) Identifying problems and trends, including analyzing customer survey and balanced measures results.

The Appeals Officers (Customer Service/Outreach) endorse the Commissioner's concept for modernizing the Internal Revenue Service to focus on:

- 1) Service to Each Taxpayer
- 2) Service to All Taxpayers
- 3) Productivity Through a Quality Work Environment

Please call **1-877-457-5055** whenever you need assistance with an Appeals tax matter.

### **Appeals on the World-Wide Web**

For further information on the Appeals organization, visit the recently updated Appeals section of the IRS Web Site at [www.irs.gov/prod/ind\\_info/appeals](http://www.irs.gov/prod/ind_info/appeals). Included are links to information on:

- ***Appeals Redesign and Program Development*** - An introduction to the Appeals organization;
- ***Appeals Expectations-Yours and Ours*** - A review of mutual commitments for the Appeals Process;

- ***Alternative Dispute Resolution Programs*** - Are you having trouble resolving your Appeals case?;
- ***Appeal Rights*** - IRS publications providing detailed information on what can be appealed;
- ***Appeals Officer (Customer Service/Outreach) Program*** - How to contact nationwide Appeals Officers (Customer Service/Outreach) and their role in the Appeals process;
- ***Other Appeals Programs*** - Collection Appeals, Innocent Spouse, Bankruptcy, Offer-In-Compromise, and Industry Specialization; and
- ***Other Sites*** - Various sites and pub-

lications including the new IRS organization, tax law questions, U.S. Tax Court Site, where to get assistance.

### **Drafting Information**

The principal author of this announcement is Thomas C. Louthan, Director, Strategic Planning and Communications (Appeals). For further information regarding this announcement contact Mr. Louthan at (202) 694-1842 or Darlene M. Marshall at (202) 694-1875 (not toll-free calls).

**Appeals Officer (Customer Service/Outreach) Program**  
*[Office Location]*

**Toll-Free Number: 1-877-457-5055**

Phoenix, AZ  
Laguna Niguel, CA  
Los Angeles, CA  
San Francisco, CA  
San Jose, CA  
Denver, CO  
East Hartford, CT  
Ft. Lauderdale, FL  
Jacksonville, FL  
Atlanta, GA  
Chicago, IL  
Indianapolis, IN  
New Orleans, LA  
Boston, MA  
Baltimore, MD  
Detroit, MI  
St. Paul, MN  
St. Louis, MO  
Greensboro, NC  
Newark, NJ  
Buffalo, NY  
Hempstead, NY  
New York, NY  
Cleveland, OH  
Oklahoma City, OK  
Philadelphia, PA  
Nashville, TN  
Austin, TX  
Dallas, TX  
Houston, TX  
Richmond, VA  
Seattle, WA  
Milwaukee, WI

## Definition of Terms

*Revenue rulings and revenue procedures (hereinafter referred to as “rulings”) that have an effect on previous rulings use the following defined terms to describe the effect:*

*Amplified* describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

*Clarified* is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

*Distinguished* describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

*Modified* is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it ap-

plies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

*Obsoleted* describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

*Revoked* describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

*Superseded* describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the

new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

*Supplemented* is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

*Suspended* is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

## Abbreviations

*The following abbreviations in current use and formerly used will appear in material published in the Bulletin.*

A—Individual.  
Acq.—Acquiescence.  
B—Individual.  
BE—Beneficiary.  
BK—Bank.  
B.T.A.—Board of Tax Appeals.  
C—Individual.  
C.B.—Cumulative Bulletin.  
CFR—Code of Federal Regulations.  
CI—City.  
COOP—Cooperative.  
Ct.D.—Court Decision.  
CY—County.  
D—Decedent.  
DC—Dummy Corporation.  
DE—Donee.  
Del. Order—Delegation Order.  
DISC—Domestic International Sales Corporation.  
DR—Donor.  
E—Estate.  
EE—Employee.

E.O.—Executive Order.  
ER—Employer.  
ERISA—Employee Retirement Income Security Act.  
EX—Executor.  
F—Fiduciary.  
FC—Foreign Country.  
FICA—Federal Insurance Contributions Act.  
FISC—Foreign International Sales Company.  
FPH—Foreign Personal Holding Company.  
F.R.—Federal Register.  
FUTA—Federal Unemployment Tax Act.  
FX—Foreign Corporation.  
G.C.M.—Chief Counsel’s Memorandum.  
GE—Grantee.  
GP—General Partner.  
GR—Grantor.  
IC—Insurance Company.  
I.R.B.—Internal Revenue Bulletin.  
LE—Lessee.  
LP—Limited Partner.  
LR—Lessor.  
M—Minor.  
Nonacq.—Nonacquiescence.  
O—Organization.  
P—Parent Corporation.

PHC—Personal Holding Company.  
PO—Possession of the U.S.  
PR—Partner.  
PRS—Partnership.  
PTE—Prohibited Transaction Exemption.  
Pub. L.—Public Law.  
REIT—Real Estate Investment Trust.  
Rev. Proc.—Revenue Procedure.  
Rev. Rul.—Revenue Ruling.  
S—Subsidiary.  
S.P.R.—Statements of Procedural Rules.  
Stat.—Statutes at Large.  
T—Target Corporation.  
T.C.—Tax Court.  
T.D.—Treasury Decision.  
TFE—Transferee.  
TFR—Transferor.  
T.I.R.—Technical Information Release.  
TP—Taxpayer.  
TR—Trust.  
TT—Trustee.  
U.S.C.—United States Code.  
X—Corporation.  
Y—Corporation.  
Z—Corporation.

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### Key to Abbreviations:

Ann	Announcement
CD	Court Decision
DO	Delegation Order
EO	Executive Order
PL	Public Law
PTE	Prohibited Transaction Exemption
RP	Revenue Procedure
RR	Revenue Ruling
SPR	Statement of Procedural Rules
TC	Tax Convention
TD	Treasury Decision
TDO	Treasury Department Order

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