

## **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**

#### **Rev. Rul. 2005-4, page 366.**

**Interest suspension; time sensitive penalties.** Section 6404(g) of the Code suspends interest and time sensitive penalties, additions to tax and additional amounts with respect to an increased tax liability reported on an individual's amended income tax return filed more than 18 months after the date that is the later of (1) the original due date of the return (without regard to extensions) or (2) the date on which the taxpayer timely filed the return.

#### **T.D. 9168, page 354.**

Final regulations under section 59 of the Code provide rules governing the time and manner for making and revoking an election to treat certain qualified expenditures which are otherwise deductible under the Code as amortized over the applicable period provided for in the statute. The regulations provide that the election may be made for any specific dollar amount of the qualified expenditures, but cannot be made by reference to a formula. To revoke the election, a taxpayer must receive the permission of the Commissioner. Permission will only be granted in rare and unusual circumstances. If permission is granted, the revocation will be effective in the taxpayer's earliest open taxable year affected by the election.

#### **T.D. 9170, page 363.**

#### **REG-139683-04, page 371.**

Final, temporary, and proposed regulations under section 1374 of the Code provide that (a) section 1374(d)(8) applies to any transaction described in that section that occurs on or after December 27, 1994, regardless of the date of the S corporation's election under section 1362; and (b) for purposes of the Tax Reform Act of 1986, as amended, a corporation's most recent S election, not an earlier election that has been revoked

or terminated, determines whether or not it is subject to current section 1374.

#### **Notice 2005-8, page 368.**

This notice states that a partnership's contributions to a partner's Health Savings Account (HSA) may be treated as distributions under section 731 of the Code or as guaranteed payments under section 707(c). HSA contributions treated as section 731 distributions are not deductible by the partnership, and may be deductible by the partner under sections 223(a) and 62(a)(19) and are excluded from net earnings from self-employment. HSA contributions treated as guaranteed payments under section 707(c) derived from the partnership's trade or business and for services rendered to the partnership may be deductible by the partnership, are included in the partner's gross income, may be deductible by the partner under sections 223(a) and 62(a)(19), and are included in net earnings from self-employment. An S corporation's contributions to 2-percent shareholder-employee's HSA for services rendered to the S corporation are treated as section 707(c) guaranteed payments. For employment tax purposes, the 2-percent shareholder-employee is treated as an employee subject to FICA, unless the requirements of section 3121(a)(2)(B) are met.

#### **Announcement 2005-6, page 377.**

In July 2004, the Service issued a revision to Form 656, *Offer in Compromise*. The purpose of this announcement is to highlight the addition of a "check-the-box" disclosure authorization (new Item 14), which allows the taxpayer to designate someone to assist him or her while the Service is processing the offer.

**(Continued on the next page)**

**Announcement of Declaratory Judgment Proceedings Under Section 7428 begins on page 380.**

**Announcements of Disbarments and Suspensions begin on page 376.**

**Finding Lists begin on page ii.**



## EMPLOYEE PLANS

### Notice 2005–9, page 369.

**Weighted average interest rate update; corporate bond indices; 30-year Treasury securities.** The weighted average interest rate for January 2005 and the resulting permissible range of interest rates used to calculate current liability and to determine the required contribution are set forth.

## EXEMPT ORGANIZATIONS

### Announcement 2005–7, page 377.

A list is provided of organizations now classified as private foundations.

### Announcement 2005–8, page 380.

Harlem Agencies for Neighborhood Development, Inc., of New York, NY, no longer qualifies as an organization to which contributions are deductible under section 170 of the Code.

## EMPLOYMENT TAX

### Notice 2005–8, page 368.

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## SELF-EMPLOYMENT TAX

### Notice 2005–8, page 368.

This notice states that a partnership's contributions to a partner's Health Savings Account (HSA) may be treated as distributions under section 731 of the Code or as guaranteed payments under section 707(c). HSA contributions treated as section 731 distributions are not deductible by the partnership, and may be deductible by the partner under sections 223(a) and 62(a)(19) and are excluded from net earnings from self-

employment. HSA contributions treated as guaranteed payments under section 707(c) derived from the partnership's trade or business and for services rendered to the partnership may be deductible by the partnership, are included in the partner's gross income, may be deductible by the partner under sections 223(a) and 62(a)(19), and are included in net earnings from self-employment. An S corporation's contributions to 2-percent shareholder-employee's HSA for services rendered to the S corporation are treated as section 707(c) guaranteed payments. For employment tax purposes, the 2-percent shareholder-employee is treated as an employee subject to FICA, unless the requirements of section 3121(a)(2)(B) are met.

## ADMINISTRATIVE

### T.D. 9165, page 357.

Final regulations under section 330 of title 31 of the U.S. Code revise regulations governing practice before the IRS (Circular 230) that set forth best practices for tax advisors providing advice to taxpayers relating to federal tax issues or submissions to the Internal Revenue Service and modify the standards for certain tax shelter opinions.

### REG–159824–04, page 372.

Proposed regulations under section 330 of title 31 of the U.S. Code amend provisions of Circular 230 (Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, etc.) relating to state or local bond opinions. A public hearing is scheduled for March 22, 2005.

### Announcement 2005–6, page 377.

In July 2004, the Service issued a revision to Form 656, *Offer in Compromise*. The purpose of this announcement is to highlight the addition of a "check-the-box" disclosure authorization (new Item 14), which allows the taxpayer to designate someone to assist him or her while the Service is processing the offer.

# 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 compiled 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 procedures 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 Other Related Items, 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 last 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 last Bulletin of each semiannual period.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

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

## Section 59.—Other Definitions and Special Rules

26 CFR 1.59-1: Optional 10-year writeoff of certain tax preferences.

### T.D. 9168

#### DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Parts 1 and 602

#### Optional 10-Year Writeoff of Certain Tax Preferences

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

**SUMMARY:** This document contains final regulations relating to the optional 10-year writeoff of certain tax preference items under section 59(e) of the Internal Revenue Code (Code). The final regulations affect taxpayers who utilize section 59(e) for the optional 10-year writeoff of certain tax preferences. These final regulations provide guidance on the time and manner of making an election under section 59(e). The regulations also provide guidance on revoking an election under section 59(e). The regulations reflect changes to the law made by the Tax Reform Act of 1986, the Technical and Miscellaneous Revenue Act of 1988, and the Omnibus Budget Reconciliation Act of 1989.

**DATES:** *Effective Date:* These regulations are effective December 22, 2004.

*Applicability Date:* These regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after December 22, 2004.

**SUPPLEMENTARY INFORMATION:**

#### Paperwork Reduction Act

The collection of information contained in these final regulations has been reviewed and approved by the Office of Management and Budget in accordance

with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545-1903. Responses to this collection of information are required to obtain the benefit of the section 59(e) election.

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 assigned by the Office of Management and Budget.

The estimated annual burden per respondent is one hour.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

Books or 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.

#### Background

This document contains amendments to 26 CFR part 1 under section 59(e) of the Code. Section 59(e)(1) allows taxpayers to elect to deduct any qualified expenditure ratably over a 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of a qualified expenditure under section 263(c), over the 60-month period beginning with the month in which such expenditure was paid or incurred). Section 59(e)(2) defines *qualified expenditure* as any amount that, but for an election under section 59(e), would have been allowed as a deduction (determined without regard to section 291) for the taxable year in which paid or incurred under section 173 (relating to circulation expenditures), section

174 (relating to research and experimental expenditures), section 263(c) (relating to intangible drilling and development expenditures), section 616(a) (relating to development expenditures), or section 617(a) (relating to mining exploration expenditures).

Section 59(e)(4)(A) states that an election under section 59(e) (section 59(e) election) may be made with respect to any portion of any qualified expenditure. The legislative history of section 59(e) suggests that this allows a section 59(e) election to be made “dollar for dollar.” See H.R. Rep. 99-426, 99th Cong., 1st Sess. 327 (1985), 1986-3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99-313, 99th Cong., 2d Sess. 539 (1986), 1986-3 (Vol. 3) C.B. 1, 539.

Section 59(e)(4)(B) states that a section 59(e) election may only be revoked with the consent of the Secretary.

Provisions similar to those currently contained in section 59(e) were originally enacted as section 58(i) under the Tax Equity and Fiscal Responsibility Act of 1982 (Public Law 97-248; 96 Stat. 324). Under section 58(i)(1), the optional 10-year writeoff was available only to individuals. Section 58(i)(5)(C) directed the Secretary to promulgate regulations governing the time and manner for making an election under section 58(i) (section 58(i) election).

Section 5f.0(a)(2)(i)(A) and (B) of the temporary Income Tax Regulations that were promulgated under section 58(i) required that a section 58(i) election be made by the later of the due date (including extensions) of the income tax return for the taxable year for which the election was to be effective, or April 15, 1983. T.D. 7870, 1983-1 C.B. 13 [48 FR 1486]. Section 5f.0(a)(3) provided that a section 58(i) election was made by attaching a statement to the income tax return (or amended return) for the taxable year in which the election was made. Section 5f.0 was redesignated as §301.9100-5T by T.D. 8435, 1992-2 C.B. 324 [57 FR 43893], on October 15, 1992.

Section 59(e) was enacted as part of the Tax Reform Act of 1986 (Public Law 99-514; 100 Stat. 2085) and, unlike section 58(i), is not limited to individuals. While both the Senate Finance Committee

Report and the House Ways and Means Committee Report state that the time and manner of the election would be governed by regulations, Congress did not include a provision similar to former section 58(i)(5)(C) directing the Secretary to promulgate regulations governing the time and manner for making a section 59(e) election. *See* H.R. Rep. No. 99-426, 99th Cong., 1st Sess. 327 (1985), 1986-3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99-313, 99th Cong., 2d Sess. 539 (1986), 1986-3 (Vol. 3) C.B. 1, 539.

A notice of proposed rulemaking (REG-124405-03, 2004-35 I.R.B. 394 [69 FR 43367]) was published in the **Federal Register** on July 20, 2004. Two requests for a public hearing were received. A public hearing was held on December 7, 2004. The IRS received written and electronic comments responding to the notice of proposed rulemaking. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision. The revisions are discussed below.

### **Summary of Comments and Explanation of Revisions**

Several commentators recommended changes regarding the information taxpayers would be required to submit as part of their section 59(e) election. Specifically, commentators requested that the IRS reconsider §1.59-1(b)(1)(ii) and (iii) of the proposed regulations, which would require taxpayers to identify (i) the type and amount, for each activity or project, of qualified expenditures identified in section 59(e)(2) the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1), and (ii) a description of each specific activity or project to which the qualified expenditures relate. The commentators suggest that the majority of taxpayers who incur research and experimentation expenditures under section 174(a) and make a section 59(e) election with respect to such expenditures do not currently maintain records on a project-by-project basis. As a result, the commentators stated that requiring taxpayers to account for their section 59(e) qualified expenditures on a project-by-project basis would be a financial and administrative burden. Some of the commentators also discussed section

1016(a)(20), which provides that proper adjustment in respect of the property shall in all cases be made for amounts allowed as deductions under section 59(e) (relating to optional 10-year writeoff of certain tax preferences). Compliance with section 1016(a)(20) requires that taxpayers be able to account for their section 59(e) expenditures through appropriate basis adjustments for each property, project, or activity.

Sections 1.59-1(b)(1)(ii) and (iii) of the proposed regulations were intended to improve compliance with section 1016(a)(20) by requiring that section 59(e) qualified expenditures be allocated among the properties, projects or activities to which they relate. Comments received regarding this provision indicate that, for taxpayers incurring section 174(a) expenditures, the basis rules of section 1016(a)(20) are only of importance when a project to which a section 59(e) election relates is disposed of, and that it is rare for a research project to be disposed of prior to the full amortization of the allocable section 59(e) qualified expenditures. As such, the commentators argue that the burden of requiring taxpayers to identify on a section 59(e) election the type and amount of qualified expenditures for each activity or project greatly exceeds the potential harm caused by non-compliance with section 1016(a)(20).

Having fully considered all comments received, the final regulations are modified to reflect the comments discussed above. Taxpayers making a section 59(e) election will not be required to identify on the election the type and amount of qualified expenditures for each activity or project nor will they be required to provide a description of each specific activity or project to which the qualified expenditures relate. Instead, taxpayers will be required only to identify the type and amount of qualified expenditures identified in section 59(e)(2) that the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1). However, taxpayers remain responsible for full compliance with the requirements of section 1016(a)(20). Specifically, taxpayers who allocate their section 59(e) expenditures to reduce the gain otherwise recognized on the disposition of a property, project, or activity must maintain books and records sufficient to support that allocation.

The preamble to the proposed regulations stated that, with respect to an otherwise valid section 59(e) election filed for a taxable year ending prior to the effective date of the final regulations, such election would not be challenged by the IRS merely because the election was made later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. One commentator requested guidance on what the IRS considers an otherwise valid section 59(e) election filed for a tax year ending prior to the effective date of the final regulations. Although the IRS will treat a section 59(e) election prepared in a manner described in the final regulations as sufficient for a tax year ending prior to the effective date of the final regulations, because the final regulations only apply prospectively the final regulations do not provide guidance on what constitutes an otherwise valid section 59(e) election filed for a tax year prior to the effective date of the final regulations.

### **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 also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collection of information in these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that the reporting burden, as discussed earlier in this preamble, is expected to be insignificant. Therefore, 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 preceding this regulation 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 these final regulations is Eric B. Lee of the Office of As-

sociate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

\* \* \* \* \*

**Adoption of Amendments to the Regulations**

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

Paragraph 1. The authority citation for part 1 reads, in part, as follows:

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

Par. 2. Section 1.59-1 is added to read as follows:

*§1.59-1 Optional 10-year writeoff of certain tax preferences.*

(a) *In general.* Section 59(e) allows any qualified expenditure to which an election under section 59(e) applies to be deducted ratably over the 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of intangible drilling and development costs deductible under section 263(c), over the 60-month period beginning with the month in which the expenditure was paid or incurred).

(b) *Election—(1) Time and manner of election.* An election under section 59(e) shall only be made by attaching a statement to the taxpayer’s income tax return (or amended return) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. The statement must be filed no later than the date prescribed by law for filing the taxpayer’s original income tax return (including any extensions of time) for the taxable year in which the

amortization of the qualified expenditures subject to the section 59(e) election begins. Additionally, the statement must include the following information —

(i) The taxpayer’s name, address, and taxpayer identification number; and

(ii) The type and amount of qualified expenditures identified in section 59(e)(2) that the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1).

(2) *Elected amount.* A taxpayer may make an election under section 59(e) with respect to any portion of any qualified expenditure paid or incurred by the taxpayer in the taxable year to which the election applies. An election under section 59(e) must be for a specific dollar amount and the amount subject to an election under section 59(e) may not be made by reference to a formula. The amount elected under section 59(e) is properly chargeable to a capital account under section 1016(a)(20), relating to adjustments to basis of property.

(c) *Revocation—(1) In general.* An election under section 59(e) may be revoked only with the consent of the Commissioner. Such consent will only be granted in rare and unusual circumstances. The revocation, if granted, will be effective in the first taxable year in which the section 59(e) election was applicable. However, if the period of limitations for the first taxable year the section 59(e) election was applicable has expired, the revocation, if granted, will be effective in the earliest taxable year for which the period of limitations has not expired.

(2) *Time and manner for requesting consent.* A taxpayer requesting the Commissioner’s consent to revoke a section 59(e) election must submit the request prior to the end of the taxable year the applicable amortization period described

in section 59(e)(1) ends. The application for consent to revoke the election must be submitted to the Internal Revenue Service in the form of a letter ruling request.

(3) *Information to be provided.* A request to revoke a section 59(e) election must contain all of the information necessary to demonstrate the rare and unusual circumstances that would justify granting revocation.

(4) *Treatment of unamortized costs.* The unamortized balance of the qualified expenditures subject to the revoked section 59(e) election as of the first day of the taxable year the revocation is effective is deductible in the year the revocation is effective (subject to the requirements of any other provision under the Code, regulations, or any other published guidance) and the taxpayer will be required to amend any federal income tax returns affected by the revocation.

(d) *Effective date.* These regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after December 22, 2004.

**PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT**

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (b) is amended by adding an entry in numerical order to the table to read as follows:

*§602.101 OMB Control numbers.*

\* \* \* \* \*

(b) \* \* \*

CFR part or section where identified and described	Current OMB Control No.
* * * * *	
1.59-1	1545-1903
* * * * *	

Mark E. Matthews,  
*Deputy Commissioner for  
Services and Enforcement.*

Approved December 15, 2004.

Gregory F. Jenner,  
*Acting Assistant Secretary of the  
Treasury (Tax Policy).*

(Filed by the Office of the Federal Register on December 21, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 22, 2004, 69 F.R. 76614)

## Section 330 (31 USC).—Best Practices for Tax Advisors

*31 CFR 10.33: Best practices for tax advisors.*

### T.D. 9165

## DEPARTMENT OF THE TREASURY Office of the Secretary 31 CFR Part 10

### Regulations Governing Practice Before the Internal Revenue Service

AGENCY: Office of the Secretary, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations revising the regulations governing practice before the Internal Revenue Service (Circular 230). These regulations affect individuals who practice before the Internal Revenue Service. These final regulations set forth best practices for tax advisors providing advice to taxpayers relating to Federal tax issues or submissions to the IRS. These final regulations also provide standards for covered opinions and other written advice.

DATES: *Effective Date:* These regulations are effective December 20, 2004.

*Applicability Date:* For dates of applicability, see §§10.33(c), 10.35(g), 10.36(b), 10.37(b), 10.38(b), 10.52(b) and 10.93.

FOR FURTHER INFORMATION CONTACT: Heather L. Dostaler at (202)

622–4940, or Brinton T. Warren at (202) 622–7800 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

#### Paperwork Reduction Act

The collection of information contained in these final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–1871. The collections of information (disclosure requirements) in these final regulations are in §10.35(e). Section 10.35(e) requires a practitioner providing a covered opinion to make certain disclosures in the beginning of marketed opinions, limited scope opinions and opinions that fail to conclude at a confidence level of at least more likely than not. In addition, certain relationships between the practitioner and a person promoting or marketing a tax shelter must be disclosed. A practitioner may be required to make one or more disclosures. The collection of this material helps to ensure that taxpayers who receive a tax shelter opinion are informed of any facts or circumstances that might limit the use of the opinion. The collection of information is mandatory.

Estimated total annual disclosure burden is 13,333 hours.

Estimated annual burden per disclosing practitioner varies from 5 to 10 minutes, depending on individual circumstances, with an estimated average of 8 minutes.

Estimated number of disclosing practitioners is 100,000.

Estimated annual frequency of responses is on occasion.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, **Office of Information and Regulatory Affairs**, Washington, DC 20503. Books or records relating to a collection of information must

be retained as long as their contents might 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.

#### Background

Section 330 of title 31 of the United States Code authorizes the Secretary of the Treasury to regulate practice before the Treasury Department. The Secretary has published the regulations in Circular 230 (31 CFR part 10). On December 30, 2003, the Treasury Department and the IRS published in the **Federal Register** (68 FR 75186) proposed amendments to the regulations (REG–122379–02, 2004–5 I.R.B. 392) (the proposed regulations) to set forth best practices for tax advisors providing advice to taxpayers relating to Federal tax issues or submissions to the IRS and to modify the standards for certain tax shelter opinions. A public hearing was held on February 19, 2004. Written public comments responding to the proposed regulations were received. After thorough consideration of the public comments, the proposed regulations are adopted as revised by this Treasury decision.

#### Explanation of Provisions

Tax advisors play a critical role in the Federal tax system, which is founded on principles of compliance and voluntary self-assessment. The tax system is best served when the public has confidence in the honesty and integrity of the professionals providing tax advice. To restore, promote, and maintain the public's confidence in those individuals and firms, these final regulations set forth best practices applicable to all tax advisors. These regulations also provide mandatory requirements for practitioners who provide covered opinions. The scope of these regulations is limited to practice before the IRS. These regulations do not alter or supplant other ethical standards applicable to practitioners.

On October 22, 2004, the President signed the American Jobs Creation Act of 2004, Public Law 108–357 (118 Stat. 1418) (the Act), which amended section 330 of title 31 of the United States Code to clarify that the Secretary may impose standards for written advice relating to a

matter that is identified as having a potential for tax avoidance or evasion. The Act also authorizes the Treasury Department and the IRS to impose a monetary penalty against a practitioner who violates any provision of Circular 230. These final regulations do not reflect amendments made by the Act. The Treasury Department and the IRS expect to propose additional regulations implementing the Act's provisions.

### *Best Practices*

The final regulations adopt the best practices set forth in the proposed regulations with modifications. These best practices are aspirational. A practitioner who fails to comply with best practices will not be subject to discipline under these regulations. Similarly, the provision relating to steps to ensure that a firm's procedures are consistent with best practices, now set forth in §10.33(b), is aspirational. Although best practices are solely aspirational, tax professionals are expected to observe these practices to preserve public confidence in the tax system.

### *Standards for Covered Opinions*

The opinion standards of §10.35 are adopted with modifications. The provisions of §10.35 in the final regulations are reorganized to clarify the provisions. Opinions subject to §10.35 are defined as *covered opinions*.

### *Definition of Covered Opinion*

Under the final regulations, the definition of a *covered opinion* includes written advice (including electronic communications) that concerns one or more Federal tax issue(s) arising from: (1) a listed transaction; (2) any plan or arrangement, the principal purpose of which is the avoidance or evasion of any tax; or (3) any plan or arrangement, a significant purpose of which is the avoidance or evasion of tax if the written advice (A) is a reliance opinion, (B) is a marketed opinion, (C) is subject to conditions of confidentiality, or (D) is subject to contractual protection. A reliance opinion is written advice that concludes at a confidence level of at least more likely than not that one or more significant Federal tax issues would be resolved in the taxpayer's favor.

Written advice will not be treated as a reliance opinion if the practitioner prominently discloses in the written advice that it was not written to be used and cannot be used for the purpose of avoiding penalties. Similarly, written advice generally will not be treated as a marketed opinion if it does not concern a listed transaction or a plan or arrangement having the principal purpose of avoidance or evasion of tax and the written advice contains this disclosure. The Treasury Department and the IRS intend to amend 26 CFR 1.6664-4 to clarify that a taxpayer may not rely upon written advice that contains this disclosure to establish the reasonable cause and good faith defense to the accuracy-related penalties.

Written advice regarding a plan or arrangement having a significant purpose of tax avoidance or evasion is excluded from the definition of a covered opinion if the written advice concerns the qualification of a qualified plan or is included in documents required to be filed with the Securities and Exchange Commission. The final regulations also adopt an exclusion for preliminary advice if the practitioner is reasonably expected to provide subsequent advice that satisfies the requirements of the regulations.

Written advice that is not a *covered opinion* for purposes of §10.35 is subject to the standards set forth in new §10.37.

### *Municipal Bond Opinions*

After careful consideration, the Treasury Department and the IRS have concluded that practitioners rendering opinions concerning the tax treatment of municipal bonds should be subject to the same professional standards that are applicable to all other practitioners. The standards for certain opinions concerning the tax treatment of municipal bonds (*State or local bond opinions*) that are included in offering materials that otherwise would be covered opinions are being issued separately in proposed form. The proposed standards will require practitioners to exercise the same degree of diligence with respect to ascertaining the relevant facts and discussing the significant Federal tax issues, but will take into account the unique circumstances of the municipal bond market.

To give bond practitioners an opportunity to comment on the proposed standards for State or local bond opinions, opinions

that are included in offering materials, including an official statement, are excluded from the definition of covered opinions in these final regulations. Thus, State or local bond opinions included in offering materials will not be subject to the opinion standards of §10.35 or proposed §10.39 until 120 days after the proposed regulations are finalized.

The exclusion for State or local bond opinions applies only to the requirements for covered opinions set forth in §10.35. State or local bond opinions are subject to the standards set forth in §10.37 relating to requirements for other written advice, and practitioners who prepare bond opinions must comply with any other applicable requirement provided in Circular 230.

### *Requirements for Covered Opinions*

In general, the requirements for all *covered opinions* are adopted as proposed. The final regulations provide that a practitioner providing a *covered opinion*, including a *marketed opinion*, must not assume that a transaction has a business purpose or is potentially profitable apart from tax benefits, or make an assumption with respect to a material valuation issue.

### *Required Disclosures*

In general, the required disclosures of §10.35(e) are adopted as proposed. These disclosures ensure that taxpayers receive information that is necessary to their evaluation of, and reliance on, a *covered opinion*.

### *Requirements for other written advice*

The final regulations also set forth requirements for written advice that is not a *covered opinion*. Under §10.37, a practitioner must not give written advice if the practitioner: (1) bases the written advice on unreasonable factual or legal assumptions; (2) unreasonably relies upon representations, statements, findings or agreements of the taxpayer or any other person; (3) fails to consider all relevant facts; or (4) takes into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be settled. Section 10.37, unlike §10.35, does not require that the practitioner describe in the written advice the relevant facts (including assumptions and



representations), the application of the law to those facts, or the practitioner's conclusion with respect to the law and the facts. The scope of the engagement and the type and specificity of the advice sought by the client, in addition to all other facts and circumstances, will be considered in determining whether a practitioner has failed to comply with the requirements of §10.37.

#### *Procedures to Ensure Compliance*

In general, the procedures to ensure compliance with requirements of §10.35 are adopted as proposed and set forth in §10.36.

#### *Advisory Committees on the Integrity of Tax Professionals*

Newly designated §10.38, formerly §10.37 in the proposed regulations, is adopted as proposed with the following modifications. Section 10.38 is modified to clarify that an advisory committee may not make recommendations about actual practitioner cases, or have access to information pertaining to actual cases. The section also is modified to clarify that the Director of the Office of Professional Responsibility should ensure that membership of these committees is balanced among those individuals who practice as attorneys, accountants and enrolled agents.

#### **Applicability Dates**

To eliminate any adverse impact that the adoption of the new requirements for *covered opinions* or other written advice could have on pending or imminent transactions, the applicability date of the standards for *covered opinions* under §10.35 and other written advice under §10.37 (and the procedures to ensure compliance as they relate to *covered opinions* under §10.36) is June 20, 2005.

#### **Special Analyses**

It has been determined that this final rule is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. Persons authorized to practice before the IRS have long been

required to comply with certain standards of conduct. The added disclosure requirements for tax shelter opinions imposed by these regulations will not have a significant economic impact on a substantial number of small entities because, as previously noted, the estimated burden of disclosures is minimal. Practitioners have the information needed to determine whether any of the disclosures will be required before the opinion is prepared and, for some disclosures, the regulations provide practitioners with the language to be included in the opinion. Therefore, 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 Internal Revenue Code, the proposed regulations preceding these regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

#### **Drafting Information**

The principal authors of the regulations are Heather L. Dostaler and Brinton T. Warren of the Office of the Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division.

\* \* \* \* \*

#### **Adoption of Amendments to the Regulations**

Accordingly, 31 CFR part 10 is amended as follows:

#### **PART 10 — PRACTICE BEFORE THE INTERNAL REVENUE SERVICE**

Paragraph 1. The authority citation for subtitle A, part 10 continues to read as follows:

[Authority: Sec. 3, 23 Stat. 258, secs. 2–12, 60 Stat. 237 *et seq.*; 5 U.S.C. 301, 500, 551–559; 31 U.S.C. 330, as amended by P.L. 108–357, 118 Stat. 1418; Reorg. Plan No. 26 of 1950, 15 FR 4935, 64 Stat. 1280, 3 CFR, 1949–1953 Comp., P. 1017.]

Par. 2. Section 10.33 is revised to read as follows:

#### *§10.33 Best practices for tax advisors.*

(a) *Best practices.* Tax advisors should provide clients with the highest quality

representation concerning Federal tax issues by adhering to best practices in providing advice and in preparing or assisting in the preparation of a submission to the Internal Revenue Service. In addition to compliance with the standards of practice provided elsewhere in this part, best practices include the following:

(1) Communicating clearly with the client regarding the terms of the engagement. For example, the advisor should determine the client's expected purpose for and use of the advice and should have a clear understanding with the client regarding the form and scope of the advice or assistance to be rendered.

(2) Establishing the facts, determining which facts are relevant, evaluating the reasonableness of any assumptions or representations, relating the applicable law (including potentially applicable judicial doctrines) to the relevant facts, and arriving at a conclusion supported by the law and the facts.

(3) Advising the client regarding the import of the conclusions reached, including, for example, whether a taxpayer may avoid accuracy-related penalties under the Internal Revenue Code if a taxpayer acts in reliance on the advice.

(4) Acting fairly and with integrity in practice before the Internal Revenue Service.

(b) *Procedures to ensure best practices for tax advisors.* Tax advisors with responsibility for overseeing a firm's practice of providing advice concerning Federal tax issues or of preparing or assisting in the preparation of submissions to the Internal Revenue Service should take reasonable steps to ensure that the firm's procedures for all members, associates, and employees are consistent with the best practices set forth in paragraph (a) of this section.

(c) *Applicability date.* This section is effective after June 20, 2005.

Par. 3. Sections 10.35, 10.36, 10.37 and 10.38 are added to subpart B to read as follows:

#### *§10.35 Requirements for covered opinions.*

(a) A practitioner who provides a covered opinion shall comply with the standards of practice in this section.

(b) *Definitions.* For purposes of this subpart—

(1) A *practitioner* includes any individual described in §10.2(e).

(2) *Covered opinion*—(i) *In general.* A *covered opinion* is written advice (including electronic communications) by a practitioner concerning one or more Federal tax issues arising from—

(A) A transaction that is the same as or substantially similar to a transaction that, at the time the advice is rendered, the Internal Revenue Service has determined to be a tax avoidance transaction and identified by published guidance as a listed transaction under 26 C.F.R. §1.6011-4(b)(2);

(B) Any partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, the principal purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code; or

(C) Any partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, a significant purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code if the written advice—

(1) Is a *reliance opinion*;

(2) Is a *marketed opinion*;

(3) Is subject to *conditions of confidentiality*; or

(4) Is subject to *contractual protection*.

(ii) *Excluded advice.* A *covered opinion* does not include—

(A) Written advice provided to a client during the course of an engagement if a practitioner is reasonably expected to provide subsequent written advice to the client that satisfies the requirements of this section; or

(B) Written advice, other than advice described in paragraph (b)(2)(i)(A) of this section (concerning listed transactions) or paragraph (b)(2)(i)(B) of this section (concerning the principal purpose of avoidance or evasion) that—

(1) Concerns the qualification of a qualified plan;

(2) Is a *State or local bond opinion*; or

(3) Is included in documents required to be filed with the Securities and Exchange Commission.

(3) A *Federal tax issue* is a question concerning the Federal tax treatment of an item of income, gain, loss, deduction, or credit, the existence or absence of a taxable transfer of property, or the value of property for Federal tax purposes. For purposes of this subpart, a *Federal tax issue* is signif-

icant if the Internal Revenue Service has a reasonable basis for a successful challenge and its resolution could have a significant impact, whether beneficial or adverse and under any reasonably foreseeable circumstance, on the overall Federal tax treatment of the transaction(s) or matter(s) addressed in the opinion.

(4) *Reliance opinion*—(i) Written advice is a *reliance opinion* if the advice concludes at a confidence level of more likely than not (a greater than 50 percent likelihood) that one or more significant Federal tax issues would be resolved in the taxpayer's favor.

(ii) For purposes of this section, written advice, other than advice described in paragraph (b)(2)(i)(A) of this section (concerning listed transactions) or paragraph (b)(2)(i)(B) of this section (concerning the principal purpose of avoidance or evasion), is not treated as a *reliance opinion* if the practitioner prominently discloses in the written advice that it was not intended or written by the practitioner to be used, and that it cannot be used by the taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer.

(5) *Marketed opinion*—(i) Written advice is a *marketed opinion* if the practitioner knows or has reason to know that the written advice will be used or referred to by a person other than the practitioner (or a person who is a member of, associated with, or employed by the practitioner's firm) in promoting, marketing or recommending a partnership or other entity, investment plan or arrangement to one or more taxpayer(s).

(ii) For purposes of this section, written advice, other than advice described in paragraph (b)(2)(i)(A) of this section (concerning listed transactions) or paragraph (b)(2)(i)(B) of this section (concerning the principal purpose of avoidance or evasion), is not treated as a *marketed opinion* if the practitioner prominently discloses in the written advice that—

(A) The advice was not intended or written by the practitioner to be used, and that it cannot be used by any taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer;

(B) The advice was written to support the promotion or marketing of the transaction(s) or matter(s) addressed by the written advice; and

(C) The taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

(6) *Conditions of confidentiality.* Written advice is subject to *conditions of confidentiality* if the practitioner imposes on one or more recipients of the written advice a limitation on disclosure of the tax treatment or tax structure of the transaction and the limitation on disclosure protects the confidentiality of that practitioner's tax strategies, regardless of whether the limitation on disclosure is legally binding. A claim that a transaction is proprietary or exclusive is not a limitation on disclosure if the practitioner confirms to all recipients of the written advice that there is no limitation on disclosure of the tax treatment or tax structure of the transaction that is the subject of the written advice.

(7) *Contractual protection.* Written advice is subject to *contractual protection* if the taxpayer has the right to a full or partial refund of fees paid to the practitioner (or a person who is a member of, associated with, or employed by the practitioner's firm) if all or a part of the intended tax consequences from the matters addressed in the written advice are not sustained, or if the fees paid to the practitioner (or a person who is a member of, associated with, or employed by the practitioner's firm) are contingent on the taxpayer's realization of tax benefits from the transaction. All the facts and circumstances relating to the matters addressed in the written advice will be considered when determining whether a fee is refundable or contingent, including the right to reimbursements of amounts that the parties to a transaction have not designated as fees or any agreement to provide services without reasonable compensation.

(8) *Prominently disclosed.* An item required to be *prominently disclosed* must be set forth in a separate section at the beginning of the written advice in a bolded typeface that is larger than any other typeface used in the written advice.

(9) *State or local bond opinion.* A *State or local bond opinion* is written advice with respect to a *Federal tax issue* included in any materials delivered to a purchaser of a State or local bond in connection with the issuance of the bond in a public or private offering, including an official statement (if one is prepared), that concerns only the excludability of interest on a State or local

bond from gross income under section 103 of the Internal Revenue Code, the application of section 55 of the Internal Revenue Code to a State or local bond, the status of a State or local bond as a qualified tax-exempt obligation under section 265(b)(3) of the Internal Revenue Code, the status of a State or local bond as a qualified zone academy bond under section 1397E of the Internal Revenue Code, or any combination of the above.

(c) *Requirements for covered opinions.* A practitioner providing a *covered opinion* must comply with each of the following requirements.

(1) *Factual matters.* (i) The practitioner must use reasonable efforts to identify and ascertain the facts, which may relate to future events if a transaction is prospective or proposed, and to determine which facts are relevant. The opinion must identify and consider all facts that the practitioner determines to be relevant.

(ii) The practitioner must not base the opinion on any unreasonable factual assumptions (including assumptions as to future events). An unreasonable factual assumption includes a factual assumption that the practitioner knows or should know is incorrect or incomplete. For example, it is unreasonable to assume that a transaction has a business purpose or that a transaction is potentially profitable apart from tax benefits. A factual assumption includes reliance on a projection, financial forecast or appraisal. It is unreasonable for a practitioner to rely on a projection, financial forecast or appraisal if the practitioner knows or should know that the projection, financial forecast or appraisal is incorrect or incomplete or was prepared by a person lacking the skills or qualifications necessary to prepare such projection, financial forecast or appraisal. The opinion must identify in a separate section all factual assumptions relied upon by the practitioner.

(iii) The practitioner must not base the opinion on any unreasonable factual representations, statements or findings of the taxpayer or any other person. An unreasonable factual representation includes a factual representation that the practitioner knows or should know is incorrect or incomplete. For example, a practitioner may not rely on a factual representation that a transaction has a business purpose if the representation does not include a specific

description of the business purpose or the practitioner knows or should know that the representation is incorrect or incomplete. The opinion must identify in a separate section all factual representations, statements or findings of the taxpayer relied upon by the practitioner.

(2) *Relate law to facts.* (i) The opinion must relate the applicable law (including potentially applicable judicial doctrines) to the relevant facts.

(ii) The practitioner must not assume the favorable resolution of any significant Federal tax issue except as provided in paragraphs (c)(3)(v) and (d) of this section, or otherwise base an opinion on any unreasonable legal assumptions, representations, or conclusions.

(iii) The opinion must not contain internally inconsistent legal analyses or conclusions.

(3) *Evaluation of significant Federal tax issues—*(i) *In general.* The opinion must consider all significant Federal tax issues except as provided in paragraphs (c)(3)(v) and (d) of this section.

(ii) *Conclusion as to each significant Federal tax issue.* The opinion must provide the practitioner's conclusion as to the likelihood that the taxpayer will prevail on the merits with respect to each significant Federal tax issue considered in the opinion. If the practitioner is unable to reach a conclusion with respect to one or more of those issues, the opinion must state that the practitioner is unable to reach a conclusion with respect to those issues. The opinion must describe the reasons for the conclusions, including the facts and analysis supporting the conclusions, or describe the reasons that the practitioner is unable to reach a conclusion as to one or more issues. If the practitioner fails to reach a conclusion at a confidence level of at least more likely than not with respect to one or more significant Federal tax issues considered, the opinion must include the appropriate disclosure(s) required under paragraph (e) of this section.

(iii) *Evaluation based on chances of success on the merits.* In evaluating the significant Federal tax issues addressed in the opinion, the practitioner must not take into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be resolved through settlement if raised.

(iv) *Marketed opinions.* In the case of a *marketed opinion*, the opinion must provide the practitioner's conclusion that the taxpayer will prevail on the merits at a confidence level of at least more likely than not with respect to each significant Federal tax issue. If the practitioner is unable to reach a more likely than not conclusion with respect to each significant Federal tax issue, the practitioner must not provide the marketed opinion, but may provide written advice that satisfies the requirements in paragraph (b)(5)(ii) of this section.

(v) *Limited scope opinions.* (A) The practitioner may provide an opinion that considers less than all of the significant Federal tax issues if—

(1) The practitioner and the taxpayer agree that the scope of the opinion and the taxpayer's potential reliance on the opinion for purposes of avoiding penalties that may be imposed on the taxpayer are limited to the Federal tax issue(s) addressed in the opinion;

(2) The opinion is not advice described in paragraph (b)(2)(i)(A) of this section (concerning listed transactions), paragraph (b)(2)(i)(B) of this section (concerning the principal purpose of avoidance or evasion) or paragraph (b)(5) of this section (a *marketed opinion*); and

(3) The opinion includes the appropriate disclosure(s) required under paragraph (e) of this section.

(B) A practitioner may make reasonable assumptions regarding the favorable resolution of a Federal tax issue (an assumed issue) for purposes of providing an opinion on less than all of the significant Federal tax issues as provided in this paragraph (c)(3)(v). The opinion must identify in a separate section all issues for which the practitioner assumed a favorable resolution.

(4) *Overall conclusion.* (i) The opinion must provide the practitioner's overall conclusion as to the likelihood that the Federal tax treatment of the transaction or matter that is the subject of the opinion is the proper treatment and the reasons for that conclusion. If the practitioner is unable to reach an overall conclusion, the opinion must state that the practitioner is unable to reach an overall conclusion and describe the reasons for the practitioner's inability to reach a conclusion.

(ii) In the case of a *marketed opinion*, the opinion must provide the practitioner's

overall conclusion that the Federal tax treatment of the transaction or matter that is the subject of the opinion is the proper treatment at a confidence level of at least more likely than not.

(d) *Competence to provide opinion; reliance on opinions of others.* (1) The practitioner must be knowledgeable in all of the aspects of Federal tax law relevant to the opinion being rendered, except that the practitioner may rely on the opinion of another practitioner with respect to one or more significant Federal tax issues, unless the practitioner knows or should know that the opinion of the other practitioner should not be relied on. If a practitioner relies on the opinion of another practitioner, the relying practitioner's opinion must identify the other opinion and set forth the conclusions reached in the other opinion.

(2) The practitioner must be satisfied that the combined analysis of the opinions, taken as a whole, and the overall conclusion, if any, satisfy the requirements of this section.

(e) *Required disclosures.* A covered opinion must contain all of the following disclosures that apply—

(1) *Relationship between promoter and practitioner.* An opinion must prominently disclose the existence of—

(i) Any compensation arrangement, such as a referral fee or a fee-sharing arrangement, between the practitioner (or the practitioner's firm or any person who is a member of, associated with, or employed by the practitioner's firm) and any person (other than the client for whom the opinion is prepared) with respect to promoting, marketing or recommending the entity, plan, or arrangement (or a substantially similar arrangement) that is the subject of the opinion; or

(ii) Any referral agreement between the practitioner (or the practitioner's firm or any person who is a member of, associated with, or employed by the practitioner's firm) and a person (other than the client for whom the opinion is prepared) engaged in promoting, marketing or recommending the entity, plan, or arrangement (or a substantially similar arrangement) that is the subject of the opinion.

(2) *Marketed opinions.* A marketed opinion must prominently disclose that—

(i) The opinion was written to support the promotion or marketing of the transac-

tion(s) or matter(s) addressed in the opinion; and

(ii) The taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

(3) *Limited scope opinions.* A limited scope opinion must prominently disclose that—

(i) The opinion is limited to the one or more Federal tax issues addressed in the opinion;

(ii) Additional issues may exist that could affect the Federal tax treatment of the transaction or matter that is the subject of the opinion and the opinion does not consider or provide a conclusion with respect to any additional issues; and

(iii) With respect to any significant Federal tax issues outside the limited scope of the opinion, the opinion was not written, and cannot be used by the taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer.

(4) *Opinions that fail to reach a more likely than not conclusion.* An opinion that does not reach a conclusion at a confidence level of at least more likely than not with respect to a significant Federal tax issue must prominently disclose that—

(i) The opinion does not reach a conclusion at a confidence level of at least more likely than not with respect to one or more significant Federal tax issues addressed by the opinion; and

(ii) With respect to those significant Federal tax issues, the opinion was not written, and cannot be used by the taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer.

(5) *Advice regarding required disclosures.* In the case of any disclosure required under this section, the practitioner may not provide advice to any person that is contrary to or inconsistent with the required disclosure.

(f) *Effect of opinion that meets these standards—*(1) *In general.* An opinion that meets the requirements of this section satisfies the practitioner's responsibilities under this section, but the persuasiveness of the opinion with regard to the tax issues in question and the taxpayer's good faith reliance on the opinion will be determined separately under applicable provisions of the law and regulations.

(2) *Standards for other written advice.* A practitioner who provides written advice that is not a covered opinion for purposes

of this section is subject to the requirements of §10.37.

(g) *Effective date.* This section applies to written advice that is rendered after June 20, 2005.

#### §10.36 Procedures to ensure compliance.

(a) *Requirements for covered opinions.* Any practitioner who has (or practitioners who have or share) principal authority and responsibility for overseeing a firm's practice of providing advice concerning Federal tax issues must take reasonable steps to ensure that the firm has adequate procedures in effect for all members, associates, and employees for purposes of complying with §10.35. Any such practitioner will be subject to discipline for failing to comply with the requirements of this paragraph if—

(1) The practitioner through willfulness, recklessness, or gross incompetence does not take reasonable steps to ensure that the firm has adequate procedures to comply with §10.35, and one or more individuals who are members of, associated with, or employed by, the firm are, or have, engaged in a pattern or practice, in connection with their practice with the firm, of failing to comply with §10.35; or

(2) The practitioner knows or should know that one or more individuals who are members of, associated with, or employed by, the firm are, or have, engaged in a pattern or practice, in connection with their practice with the firm, that does not comply with §10.35 and the practitioner, through willfulness, recklessness, or gross incompetence, fails to take prompt action to correct the noncompliance.

(b) *Effective date.* This section is applicable after June 20, 2005.

#### §10.37 Requirements for other written advice.

(a) *Requirements.* A practitioner must not give written advice (including electronic communications) concerning one or more Federal tax issues if the practitioner bases the written advice on unreasonable factual or legal assumptions (including assumptions as to future events), unreasonably relies upon representations, statements, findings or agreements of the taxpayer or any other person, does not consider all relevant facts that the practitioner knows or should know, or, in evaluating

a Federal tax issue, takes into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be resolved through settlement if raised. All facts and circumstances, including the scope of the engagement and the type and specificity of the advice sought by the client will be considered in determining whether a practitioner has failed to comply with this section. In the case of an opinion the practitioner knows or has reason to know will be used or referred to by a person other than the practitioner (or a person who is a member of, associated with, or employed by the practitioner's firm) in promoting, marketing or recommending to one or more taxpayers a partnership or other entity, investment plan or arrangement a significant purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code, the determination of whether a practitioner has failed to comply with this section will be made on the basis of a heightened standard of care because of the greater risk caused by the practitioner's lack of knowledge of the taxpayer's particular circumstances.

(b) *Effective date.* This section applies to written advice that is rendered after June 20, 2005.

#### *§10.38 Establishment of Advisory Committees.*

(a) *Advisory committees.* To promote and maintain the public's confidence in tax advisors, the Director of the Office of Professional Responsibility is authorized to establish one or more advisory committees composed of at least five individuals authorized to practice before the Internal Revenue Service. The Director should ensure that membership of an advisory committee is balanced among those who practice as attorneys, accountants, and enrolled agents. Under procedures prescribed by the Director, an advisory committee may review and make general recommendations regarding professional standards or best practices for tax advisors, including whether hypothetical conduct would give rise to a violation of §§10.35 or 10.36.

(b) *Effective date.* This section applies after December 20, 2004.

Par. 4. Section 10.52 is amended to read as follows:

#### *§10.52 Violation of regulations.*

(a) *Prohibited conduct.* A practitioner may be censured, suspended or disbarred from practice before the Internal Revenue Service for any of the following:

(1) Willfully violating any of the regulations (other than §10.33) contained in this part; or

(2) Recklessly or through gross incompetence (within the meaning of §10.51(l)) violating §§10.34, 10.35, 10.36 or 10.37.

(b) *Effective date.* This section applies after June 20, 2005.

Par. 5. Section 10.93 is revised to read as follows:

#### *§10.93 Effective date.*

Except as otherwise provided in each section and subject to §10.91, Part 10 is applicable on July 26, 2002.

Mark E. Matthews,  
*Deputy Commissioner for  
Services and Enforcement.*

Approved December 8, 2004.

Arnold I. Havens,  
*General Counsel, Department  
of the Treasury.*

(Filed by the Office of the Federal Register on December 17, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 20, 2004, 69 F.R. 75839)

## **Section 707.—Transactions Between Partner and Partnership**

A notice describes a partnership's contribution to a partner's health savings account treated as a section 707(c) distribution. See Notice 2005-8, page 368.

## **Section 731.—Extent of Recognition of Gain or Loss on Distribution**

A notice describes a partnership's contribution to a partner's health savings account treated as a section 731 distribution. See Notice 2005-8, page 368.

## **Section 1372.—Partnership Rules to Apply for Fringe Benefit Purposes**

A notice describes an S corporation's contribution to the health savings account of a 2-percent shareholder-employee for services rendered to the S corporation. See Notice 2005-8, page 368.

## **Section 1374.—Tax Imposed on Certain Built-In Gains**

*26 CFR 1.1374-8: Section 1374(d)(8) transactions.*

### **T.D. 9170**

## **DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 1**

### **Section 1374 Effective Dates**

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: These temporary regulations provide guidance concerning the applicability of section 1374 to S corporations that acquire assets in carryover basis transactions from C corporations on or after December 27, 1994, and to certain corporations that terminate S corporation status and later elect again to become S corporations. The text of the temporary regulations also serves as the text of the proposed regulations (REG-139683-04) set forth in the notice of proposed rulemaking on this subject in this issue of the Bulletin.

DATES: *Effective Date:* These regulations are effective December 22, 2004.

*Applicability Date:* Section 1.1374-8T applies to any transaction described in section 1374(d)(8) that occurs on or after December 27, 1994. Section 1.1374-10T applies for taxable years beginning after December 22, 2004. The applicability of §1.1374(d)-8T and §1.1374(d)-10T will expire on or before December 20, 2007.

FOR FURTHER INFORMATION CONTACT: Stephen R. Cleary, (202) 622-7750, (not a toll-free number).

## SUPPLEMENTARY INFORMATION:

### Background and Explanation of Provisions

#### 1. Section 1374 and its Effective Dates

Under the *General Utilities* doctrine, see *General Utilities & Operating Co. v. Helvering*, 296 U.S. 200 (1935), a C corporation, in certain cases, could distribute appreciated assets to its shareholders or sell appreciated assets without recognizing gain. Section 1374 of the Internal Revenue Code of 1986 (Code), amended in the Tax Reform Act of 1986 (TRA) as part of the repeal of the *General Utilities* doctrine, prevents a corporation from circumventing *General Utilities* repeal by converting to S corporation status before distributing appreciated assets to its shareholders or selling appreciated assets.

Section 1374 generally imposes a corporate level tax on an S corporation's net recognized built-in gain attributable to assets that it held on the date it converted from a C corporation to an S corporation. This tax is imposed on built-in gain recognized during the 10-year period beginning on the first day the corporation is an S corporation. Section 1374(d)(8), which was added by the Technical and Miscellaneous Revenue Act of 1988 (TAMRA), imposes a corporate level tax on an S corporation's net recognized built-in gain attributable to assets that it acquired in a carryover basis transaction from a C corporation for the 10-year recognition period beginning on the day of the carryover basis transaction.

Under section 1374(d)(9), which also was added by TAMRA, any reference in section 1374 to the first taxable year the corporation was an S corporation is a reference to the first taxable year it was an S corporation pursuant to its most recent S corporation election under section 1362.

Section 1019 of TAMRA states that, except as otherwise provided, any amendments made by TAMRA are effective as if included in the provision of TRA to which such amendment relates.

The current version of section 1374 replaced a prior version of section 1374 that generally only taxed income or gain recognized within the three year period following the date the corporation converted from C to S status. Section 633 of TRA,

as amended by TAMRA, provides the effective dates of the current version of section 1374. Specifically, section 633(b)(1) of TRA, as amended by TAMRA, provides that the amendments to section 1374 apply to taxable years beginning after December 31, 1986, but only in cases where the return for the taxable year is filed pursuant to an S election made after December 31, 1986. Section 633(d)(8) of TRA, as amended by TAMRA, provides a transition rule granting a limited postponement of the above effective date for "qualified corporations", which are certain small corporations as defined in that section. Under the transition rule, if a C corporation that is a qualified corporation makes an election to be an S corporation under section 1362 before January 1, 1989, then it is subject to former section 1374 for dispositions of long-term capital gain assets and current section 1374 for dispositions of short-term capital gain assets and ordinary income assets, without regard to whether such corporation is completely liquidated.

#### 2. Section 1374(d)(8)

As discussed above, the general effective date of current section 1374, which is contained in section 633(b)(1) of the TRA, as amended by TAMRA, provides that current section 1374 applies to tax years beginning after December 31, 1986, but only in cases where the return for the taxable year is filed pursuant to an S election made after December 31, 1986. In TAMRA, Congress added subsection (d)(8) to section 1374, and provided that the provision was effective as if included in TRA.

Section 1.1374-8 provides regulations interpreting section 1374(d)(8). Example 1 of §1.1374-8(d) applies section 1374(d)(8) to a merger of a C corporation into an S corporation that elected S status before the effective date of TRA amendments, as further amended by TAMRA, to section 1374. Section 1.1374-10(a) provides that §1.1374-8 applies for taxable years ending on or after December 27, 1994, but only in cases where the corporation's tax return is filed pursuant to an S election or a section 1374(d)(8) transaction occurring after December 27, 1994 (emphasis added).

Despite the provisions of §1.1374-8 and the effective date provisions of §1.1374-10, the IRS understands that

some taxpayers contend that section 1374(d)(8) does not apply to carryover basis transfers from C corporations to S corporations that filed S elections before January 1, 1987, because the provisions in TAMRA that added section 1374(d)(8) indicated that the amendment was effective only if the return for the taxable year was filed pursuant to an S election made after December 31, 1986.

Section 337(d)(1) authorizes the Secretary to prescribe regulations to prevent the circumvention of the purposes of the repeal of the *General Utilities* doctrine through the use of any provision of law or regulations. The Treasury Department and the IRS believe that these temporary regulations are necessary to implement *General Utilities* repeal to prevent the use of corporations with pre-1987 S elections as a method for C corporations to transfer appreciated assets out of C corporation solution without gain recognition. Accordingly, these regulations confirm that section 1374(d)(8) applies to any transaction described in that section that occurs on or after December 27, 1994, the effective date of §1.1374-8, regardless of the date of the S corporation's election under section 1362.

#### 3. Revocation and Re-election of S Corporation Status

As discussed above, section 633(d)(8) of TRA, as amended by TAMRA, provides a transition rule granting a limited postponement of the general effective date of current section 1374 for qualified corporations that make an election to be an S corporation under section 1362 before January 1, 1989. In *Colorado Gas Compression, Inc. v. Commissioner*, 366 F.3d 863 (10<sup>th</sup> Cir. 2004), reversing and remanding 116 T.C. 1 (2001), a qualified corporation eligible for the special transition rule elected S corporation status on February 1, 1988 (before the extended effective date of January 1, 1989), revoked S status on December 1, 1989, and subsequently re-elected S status effective on January 1, 1994. During the years 1994 through 1996, the taxpayer sold assets. The Tax Court held that such sales were subject to current section 1374, and that the transition rule did not preclude the application of current section 1374 because the taxpayer's most recent S election was

made after 1989. The Tax Court concluded that section 1374(d)(9) requires that the 1994 election, the taxpayer's most recent election, be the election considered for effective date purposes. The Tenth Circuit reversed the Tax Court, holding that, because the 1988 election was made before the extended effective date, the corporation was exempt from current section 1374 despite the intervening revocation of S status.

The Treasury Department and the IRS believe that the Tenth Circuit's holding is inconsistent with the legislative history and underlying policy of section 633 of TRA, as amended by TAMRA, and believe the Tax Court was correct in holding that a corporation's most recent S election must have been made before the deadline of the transition rule (*i.e.*, before January 1, 1989) in order for the corporation to be entitled to the benefit of the transition rule. As indicated above, section 337(d)(1) authorizes the Secretary to prescribe regulations to prevent the circumvention of the purposes of the repeal of the *General Utilities* doctrine through the use of any provision of law or regulations. The Treasury Department and the IRS believe that these temporary regulations are necessary to implement *General Utilities* repeal to prevent avoidance of corporate level tax on appreciation in the assets of a C corporation attributable to periods after the extended effective date of January 1, 1989. Accordingly, these regulations provide that the transition rule regarding qualified corporations in section 633(d)(8) of TRA, as amended by TAMRA, applies only if the corporation's most recent S election was made before January 1, 1989. Although these regulations apply to built-in gain recognized in taxable years beginning after December 22, 2004, the IRS will continue to assert this position for prior taxable years.

In summary, the temporary regulations provide that (1) section 1374(d)(8) applies to any transaction described in that section that occurs on or after December 27, 1994, regardless of the date of the S corporation's election under section 1362, and (2) for purposes of section 633(d)(8) of TRA, as amended by TAMRA, a corporation's most recent S election, not an earlier election that has been revoked or terminated, determines whether or not it is subject to current section 1374.

## Special Analyses

It has been determined that this temporary regulation is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to §1.1374-8T(a)(2) of these regulations. With respect to §1.1374-10T(c) of these regulations, it has been determined, pursuant to 5 U.S.C. 553(b)(B), that it would be contrary to the public interest to issue the regulations with notice and public procedure and, pursuant to 5 U.S.C. 553(d)(3), that good cause exists to dispense with a delayed effective date. The regulations are necessary to provide immediate guidance to taxpayers with respect to the application of the transition rule regarding qualified corporations in section 633(d)(8) of TRA, as amended by TAMRA, and, accordingly, with respect to the application of current section 1374 to asset dispositions which occur during taxable years beginning after December 22, 2004. For applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), refer to the Special Analysis section of the Notice of Proposed Rulemaking published in this issue of the Bulletin. Pursuant to section 7805(f) of the Code, these temporary regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

## Drafting Information

The principal author of these regulations is Stephen R. Cleary of the Office of Associate Chief Counsel (Corporate). Other personnel from Treasury and the IRS participated in their development.

\* \* \* \* \*

## Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

### PART 1 — INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding entries in numerical order to read as follows:

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

Section 1.1374-8T also issued under 26 U.S.C. 337(d) and 1374(e).\* \* \*

Section 1.1374-10T also issued under 26 U.S.C. 337(d) and 1374(e).\* \* \*

Par. 2. Section 1.1374-8 is amended by redesignating paragraph (a) as paragraph (a)(1) and adding paragraph (a)(2) to read as follows:

*§1.1374-8 Section 1374(d)(8) transactions.*

(a)(1) \* \* \*

(2) (Reserved) For further guidance, see §1.1374-8T(a)(2).

\* \* \* \* \*

Par. 3. Section 1.1374-8T is added to read as follows:

*§1.1374-8T Section 1374(d)(8) transactions (temporary).*

(a)(1) (Reserved) For further guidance, see §1.1374-8(a).

(2) Section 1374(d)(8) applies to any section 1374(d)(8) transaction, as defined in paragraph (a)(1) of this regulation, that occurs on or after December 27, 1994, without regard to the date of the corporation's election to be an S corporation under section 1362.

(b) through (d) (Reserved) For further guidance, see §1.1374-8(b) through (d).

Par. 4. Section 1.1374-10 is amended by adding paragraph (c) to read as follows:

*§1.1374-10 Effective date and additional rules.*

\* \* \* \* \*

(c) (Reserved) For further guidance, see §1.1374-10T(c).

Par. 5. Section 1.1374-10T is added to read as follows:

*§ 1.1374-10T Effective date and additional rules (temporary).*

(a) through (b)(4) (Reserved) For further guidance, see § 1.1374-10(a) through (b)(4).

(c) *Revocation and re-election of S corporation status—(1) In general.* For purposes of section 633(d)(8) of the Tax Reform Act of 1986, as amended, any reference to an election to be an S corporation under section 1362 shall be treated as a reference to the corporation's most recent election to be an S corporation under

section 1362. This paragraph (c) applies for taxable years beginning after December 22, 2004, without regard to the date of the corporation's most recent election to be an S corporation under section 1362.

(2) *Example.* The following example illustrates the rules of this paragraph (c):

*Example.* (i) On February 1, 1988, X, a C corporation that is a qualified corporation under section 633(d) of the Tax Reform Act of 1986, as amended, elects to be an S corporation under section 1362. On December 1, 1989, X revokes its S status and becomes a C corporation. On January 1, 2004, X again elects to be an S corporation under section 1362. X disposes of assets in 2006, 2007, and 2008, recognizing gain.

(ii) X is not eligible for treatment under the transition rule of section 633(d)(8) of the Tax Reform Act of 1986, as amended, with respect to these assets. Accordingly, X is subject to section 1374, as amended by the Tax Reform Act of 1986 and TAMRA, and the 10-year recognition period begins on January 1, 2004.

(iii) To the extent the gain that X recognizes on the asset sales in 2006, 2007, and 2008 reflects built-in gain inherent in such assets in X's hands on January 1, 2004, such gain is subject to tax under section 1374 as amended by the Tax Reform Act of 1986 and TAMRA.

Mark E. Matthews,  
*Deputy Commissioner for  
Services and Enforcement.*

Approved December 15, 2004.

Gregory F. Jenner,  
*Acting Assistant of the Treasury.*

(Filed by the Office of the Federal Register on December 21, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 22, 2004, 69 F.R. 76612)

## Section 1402.—Definitions

A notice describes a partnership's contribution to the health savings account (HSA) of a partner, treated as a section 707(c) guaranteed payment or as a section 731 distribution, and an S corporation's contribution to the HSA of a 2-percent shareholder-employee for services rendered to the S corporation. See Notice 2005-8, page 368.

## Section 6404(g).—Suspension of Interest and Certain Penalties Where Secretary Fails to Contact Taxpayer

**Interest suspension; time sensitive penalties.** Section 6404(g) of the Code suspends interest and time sensitive penalties, additions to tax and additional amounts with respect to an increased tax liability reported on an individual's

amended income tax return filed more than 18 months after the date that is the later of (1) the original due date of the return (without regard to extensions) or (2) the date on which the taxpayer timely filed the return.

## Rev. Rul. 2005-4

### ISSUES

Does section 6404(g) suspend interest and time sensitive penalties, additions to tax and additional amounts with respect to an increased tax liability reported on an individual's amended income tax return (or other written notice to the Service of additional liability not listed on the original return) that is filed after the individual files a timely return? If so, when does the accrual of interest and time sensitive penalties, additions to tax and additional amounts begin and end with respect to the additional amount?

### FACTS

Situation 1. TP, an individual taxpayer, files an income tax return for the 2002 taxable year on the due date of April 15, 2003. On October 4, 2004, within 18 months after the due date of TP's return, TP files an amended income tax return that reports additional tax due for 2002. TP files the amended return before the Service notifies TP of the amount or the basis for the additional tax reported on the amended return. TP does not pay the additional tax due with the amended return.

Situation 2. The facts are the same as in Situation 1, except that TP files the amended return on November 26, 2004, more than 18 months after the due date of TP's return, and TP remits payment with the amended return.

Situation 3. The facts are the same as Situation 2, except that TP does not remit payment with the amended return.

### LAW AND ANALYSIS

Section 6601 requires the payment of interest on any amount of tax imposed by Title 26 that is not paid on or before the last date prescribed for payment of the tax. Interest is computed using the underpayment rate established under section 6621. Section 6151 provides that the date for payment of tax is the date a taxpayer must

file the return reporting the tax due (determined without regard to any extension for filing the return). Section 6072(a) provides that individuals shall file income tax returns made on a calendar year basis on or before April 15<sup>th</sup> of the year following the calendar year for which the tax is due. Accordingly, interest is imposed on individual calendar year taxpayers under section 6601 on any underpayment that is not paid on or before April 15<sup>th</sup> of the year following the calendar year for which the tax is due for the period from April 15<sup>th</sup> until the date on which the tax is paid.

Section 6404(g) requires the Secretary to suspend the accrual of interest and time sensitive penalties if the Secretary does not provide a notice specifically stating the amount and basis for the taxpayer's liability within 18 months following the date that is the later of (1) the original due date of the return (without regard to extensions) or (2) the date on which the taxpayer timely filed the return (the "notification period"). The suspension of the accrual of interest and penalties begins upon the expiration of the notification period and ends 21 days after the date on which the Service provides the notice to the taxpayer (the "suspension period"). Section 6404(g)(3). The legislative history to section 6404(g) states that section 6404(g) was enacted to limit the period during which interest and penalties accrue because the IRS should promptly inform taxpayers of their obligations with respect to tax deficiencies and additional amounts due. S. Rep. No. 174, 105<sup>th</sup> Cong., 2d Sess., at 64-65, 1998-3 C.B. 537, 600-01.

Section 6404(g)(1) provides that the suspension of the accrual of interest and penalties under section 6404(g) only applies to taxpayers who file an income tax return "on or before the due date for the return (including extensions)." (Emphasis added.) Section 6404(g)(2)(C) provides that "any tax liability shown on the return" is excluded from the suspension provisions of section 6404(g)(1). (Emphasis added.) Because section 6404(g)(2) provides exceptions to 6404(g)(1), "the return" referred to in section 6404(g)(2)(C) is the timely filed return described in section 6404(g)(1), *i.e.*, the original return.

An amended return (or other written notice to the Service of additional liability not listed on the original return) filed after the due date (including extensions) is not "the



return” described in sections 6404(g)(1) and 6404(g)(2)(C). Accordingly, interest and time sensitive penalties are suspended under section 6404(g) with respect to any tax shown on an amended return (or other written notice to the Service of additional liability not listed on the original return) if the Service does not provide to the taxpayer the notice described under section 6404(g)(1) within the notification period.

When a taxpayer files an amended return (or other written notice to the Service of additional liability not listed on the original return), the taxpayer knows the amount and the basis for the additional tax reported on the amended return. The filing of the amended return (or other written notice to the Service of additional liability not listed on the original return), therefore, renders unnecessary notice to the taxpayer under section 6404(g)(1).

In Situation 1, TP filed an amended return on October 4, 2004, within 18 months of filing the income tax return. TP’s amended return renders unnecessary notice of the amount and the basis for the additional tax reported on the amended return prior to the termination of the notification period. Section 6404(g)(1) will not suspend interest and time sensitive penalties with respect to the additional tax liability reported on the amended return. Interest and time sensitive penalties will accrue on the additional tax liability from the due date of the original return.

In Situation 2, TP filed an amended return on November 26, 2004, more than 18

months after the filing of an income tax return. The Service did not provide TP with the notice required to be provided under section 6404(g) prior to October 14, 2004, the date on which the notification period expired. Section 6404(g) suspends the imposition of interest and time sensitive penalties beginning on October 15, 2004, until November 26, 2004, the date on which TP filed the amended return and paid the additional tax due.

In Situation 3, TP filed an amended return on November 26, 2004, more than 18 months after the filing of an income tax return, but did not pay the additional tax due. The Service did not provide TP with the notice required to be provided under section 6404(g) before October 14, 2004, the date on which the notification period expired. Section 6404(g) suspends the imposition of interest and time sensitive penalties beginning on October 15, 2004, and ending on December 17, 2004, the date that is 21 days after November 26, 2004, the date that TP filed an amended return.

#### HOLDINGS

Section 6404(g) suspends interest and time sensitive penalties, additions to tax and additional amounts with respect to an increased tax liability reported on an individual’s amended income tax return filed more than 18 months after the date that is the later of (1) the original due date of the return (without regard to extensions) or (2) the date on which the taxpayer timely filed

the return. The suspension of the accrual of interest and time sensitive penalties, additions to tax and additional amounts begins 18 months and one day after the date that is the later of (1) the original due date of the return (without regard to extensions) or (2) the date on which the individual timely filed the return. The suspension of the accrual of interest and time sensitive penalties, additions to tax and additional amounts ends (1) on the date on which the individual files an amended return if the individual pays the additional tax due with the amended return or (2) on the date that is 21 days after the date on which the individual files the amended return if the individual does not pay the additional tax due with the amended return.

#### EFFECTIVE DATE

This revenue ruling is effective for tax years ending after July 22, 1998, for which the period of limitations on filing a claim for refund has not expired.

#### DRAFTING INFORMATION

The principal author of this revenue ruling is Julie A. Jebe of the Office of Associate Chief Counsel (Procedure & Administration), Administrative Provisions and Judicial Practice Division. For further information regarding this revenue ruling, contact Julie A. Jebe at (202) 622-7950 (not a toll-free call).

## Part III. Administrative, Procedural, and Miscellaneous

### Health Savings Accounts — Partnership Contributions to a Partner's Health Savings Account (HSA); S Corporation's Contributions to a 2-Percent Shareholder-Employee's HSA

#### Notice 2005-8

##### PURPOSE

This notice provides guidance on a partnership's contributions to a partner's Health Savings Account (HSA) and an S corporation's contributions to a 2-percent shareholder-employee's HSA.

##### BACKGROUND

Section 1201 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, Pub. L. No. 108-173, added section 223 to the Internal Revenue Code to permit eligible individuals to establish Health Savings Accounts (HSAs) for taxable years beginning after December 31, 2003. Generally, contributions made to an HSA, within permissible limits, by or on behalf of a taxpayer who is an eligible individual are deductible by a taxpayer under section 223(a). The deduction is an adjustment to gross income (*i.e.*, an above the line deduction) under section 62(a)(19). If an employer makes a contribution, within permissible limits, to the HSA on behalf of an employee who is an eligible individual, the contribution is excluded from the employee's gross income and wages. *See* section 106(d). A partnership may also contribute to a partner's HSA and an S corporation may contribute to the HSA of a 2-percent shareholder-employee (as defined below). The Questions and Answers below discuss the tax treatment of HSA contributions made on behalf of such partners and 2-percent shareholder-employees who are eligible individuals.

##### QUESTIONS AND ANSWERS

Q-1. What is the tax treatment of a partnership's contributions to a partner's HSA that are treated as distributions to the partner under section 731?

A-1. Contributions by a partnership to a *bona fide* partner's HSA are not contributions by an employer to the HSA of an employee. *See* Rev. Rul. 69-184, 1969-1 C.B. 256. Contributions by a partnership to a partner's HSA that are treated as distributions to the partner under section 731 are not deductible by the partnership and do not affect the distributive shares of partnership income and deductions. *See* Rev. Rul. 91-26, 1991-1 C.B. 184 (analysis of situation 1, last paragraph). The contributions are reported as distributions of money on Schedule K-1 (Form 1065). These distributions are not included in the partner's net earnings from self-employment under section 1402(a) because the distributions under section 731 do not affect a partner's distributive share of partnership income or loss under section 702(a)(8). The partner, if an eligible individual as defined in section 223(c)(1), is entitled under sections 223(a) and 62(a)(19) to deduct the amount of the contributions made to the partner's HSA during the taxable year as an adjustment to gross income on his or her federal income tax return.

Q-2. What is the tax treatment of a partnership's contributions to a partner's HSA that are treated as guaranteed payments under section 707(c), are derived from the partnership's trade or business, and are for services rendered to the partnership?

A-2. Contributions by a partnership to a *bona fide* partner's HSA are not contributions by an employer to the HSA of an employee. *See* Rev. Rul. 69-184. Contributions by a partnership to a partner's HSA for services rendered to the partnership that are treated as guaranteed payments under section 707(c) are deductible by the partnership under section 162 (if the requirements of that section are satisfied (taking into account the rules of section 263)) and are includible in the partner's gross income. The contributions are not excludible from the partner's gross income under section 106(d) because the contributions are treated as a distributive share of partnership income under § 1.707-1(c) of the Income Tax Regulations for purposes of all Code sections other than sections 61(a) and 162(a). *See* Rev. Rul. 91-26. Contributions by a partnership to a partner's HSA that are

treated as guaranteed payments under section 707(c), are reported as guaranteed payments on Schedule K-1 (Form 1065). Because the contributions are guaranteed payments that are derived from the partnership's trade or business, and are for services rendered to the partnership, the contributions are included in the partner's net earnings from self-employment under section 1402(a) on the partner's Schedule SE (Form 1040). The partner, if an eligible individual as defined in section 223(c)(1), is entitled under sections 223(a) and 62(a)(19) to deduct the amount of the contributions made to the partner's HSA during the taxable year as an adjustment to gross income on his or her federal income tax return.

The following example illustrates the answers in A-1 and A-2.

*Example.* Partnership is a limited partnership with three equal individual partners, A (a general partner), B (a limited partner), and C (a limited partner). C is to be paid \$500 annually for services rendered to Partnership in his capacity as a partner and without regard to Partnership income (a section 707(c) guaranteed payment). The \$500 payment to C is derived from Partnership's trade or business. Partnership has no employees. A, B, and C are eligible individuals as defined in section 223(c)(1) and each has an HSA. During Partnership's Year 1 taxable year, Partnership makes the following contributions: a \$300 contribution to each of A's and B's HSAs which are treated by Partnership as section 731 distributions to A and B; and a \$500 contribution to C's HSA in lieu of paying C the guaranteed payment directly.

Partnership's contributions to A's and B's HSAs are not deductible by Partnership and, therefore, do not affect Partnership's calculation of its taxable income or loss. *See* Rev. Rul. 91-26. A and B are entitled to an above the line deduction, under sections 223(a) and 62(a)(19), for the amount of the contributions made to their individual HSAs. The section 731 distributions to A's and B's individual HSAs are reported as cash distributions to A and B on A's and B's Schedule K-1 (Form 1065). The distributions to A's and B's HSAs are not includible in A's and B's net earnings from self-employment under section 1402(a), because distributions under section 731 do not affect a partner's distributive share of the partnership's income or loss under section 702(a)(8).

Partnership's contribution to C's HSA that is treated as a guaranteed payment under section 707(c) for services rendered to the partnership is deductible by Partnership under section 162 (if the requirements of that section are satisfied (taking into account the rules of section 263)) and is includible in C's gross income. The contribution is not excludible from C's gross income under section 106(d) because the contribution is treated as a distributive share of partnership income for purposes of all Code sections other than sections 61(a) and 162(a), and a guaranteed

payment to a partner is not treated as compensation to an employee. See Rev. Rul. 91-26. The payment to C's HSA should be reported as a guaranteed payment on Schedule K-1 (Form 1065). Because the contribution is a guaranteed payment that is derived from the partnership's trade or business and is for services rendered to the partnership, the contribution constitutes net earnings from self-employment to C under section 1402(a) which should be reported on Schedule SE (Form 1040). C is entitled under sections 223(a) and 62(a)(19) to deduct as an adjustment to gross income the amount of the contribution made to C's HSA.

**Q-3.** What is the tax treatment of an S corporation's contributions to the HSA of a 2-percent shareholder (as defined in section 1372(b)) who is also an employee (2-percent shareholder-employee) in consideration for services rendered to the S corporation?

**A-3.** Under section 1372, for purposes of applying the provisions of Subtitle A that relate to fringe benefits, an S corporation is treated as a partnership, and any 2-percent shareholder of the S corporation is treated as a partner of such partnership. Therefore, contributions by an S corporation to an HSA of a 2-percent shareholder-employee in consideration for services rendered are treated as guaranteed payments under section 707(c). Accordingly, the contributions are deductible by the S corporation under section 162 (if the requirements of that section are satisfied (taking into account the rules of section 263)) and are includible in the 2-percent shareholder-employee's gross income. In addition, the 2-percent shareholder-employee is not entitled to exclude the contribution from gross income under section 106(d). See Rev. Rul. 91-26.

For employment tax purposes, when contributions are made by an S corporation to an HSA of a 2-percent shareholder-employee, the 2-percent shareholder-employee is treated as an employee subject to Federal Insurance Contributions Act (FICA) tax and not as an individual subject to Self-Employment Contributions Act (SECA) tax. (See Announcement 92-16, 1992-5 I.R.B. 53, clarifying the FICA (Social Security and Medicare) tax

treatment of accident and health premiums paid by an S corporation on behalf of a 2-percent shareholder-employee.) However, if the requirements for the exclusion under section 3121(a)(2)(B) are satisfied, the S corporation's contributions to an HSA of a 2-percent shareholder-employee are not wages subject to FICA tax, even though the amounts must be included in wages for income tax withholding purposes on the 2-percent shareholder-employee's Form W-2, *Wage and Tax Statement*. The 2-percent shareholder-employee, if an eligible individual as defined in section 223(c)(1), is entitled under sections 223(a) and 62(a)(19) to deduct the amount of the contributions made to the 2-percent shareholder-employee's HSA during the taxable year as an adjustment to gross income on his or her federal income tax return. See Notice 2004-2, Q&A 19, 2004-2 I.R.B. 269, for employment tax rules for employer contributions to HSAs of employees other than 2-percent shareholder-employees.

#### DRAFTING INFORMATION

The principal authors of this notice are Elizabeth Purcell of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities) and Pietro E. Canestrelli of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding HSA issues in this notice, contact Ms. Purcell at (202) 622-6080. For information regarding partnership or S corporation issues, contact Mr. Canestrelli at (202) 622-3060 (not toll-free calls).

## Weighted Average Interest Rates Update

### Notice 2005-9

This notice provides guidance as to the corporate bond weighted average interest rate and the permissible range of interest

rates specified under § 412(b)(5)(B)(ii)(II) of the Internal Revenue Code. In addition, it provides guidance as to the interest rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II), and the weighted average interest rate and permissible ranges of interest rates based on the 30-year Treasury securities rate.

#### CORPORATE BOND WEIGHTED AVERAGE INTEREST RATE

Sections 412(b)(5)(B)(ii) and 412(l)(7)(C)(i), as amended by the Pension Funding Equity Act of 2004, provide that the interest rates used to calculate current liability and to determine the required contribution under § 412(l) for plan years beginning in 2004 or 2005 must be within a permissible range based on the weighted average of the rates of interest on amounts invested conservatively in long term investment grade corporate bonds during the 4-year period ending on the last day before the beginning of the plan year.

Notice 2004-34, 2004-18 I.R.B. 848, provides guidelines for determining the corporate bond weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability. That notice establishes that the corporate bond weighted average is based on the monthly composite corporate bond rate derived from designated corporate bond indices.

The composite corporate bond rate for December 2004 is 5.57 percent. Pursuant to Notice 2004-34, the Service has determined this rate as the average of the monthly yields for the included corporate bond indices for that month.

The following corporate bond weighted average interest rate was determined for plan years beginning in the month shown below.

Month	For Plan Years Beginning in:	Year	Corporate Bond Weighted Average	90% to 110% Permissible Range
January		2005	6.10	5.49 to 6.10

**30-YEAR TREASURY SECURITIES  
WEIGHTED AVERAGE INTEREST  
RATE**

Section 417(e)(3)(A)(ii)(II) defines the applicable interest rate, which must be used for purposes of determining the minimum present value of a participant's benefit under § 417(e)(1) and (2), as the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such other time as the Secretary may by regulations prescribe. Section 1.417(e)-1(d)(3) of the Income

Tax Regulations provides that the applicable interest rate for a month is the annual interest rate on 30-year Treasury securities as specified by the Commissioner for that month in revenue rulings, notices or other guidance published in the Internal Revenue Bulletin.

Section 404(a)(1) of the Code, as amended by the Pension Funding Equity Act of 2004, permits an employer to elect to disregard subclause (II) of § 412(b)(5)(B)(ii) to determine the maximum amount of the deduction allowed under § 404(a)(1).

imum amount of the deduction allowed under § 404(a)(1).

The rate of interest on 30-year Treasury securities for December 2004 is 4.86 percent. Pursuant to Notice 2002-26, 2002-1 C.B. 743, the Service has determined this rate as the monthly average of the daily determination of yield on the 30-year Treasury bond maturing in February 2031.

The following 30-year Treasury rates were determined for the plan years beginning in the month shown below.

Month	For Plan Years Beginning in:	Year	30-Year Treasury Weighted Average	90% to 105% Permissible Range	90% to 110% Permissible Range
January		2005	5.10	4.59 to 5.35	4.59 to 5.61

**Drafting Information**

The principal authors of this notice are Paul Stern and Tony Montanaro of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, please contact the Employee Plans' taxpayer assistance telephone service at 1-877-829-5500 (a toll-free number), between the hours of 8:00 a.m. and 6:30 p.m. Eastern time, Monday through Friday. Mr. Stern may be reached at 1-202-283-9703. Mr. Montanaro may be reached at 1-202-283-9714. The telephone numbers in the preceding sentences are not toll-free.

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Friday. Mr. Stern may be reached at 1-202-283-9703. Mr. Montanaro may be reached at 1-202-283-9714. The telephone numbers in the preceding sentences are not toll-free.

# Part IV. Items of General Interest

## Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations

### Section 1374 Effective Dates

#### REG-139683-04

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: In this issue of the Bulletin, the IRS is issuing temporary regulations (T.D. 9170) that provide guidance concerning the applicability of section 1374 to S corporations that acquire assets in carryover basis transactions from C corporations on or after December 27, 1994, and to certain corporations that terminate S corporation status and later elect again to become S corporations. The text of those regulations also serves as the text of these proposed regulations.

DATES: Written or electronic comments, and a request for a public hearing, must be received by March 22, 2005.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-139683-04), room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-139683-04), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the IRS internet site at [www.irs.gov/reg](http://www.irs.gov/reg) or via the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov) (indicate IRS and REG-139683-04).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Stephen R. Cleary, (202) 622-7750, concerning submissions of comments, Sonya Cruse, (202) 622-4693 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

##### Background and Explanation of Provisions

Temporary Regulations in this issue of the Bulletin amend 26 CFR Part 1 relating to section 1374. The temporary regulations provide that (a) section 1374(d)(8) applies to any transaction described in that section that occurs on or after December 27, 1994, regardless of the date of the S corporation's election under section 1362, and (b) for purposes of section 633(d)(8) of the Tax Reform Act of 1986, as amended by the Technical and Miscellaneous Revenue Act of 1988, a corporation's most recent S election, not an earlier election that has been revoked or terminated, determines whether or not it is subject to current section 1374. The text of those regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the amendments.

##### Special Analysis

It has been determined that this proposed regulation is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to §1.1374-8(a)(2) of these regulations. Because §1.1374-8(a)(2) does not impose a collection of information on small entities, it is not subject to the provisions of the Regulatory Flexibility Act (5 U.S.C. chapter 6). It is hereby certified that §1.1374-10(c) of this regulation will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that §1.1374-10(c) of this regulation addresses an uncommon fact situation not likely to affect a significant number of small entities. Therefore, a regulatory flexibility analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these proposed regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

##### Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they may be made easier to understand. All comments will be available for public inspection and copying. A public hearing may be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

##### Drafting Information

The principal author of these regulations is Stephen R. Cleary of the Office of Associate Chief Counsel (Corporate). Other personnel from Treasury and the IRS participated in their development.

\* \* \* \* \*

##### Proposed Amendments to the Regulations

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

#### PART 1 — INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read, in part, as follows:  
Authority: 26 U.S.C. 7805 \* \* \*

Par. 2. Section 1.1374-8 is amended by redesignating paragraph (a) as paragraph (a)(1) and adding paragraph (a)(2) to read as follows:

*§1.1374-8 Section 1374(d)(8) transactions.*

(a)(1) \* \* \*

(2) [The text of the proposed amendment to §1.1374-8(a)(2) is the same as the text of §1.1374-8T(a)(2) published elsewhere in this issue of the Bulletin.]

\* \* \* \* \*

Par. 3. In §1.1374-10, paragraph (c) is added to read as follows:

§1.1374-10 Effective date and additional rules.

\* \* \* \* \*

(c) [The text of proposed §1.1374-10(c) is the same as the text of §1.1374-10T(c) published elsewhere in this issue of the Bulletin].

Mark E. Matthews,  
Deputy Commissioner for  
Services and Enforcement.

(Filed by the Office of the Federal Register on December 21, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 22, 2004, 69 F.R. 76635)

## Notice of Proposed Rulemaking and Notice of Public Hearing

### Regulations Governing Practice Before the Internal Revenue Service

#### REG-159824-04

AGENCY: Office of the Secretary, Treasury.

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

SUMMARY: This notice proposes amendments to the regulations governing practice before the Internal Revenue Service (Circular 230). These regulations affect individuals who are eligible to practice before the IRS. The proposed modifications set forth standards for *State or local bond opinions*. This document also provides notice of a public hearing regarding the proposed regulations.

DATES: Written or electronically generated comments and outlines of topics to be discussed at the public hearing scheduled for March 22, 2005, must be received by March 1, 2005.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-159824-04), room 5203, 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 4 p.m. to: CC:PA:LPD:PR (REG-159824-04), Courier's Desk, Internal Revenue Service,

1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via the IRS Internet site at: [www.irs.gov/regs](http://www.irs.gov/regs). The hearing will be held in the Internal Revenue Service auditorium on the seventh floor.

FOR FURTHER INFORMATION CONTACT: Concerning issues for comment, Heather L. Dostaler at (202) 622-4940 or Vicki Tsilas at (202) 622-3980; concerning submissions of comments, Treena Garrett of the Publications and Regulations Branch at (202) 622-7180 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

##### Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collection of information should be received by February 18, 2005. Comments are specifically requested concerning:

Whether the proposed collection of information and retention is necessary for the proper performance of the Office of Professional Responsibility, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proper collection and retention of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection and retention of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and

purchase of services to provide information.

The collection of information in these proposed regulations is in §10.39. This information is required to ensure practitioners comply with minimum standards when writing a State or local bond opinion. This information will assist the Commissioner, through the Office of Professional Responsibility, to ensure that practitioners properly advise taxpayers regarding state or local bonds. The collection of information is mandatory. The likely recordkeepers and respondents are individuals.

To comply with §10.39, a practitioner may provide a single *State or local bond opinion* or may provide a combination of documents, but only if the documents, taken together, satisfy the requirements of §10.39. The estimates below are based on an average of 10 opinions given by a practitioner per year with an average increased time of 1 to 3 hours per opinion.

Estimated total recordkeeping and reporting burden is 30,000 hours.

Estimated annual burden per practitioner varies from 10 to 30 hours, depending on individual circumstances, with an estimated average of 20 hours.

Estimated number of affected practitioners is 1,500.

Estimated annual frequency of responses (providing a *State or local bond opinion* or a combination of documents) is on occasion.

An agency may not conduct or sponsor, and a person is not required to respond to a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or 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 section 6103 of the Internal Revenue Code.

##### Background

Section 330 of title 31 of the United States Code authorizes the Secretary of the Treasury to regulate the practice of representatives before the Treasury Department. The Secretary has published the regulations governing standards of practice in Circular 230 (31 CFR part 10).

Municipal bond opinions have been excluded from the standards for tax shelter opinions since the Treasury Department and the IRS first published standards for tax shelter opinions in Circular 230. On December 30, 2003, the Treasury Department and the IRS proposed amendments to the standards of practice that would have eliminated the exclusion for municipal bond opinions. See 68 FR 75186 (REG-122379-02, 2004-5 I.R.B. 392). Public comments were submitted in response to the proposed amendments addressing the special characteristics of the market for municipal bond opinions.

After careful consideration, the Treasury Department and the IRS have concluded that practitioners rendering opinions concerning the tax treatment of municipal bonds should be subject to the same professional standards that are applicable to other practitioners. Recognizing the special characteristics of the bond market, the Treasury Department and the IRS are proposing regulations that provide standards of practice for practitioners rendering municipal bond opinions.

The proposed regulations are substantially similar to the standards of practice for covered opinions that were promulgated on December 20, 2004, which included final regulations providing best practices for tax advisors, minimum standards for covered opinions and other written advice and procedures to ensure compliance with the minimum standards. Under the final regulations, a practitioner providing a *covered opinion* must comply with the minimum standards set forth in §10.35. Specifically, a practitioner providing a *covered opinion* must: (1) identify and ascertain all relevant facts; (2) relate the applicable law to the relevant facts; (3) evaluate each significant Federal tax issue; and (4) provide an overall conclusion. In addition, *covered opinions* may be required to contain certain disclosures provided in §10.35(e), if applicable. Under §10.35, the definition of a covered opinion excludes State or local bond opinions. The definition of a *State or local bond opinion* contemplates opinions that issuers routinely receive at the time bonds are issued. Specifically, a *State or local bond opinion* is written advice that is included in the offering materials for the issuance of a State or local bond and that concerns only the excludability of interest on a State or

local bond from gross income under section 103, the application of section 55, the status of the bond as a qualified tax-exempt obligation under section 265(b)(3), the status of the bond as a qualified zone academy bond under section 1397E, or any combination of these issues. Offering materials include any written material delivered to a purchaser of a State or local bond in connection with the issuance of the bond in a private or public placement (bond offering materials).

### Explanation of Provisions

Under §10.35(b)(2)(ii)(B)(2), a *covered opinion* does not include a *State or local bond opinion*. Under proposed §10.35(b)(9), a *State or local bond opinion* is written advice, included in bond offering materials for the issuance of a State or local bond, if (1) the written advice as to Federal tax matters addressed in the bond offering materials consists only of advice that concerns specified issues under section 103, section 55, section 265(b)(3), or section 1397E, or any combination of those issues; and (2) the practitioner separately provides to the issuer of the bond, and includes in the transcript of proceedings if one is prepared, written advice that satisfies the requirements set forth in §10.39.

An opinion is a *State or local bond opinion* even if the written advice addresses matters not directly related to a Federal tax issue, e.g., a State law issue. An opinion also is a *State or local bond opinion* if the opinion is redelivered unchanged, e.g., if the opinion is redelivered with a qualified tender bond that is tendered to the remarketing agent and remarketed. If the *State or local bond opinion* with respect to that bond issue is changed or otherwise updated after bonds are issued, the altered opinion is not a *State or local bond opinion*, and is subject to the requirements of §10.35.

The Treasury Department and the IRS recognize the special characteristics of the market for municipal bonds and are proposing amendments to the requirements of Circular 230 that take into account these characteristics. The manner in which practitioners provide State or local bond opinions suggests that the form of these bond opinions should be more flexible than §10.35 permits. The proposed

regulations exclude a *State or local bond opinion* from the requirements of §10.35, if the practitioner provides the issuer with separate written advice that satisfies the requirements of §10.39.

Proposed §10.39 sets forth the minimum requirements for a *State or local bond opinion*. Although the minimum requirements are substantially similar to those of §10.35(c), §10.39 is tailored to take into account the customary practice and special circumstances of the market for municipal bonds. Furthermore, the proposed regulations provide practitioners flexibility in determining how the separate written advice should be conveyed. The practitioner may provide the separate written advice in a tax certificate that customarily would be prepared for inclusion in the transcript of proceedings, or in a tax certificate and an additional memorandum or letter, or in any other combination of documents that are made available to the issuer and included in the transcript of proceedings, if one is prepared. The requirements for all *State or local bond opinions* include: (1) identifying and considering all relevant facts and not relying on unreasonable factual assumptions or unreasonable representations; (2) relating the applicable law (including potentially applicable judicial doctrines) to the relevant facts and not relying on any unreasonable legal assumptions, representations or conclusions; and (3) considering all significant Federal tax issues relevant to reaching the overall conclusion with respect to the Federal tax treatment of the bonds and reaching a conclusion, supported by the facts and the law, with respect to each significant Federal tax issue. As provided in §10.35(b)(3), a Federal tax issue is significant if the Internal Revenue Service has a reasonable basis for a successful challenge and its resolution could have a significant impact, whether beneficial or adverse and under any reasonably foreseeable circumstance, on the overall Federal tax treatment of the transaction(s) or matter(s) addressed in the opinion.

A practitioner must not base the written advice on an assumption or factual representation, statement or finding of any person unless the practitioner has exercised due diligence in identifying and ascertaining the relevant facts. Even if a third party has certified a representation, the practitioner is responsible for

exercising due diligence. For example, a practitioner may not rely on a representation, certified or otherwise, to conclude that the requirements of the safe harbor for establishing the fair market value of a guaranteed investment contract in 26 CFR 1.148-5(d)(6)(iii) were met if the representation does not include a specific description of how those requirements were satisfied or if the practitioner knows or should know that the representation was incorrect or incomplete.

Proposed §10.39 permits a practitioner to incorporate the facts, factual assumptions, and findings, representations and statements of any person by reference to another document, such as a tax certificate, provided that the document is included in the transcript of proceedings. Similarly, the legal analysis may be appended or included in a tax certificate or similar document, provided that it is clear that the practitioner provided the written advice. Unlike §10.35(e) with respect to covered opinions, proposed §10.39 does not require any disclosures in the written advice.

Proposed §§10.35(b)(9) and 10.39 will require that the written advice the practitioner is required to provide separately to the issuer of a state or local bond be included in the transcript of proceedings if one is prepared or in a document available to the issuer if no transcript is prepared. Inclusion of the written advice in the transcript of proceedings is intended to ensure that the practitioner's written advice is made available to the issuer and is intended to be consistent with the current practice of including the tax certificate and other documents supporting the State or local bond opinion in the transcript of proceedings. The Treasury Department and the IRS request comments regarding this requirement.

#### Proposed Effective Date

Consistent with Announcement 2004-29, 2004-17 I.R.B. 828 (April 26, 2004), these proposed regulations will be applicable no sooner than 120 days after the final regulations are published in the **Federal Register**.

#### 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 is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. Persons authorized to practice before the IRS have long been required to comply with certain standards of conduct. Therefore, 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 Internal Revenue 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 businesses.

#### Comments and Public Hearing

Before the regulations are adopted as final regulations, consideration will be given to any written comments and electronic comments that are submitted timely to the IRS. The Treasury Department and the IRS specifically request comments on the clarity of the proposed regulations and how they can be made easier to understand. All comments will be available for public inspection and copying.

The public hearing is scheduled for March 22, 2005, at 10:00 a.m., and will be held in the Internal Revenue Service auditorium on the seventh floor. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. All visitors must present photo identification to enter the building. Visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the FOR FURTHER INFORMATION CONTACT section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written or electronic comments and submit an outline of the topics to be discussed and the time to be devoted to each topic by March 1, 2005. A period of 10 minutes will be allocated 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 authors of the regulations are Heather L. Dostaler and Brinton T. Warren of the Office of the Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division, and Vicki Tsilas of the Office of the Associate Chief Counsel (Tax Exempt/Government Entities).

\* \* \* \* \*

#### Proposed Amendments to the Regulations

Accordingly, 31 CFR part 10 is proposed to be amended as follows:

#### PART 10—PRACTICE BEFORE THE INTERNAL REVENUE SERVICE

Paragraph 1. The authority citation for subtitle A, part 10 continues to read as follows:

[Authority: Sec. 3, 23 Stat. 258, secs. 2-12, 60 Stat. 237 *et seq.*; 5 U.S.C. 301, 500, 551-559; 31 U.S.C. 330; Reorg. Plan No. 26 of 1950, 15 FR 4935, 64 Stat. 1280, 3 CFR, 1949-1953 Comp., P. 1017.]

Par. 2. Section 10.35 is amended by revising paragraph (b)(9) to read as follows:

#### §10.35 Requirements for covered opinions.

\* \* \* \* \*

(b) \* \* \*

(9) *State or local bond opinion*. Written advice, included in *bond offering materials* (as defined in §10.39(c)) for the issuance of a State or local bond, is a *State or local bond opinion* if—

(i) The written advice as to Federal tax matters addressed in the *bond offering materials* consists only of advice that concerns the excludability of interest on a State or local bond from gross income under section 103 of the Internal Revenue Code, the application of section 55 of the Internal Revenue Code to a State or local bond, the status of a State or local bond as a qualified tax-exempt obligation under section 265(b)(3) of the Internal Revenue Code, the status of a State or local bond as



a qualified zone academy bond under section 1397E of the Internal Revenue Code, or any combination of the above; and

(ii) The practitioner separately provides to the issuer of the bond written advice that satisfies the requirements set forth in §10.39.

\* \* \* \* \*

Par. 3. Section 10.36 is revised to read as follows:

*§10.36 Procedures to ensure compliance.*

(a) *Requirements for covered opinions.* Any practitioner who has (or practitioners who have or share) principal authority and responsibility for overseeing a firm's practice of providing advice concerning Federal tax issues must take reasonable steps to ensure that the firm has adequate procedures in effect for all members, associates, and employees for purposes of complying with §§10.35 and 10.39, as applicable. Any such practitioner will be subject to discipline for failing to comply with the requirements of this paragraph if—

(1) The practitioner through willfulness, recklessness, or gross incompetence does not take reasonable steps to ensure that the firm has adequate procedures to comply with §§10.35 and 10.39, as applicable, and one or more individuals who are members of, associated with, or employed by, the firm are, or have, engaged in a pattern or practice, in connection with their practice with the firm, of failing to comply with §§10.35 and 10.39, as applicable; or

(2) The practitioner knows or should know that one or more individuals who are members of, associated with, or employed by, the firm are, or have, engaged in a pattern or practice, in connection with their practice with the firm, that does not comply with §§10.35 and 10.39, as applicable, and the practitioner, through willfulness, recklessness, or gross incompetence fails to take prompt action to correct the non-compliance.

(c) *Effective date.* This section is applicable on the date that is 120 days after publication of the final regulations in the **Federal Register**.

Par. 4. Section 10.38 is revised to read as follows:

*§10.38 Establishment of Advisory Committees.*

(a) *Advisory committees.* To promote and maintain the public's confidence in tax advisors, the Director of the Office of Professional Responsibility is authorized to establish one or more advisory committees composed of at least five individuals authorized to practice before the Internal Revenue Service. The Director should ensure that membership of an advisory committee is balanced among those who practice as attorneys, accountants, and enrolled agents. Under procedures prescribed by the Director, an advisory committee may review and make general recommendations regarding professional standards or best practices for tax advisors, including whether hypothetical conduct would give rise to a violation of §§10.35, 10.36 or 10.39.

(b) *Effective date.* This section is applicable 120 days after publication of the final regulations in the **Federal Register**.

Par. 5. Section 10.39 is added to read as follows:

*§10.39 Requirements for State or local bond opinions.*

(a) *In general.* A practitioner who provides a *State or local bond opinion* shall comply with the standards of practice in this section.

(b) *Requirements for separately provided written advice.* A practitioner providing a *State or local bond opinion* must separately provide to the issuer of the bond written advice that satisfies each of the following requirements. For purposes of this section, the written advice may be set forth in a tax certificate or in other documents included in the transcript of proceedings, or, if no transcript is prepared, in one or more other documents made available to the issuer, provided that the documents constituting the written advice taken together satisfy each of the following requirements.

(1) *Factual matters.* (i) The practitioner must use reasonable efforts to identify and ascertain the facts, which may relate to future events, and to determine which facts are relevant. The written advice must identify and consider all facts that the practitioner determines to be relevant.

(ii) The practitioner must not base the written advice on any unreasonable factual assumptions (including assumptions as to future events). An unreasonable factual assumption includes a factual assumption that the practitioner knows or should know is incorrect or incomplete. A factual assumption includes reliance on a projection, financial forecast or appraisal. It is unreasonable for a practitioner to rely on a projection, financial forecast or appraisal if the practitioner knows or should know that the projection, financial forecast or appraisal is incorrect or incomplete or was prepared by a person lacking the skills or qualifications necessary to prepare such projection, financial forecast or appraisal. The written advice must identify in a separate section all factual assumptions relied upon by the practitioner.

(iii) The practitioner must not base the written advice on any unreasonable factual representations, statements or findings of any person. An unreasonable factual representation includes a factual representation that the practitioner knows or should know is incorrect or incomplete. The written advice must identify in a separate section all factual representations, statements or findings relied upon by the practitioner.

(iv) If the facts required to be identified and considered under this paragraph (b)(1) are set forth in a tax certificate or other similar document that is included in the transcript of proceedings and the analysis required by paragraphs (b)(2) and (b)(3) of this section is set forth in a separate document, the practitioner may incorporate the facts required to be identified or considered in the separate document by reference to the tax certificate or other document.

(2) *Relate law to facts.* (i) The written advice must relate the applicable law (including potentially applicable judicial doctrines) to the relevant facts.

(ii) The practitioner must not assume the favorable resolution of any significant Federal tax issue except as provided in paragraph (d) of this section, or otherwise base an opinion on any unreasonable legal assumptions, representations, or conclusions.

(iii) The written advice must not contain internally inconsistent legal analysis or conclusions.

(3) *Evaluation of significant Federal tax issues—(i) In general.* The written advice must consider all significant Federal

tax issues that are relevant to the overall conclusion provided in the State or local bond opinion with respect to the application of section 103 of the Internal Revenue Code, section 55 of the Internal Revenue Code, section 265(b)(3) of the Internal Revenue Code, or section 1397E of the Internal Revenue Code, or any combination thereof, except as provided in paragraph (d) of this section.

(ii) *Conclusion as to each significant Federal tax issue.* The written advice must provide the practitioner's conclusion as to the likelihood that a taxpayer will prevail on the merits with respect to each significant Federal tax issue considered in the written advice. The written advice must describe the reasons for the conclusions, including the facts and analysis supporting the conclusions.

(iii) *Evaluation based on chances of success on the merits.* In evaluating the significant Federal tax issue(s) addressed in the written advice, the practitioner must not take into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be resolved through settlement if raised.

(c) *Bond offering materials.* The term *bond offering materials* means any written materials delivered to a purchaser of a State or local bond in connection with the issuance of the bond in a public or private

offering, including an official statement (if one is prepared).

(d) *Competence to provide opinion; reliance on opinions of others.* (1) The practitioner must be knowledgeable in all of the aspects of Federal tax law relevant to the opinion being rendered, except that the practitioner may rely on the opinion of another practitioner with respect to one or more Federal tax issues unless the practitioner knows or should know that the opinion of the other practitioner should not be relied on. If a practitioner relies on the opinion of another practitioner regarding a significant Federal tax issue, the relying practitioner must identify the other opinion and set forth in the written advice the conclusions reached in the other opinion.

(2) The practitioner must be satisfied that the combined analysis of the opinions, taken as a whole satisfy the requirements of this section.

(e) *Effective date.* This section applies to State or local bond opinions that are rendered on a date that is on or after 120 days after publication of the final regulations in the **Federal Register**.

Par. 6. Section 10.52 is revised to read as follows:

*§10.52 Violation of regulations.*

(a) *Prohibited conduct.* A practitioner may be censured, suspended or disbarred

from practice before the Internal Revenue Service for any of the following:

(1) Willfully violating any of the regulations (other than §10.33) contained in this part; or

(2) Recklessly or through gross incompetence (within the meaning of §10.51(l)) violating §§10.34, 10.35, 10.36, 10.37 or 10.39.

(b) *Effective date.* This section is applicable 120 days after publication of the final regulations in the **Federal Register**.

Mark E. Matthews,  
*Deputy Commissioner for  
Services and Enforcement.*

Approved December 8, 2004.

Arnold I. Havens,  
*General Counsel, Department  
of the Treasury.*

(Filed by the Office of the Federal Register on December 17, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 20, 2004, 69 F.R. 75887)

# Announcement of Disciplinary Actions Involving Attorneys, Certified Public Accountants, Enrolled Agents, and Enrolled Actuaries — Suspensions, Censures, Disbarments, and Resignations

## Announcement 2005-2

Under Title 31, Code of Federal Regulations, Part 10, attorneys, certified public accountants, enrolled agents, and enrolled actuaries may not accept assistance from, or assist, any person who is under disbarment or suspension from practice before the Internal Revenue Service if the assistance relates to a matter constituting practice before the Internal Revenue Service and may not knowingly aid or abet another

person to practice before the Internal Revenue Service during a period of suspension, disbarment, or ineligibility of such other person.

To enable attorneys, certified public accountants, enrolled agents, and enrolled actuaries to identify persons to whom these restrictions apply, the Director, Office of Professional Responsibility, will announce in the Internal Revenue Bulletin

their names, their city and state, their professional designation, the effective date of disciplinary action, and the period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletins for five successive weeks.

# Consent Suspensions From Practice Before the Internal Revenue Service

Under Title 31, Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent, or enrolled actuary, in order to avoid institution or conclusion of a proceeding for his or her disbarment or suspension from practice be-

fore the Internal Revenue Service, may offer his or her consent to suspension from such practice. The Director, Office of Professional Responsibility, in his discretion, may suspend an attorney, certified public accountant, enrolled agent, or enrolled ac-

tuary in accordance with the consent offered.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Date of Suspension
Nadler, Herbert	New York, NY	Enrolled Actuary	November 1, 2004 to February 28, 2005

## Check-the-Box Disclosure Authority

### Announcement 2005-6

In July 2004, the Internal Revenue Service issued a revision to Form 656, *Offer in Compromise*. Form 656 is used by taxpayers to request that the Service enter into an agreement between the taxpayer and the government that settles a tax liability for payment of less than the full amount owed. The purpose of this announcement is to highlight the addition of a "check-the-box" disclosure authorization on Form 656.

The check-the-box authorization, which is provided in Item 14 on Form 656, allows a taxpayer to designate the person identified in the taxpayer's Form 2848, *Power of Attorney and Declaration of Representative*, or another third party to assist the taxpayer by discussing the offer in compromise and related return information with the Service. The check-the-box authorization facilitates the processing of the offer in compromise by enabling the Service to discuss the offer with the third party so that the Service is able to obtain information needed to complete the processing of the offer.

The authorization of a third party to discuss the offer with the Service is limited to assisting the taxpayer in providing information to the Service for the initial processing of the taxpayer's offer in compromise. The authorization does not permit the designated third party to practice before the Service, including the Service's

collection function, under Circular 230, 31 C.F.R. pt. 10, § 10.2(d), unless the designated person is an attorney, a CPA, or an enrolled agent. If the designated person is an attorney, a CPA, or an enrolled agent, and the taxpayer has attached a properly completed Form 2848 to the Form 656, the designated person may represent the taxpayer before the Service with respect to the offer in compromise.

#### DRAFTING INFORMATION

The principal author of this announcement is Debra A. Kohn of the Office of Associate Chief Counsel (Procedure and Administration), Collection, Bankruptcy & Summonses Division. For further information regarding this announcement, contact Branch 2 of Collection, Bankruptcy & Summonses at (202) 622-3620 (not a toll-free call).

## Foundations Status of Certain Organizations

### Announcement 2005-7

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does not indicate that the organizations have lost

their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

*Former Public Charities.* The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

2111 Foundation for Exploration,  
La Jolla, CA  
Access to Lifelong Fitness, Inc.,  
Santa Barbara, CA  
African Heritage Association,  
Houston, TX  
African Pastors Training Institute, Inc.,  
San Jose, CA  
Alexander Foundation, Houston, TX  
Alpha Beta Sigma Chapter Scholarship  
Fund, Houston, TX  
American Bicycle Racing, Incorporated,  
Tinley Park, IL  
American Indian Wilderness School,  
Nederland, CO  
Anderson-Terrell-Keller Community  
Development Corporation,  
New Orleans, LA  
Angel Academy, Inc., Houston, TX  
Angels Way Group Home,  
Los Angeles, CA  
Apple-Barrell Foundation, Inc.,  
Houston, TX  
Arctic Cultural Institute of the United  
States, Greenwood Village, CO  
Arise Woman Arise, Dallas, TX  
Athena Art Project, Houston, TX  
Aurora Project, Aurora, CO  
Ayl-Rams (Aurora Youth League-Rams  
Football/Baseball, Aurora, CO

Backcountry Horsemen Education  
 Foundation of America, Garham, WA  
 Big Country Boys Productions, Inc.,  
 Abilene, TX  
 Big Island Residential, Inc., Honolulu, HI  
 Born Again Marriages, Inc., Sonora, CA  
 Brighter Beginning Community  
 Development Corporation,  
 Cedarhill, TX  
 Broken Promises, Inc., Richardson, TX  
 Bucket Productions, Dallas, TX  
 California Latino Agricultural  
 Association, Watsonville, CA  
 California Wild Mustang & Burro  
 Sanctuary, Sequim, WA  
 Camp Hope America, Inc.,  
 Arroyo Grande, CA  
 Caption Works of the Deaf, Inc.,  
 Farmington Hills, MI  
 Castaway Ministry International,  
 The Woodlands, TX  
 Cedar Crest Community Development  
 Corporation, Dallas, TX  
 Celama Educational Charities Tr.,  
 Sugar Land, TX  
 Center for Non-Profit Organization  
 Development, Inc., Houston, TX  
 Center of Hope, Inc., Long Beach, CA  
 Central America for Christ,  
 Sugar Land, TX  
 Central California Down Syndrome  
 Foundation, Sunnyvale, CA  
 Champions for Kids, Incorporated,  
 Raleigh, NC  
 Chardi Kalaa Sikh Community Center,  
 Palo Alto, CA  
 Cheltenham York Road Nursing  
 and Rehabilitation Center, Inc.,  
 Philadelphia, PA  
 Childrens Art Car Project, Houston, TX  
 Childrens Home Society Services of  
 North Florida, Tallahassee, FL  
 Christian Challenge of Modesto,  
 Modesto, CA  
 Chrysalis, Inc., Denver, CO  
 Citizens for Childrens Rights,  
 Cheyenne, WY  
 Citizens for the Carpinteria Bluffs, Inc.,  
 Carpinteria, CA  
 City County Preservation Committee,  
 Marlowton, MT  
 City Gates Ministries, Inc., Houston, TX  
 City of Dreams, Golden, CO  
 Colorado Center for Healthy  
 Communities, Denver, CO  
 Colorado General Aviation Council, Inc.,  
 Englewood, CO  
 Community Hospice Memorial  
 Foundation, Inc., Denver, CO  
 Conadec, Kingwood, TX  
 Concrete Classic, Inc., Coralville, IA  
 Dalhart Hispanic Organization, Inc.,  
 Dalhart, TX  
 Dallas First Priority, Plano, TX  
 Dal-Tex Computer Learning Center,  
 Dallas, TX  
 Delano Police Activities League,  
 Delano, CA  
 Dr. Watsons Neglected Patients,  
 Broomfield, CO  
 Education & Resource Center, Inc.,  
 Greenville, TX  
 Educational Learning Opportunities  
 Foundation, Richmond, VA  
 El Gran Mandamiento, Inc., Merkel, TX  
 El Rio Community Gymnasium  
 Commission, Oxnard, CA  
 Elite Houston, Inc., Houston, TX  
 Embrace the Cross Foundation,  
 Houston, TX  
 Ephesus Outreach Ministries, Inc.,  
 Oklahoma City, OK  
 Family Harvest Ministry, Dayton, TX  
 Family Tree a Supervised Visitation  
 Program, Cupertino, CA  
 Farmington Valley Antiques Guild,  
 Farmington, CT  
 FDS Ministry, Chicago, IL  
 Fifteen Twelve Foundation, Inc.,  
 Cripple Creek, CO  
 Fifty-Fifty Leadership, Inc., Glendale, CA  
 Final Destiny Ministries, Inc.,  
 Missoula, MT  
 Food Fest, Inc., Beaumont, TX  
 Forgotten Children, Fort Worth, TX  
 Fort Bend Youth Foundation,  
 Sugar Land, TX  
 Forward USA, Inc., San Jose, CA  
 Foundation for Literacy in Science and  
 Technology, Houston, TX  
 Foundation Prison Ministries, Inc.,  
 Grandview, TX  
 Freedmans Foundation, Dallas, TX  
 Fresno H.O.P.E. Animal Foundation,  
 Fresno, CA  
 Friends of the Library, Preston, ID  
 Friends of the Waller County Library -  
 Brookshire Branch, Brookshire, TX  
 Friends of Weiser River Trail, Inc.,  
 Eagle, ID  
 Garland Hispanic Business Resource and  
 Community Center, Garland, TX  
 Gerlena Griffin Foundation, Inc.,  
 St. Mary's, GA  
 Gift to the World Ministries, Inc.,  
 Houston, TX  
 Giving Stage, Inc., Boulder, CO  
 Golden Triangle First Priority, Inc.,  
 Ogden, UT  
 Greater Houston Sports Association, Inc.,  
 Houston, TX  
 Greenbucks Foundation, Inc., Denver, CO  
 Hackmaster Foundation, Clovis, CA  
 Heal the Earth Celebration, Tucson, AZ  
 Higher Ground Ministries, Inc.,  
 Monte Vista, CO  
 His Mother Servants of the Holy Spirit,  
 The Colony, TX  
 His Way Community Development  
 Organization, Los Angeles, CA  
 Hispanic Education Scholarship, Inc.,  
 Fort Worth, TX  
 Hispanic Firefighter of the Year Awards,  
 Houston, TX  
 Hispanic Nurses Association Houston  
 Chapter - HNA Houston, Houston, TX  
 Hmong Youth Foundation, Fresno, CA  
 Holy Shroud Institute, Inc., Corvallis, OR  
 Homeless Employment Resource  
 Operation, Ventura, CA  
 Hope Ward Scholarship Fund and  
 Educational Assistance Program, Inc.,  
 Houston, TX  
 House by the Side of the Road,  
 Windsor, CO  
 Houston Area Leadership Scholarship  
 Fund, Inc., Houston, TX  
 Houston Serving Needy Families,  
 Houston, TX  
 Howard County D-Fy-It, Inc.,  
 Big Spring, TX  
 Hughson Police Department Reserve  
 Fund, Hughson, CA  
 Idaho Justice Center, Inc., Boise, ID  
 Institute for Salubrious Living, Inc.,  
 Mabank, TX  
 International Association of  
 Geomagnetism and Aeronomy,  
 Boulder, CO  
 International Elephant Survival  
 Foundation, Kountze, TX  
 JIVA Institute for Vaisnava Studies, Inc.,  
 Visalia, CA  
 Johnson County Emu Association,  
 Cleburne, TX  
 Josh the Cat Foundation,  
 Boulder Creek, CA  
 Journey Home, Seaside, CA  
 Juventus F C, Inc., Spring, TX  
 Kelly Village Resident Council, Inc.,  
 Houston, TX

Khalsa Religious & Cultural Corporation,  
 Turlock, CA  
 Kidswish Foundation, Humble, TX  
 Kingsburg Community Educational  
 Foundation, Kingsburg, CA  
 Korea Liberation Association of San  
 Francisco, Inc., Dublin, CA  
 KRV Friends of the Animals A Human  
 Society, Weldon, CA  
 Lakewood Foundation, Dallas, TX  
 LAO Community Cultural Center of  
 Fresno, Clovis, CA  
 Lasu Community Development, Inc.,  
 Houston, TX  
 Laura Lynn Graef Swimming and Diving  
 Scholarship Foundation, Houston, TX  
 Lee Guardianship Services, Inc.,  
 Fort Myers, FL  
 Lewis-Toran Retirement Community,  
 Inc., Lufkin, TX  
 Liberty Ministries, Inc., Agoura Hills, CA  
 Lifework, Inc., Denver, CO  
 Light of the Word Ministries, Inc.,  
 Houston, TX  
 Lincoln Park Resident Council, Inc.,  
 Houston, TX  
 Lion of Judah Ministries International,  
 Fort Worth, TX  
 Local Organizing Committee, Fresno, CA  
 Lone Star Search and Rescue Dog  
 Association, Houston, TX  
 Loving Life Cancer Recovery, Inc.,  
 Irving, TX  
 Marantha Ministries, Hollidaysburg, PA  
 Matland Foundation, Houston, TX  
 Matthew J. Dovey Difference Education  
 Foundation, Englewood, CO  
 Mayor Lee Duggan Scholarship,  
 Sugar Land, TX  
 Mentor Program, Aurora, CO  
 Metro Foundation, Inc., San Jose, CA  
 Mikes Place, Inc., Hurst, TX  
 Mind & Spirit Counseling Center,  
 Milpitas, CA  
 Mindmender, Inc., Douglasville, GA  
 Minh Van Foundation, Houston, TX  
 Ministerio Evangelistico Revelacion,  
 Porterville, CA  
 Mission for Children Foundation, Ltd.,  
 West Sacramento, CA  
 Moomoo Productions, Inc., Theatre for a  
 New Day, Dallas, TX  
 Mooney Grove Amphitheater  
 Corporation, Hanford, CA  
 My Father's House of Erie, Erie, PA  
 Naomi's House, Inc., Dallas, TX  
 National Aids Foundation, San Diego, CA  
 Nautic Scepter, Gibraltar, MI  
 No Pro Housing, Jackson, WY  
 Noetic Center, Inc., Grand Junction, CO  
 North Texas Families for Adoption,  
 Dallas, TX  
 Nursenet Community Medical Services,  
 Inc., Dallas, TX  
 Oduduwa of Houston, Inc., Houston, TX  
 On His Way, Inc., Otis, MA  
 One Hope, Fort Worth, TX  
 Operation Hes My Brother, Memphis, TN  
 Operation Second Choice,  
 Newport Beach, CA  
 Oriki Theater, Mountain View, CA  
 Our Savior's Business, Inc.,  
 Baltimore, MD  
 Outreached Hands, Inc., Houston, TX  
 Palo Pinto Area Wildland Strike Team,  
 Santo, TX  
 Panhandle Military Veterans Awareness  
 Association, Inc., Amarillo, TX  
 Park Creek Housing, Inc.,  
 Wheat Ridge, CO  
 PBL Institute for Innovative Learning,  
 Marina, CA  
 Pebaseman Development Agency,  
 Lake Dallas, TX  
 Peoples Help Institute, Melrose, PA  
 Pet Psysc Youth Programs, Inc.,  
 Monterey, CA  
 Plasticare of Kids, Inc., Engelwood, CO  
 Playtime, Houston, TX  
 Prairie House Home Agency,  
 Plainview, TX  
 Prairie House Retirement Living,  
 Plainview, TX  
 Pre-Admission Association, Honolulu, HI  
 Pure Land Learning Center, Inc.,  
 Cupertino, CA  
 Radian Water Polo Club, Santa Cruz, CA  
 R A I N Team, Inc., Arlington, TX  
 Recycled Technology for Education  
 Foundation, Pueblo, CO  
 Renewed Life, Irving, TX  
 Resource Centers for the Insured,  
 Arvada, CO  
 Respite Services of Texas, Richmond, TX  
 Roanoke Sports Association,  
 Roanoke, TX  
 Rockwall Jazz Softball Organization,  
 Heath, TX  
 Ruach Haaretz, Inc., Carmel, CA  
 Safari Run, Anahuac, TX  
 Safe View, Inc., Houston, TX  
 Samurai Foundation, Santa Cruz, CA  
 San Juan Performing Arts Foundation,  
 Ridgway, CO  
 Santa Barbara Flash Girls Basketball,  
 Santa Barbara, CA  
 Santa Cruz Athletic Training Support  
 Program, Inc., Soquel, CA  
 Santa Cruz Sailing Foundation,  
 Santa Cruz, CA  
 Save-Our-Sign Foundation,  
 Bakersfield, CA  
 Save Our Strays SOS, Galveston, TX  
 Sereno W. & Doris L. Johnson  
 Memorial Scholarship Foundation,  
 Marco Island, FL  
 Set for Life, Inc., Portland, OR  
 Shanna Zerpoli Foundation, Clovis, CA  
 Shepherds Hand, Bayfield, CO  
 Silver Cross Ministries, Sunnyvale, CA  
 Sisters of Shangrila WA, Rosser, TX  
 Sobriety Awareness Fellowship,  
 San Jose, CA  
 Society of Iranian Boy Scouts, Inc.,  
 Houston, TX  
 Soda Creek Open Space Association, Inc.,  
 Dillon, CO  
 South Central Association for Southern  
 Reenacting & Living History, Inc.,  
 The Colony, TX  
 South Texas Youth Sports Association,  
 Katy, TX  
 Southeast Texas Canine Officers  
 Association, Inc., Spring, TX  
 Spirit at Work, Inc., Louisville, CO  
 St. Thomas More Society of Santa Clara  
 County, Santa Clara, CA  
 Star Jasmine Foundation,  
 Santa Barbara, CA  
 Summer Incentive Program Foundation,  
 Cincinnati, OH  
 Suncreek Films, Inc., Billings, MT  
 Susie Kay Ministries, Inc., Humble, TX  
 Tactical Police Foundation, Inc.,  
 Dallas, TX  
 Team Health Empowerment Endeavor,  
 Inc., Angleton, TX  
 Teclab, Inc., Houston, TX  
 Teen Intervention Prevention Services,  
 Inc., Houston, TX  
 Tehachapi Help and Hope, Tehachapi, CA  
 Texas Amateur Golfers Against Abuse,  
 Colleyville, TX  
 Texas Federation of Parents, Houston, TX  
 Texas Humanitarian Services Group,  
 Inc./Cultural Music Society,  
 Houston, TX  
 Texas Incorporated Citizens Property  
 Rights Organization, Houston, TX  
 Texas Steinway Society, Dallas, TX  
 Third Coast Historic Preservations, Inc.,  
 Friendswood, TX  
 Thomas E. Keel Ministries, Silsbee, TX  
 Thyme Square Charities, Spring, TX

Tonglen Foundation, Los Angeles, CA  
 Touch'e Manufacturing Community  
 Development Foundation, San Jose, CA  
 United Black Family, Inc., Ft. Worth, TX  
 United Faith, Houston, TX  
 University Committee of Merced  
 Foundation, Inc., Merced, CA  
 Victims of Violence, Littleton, CO  
 Villa Pines Living Center, Inc.,  
 Orlando, FL  
 Visions of Light Ministries, Houston, TX  
 Vocational Opportunities in Aquaculture  
 for Persons With Disabilities, Inc.,  
 Bay City, TX  
 Voice of an Angel Ministries, Conifer, CO  
 Volunteer Corps Community Resource  
 Center, Inc., Ventura, CA  
 Waking Spirit Foundation, Louisville, CO  
 We Can Recover, Inc., Houston, TX  
 Welcome House, Sandpoint, ID  
 Wellness Foundation, Hugo, CO  
 Wellness Institute International,  
 Phoenix, AZ  
 West Texas Old Fighter Pilots for  
 Highway Safety, Midland, TX  
 Western Hills Counseling and Family  
 Enrichment Center, Fort Worth, TX  
 Willow Creek II Swim Team,  
 Englewood, CO  
 Wilmington House Apts Resident  
 Council, Inc., Houston, TX  
 World of Challenge All Inclusive Daycare  
 Center, Houston, TX  
 WS Senior Care Foundation,  
 Bakersfield, CA  
 Youth Education Sponsors, Ventura, CA  
 Youthbuild Fort Worth, Fort Worth, TX

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

## **Deletions From Cumulative List of Organizations Contributions to Which are Deductible Under Section 170 of the Code**

### **Announcement 2005-8**

The name of an organization that no longer qualifies as an organization described in section 170(c)(2) of the Internal Revenue Code of 1986 is listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on January 24, 2005, and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is \$1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Harlem Agencies for Neighborhood  
 Development, Inc.  
 New York, NY

## **Section 7428(c) Validation of Certain Contributions Made During Pendency of Declaratory Judgment Proceedings**

### **Announcement 2005-9**

This announcement serves notice to potential donors that the organization listed below has recently filed a timely declaratory judgment suit under section 7428 of the Code, challenging revocation of its status as an eligible donee under section 170(c)(2).

Protection under section 7428(c) of the Code begins on the date that the notice of revocation is published in the Internal Revenue Bulletin and ends on the date on which a court first determines that an organization is not described in section 170(c)(2), as more particularly set forth in section 7428(c)(1).

In the case of individual contributors, the maximum amount of contributions protected during this period is limited to \$1,000.00, with a husband and wife being treated as one contributor. This protection is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for the revocation. This protection also applies (but without limitation as to amount) to organizations described in section 170(c)(2) which are exempt from tax under section 501(a). If the organization ultimately prevails in its declaratory judgment suit, deductibility of contributions would be subject to the normal limitations set forth under section 170.

Rameses School of San Antonio, Texas  
 San Antonio, TX

# 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 applies 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 laws 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 a 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.—Statement 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.

## **Numerical Finding List<sup>1</sup>**

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<sup>1</sup> A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2004–27 through 2004–52 is in Internal Revenue Bulletin 2004–52, dated December 27, 2004.



## **Finding List of Current Actions on Previously Published Items<sup>1</sup>**

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#### **2004-4**

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Rev. Proc. 2005-4, 2005-1 I.R.B. 128

#### **2004-5**

Superseded by  
Rev. Proc. 2005-5, 2005-1 I.R.B. 170

#### **2004-6**

Superseded by  
Rev. Proc. 2005-6, 2005-1 I.R.B. 200

#### **2004-7**

Superseded by  
Rev. Proc. 2005-7, 2005-1 I.R.B. 240

### **Revenue Procedures— Continued:**

#### **2004-8**

Superseded by  
Rev. Proc. 2005-8, 2005-1 I.R.B. 243

#### **2004-35**

Corrected by  
Ann. 2005-4, 2005-2 I.R.B. 319

#### **2004-60**

Superseded by  
Rev. Proc. 2005-10, 2005-3 I.R.B. 341

### **Revenue Rulings:**

#### **92-63**

Modified and superseded by  
Rev. Rul. 2005-3, 2005-3 I.R.B. 334

#### **95-63**

Modified and superseded by  
Rev. Rul. 2005-3, 2005-3 I.R.B. 334

#### **2004-103**

Superseded by  
Rev. Rul. 2005-3, 2005-3 I.R.B. 334

<sup>1</sup> A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2004-27 through 2004-52 is in Internal Revenue Bulletin 2004-52, dated December 27, 2004.