

## **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.

### **SPECIAL ANNOUNCEMENT**

#### **Announcement 2010-86, page 604.**

The Twenty-Third Annual Institute on Current Issues in International Taxation, jointly sponsored by the Internal Revenue Service and The George Washington University Law School, will be held on December 9 and 10, 2010, at the J.W. Marriott Hotel in Washington, DC.

### **INCOME TAX**

#### **Rev. Rul. 2010-25, page 571.**

**Limitations on qualified residence interest.** This ruling holds that indebtedness in excess of \$1 million that a taxpayer incurs to acquire, construct, or substantially improve a qualified residence may constitute home equity indebtedness within the meaning of section 163(h)(3)(C) of the Code.

#### **Rev. Rul. 2010-26, page 573.**

**Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate.** For purposes of sections 382, 642, 1274, 1288, and other sections of the Code, tables set forth the rates for November 2010.

#### **T.D. 9497, page 558.**

#### **REG-142800-09, page 580.**

Temporary and proposed regulations under section 108(i) of the Code provide guidance to C corporations regarding the acceleration of deferred COD income and deferred OID deductions including special rules for members of consolidated groups. In addition, these regulations provide rules applicable to all taxpayers regarding deferred OID deductions.

### **EMPLOYEE PLANS**

#### **Notice 2010-70, page 576.**

**Weighted average interest rate update; corporate bond indices; 30-year Treasury securities; segment rates.**

This notice contains updates for the corporate bond weighted average interest rate for plan years beginning in October 2010; the 24-month average segment rates; the funding transitional segment rates applicable for October 2010; and the minimum present value transitional rates for September 2010.

### **EXEMPT ORGANIZATIONS**

#### **Announcement 2010-84, page 603.**

The IRS has revoked its determinations that the American Children's Safety Source of Michigan Center; MI; Anna Foundation, Inc., of Melville, NY; California Consumer Credit of Los Angeles, CA; Consumer Counseling Centers of America of Washington, DC; The Cruffel Foundation of Jackson, WY; Interpreter Referral Service dba Chicago Area Interpreter Referral Service of Chicago, IL; Museum of Military History of Chandler, AZ; Debicated Consumer Counseling, Inc., of Centerport, NY; and United Children's Fund of Michigan Center; MI, qualify as organizations described in sections 501(c)(3) and 170(c)(2) of the Code.

(Continued on the next page)

Announcement of Declaratory Judgment Proceedings Under Section 7428 begins on page 604.  
Finding Lists begin on page ii.



## **EXCISE TAX**

### **Notice 2010–68, page 576.**

This notice maintains the current system in Alaska for fuel distribution and nontaxable use and provides that Alaska continues to remain exempt from the dyeing requirements for nontaxable use of diesel fuel and kerosene.

## **ADMINISTRATIVE**

### **Notice 2010–69, page 576.**

This notice provides interim relief to employers with respect to reporting the cost of coverage under an employer-sponsored group health plan on Form W-2, *Wage and Tax Statement*, pursuant to section 6051(a)(14) of the Code.

### **REG–138637–07, page 581.**

Proposed regulations modify the general standards of practice before the IRS and the standards with respect to tax returns.

# The IRS Mission

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

force the 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.

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

## Section 42.—Low-Income Housing Credit

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

## Section 108.—Income From Discharge of Indebtedness

26 CFR 1.108(i)-1T: *Deferred discharge of indebtedness income and deferred original issue discount deductions of C corporations (temporary).*

T.D. 9497

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

### Guidance Regarding Deferred Discharge of Indebtedness Income of Corporations and Deferred Original Issue Discount Deductions

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations under section 108(i) of the Internal Revenue Code (Code). These regulations primarily affect C corporations regarding the acceleration of deferred discharge of indebtedness (COD) income (deferred COD income) and deferred original issue discount (OID) deductions (deferred OID deductions) under section 108(i)(5)(D), and the calculation of earnings and profits as a result of an election under section 108(i). In addition, these regulations provide rules applicable to all taxpayers regarding deferred OID deductions under section 108(i) as a result of a reacquisition of an applicable debt instrument by an issuer or related party. The text of these temporary regulations also serves as the text of proposed regulations (REG-142800-09) set forth in the notice

of proposed rulemaking on this subject in this issue of the Bulletin.

**DATES: *Effective Dates:*** These regulations are effective on August 11, 2010.

***Applicability Dates:*** For dates of applicability, see §1.108(i)-0T(b).

FOR FURTHER INFORMATION CONTACT: Concerning the acceleration rules for deferred COD income and deferred OID deductions, and the rules for earnings and profits, Robert M. Rhyne (202) 622-7790; concerning the rules for deferred OID deductions, Rubin B. Ranat (202) 622-7530 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

#### Paperwork Reduction Act

These temporary regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. 553). For this reason, the collection of information contained in these regulations has been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545-2147. Responses to this collection of information are required in order for a member of a consolidated group to make the election described in §1.108(i)-1T(b)(3).

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.

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden, and suggestions for reducing this burden, please refer to the preamble to the cross-referencing notice of proposed rulemaking on this subject in this issue of the Bulletin.

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. See 26 U.S.C. 6001. Generally, tax returns

and tax return information are confidential, as required by 26 U.S.C. 6103.

#### Background

Under section 61(a)(12), a taxpayer includes in gross income any discharge of indebtedness (COD income) if the taxpayer's obligation to repay its indebtedness is discharged in whole or in part. Section 108 provides special rules for the treatment of COD income in certain cases.

Section 108(i) was added to the Code by section 1231 of the American Recovery and Reinvestment Tax Act of 2009 (Public Law 111-5, 123 Stat. 338), enacted on February 17, 2009. Section 108(i)(1) provides an election for deferral of the inclusion of COD income (deferred COD income) arising in connection with the reacquisition after December 31, 2008, and before January 1, 2011, of an applicable debt instrument. If a taxpayer makes the election, the deferred COD income generally is includible in gross income ratably over a 5-taxable-year period, beginning with the taxpayer's fourth or fifth taxable year following the taxable year of the reacquisition (inclusion period). If, as part of a reacquisition to which section 108(i)(1) applies, a debt instrument is issued (or is treated as issued) for the applicable debt instrument and there is any OID with respect to the newly issued debt instrument, then the deduction for all or a portion of the OID may be deferred (deferred OID deductions) under section 108(i)(2). (See the discussion of section 108(i)(2) later in this preamble.)

An applicable debt instrument means any debt instrument (within the meaning of section 1275(a)(1)) issued by a C corporation, or any other person in connection with the conduct of a trade or business by such a person. Section 108(i)(3). Section 108(i)(4)(A) defines a *reacquisition* as any acquisition of the debt instrument by the debtor which issued (or is otherwise the obligor under) the debt instrument, or by a person related to the debtor within the meaning of section 108(e)(4). An *acquisition* includes acquisitions for cash or other property, for another debt instrument, for corporate stock or a partnership interest, or as a contribution of the debt instrument to

capital. The term also includes the complete forgiveness of the indebtedness by the holder of the debt instrument. Section 108(i)(4)(B).

Section 108(i)(5)(D) requires a taxpayer to accelerate the inclusion of any remaining items of deferred COD income or deferred (and otherwise allowable) OID deduction (deferred items) under certain circumstances, including the death of the taxpayer, the liquidation or sale of substantially all the assets of the taxpayer (including in a title 11 or similar case), the cessation of business by the taxpayer, or similar circumstances. Section 108(i)(7) authorizes the Secretary to issue guidance necessary or appropriate for purposes of applying section 108(i), including extending the application of the rules of section 108(i)(5)(D) to other appropriate circumstances.

On August 17, 2009, the IRS and Treasury Department issued Rev. Proc. 2009-37, 2009-36 I.R.B. 309, providing procedures for taxpayers to make a section 108(i) election, and requiring the annual reporting of additional information. See §601.601(d)(2)(ii)(b). The revenue procedure also announced the intention to issue additional guidance, and that the additional guidance may be retroactive.

## Explanation of Provisions

### *I. Mandatory Acceleration Events for Deferred COD Income*

The IRS and Treasury Department believe that the deferral rules of section 108(i) generally are intended to facilitate debt workouts and to alleviate taxpayer liquidity concerns by deferring the tax liability associated with COD income. These taxpayer-favorable deferral rules are tempered, however, by section 108(i)(5)(D), which operates to accelerate the inclusion of a taxpayer's remaining deferred COD income in the case of the death of the taxpayer, the liquidation or sale of substantially all the assets of the taxpayer (including in a title 11 or similar case), the cessation of business by the taxpayer or similar circumstances (acceleration events).

A common trait of these enumerated acceleration events is that they involve situations where collection of the tax liability associated with a taxpayer's deferred

COD income may be hindered, either because the taxpayer has ceased to exist or because the taxpayer has disposed of the business to which the COD income relates. Section 108(i) poses unique concerns regarding collectability of the incipient tax liability associated with deferred COD income. In other contexts in which gain or income is deferred, the deferral is generally associated with a particular asset or its replacement. For example, gain on the sale of an asset under the installment method of accounting is deferred until payments are received under the installment obligation, or until the taxpayer disposes of the installment obligation. Collectability of the tax liability associated with the deferred gain is preserved in that context because the taxpayer has either the installment obligation or the proceeds therefrom. Section 108(i) deferral, in contrast, is not linked to a particular asset or a particular replacement asset. In the absence of acceleration events, the government's ability to ensure appropriate inclusion of the deferred COD income and the collectability of the associated tax liability would be jeopardized.

The enumerated acceleration events apply, however, to a broad range of taxpayers, including individuals and passthrough entities as well as corporations. Applied literally, the statutory rules would require acceleration in circumstances, such as certain corporate nonrecognition transactions, that do not pose particular concerns regarding collectability. For example, the statute treats a sale of substantially all the assets of the taxpayer as an acceleration event. If construed broadly, any asset disposition involving the transfer of substantially all of the assets of a corporation that made a section 108(i) election (for example, a reorganization exchange described in section 368(a)(1)(C)) would constitute an acceleration event. However, commentators noted that it did not seem consistent with the purposes of section 108(i) to require the acceleration of an electing corporation's deferred items in the case of a transaction to which section 381(a) applies. As discussed further in this preamble, the IRS and Treasury Department generally agree.

The rules provided in these temporary regulations with respect to a C corporation with deferred COD income by reason of a section 108(i) election (electing corporation) are intended to focus more pre-

cisely on the underlying purpose of section 108(i)(5)(D) to ensure that the government's ability to collect the tax liability associated with the deferred COD income is not impaired. Thus, with respect to electing corporations, the rules provided in these regulations generally reflect a narrower interpretation of the statutory acceleration events.

In addition, however, the nature of the corporate entity introduces concerns not present for other types of taxpayers. In particular, a corporation can dissipate its assets (for example, by distributions to its shareholders) without harming the economic interests of its shareholders. As a result, there may be a greater incentive for the owners of a corporation to make the corporation judgment-proof with respect to its tax liability. This is illustrated by the intermediary transactions described in Notice 2008-111, 2008-2 C.B. 1299. The IRS and Treasury Department believe that the acceleration rules should be tailored to foreclose such opportunities.

Accordingly, while these temporary regulations do not require acceleration in every instance enumerated in the statute, they provide instead for acceleration in a limited number of circumstances in which corporations have impaired their ability to pay their incipient tax liability. This approach is broadly consistent with the approach advanced by commentators who suggested, for example, that a transfer of a corporation's business assets for stock in a section 351 exchange should not be an acceleration event, despite the literal language of section 108(i)(5)(D).

Specifically, these temporary regulations generally provide that an electing corporation will accelerate deferred COD income under section 108(i)(5)(D) if the electing corporation (i) changes its tax status, (ii) ceases its corporate existence in a transaction to which section 381(a) does not apply, or (iii) engages in a transaction that impairs its ability to pay the tax liability associated with its deferred COD income (the net value acceleration rule). Under these temporary regulations, the foregoing three rules are the only events that accelerate an electing corporation's deferred COD income. In addition to these temporary regulations, however, the rules under §1.108(i)-2T apply to C corporations that are direct or indirect partners of a partnership.

The acceleration rules provided in these temporary regulations generally are different from the rules for passthrough entities. For example, a sale of substantially all of the assets of a passthrough entity is an acceleration event for an S corporation while that transaction, standing alone, is not an acceleration event for an electing corporation. The IRS and Treasury Department believe that it is appropriate to provide different acceleration rules for passthrough entities and electing corporations because the statute requires the debt instrument of a passthrough entity to be issued in connection with a trade or business. Accordingly, consistent with the trade or business requirement, it is appropriate to accelerate the deferred COD income of a passthrough entity if the entity sells substantially all of its assets.

#### *A. Net value acceleration rule*

Under the net value acceleration rule, an electing corporation generally is required to accelerate all of its remaining deferred COD income if it engages in an impairment transaction, and immediately after the transaction, the value of its assets fails to satisfy a minimum threshold (as further described herein). In general, impairment transactions are volitional transactions that reduce an electing corporation's asset base.

As provided in these regulations, impairment transactions are any transactions, however effected, that impair an electing corporation's ability to pay the amount of Federal income tax liability on its deferred COD income and include, for example, distributions (including section 381(a) transactions), redemptions, below market sales, and donations, and the incurrence of additional indebtedness without a corresponding increase in asset value. However, value-for-value sales or exchanges (including, for example, an exchange to which section 351 or section 721 applies) are not impairment transactions. The IRS and Treasury Department believe that the receipt of replacement assets in these cases adequately protects the government's interests and ensures continued collectability of any incipient tax liability. Under this rule, an electing corporation's investments and expenditures in pursuance of its good faith business judgment are not impairment transactions, merely because,

for example, acquired assets are riskier or less liquid than the electing corporation's previous assets. In addition, mere declines in the market value of an electing corporation's assets are not impairment transactions. Although the decline may impair an electing corporation's ability to pay its tax liability, a different rule would require continuous valuations and is contrary to the transactional approach taken in the statute and these regulations, and the realization requirement generally.

Under the net value acceleration rule, an electing corporation generally is required to accelerate its remaining deferred COD income if immediately after an impairment transaction, the gross value of the corporation's assets (gross asset value) is less than one hundred and ten percent of the sum of its total liabilities and the tax on the net amount of its deferred items (the net value floor). Solely for purposes of computing the net value floor, the tax on the net amount of the electing corporation's deferred items is determined by applying the highest rate of tax specified in section 11(b) for the taxable year (even though the corporation's actual tax rate for the taxable year may differ).

The net value acceleration rule has a mitigating provision that allows an electing corporation to avoid accelerated inclusion of its deferred COD income if value is restored to the corporation by the due date of the electing corporation's tax return (including extensions). In general, the amount required to be restored is the lesser of: (i) the amount of value that was removed (net of amounts previously restored under this rule) from the electing corporation in one or more impairment transactions; or (ii) the amount by which the electing corporation's net value floor exceeds its gross asset value. For example, assume an electing corporation incurs \$50 of indebtedness, distributes the \$50 of proceeds to its shareholder, and immediately after the distribution, the electing corporation's gross asset value is \$25 below the net value floor. The electing corporation may avoid application of the net value acceleration rule if, as a result of a transaction, assets with a value of \$25 are restored to the corporation before the due date of its tax return (including extensions) for the taxable year that includes the distribution. For purposes of this provision, the value that must be restored is determined at the

time of the impairment transaction, and is determined upon a net value basis (for example, additional borrowings by an electing corporation do not restore value).

The IRS and Treasury Department believe that the net value acceleration rule is an appropriate interpretation of section 108(i) because, consistent with the purpose of facilitating workouts, the rule allows electing corporations the flexibility to realign business operations through strategic acquisitions and dispositions within the objective standard of the net value floor. Although the net value acceleration rule contains a valuation component, a valuation will be required only if an electing corporation engages in an impairment transaction. Moreover, the IRS and Treasury Department believe that the net value acceleration rule is a more objective rule than requiring corporations to determine the amount of business assets that would have to be retained simply to preserve the deferral benefit of section 108(i).

#### *1. Consolidated Groups*

In the case of consolidated groups, the determination of whether an electing corporation that is a member of a consolidated group (electing member) has engaged in an impairment transaction is made on a group-wide basis. Thus, an electing member is treated as engaging in an impairment transaction if any member's transaction impairs the group's ability to pay the tax liability associated with the group's deferred COD income. See §1.1502-6. Accordingly, intercompany transactions are not impairment transactions. Similarly, the net value acceleration rule is applied by reference to the gross asset value of all members (excluding stock of members whether or not the stock is described in section 1504(a)(4)), the liabilities of all members, and the tax on all members' deferred items. For example, assume P is the common parent of the P-S consolidated group, S has a section 108(i) election in effect, and S makes a \$100 distribution to P, which, on a separate entity basis, would reduce S's gross asset value below the net value floor. S's intercompany distribution to P is not an impairment transaction. However, if P makes a \$100 distribution to its shareholder, P's distribution, subject to an exception described in section I.A.2 of this preamble, is an impairment transac-

tion, and the net value acceleration rule is applied by reference to the assets, liabilities, and deferred items of the P-S group.

Special rules are provided when an electing member that previously engaged in an impairment transaction on a separate entity basis leaves a consolidated group. If the electing member ceases to be a member of a consolidated group, the cessation is treated as an impairment transaction and the net value acceleration rule is applied on a separate entity basis (by reference to the assets, liabilities, and deferred items of the electing member only) immediately after it ceases to be a member. If the electing member's gross asset value is less than the net value floor, then the electing member's remaining deferred COD income must be taken into account immediately before the electing member ceases to be a member (unless value is restored). In the case of an electing member that becomes a member of another consolidated group, the cessation is treated as an impairment transaction and the net value acceleration rule is applied by reference to the assets, liabilities, and deferred items of the members of the acquiring group immediately after the transaction. If the gross asset value of the acquiring group is less than its net value floor, the electing member's remaining deferred COD income is taken into account immediately before the electing member ceases to be a member of the former group. If accelerated inclusion is not required, the common parent of the acquiring group succeeds to the reporting requirements of section 108(i) with respect to the electing member.

## 2. Exception for Distributions and Charitable Contributions Consistent with Historical Practice — In General

The IRS and Treasury Department believe it is appropriate to allow an electing corporation to continue to make distributions to the extent the distributions are consistent with its historical practice. Accordingly, these distributions are not treated as impairment transactions (and are not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction). For this purpose, distributions are consistent with an electing corporation's historical practice to the extent the distributions are described in section 301(c) and

the amount of these distributions, in the aggregate, for the applicable taxable year (applicable distribution amount) does not exceed the annual average amount of section 301(c) distributions over the preceding three taxable years (average distribution amount). Any excess of the applicable distribution amount over the average distribution amount is treated as an impairment transaction and is taken into account when applying the net value acceleration rule. For purposes of this rule, appropriate adjustments must be made to take into account any issuances or redemptions of stock, or similar transactions, occurring during a relevant taxable year. In addition, if the electing corporation has a short taxable year for the year of the distribution or for any of the years relied upon in computing the average distribution amount, the applicable distribution amount and the average distribution amount are determined on an annualized basis. If an electing corporation has been in existence for less than three years, the average distribution amount is computed by substituting the period during which the electing corporation has been in existence for the preceding three taxable years. The regulations also provide similar rules that exclude from impairment transaction status an electing corporation's charitable contributions (within the meaning of section 170(c)) that are consistent with its historical practice.

## 3. Special Rules for Regulated Investment Companies (RICs) and Real Estate Investment Trusts (REITs)

In the case of a RIC or REIT, any distributions with respect to stock that are treated as a dividend under section 852 or 857 are not treated as impairment transactions (and are not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction). In addition, any redemption of a redeemable security, as defined in 15 U.S.C. section 80a-2(a)(32), by a RIC in the ordinary course of business is not treated as an impairment transaction (and is not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction).

## B. Other mandatory acceleration events

### 1. Changes in Tax Status

To preserve the government's ability to collect the incipient tax liability associated with a C corporation's deferred COD income, these regulations provide that an electing corporation must take into account its remaining deferred COD income immediately before a change in its tax status. An example of such a change includes a C corporation that becomes a tax-exempt entity, or a C corporation that begins operating as a cooperative. Other changes in tax status are more fully described herein.

If a C corporation elects to be treated as an S corporation, the S corporation is subject to tax on its net recognized built-in gains during the recognition period. Section 1374(a). Although an item of income, such as deferred COD income, can constitute recognized built-in gain, recognition of the gain for any taxable year may be limited under §1.1374-2. Accordingly, if an electing corporation elects to be treated as an S corporation, the S corporation would not pay tax on its deferred COD income to the extent that the S corporation's COD income and other recognized built-in gains exceed the limitation.

The IRS and Treasury Department have determined that permanent exclusion of a corporate tax liability associated with a section 108(i) election is inconsistent with congressional intent to provide for deferral of corporate tax liability with respect to COD income. Accordingly, these temporary regulations provide that if an electing corporation elects to become an S corporation, the C corporation must take into account its deferred COD income immediately before the S corporation election is effective.

Similarly, these temporary regulations provide that an electing corporation that elects to be treated as a RIC or REIT must take into account its remaining deferred COD income immediately before the election is effective.

### 2. Cessation of Existence

Section 108(i)(5)(D) provides that in the case of the cessation of business by a taxpayer, deferred items must be taken into account in the taxable year of the cessation. Consistent with this provision, in



general, these temporary regulations provide that an electing corporation must accelerate its remaining deferred COD income in the taxable year that the corporation ceases to exist.

As noted in section I of the preamble, commentators suggested that continued deferral of an electing corporation's COD income is appropriate if the corporation ceases to exist in a reorganization or liquidation to which section 381(a) applies. The IRS and Treasury Department agree that, in these transactions, the policies that support nonrecognition for corporations also support continued deferral of COD income. In addition, an exception for these transactions affords corporations maximum flexibility in structuring transactions as asset reorganizations or stock reorganizations to meet business exigencies.

Therefore, these temporary regulations generally provide that if the assets of the electing corporation are acquired in a transaction to which section 381(a) applies (the section 381 exception), the electing corporation's deferred COD income is not accelerated. In such a case, the acquiring corporation succeeds to the electing corporation's remaining deferred COD income, and becomes subject to section 108(i), including all of its reporting requirements. However, these temporary regulations limit the applicability of the section 381 exception in certain circumstances, some of which are described herein. Moreover, a section 381(a) transaction may still constitute an impairment transaction. (See Example 3 of §1.108(i)-1T(c)).

#### a. Outbound section 381(a) transactions

If the assets of a domestic electing corporation are acquired by a foreign corporation in a transaction to which section 381(a) applies, the electing corporation's deferred COD income may not be subject to U.S. tax when it is includible in the foreign acquirer's gross income. Accordingly, to ensure that the COD income is appropriately taxed, these temporary regulations provide that the electing corporation takes into account its remaining deferred COD income immediately before the transaction.

#### b. Inbound section 381(a) transactions

As more fully described in section III, in general, deferred COD income

increases the earnings and profits of an electing corporation, including a foreign electing corporation, in the year the debt is discharged. Accordingly, if the assets of a foreign electing corporation are acquired by a domestic corporation in a transaction to which section 381(a) applies, the increase in earnings and profits is taken into account in computing the foreign corporation's all earnings and profits amount and therefore, may be subject to U.S. taxation as a deemed dividend pursuant to §1.367(b)-3(b)(3). To prevent the deferred COD income from being subject to U.S. tax a second time when the deferred COD income is includible in the domestic acquirer's gross income, these temporary regulations provide that a foreign electing corporation takes into account its remaining deferred COD income immediately before the transaction if, as a result of the transaction, one or more exchanging shareholders include in income as a deemed dividend the all earnings and profits amount with respect to stock in the foreign electing corporation pursuant to §1.367(b)-3(b)(3).

#### c. Acquisition of assets of an electing corporation by a RIC or REIT or by an S corporation

To ensure that the corporate tax liability associated with deferred COD income is appropriately preserved, these temporary regulations provide that if the assets of an electing corporation are acquired by a RIC or REIT in a transaction that is subject to §1.337(d)-7 and section 381(a) (a conversion transaction), the electing corporation takes into account its remaining deferred COD income immediately before the conversion transaction. Similarly, if the assets of an electing C corporation are acquired by an S corporation in a transaction to which sections 1374(d)(8) and section 381(a) apply, the electing C corporation takes into account its remaining deferred COD income immediately before the transaction.

#### C. Title 11 (or similar case)

Under section 108(i)(5)(D), if an electing corporation ceases to do business, liquidates or sells substantially all of its assets in a proceeding under title 11 (or a similar case), the corporation's deferred items are

taken into account the day before the petition is filed. The IRS and Treasury Department believe that the acceleration rules (outlined in section I) are sufficient to protect the collectability of tax relating to deferred COD income. Accordingly, no special acceleration rules for an electing corporation in a title 11 or similar case are provided.

## II. *Elective Acceleration for Electing Members of a Consolidated Group*

These temporary regulations provide an elective provision under which an electing member of a consolidated group (other than the common parent) may at any time accelerate in full (and not in part) the inclusion of its remaining deferred COD income with respect to all applicable debt instruments. Elective acceleration within a consolidated group is consistent with other consolidated return provisions that mitigate the double taxation of income or gain.

## III. *Earnings and Profits*

In Rev. Proc. 2009-37, the IRS and Treasury Department announced its intention to issue regulations regarding the computation of a corporation's earnings and profits in connection with an election under section 108(i). See §601.601(d)(2)(ii)(b). Consistent with the revenue procedure, these temporary regulations provide that deferred COD income generally increases earnings and profits in the taxable year that it is realized, and deferred OID deductions generally decrease earnings and profits in the taxable year or years in which the deductions would be allowed without regard to the deferral rules of section 108(i).

Although §1.312-6(a) generally states that adjustments to earnings and profits are dependent upon the method of accounting properly employed in computing taxable income (or net income, as the case may be), the IRS and Treasury Department believe this principle should not apply in the case of an electing corporation.

Section 312(n)(5) provides that in the case of any installment sale, earnings and profits shall be computed as if the corporation did not use the installment sale method. Some commentators have suggested that because the deferral of COD income under section 108(i) is analogous

to the deferral of gain from an installment sale, a rule consistent with section 312(n)(5) should apply for purposes of determining the timing of adjustments to earnings and profits with respect to deferred items under section 108(i). The IRS and Treasury Department agree that the policies underlying section 312(n) inform the treatment of deferred COD income under section 108(i).

The legislative history to section 312(n)(5) focuses on the fact that a taxpayer may realize cash or its equivalent under the installment method in the year of the sale, but is not required to take income into account until later years. *S. Rep. No. 98-169, at 198-99 (1984)*. As in the case of an installment sale, an electing corporation realizes economic income in the year of discharge. Even though the electing corporation is not required to recognize income until later years, its dividend paying capacity is enhanced immediately, not during the inclusion period, or at the time the deferred COD income may be accelerated into income.

These temporary regulations also provide certain exceptions to current year adjustments to earnings and profits. In the case of RICs and REITs, deferred COD income increases earnings and profits in the taxable year or years in which the deferred COD income is includible in gross income and not in the year that the deferred COD income is realized, and deferred OID deductions decrease earnings and profits in the taxable year or years that the deferred OID deductions are deductible. This rule is intended to ensure that a RIC or REIT has sufficient earnings and profits to claim a dividends paid deduction in the taxable year that the deferred COD income is included in taxable income. In addition, for purposes of calculating alternative minimum taxable income, deferred items increase or decrease, as the case may be, adjusted current earnings under section 56(g)(4) in the taxable year or years that the item is includible or deductible.

#### IV. Deferred OID Deductions

Section 108(i)(2) generally provides that if, as part of a reacquisition to which section 108(i)(1) applies, a debt instrument is issued (or is treated as issued under section 108(e)(4)) for the applicable debt

instrument being reacquired and there is any OID with respect to the debt instrument, no deduction otherwise allowable is allowed for the portion of the OID that accrues before the inclusion period and that does not exceed the COD income with respect to the applicable debt instrument being reacquired. The aggregate amount of deferred OID deductions is allowed ratably over the inclusion period. If the amount of OID accruing before the inclusion period exceeds the deferred COD income with respect to the applicable debt instrument being reacquired, the deductions are disallowed in the order in which the OID is accrued.

Under section 108(i)(2)(B), if a debt instrument is issued by an issuer and the proceeds of the debt instrument are used directly or indirectly by the issuer to reacquire an applicable debt instrument of the issuer, then the debt instrument is treated as issued for the applicable debt instrument being reacquired. If only a portion of the proceeds of the debt instrument are used directly or indirectly to reacquire the applicable debt instrument, then the rules in section 108(i)(2)(A) apply to the portion of any OID on the debt instrument that is equal to the portion of the proceeds used to reacquire the applicable debt instrument.

##### A. Application of §1.1502-13(g)(5)

The intercompany obligation rules of §1.1502-13(g) operate to minimize the effect on consolidated taxable income of items of income, gain, deduction, or loss arising from intercompany debt. These rules generally match the amount, timing, and character of the creditor and debtor member's items, and ensure that future items similarly correspond. Thus, for example, assume that S holds a B note with an adjusted issue price and basis of \$100 and a fair market value of \$70, and that S sells the B note to a nonmember for \$70. Under §1.1502-13(g)(3), B is deemed, immediately before the sale to X, to satisfy the note for its fair market value of \$70, resulting in \$30 of COD income for B and \$30 of loss for S (which is treated as ordinary loss under the attribute redetermination rule of §1.1502-13(c)(4)(i)). Because the debtor's COD income matches the creditor's ordinary loss, in cases where the intercompany obligation becomes a non-intercompany obligation (and in intra-

group transactions), there is no benefit to the group to elect deferral of COD income under section 108(i).

However, for those transactions in which a non-intercompany obligation becomes an intercompany obligation (as described in §1.1502-13(g)(5)), the timing and attributes of the debtor and creditor member's items from the deemed satisfaction are determined on a separate entity basis. In such cases, the elective deferral rules of section 108(i) may be beneficial. Accordingly, these temporary regulations limit the application of section 108(i) by providing that in the case of an intercompany obligation (as defined in §1.1502-13(g)(2)(ii)), the term *applicable debt instrument* includes only a debt instrument for which COD income is realized upon the debt instrument's deemed satisfaction under §1.1502-13(g)(5).

##### B. Deemed debt-for-debt exchanges

Pursuant to the regulatory authority in section 108(i)(7), the temporary regulations provide that, for purposes of section 108(i)(2) (relating to deferred OID deductions that arise in certain debt-for-debt exchanges involving the reacquisition of an applicable debt instrument), if the proceeds of any debt instrument are used directly or indirectly by the issuer or a person related to the issuer (within the meaning of section 108(i)(5)(A)) to reacquire an applicable debt instrument, the debt instrument shall be treated as issued for the applicable debt instrument being reacquired. Therefore, section 108(i)(2) may apply, for example, to a debt instrument issued by a corporation for cash in which some or all of the proceeds are used directly or indirectly by the corporation's related subsidiary in the reacquisition of the subsidiary's applicable debt instrument. The rule in the temporary regulations is intended to prevent related parties from avoiding the rules for deferred OID deductions.

##### C. Directly or indirectly

In response to comments received by the IRS and Treasury Department, the temporary regulations provide principles similar to those of §1.279-3(b) for purposes of determining when the proceeds of a debt instrument will be treated as having been used "directly or indirectly" to reacquire

an applicable debt instrument. Generally, whether the proceeds from an issuance of a debt instrument are used directly or indirectly by the issuer of the debt instrument or a person related to the issuer to reacquire an applicable debt instrument will depend upon all of the facts and circumstances surrounding the issuance and the reacquisition. The proceeds of an issuance of a debt instrument will be treated as being used indirectly to reacquire an applicable debt instrument if: (i) at the time of the issuance of the debt instrument, the issuer of the debt instrument anticipated that an applicable debt instrument of the issuer or a person related to the issuer would be reacquired by the issuer, and the debt instrument would not have been issued if the issuer had not so anticipated such reacquisition; (ii) at the time of the issuance of the debt instrument, the issuer of the debt instrument or a person related to the issuer anticipated that an applicable debt instrument would be reacquired by a related person and the related person receives cash or property that it would not have received unless the reacquisition had been so anticipated; or (iii) at the time of the reacquisition, the issuer or a person related to the issuer foresaw or reasonably should have foreseen that it would be required to issue a debt instrument, which it would not have otherwise been required to issue if the reacquisition had not occurred, in order to meet its future economic needs.

#### D. Proportional rule for accruals of OID

If a portion of the proceeds of a debt instrument with OID are used directly or indirectly to reacquire an applicable debt instrument, then the temporary regulations provide that the amount of the issuer's deferred OID deductions generally is equal to the product of the amount of OID that accrues in the taxable year under section 1272 or section 1275 (and the regulations under those sections), whichever section is applicable, and a fraction, the numerator of which is the portion of the total proceeds of the debt instrument used directly or indirectly to reacquire the applicable debt instrument and the denominator of which is the total proceeds of the debt instrument. However, if the total amount of OID that accrues before the inclusion period is greater than the total amount of deferred COD income under section 108(i), then the

OID deductions are disallowed in the order in which the OID is accrued, subject to the total amount of deferred COD income.

#### E. Acceleration events for deferred OID deductions

The temporary regulations provide rules for the acceleration of deferred OID deductions by an issuer that is a C corporation (C corporation issuer). The IRS and Treasury Department believe that it is appropriate to accelerate deferred OID deductions with respect to a debt instrument when the corresponding deferred COD income is taken into account. Accordingly, these temporary regulations provide that all or a portion of a C corporation issuer's deferred OID deductions with respect to a debt instrument are taken into account to the extent that an electing entity or its owners include all or a portion of the deferred COD income to which the C corporation issuer's deferred OID deductions relate.

These temporary regulations also include special rules to accelerate a C corporation issuer's remaining deferred OID deductions even though the deferred COD income to which it relates continues to be deferred. Under these rules, a C corporation issuer takes into account all of its remaining deferred OID deductions if the issuer (i) changes its tax status, or (ii) ceases to exist in a transaction to which section 381(a) does not apply, taking into account the application of §1.1502-34. See §1.1502-80(g).

With respect to all taxpayers with deferred OID deductions, the temporary regulations also provide that any remaining deferred OID deductions are not accelerated solely by reason of the retirement of any debt instrument subject to section 108(i)(2).

#### V. Effective/Applicability Dates

In general, the rules regarding deferred COD income and the calculation of earnings and profits apply to reacquisitions of applicable debt instruments in taxable years ending after December 31, 2008. In addition, the rules regarding deferred OID deductions generally apply to debt instruments issued after December 31, 2008 in connection with the reacquisition of an applicable debt instrument.

However, the rules with respect to the acceleration of deferred COD income and

deferred OID deductions apply prospectively to acceleration events occurring on or after August 11, 2010. Electing corporations and C corporation issuers are given the option to apply these rules to all acceleration events occurring prior to August 11, 2010, by taking a return position consistent with these provisions. In the case of a consolidated group, this option is available only if the acceleration rules are applied to all acceleration events with respect to all members of the group. In addition, certain transitional rules are provided in order to allow electing corporations the ability to use provisions in the acceleration rules that are time sensitive.

To the extent an electing corporation or C corporation issuer does not apply these acceleration rules to acceleration events occurring prior to August 11, 2010, then all deferred items are subject to the rules of section 108(i)(5)(D)(i).

#### Comments

The text of these temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in this issue of the Bulletin. Please see the "Comments and Requests for a Public Hearing" section of the notice of proposed rulemaking for the procedures to follow in submitting comments on the proposed regulations on this subject.

#### 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. For applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), refer to the Special Analyses section of the preamble to the cross-referenced notice of proposed rulemaking published in this issue of the Bulletin. Pursuant to section 7805(f) of the Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Section 108(i) applies to the reacquisition of an applicable debt instrument during the brief election period, January 1, 2009 through December 31, 2010. These temporary regulations provide necessary

guidance regarding the application of this new section 108(i) in order for corporations to timely file their tax returns. For this reason, it has been determined pursuant to 5 U.S.C. 553(b)(3)(B), that prior notice and public procedure are impracticable and contrary to the public interest. For the same reason, it has been determined pursuant to 5 U.S.C. 553(d)(3) that good cause exists for not delaying the effective date of these temporary regulations.

### Drafting Information

The principal authors of these regulations are Robert M. Rhyne and Rubin B. Ranat of the Office of Associate Chief Counsel (Corporate). Other personnel from the IRS and Treasury Department participated in their development.

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### Amendments to the Regulations

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

#### PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding the entry for §1.108(i)-0T, §1.108(i)-1T, and §1.108(i)-3T, to read, in part, as follows:

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

Section 1.108(i)-0T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Section 1.108(i)-1T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Section 1.108(i)-3T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Par. 2. Section 1.108(i)-0T is added to read as follows:

#### §1.108(i)-0T Definitions (temporary).

(a) *Definitions.* For purposes of regulations under section 108(i)—

(1) *Acquisition.* An *acquisition*, with respect to any applicable debt instrument, includes an acquisition of the debt instrument for cash or other property, the exchange of the debt instrument for another debt instrument (including an exchange resulting from a modification of the debt instrument), the exchange of the debt instrument for corporate stock or a partnership

interest, the contribution of the debt instrument to capital, the complete forgiveness of the indebtedness by the holder of the debt instrument, and a direct or an indirect acquisition within the meaning of §1.108-2;

(2) *Applicable debt instrument.* An *applicable debt instrument* is a debt instrument that was issued by a C corporation or any other person in connection with the conduct of a trade or business by such person. In the case of an intercompany obligation (as defined in §1.1502-13(g)(2)(ii)), *applicable debt instrument* includes only an instrument for which COD income is realized upon the instrument's deemed satisfaction under §1.1502-13(g)(5);

(3) *C corporation issuer.* *C corporation issuer* means a C corporation that issues a debt instrument with any deferred OID deduction;

(4) *C corporation partner.* A *C corporation partner* is a C corporation that is a direct or indirect partner of an electing partnership or a related partnership;

(5) *COD income.* *COD income* means income from the discharge of indebtedness, as determined under sections 61(a)(12) and 108(a) and the regulations under those sections;

(6) *COD income amount.* A *COD income amount* is a partner's distributive share of COD income with respect to an applicable debt instrument of an electing partnership;

(7) *Debt instrument.* *Debt instrument* means a bond, debenture, note, certificate, or any other instrument or contractual arrangement constituting indebtedness (within the meaning of section 1275(a)(1));

(8) *Deferral period.* For a reacquisition that occurs in 2009, *deferral period* means the taxable year of the reacquisition and the four taxable years following such taxable year. For a reacquisition that occurs in 2010, *deferral period* means the taxable year of the reacquisition and the three taxable years following such taxable year;

(9) *Deferred amount.* A *deferred amount* is the portion of a partner's COD income amount with respect to an applicable debt instrument that is deferred under section 108(i);

(10) *Deferred COD income.* *Deferred COD income* means COD income that is deferred under section 108(i);

(11) *Deferred item.* A *deferred item* is any item of deferred COD income or deferred OID deduction that has not been previously taken into account under section 108(i);

(12) *Deferred OID deduction.* A *deferred OID deduction* means an otherwise allowable deduction for OID that is deferred under section 108(i)(2) with respect to a debt instrument issued (or treated as issued under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in §1.108(i)-3T(a);

(13) *Deferred section 465 amount.* A *deferred section 465 amount* is described in paragraph (d)(3) of §1.108(i)-2T;

(14) *Deferred section 752 amount.* A *deferred section 752 amount* is described in paragraph (b)(3) of §1.108(i)-2T;

(15) *Direct partner.* A *direct partner* is a person that owns a direct interest in a partnership;

(16) *Electing corporation.* An *electing corporation* is a C corporation with deferred COD income by reason of a section 108(i) election;

(17) *Electing entity.* An *electing entity* is an entity that is a taxpayer that makes an election under section 108(i);

(18) *Electing member.* An *electing member* is an electing corporation that is a member of an affiliated group that files a consolidated return;

(19) *Electing partnership.* An *electing partnership* is a partnership that makes an election under section 108(i);

(20) *Electing S corporation.* An *electing S corporation* is an S corporation that makes an election under section 108(i);

(21) *Included amount.* An *included amount* is the portion of a partner's COD income amount with respect to an applicable debt instrument that is not deferred under section 108(i) and is included in the partner's distributive share of partnership income for the taxable year of the partnership in which the reacquisition occurs;

(22) *Inclusion period.* The *inclusion period* is the five taxable years following the last taxable year of the deferral period;

(23) *Indirect partner.* An *indirect partner* is a person that owns an interest in a partnership through an S corporation and/or one or more partnerships;

(24) *Issuing entity.* An *issuing entity* is any entity that is—

(i) A related partnership;  
(ii) A related S corporation;  
(iii) An electing partnership that issues a debt instrument (or is treated as issuing a debt instrument under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in §1.108(i)-3T(a); or

(iv) An electing S corporation that issues a debt instrument (or is treated as issuing a debt instrument under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in §1.108(i)-3T(a);

(25) *OID*. *OID* means original issue discount, as determined under sections 1271 through 1275 (and the regulations under those sections). If the amount of OID with respect to a debt instrument is less than a *de minimis* amount as determined under §1.1273-1(d), the OID is treated as zero for purposes of section 108(i)(2);

(26) *Reacquisition*. A *reacquisition*, with respect to any applicable debt instrument, is any event occurring after December 31, 2008 and before January 1, 2011, that causes COD income with respect to such applicable debt instrument, including any acquisition of the debt instrument by the debtor that issued (or is otherwise the obligor under) the debt instrument or a person related to such debtor (within the meaning of section 108(i)(5)(A));

(27) *Related partnership*. A *related partnership* is a partnership that is related to the electing entity (within the meaning of section 108(i)(5)(A)) and that issues a debt instrument in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in §1.108(i)-3T(a);

(28) *Related S corporation*. A *related S corporation* is an S corporation that is related to the electing entity (within the meaning of section 108(i)(5)(A)) and that issues a debt instrument in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in §1.108(i)-3T(a);

(29) *Separate interest*. A *separate interest* is a direct interest in an electing partnership or in a partnership or S corporation that is a direct or indirect partner of an electing partnership;

(30) *S corporation partner*. An *S corporation partner* is an S corporation that is a direct or indirect partner of an electing partnership or a related partnership.

(b) *Effective/Applicability dates*—(1) *In general*. This section, §1.108(i)-2T, and, except as provided in paragraph (b)(2) of this section, §1.108(i)-1T apply to reacquisitions of applicable debt instruments in taxable years ending after December 31, 2008. In addition, §1.108(i)-3T applies to debt instruments issued after December 31, 2008, in connection with reacquisitions of applicable debt instruments in taxable years ending after December 31, 2008.

(2) *Acceleration events*—(i) *In general*. Section 1.108(i)-1T(b) (acceleration rules) generally applies to acceleration events occurring on or after August 11, 2010. However, an electing corporation or C corporation issuer may apply the acceleration rules to all acceleration events occurring prior to August 11, 2010, by taking a return position consistent with these provisions beginning with the first acceleration event occurring prior to August 11, 2010. Also, in the case of a consolidated group, if the common parent of the consolidated group applies the acceleration rules on behalf of one member of the consolidated group, then the common parent must apply the acceleration rules to all acceleration events with respect to all members of the group. If the electing corporation, common parent (under the preceding sentence), or C corporation issuer, as the case may be, does not apply the acceleration rules to all acceleration events occurring prior to August 11, 2010, then it is, with respect to all deferred items, subject to the rules of section 108(i)(5)(D)(i).

(3) *Transitional rules*—(i) *Net value acceleration rule and corrective action to restore net value rule*. If an electing corporation applies the acceleration rules of §1.108(i)-1T(b) to all acceleration events occurring prior to August 11, 2010, and the due date of its tax return (including extensions) for the taxable year of the mandatory acceleration event occurs prior to August 11, 2010, then for purposes of the net value acceleration rule described in §1.108(i)-1T(b)(2)(iii), an electing corporation may restore value by the fifteenth day of the ninth month following August 11, 2010.

(ii) *Elective acceleration*. If an electing member cannot timely file an election under §1.108(i)-1T(b)(3) to accelerate its remaining deferred COD income by the due date of the electing member's tax return (including extensions) which occurs prior to August 11, 2010, then an amended return must be filed with the required information statement by the fifteenth day of the ninth month following August 11, 2010.

Par. 3. Section 1.108(i)-1T is added to read as follows:

*§1.108(i)-1T Deferred discharge of indebtedness income and deferred original issue discount deductions of C corporations (temporary)*.

(a) *Overview*. Section 108(i)(1) provides an election for the deferral of COD income arising in connection with the reacquisition of an applicable debt instrument. An electing corporation generally includes deferred COD income ratably over the inclusion period. Paragraph (b) of this section provides rules for the mandatory acceleration of an electing corporation's remaining deferred COD income, the mandatory acceleration of a C corporation issuer's deferred OID deductions, and for the elective acceleration of an electing member's (other than the common parent's) remaining deferred COD income. Paragraph (c) of this section provides examples illustrating the application of the mandatory and elective acceleration rules. Paragraph (d) of this section provides rules for the computation of an electing corporation's earnings and profits. Paragraph (e) of this section refers to the effective/applicability dates.

(b) *Acceleration events*—(1) *Deferred COD income*. Except as otherwise provided in paragraphs (b)(2) and (3) of this section, and §1.108(i)-2T(b)(6) (in the case of a corporate partner), an electing corporation's deferred COD income is taken into account ratably over the inclusion period.

(2) *Mandatory acceleration events*. An electing corporation takes into account all of its remaining deferred COD income, including its share of an electing partnership's deferred COD income, immediately before the occurrence of any one of the events described in this paragraph (b)(2) (mandatory acceleration events).

(i) *Changes in tax status.* The electing corporation changes its tax status. For purposes of the preceding sentence, an electing corporation is treated as changing its tax status if it becomes one of the following entities:

(A) A tax-exempt entity as defined in §1.337(d)-4(c)(2).

(B) An S corporation as defined in section 1361(a)(1).

(C) A qualified subchapter S subsidiary as defined in section 1361(b)(3)(B).

(D) An entity operating on a cooperative basis within the meaning of section 1381.

(E) A regulated investment company (RIC) as defined in section 851 or a real estate investment trust (REIT) as defined in section 856.

(F) A qualified REIT subsidiary as defined in section 856(i), but only if the qualified REIT subsidiary was not a REIT immediately before it became a qualified REIT subsidiary.

(ii) *Cessation of corporate existence—(A) In general.* The electing corporation ceases to exist for Federal income tax purposes.

(B) *Exception for section 381(a) transactions—(1) In general.* The electing corporation is not treated as ceasing to exist and is not required to take into account its remaining deferred COD income solely because its assets are acquired in a transaction to which section 381(a) applies. In such a case, the acquiring corporation succeeds to the electing corporation's remaining deferred COD income and becomes subject to section 108(i) and the regulations thereunder, including all reporting requirements, as if the acquiring corporation were the electing corporation. A transaction is not treated as one to which section 381(a) applies for purposes of this paragraph (b)(2)(ii)(B) in any one of the following circumstances:

(i) The acquisition of the assets of an electing corporation by an S corporation, if the acquisition is described in section 1374(d)(8).

(ii) The acquisition of the assets of an electing corporation by a RIC or REIT, if the acquisition is described in §1.337(d)-7(a)(2)(ii).

(iii) The acquisition of the assets of a domestic electing corporation by a foreign corporation.

(iv) The acquisition of the assets of a foreign electing corporation by a domestic corporation, if as a result of the transaction, one or more exchanging shareholders include in income as a deemed dividend the all earnings and profits amount with respect to stock in the foreign electing corporation pursuant to §1.367(b)-3(b)(3).

(v) The acquisition of the assets of an electing corporation by a tax-exempt entity as defined in §1.337(d)-4(c)(2).

(vi) The acquisition of the assets of an electing corporation by an entity operating on a cooperative basis within the meaning of section 1381.

(2) *Special rules for consolidated groups—(i) Liquidations.* For purposes of paragraph (b)(2)(ii)(B) of this section, the acquisition of assets by distributee members of a consolidated group upon the liquidation of an electing corporation is not treated as a transaction to which section 381(a) applies, unless immediately prior to the liquidation, one of the distributee members owns stock in the electing corporation meeting the requirements of section 1504(a)(2) (without regard to §1.1502-34). See §1.1502-80(g).

(ii) *Taxable years.* In the case of an intercompany transaction to which section 381(a) applies, the transaction does not cause the transferor or distributor to have a short taxable year for purposes of determining the taxable year of the deferral and inclusion period.

(iii) *Net value acceleration rule—(A) In general.* The electing corporation engages in an impairment transaction and, immediately after the transaction, the gross value of the electing corporation's assets (gross asset value) is less than one hundred and ten percent of the sum of its total liabilities and the tax on the net amount of its deferred items (the net value floor) (the net value acceleration rule). Impairment transactions are any transactions, however effected, that impair an electing corporation's ability to pay the amount of Federal income tax liability on its deferred COD income and include, for example, distributions (including section 381(a) transactions), redemptions, below-market sales, charitable contributions, and the incurrence of additional indebtedness without a corresponding increase in asset value. Value-for-value sales or exchanges (for example, an exchange to which section 351 or section 721 applies), or mere

declines in the market value of the electing corporation's assets are not impairment transactions. In addition, an electing corporation's investments and expenditures in pursuance of its good faith business judgment are not impairment transactions. For purposes of determining an electing corporation's gross asset value, the amount of any distribution that is not treated as an impairment transaction under paragraph (b)(2)(iii)(D) of this section (distributions and charitable contributions consistent with historical practice) or under paragraph (b)(2)(iii)(E) of this section (special rules for RICs and REITs) is treated as an asset of the electing corporation. Solely for purposes of computing the amount of the net value floor, the tax on the deferred items is determined by applying the highest rate of tax specified in section 11(b) for the taxable year.

(B) *Transactions integrated.* Any transaction that occurs before the reacquisition of an applicable debt instrument, but that occurs pursuant to the same plan as the reacquisition, is taken into account in determining whether the gross asset value of the electing corporation is less than the net value floor.

(C) *Corrective action to restore net value.* An electing corporation is not required to take into account its deferred COD income under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section if, before the due date of the electing corporation's return (including extensions), value is restored in a transaction in an amount equal to the lesser of—

(1) The amount of value that was removed from the electing corporation in one or more impairment transactions (net of amounts previously restored under this paragraph (b)(2)(iii)(C)); or

(2) The amount by which the electing corporation's net value floor exceeds its gross asset value. For purposes of this paragraph (b)(2)(iii)(C), for example, assume an electing corporation incurs \$50 of debt, distributes the \$50 of proceeds to its shareholder, and immediately after the distribution, the electing corporation's gross asset value is below the net value floor by \$25. The electing corporation may avoid the inclusion of its remaining deferred COD income if value of at least \$25 is restored to it before the due date of the electing corporation's tax return (including extensions) for the taxable year

that includes the distribution. The value that must be restored is determined at the time of the impairment transaction on a net value basis (for example, additional borrowings by an electing corporation do not restore value).

(D) *Exceptions for distributions and charitable contributions that are consistent with historical practice.* An electing corporation's distributions are not treated as impairment transactions (and are not taken into account as a reduction of the electing corporation's gross asset value when applying the net value acceleration rule to any impairment transaction), to the extent that the distributions are described in section 301(c) and the amount of these distributions, in the aggregate, for the applicable taxable year (applicable distribution amount) does not exceed the annual average amount of section 301(c) distributions over the preceding three taxable years (average distribution amount). If an electing corporation's applicable distribution amount exceeds its average distribution amount (excess amount), then the amount of the impairment transaction equals the excess amount. Appropriate adjustments must be made to take into account any issuances or redemptions of stock, or similar transactions, occurring during the year of distribution or any of the three preceding years. If the electing corporation has a short taxable year for the year of the distribution or for any of the three preceding years, the amounts are determined on an annualized basis. If an electing corporation has been in existence for less than three years, the period during which the electing corporation has been in existence is substituted for the preceding three taxable years. For purposes of determining an electing corporation's average distribution amount, the electing corporation does not take into account the distribution history of a distributor or transferor in a transaction to which section 381(a) applies (other than a transaction described in section 368(a)(1)(F)). Rules similar to those prescribed in this paragraph (b)(2)(iii)(D) also apply to an electing corporation's charitable contributions (within the meaning of section 170(c)) that are consistent with its historical practice.

(E) *Special rules for RICs and REITs—(1) Distributions.* Notwithstanding paragraph (b)(2)(iii)(D)

of this section, in the case of a RIC or REIT, any distribution with respect to stock that is treated as a dividend under section 852 or 857 is not treated as an impairment transaction (and is not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction).

(2) *Redemptions by RICs.* Any redemption of a redeemable security, as defined in 15 U.S.C. section 80a-2(a)(32), by a RIC in the ordinary course of business is not treated as an impairment transaction (and is not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction).

(F) *Special rules for consolidated groups—(1) Impairment transactions and net value acceleration rule.* In the case of an electing member, the determination of whether the member has engaged in an impairment transaction is made on a group-wide basis. An electing member is treated as engaging in an impairment transaction if any member's transaction impairs the group's ability to pay the tax liability associated with all electing members' deferred COD income. Accordingly, intercompany transactions are not impairment transactions. Similarly, the net value acceleration rule is applied by reference to the gross asset value of all members (excluding stock of members whether or not described in section 1504(a)(4)), the liabilities of all members, and the tax on all members' deferred items. For example, assume P is the common parent of the P-S consolidated group, S has a section 108(i) election in effect, and S makes a \$100 distribution to P which, on a separate entity basis, would reduce S's gross asset value below the net value floor. S's intercompany distribution to P is not an impairment transaction. However, if P makes a \$100 distribution to its shareholder, P's distribution is an impairment transaction (unless the distribution is consistent with its historical practice under paragraph (b)(2)(iii)(D) of this section), and the net value acceleration rule is applied by reference to the assets, liabilities, and deferred items of the P-S group.

(2) *Departing member.* If an electing member that previously engaged in one or more impairment transactions on a separate entity basis ceases to be a member of

a consolidated group (departing member), the cessation is treated as an impairment transaction and the net value acceleration rule under paragraph (b)(2)(iii)(A) of this section is applied to the departing member on a separate entity basis immediately after ceasing to be a member (and taking into account the impairment transaction(s) that occurred on a separate entity basis). If the departing member's gross asset value is below the net value floor, the departing member's remaining deferred COD income is taken into account immediately before the departing member ceases to be a member (unless value is restored under paragraph (b)(2)(iii)(C) of this section). If the departing member's deferred COD income is not accelerated, the departing member is subject to the reporting requirements of section 108(i) on a separate entity basis. If the departing member becomes a member of another consolidated group, the cessation is treated as an impairment transaction and the net value acceleration rule under paragraph (b)(2)(iii)(A) of this section is applied by reference to the assets, liabilities, and the tax on deferred items of the members of the acquiring group immediately after the transaction. If the acquiring group's gross asset value is below the net value floor, the departing member's remaining deferred COD income is taken into account immediately before the departing member ceases to be a member (unless value is restored under paragraph (b)(2)(iii)(C) of this section). If the departing member's remaining deferred COD income is not accelerated, the common parent of the acquiring group succeeds to the reporting requirements of section 108(i) with respect to the departing member.

(3) *Elective acceleration for certain consolidated group members—(i) In general.* An electing member (other than the common parent) of a consolidated group may elect at any time to accelerate in full (and not in part) the inclusion of its remaining deferred COD income with respect to all applicable debt instruments by filing a statement described in paragraph (b)(3)(ii) of this section. Once made, an election to accelerate deferred COD income under this paragraph (b)(3) is irrevocable.

(ii) *Time and manner for making election—(A) In general.* The election to accelerate the inclusion of an electing member's remaining deferred COD income with respect to all applicable debt in-

struments is made on a statement attached to a timely filed tax return (including extensions) for the year in which the deferred COD income is taken into account. The election is made by the common parent on behalf of the electing member. See §1.1502-77(a).

(B) *Additional information.* The statement must include—

(1) *Label.* A label entitled “SECTION 1.108(i)-1T ELECTION AND INFORMATION STATEMENT BY [INSERT NAME AND EMPLOYER IDENTIFICATION NUMBER OF THE ELECTING MEMBER]”; and

(2) *Required information.* An identification of each applicable debt instrument to which an election under this paragraph (b)(3) applies and the corresponding amount of—

(i) Deferred COD income that is accelerated under this paragraph (b)(3); and

(ii) Deferred OID deductions that are accelerated under paragraph (b)(4) of this section.

(4) *Deferred OID deductions—(i) In general.* Except as otherwise provided in paragraph (b)(4)(ii) of this section and §1.108(i)-2T(b)(6) (in the case of a C corporation partner), a C corporation issuer’s deferred OID deductions are taken into account ratably over the inclusion period.

(ii) *OID acceleration events.* A C corporation issuer takes into account all of its remaining deferred OID deductions with respect to a debt instrument immediately before the occurrence of any one of the events described in this paragraph (b)(4)(ii).

(A) *Inclusion of deferred COD income.* An electing entity or its owners take into account all of the remaining deferred COD income to which the C corporation issuer’s deferred OID deductions relate. If, under §1.108(i)-2T(b) or (c), an electing entity or its owners take into account only a portion of the deferred COD income to which the deferred OID deductions relate, then the C corporation issuer takes into account a proportionate amount of the remaining deferred OID deductions.

(B) *Changes in tax status.* The C corporation issuer changes its tax status within the meaning of paragraph (b)(2)(i) of this section.

(C) *Cessation of corporate existence—(1) In general.* The C corporation

issuer ceases to exist for Federal income tax purposes.

(2) *Exception for section 381(a) transactions—(i) In general.* A C corporation issuer is not treated as ceasing to exist and does not take into account its remaining deferred OID deductions in a transaction to which section 381(a) applies, taking into account the application of §1.1502-34, as appropriate. See §1.1502-80(g). This exception does not apply to a transaction which is not treated as one to which section 381(a) applies under paragraph (b)(2)(iii)(B)(I) of this section.

(ii) *Taxable years.* In the case of an intercompany transaction to which section 381(a) applies, the transaction does not cause the transferor or distributor to have a short taxable year for purposes of determining the taxable year of the deferral and inclusion period.

(c) *Examples.* The application of this section is illustrated by the following examples. Unless otherwise stated, P, S, S1, and X are domestic C corporations, and each files a separate return on a calendar year basis:

*Example 1. Net value acceleration rule. (i) Facts.* On January 1, 2009, S reacquires its own note and realizes \$400 of COD income. Pursuant to an election under section 108(i), S defers recognition of the entire \$400 of COD income. Therefore, absent a mandatory acceleration event, S will take into account \$80 of its deferred COD income in each year of the inclusion period. On December 31, 2010, S makes a \$25 distribution to its sole shareholder, P, and this is the only distribution made by S in the past four years. Immediately following the distribution, S’s gross asset value is \$100, S has no liabilities, and the Federal income tax on S’s \$400 of deferred COD income is \$140. Accordingly, S’s net value floor is \$154 (110% x \$140).

(ii) *Analysis.* Under paragraph (b)(2)(iii)(A) of this section, S’s distribution is an impairment transaction. Immediately following the distribution, S’s gross asset value of \$100 is less than the net value floor of \$154. Accordingly, under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section, S takes into account its \$400 of deferred COD income immediately before the distribution.

(iii) *Corrective action to restore value.* The facts are the same as in paragraph (i) of this *Example 1*, except that P contributes assets with a value of \$25 to S before the due date of S’s 2010 return (including extensions). Because P restores \$25 of value to S (the lesser of the amount of value removed in the distribution (\$25) or the amount by which S’s net value floor exceeds its gross asset value (\$54)), under paragraph (b)(2)(iii)(C) of this section, S does not take into account its \$400 of deferred COD income.

*Example 2. Distributions consistent with historical practice. (i) Facts.* P, a publicly traded corporation, makes a valid section 108(i) election with respect to COD income realized in 2009. On December 31, 2009, P distributes \$25 million on

its 5 million shares of common stock outstanding. As of January 1, 2006, P has 10 million shares of common stock outstanding, and on March 31, 2006, P distributes \$10 million on those 10 million shares. On September 15, 2006, P effects a 2:1 reverse stock split, and on December 31, 2006, P distributes \$10 million on its 5 million shares of common stock outstanding. In each of 2007 and 2008, P distributes \$5 million on its 5 million shares of common stock outstanding. All of the distributions are described in section 301(c).

(ii) *Amount of impairment transaction.* Under paragraph (b)(2)(iii)(D) of this section, P’s 2009 distributions are not treated as impairment transactions (and are not taken into account as a reduction of P’s gross asset value when applying the net value acceleration rule to any impairment transaction), to the extent that the aggregate amount distributed in 2009 (the applicable distribution amount) does not exceed the annual average amount of distributions (the average distribution amount) over the preceding three taxable years. Accordingly, P’s applicable distribution amount for 2009 is \$25 million, and its average distribution amount is \$10 million (\$20 million (2006) plus \$5 million (2007) plus \$5 million (2008) divided by 3). The reverse stock split in 2006 is not a transaction requiring an adjustment to the determination of the average distribution amount. Because P’s applicable distribution amount of \$25 million exceeds its average distribution amount of \$10 million, under paragraph (b)(2)(iii)(D) of this section, the amount of P’s 2009 distribution that is treated as an impairment transaction is \$15 million. The balance of the 2009 distribution, \$10 million, is not treated as an impairment transaction (and is not taken into account as a reduction in P’s gross asset value when applying the net value acceleration rule to any impairment transaction).

(iii) *Distribution history.* The facts are the same as in paragraph (i) of this *Example 2*, except that in 2010, P merges into X in a transaction to which section 381(a) applies, with X succeeding to P’s deferred COD income, and X makes a distribution to its shareholders. For purposes of determining whether X’s distribution is consistent with its historical practice, the average distribution amount is determined solely with respect to X’s distribution history.

*Example 3. Cessation of corporate existence. (i) Transaction to which section 381(a) applies.* P owns all of the stock of S. In 2009, S reacquires its own note and elects to defer recognition of its \$400 of COD income under section 108(i). On December 31, 2010, S liquidates into P in a transaction that qualifies under section 332. Under paragraph (b)(2) of this section, S must take into account all of its remaining deferred COD income upon the occurrence of any one of the mandatory acceleration events. Although S ceases its corporate existence as a result of the liquidation, S is not required to take into account its remaining deferred COD income under the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. However, under paragraph (b)(2)(iii)(A) of this section, S’s distribution to P is an impairment transaction and the net value acceleration rule is applied with respect to the assets, liabilities, and deferred items of P (S’s successor) immediately following the distribution. If S’s deferred COD income is not taken into account under the net value acceleration rule of



(b)(2)(iii) of this section, P succeeds to S's remaining deferred COD income and to S's reporting requirements as if P were the electing corporation.

(ii) *Debt-laden distributee*. The facts are the same as in paragraph (i) of this *Example 3*, except that in the liquidation, S distributes \$100 of assets to P, a holding company whose only asset is its stock in S. Assume that immediately following the distribution, P's gross asset value is \$100, P has \$60 of liabilities, and the Federal income tax on the \$400 of deferred COD income is \$140. Under paragraph (b)(2) of this section, S must take into account all of its remaining deferred COD income upon the occurrence of any one of the mandatory acceleration events. Although S ceases its corporate existence as a result of the liquidation, S is not required to take into account its remaining deferred COD income under the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. However, under paragraph (b)(2)(iii)(A) of this section, S's distribution to X is an impairment transaction and the net value acceleration rule is applied with respect to the assets, liabilities, and deferred items of P (S's successor). Immediately following the distribution, P's gross asset value of \$100 is less than the net value floor of \$220 [ $110\% \times (\$60 + \$140)$ ]. Accordingly, under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section, S is required to take into account its \$400 of deferred COD income immediately before the distribution, unless value is restored to P pursuant to (b)(2)(iii)(C) of this section.

(iii) *Foreign acquirer*. The facts are the same as in paragraph (i) of this *Example 3*, except that P is a foreign corporation. Although S's assets are acquired in a transaction to which section 381(a) applies, under paragraph (b)(2)(ii)(B)(J)(iii) of this section, the exception to accelerated inclusion does not apply and S takes into account its remaining deferred COD income immediately before the liquidation. See also section 367(e)(2) and the regulations thereunder.

(iv) *Section 338 transaction*. P, the common parent of a consolidated group (P group), owns all the stock of S1, one of the members of the P group. In 2009, S1 reacquires its own indebtedness and realizes \$30 of COD income. Pursuant to an election under section 108(i), S1 defers recognition of the entire \$30 of COD income. In 2010, P sells all the stock of S1 to X, an unrelated corporation, for \$300, and P and X make a timely section 338(h)(10) election with respect to the sale. Under paragraph (b)(2)(ii)(A) of this section, an electing corporation takes into account its remaining deferred COD income when it ceases its existence for Federal income tax purposes unless the exception in paragraph (b)(2)(ii)(B) of this section applies. Pursuant to section 338(h)(10) and the regulations, S1 is treated as transferring all of its assets to an unrelated person in exchange for consideration that includes the discharge of its liabilities. This deemed value-for-value exchange is not an impairment transaction. Following the deemed sale, while S1 is still a member of the P group, S1 is treated as distributing all of its assets to P and as ceasing its existence. Under these facts, the distribution of all of S1's assets constitutes a deemed liquidation, and is a transaction to which sections 332 and 381(a) apply. Although S1 ceases its corporate existence as a result of the liquidation, S1 is not required to take into account its remaining deferred COD income under

the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. P succeeds to S1's remaining deferred COD income and to S1's reporting requirements as if P were the electing corporation. Under paragraph (b)(2)(iii)(F)(I) of this section, the intercompany distribution from S1 to P is not an impairment transaction.

(d) *Earnings and profits*—(1) *In general*. Deferred COD income increases earnings and profits in the taxable year that it is realized and not in the taxable year or years that the deferred COD income is includible in gross income. Deferred OID deductions decrease earnings and profits in the taxable year or years in which the deduction would be allowed without regard to section 108(i).

(2) *Exceptions*—(i) *RICs and REITs*. Notwithstanding paragraph (d)(1) of this section, deferred COD income increases earnings and profits of a RIC or REIT in the taxable year or years in which the deferred COD income is includible in gross income and not in the year that the deferred COD income is realized. Deferred OID deductions decrease earnings and profits of a RIC or REIT in the taxable year or years that the deferred OID deductions are deductible.

(ii) *Alternative minimum tax*. For purposes of calculating alternative minimum taxable income, any items of deferred COD income or deferred OID deduction increase or decrease, respectively, adjusted current earnings under section 56(g)(4) in the taxable year or years that the item is includible or deductible.

(e) *Effective/applicability dates*. For *effective/applicability dates*, see §1.108(i)-0T(b).

(f) *Expiration date*. This section expires August 9, 2013.

Par. 4. Section 1.108(i)-3T is added to read as follows:

*§1.108(i)-3T Rules for the deduction of OID (temporary).*

(a) *Deemed debt-for-debt exchanges*—(1) *In general*. For purposes of section 108(i)(2) (relating to deferred OID deductions that arise in certain debt-for-debt exchanges involving the reacquisition of an applicable debt instrument), if the proceeds of any debt instrument are used directly or indirectly by the issuer or a person related to the issuer (within the meaning of section

108(i)(5)(A)) to reacquire an applicable debt instrument, the debt instrument shall be treated as issued for the applicable debt instrument being reacquired. Therefore, section 108(i)(2) may apply, for example, to a debt instrument issued by a corporation for cash in which some or all of the proceeds are used directly or indirectly by the corporation's related subsidiary in the reacquisition of the subsidiary's applicable debt instrument.

(2) *Directly or indirectly*. Whether the proceeds of an issuance of a debt instrument are used directly or indirectly to reacquire an applicable debt instrument depends upon all of the facts and circumstances surrounding the issuance and the reacquisition. The proceeds of an issuance of a debt instrument will be treated as being used indirectly to reacquire an applicable debt instrument if—

(i) At the time of the issuance of the debt instrument, the issuer of the debt instrument anticipated that an applicable debt instrument of the issuer or a person related to the issuer would be reacquired by the issuer, and the debt instrument would not have been issued if the issuer had not so anticipated such reacquisition;

(ii) At the time of the issuance of the debt instrument, the issuer of the debt instrument or a person related to the issuer anticipated that an applicable debt instrument would be reacquired by a related person and the related person receives cash or property that it would not have received unless the reacquisition had been so anticipated; or

(iii) At the time of the reacquisition, the issuer or a person related to the issuer foresaw or reasonably should have foreseen that the issuer or a person related to the issuer would be required to issue a debt instrument, which it would not have otherwise been required to issue if the reacquisition had not occurred, in order to meet its future economic needs.

(b) *Proportional rule for accruals of OID*. For purposes of section 108(i)(2), if only a portion of the proceeds from the issuance of a debt instrument are used directly or indirectly to reacquire an applicable debt instrument, the rules of section 108(i)(2)(A) will apply to the portion of OID on the debt instrument that is equal to the portion of the proceeds from such instrument used to reacquire the outstanding applicable debt instrument. Except

as provided in the last sentence of section 108(i)(2)(A), the amount of deferred OID deduction that is subject to section 108(i)(2)(A) for a taxable year is equal to the product of the amount of OID that accrues in the taxable year under section 1272 or section 1275 (and the regulations under those sections), whichever section is applicable, and a fraction, the numerator of which is the portion of the total proceeds from the issuance of the debt instrument used directly or indirectly to reacquire the applicable debt instrument and the denominator of which is the total proceeds from the issuance of the debt instrument.

(c) *No acceleration*—(1) *Retirement*. Retirement of a debt instrument subject to section 108(i)(2) does not accelerate deferred OID deductions.

(2) *Cross-reference*. See §1.108(i)-1T and §1.108(i)-2T for rules relating to the acceleration of deferred OID deductions.

(d) *Examples*. The application of this section is illustrated by the following examples. Unless otherwise stated, all taxpayers in the following examples are calendar-year taxpayers, and P and S each file separate returns:

*Example 1.* (i) *Facts*. P, a domestic corporation, owns all of the stock of S, a domestic corporation. S has a debt instrument outstanding that has an adjusted issue price of \$100,000. On January 1, 2010, P issues for \$160,000 a four-year debt instrument that has an issue price of \$160,000 and a stated redemption price at maturity of \$200,000, resulting in \$40,000 of OID. In P's discussion with potential lenders/holders, and as described in offering materials provided to potential lenders/holders, P disclosed that it planned to use all or a portion of the proceeds from the issuance of the debt instrument to reacquire outstanding debt of P and its affiliates. Following the issuance, P makes a \$70,000 capital contribution to S. S then reacquires its debt instrument from X, a person not related to S within the meaning of section

108(i)(5)(A), for \$70,000. At the time of the reacquisition, the adjusted issue price of S's debt instrument is \$100,000. Under §1.61-12(c), S realizes \$30,000 of COD income. S makes a section 108(i) election for the \$30,000 of COD income.

(ii) *Analysis*. Under the facts, at the time of P's issuance of its \$160,000 debt instrument, P anticipated that the loan proceeds would be used to reacquire the debt of S, and P's debt instrument would not have been issued for an amount greater than \$90,000 if P had not anticipated that S would use the proceeds to reacquire its debt. Pursuant to paragraph (a) of this section, the proceeds from P's issuance of its debt instrument are treated as being used indirectly to reacquire S's applicable debt instrument. Therefore, section 108(i)(2)(B) applies to P's debt instrument and P's OID deductions on its debt instrument are subject to deferral under section 108(i)(2)(A). However, because only a portion of the proceeds from P's debt instrument are used by S to reacquire its applicable debt instrument, only a portion of P's total OID deductions will be deferred under section 108(i)(2)(A). See section 108(i)(2)(B). Accordingly, a maximum of \$17,500 (\$40,000 x \$70,000/\$160,000) of P's \$40,000 total OID deductions is subject to deferral under section 108(i)(2)(A). Under paragraph (b) of this section, the amount of P's deferred OID deduction each taxable year under section 108(i)(2)(A) is equal to the product of the amount of OID that accrues in the taxable year under section 1272 for the debt instrument and a fraction (\$70,000/\$160,000). As a result, P's deferred OID deductions are the following amounts: \$4,015.99 for 2010 (\$ 9,179.40 x \$70,000/\$160,000); \$4,246.39 for 2011 (\$9,706.04 x \$70,000/\$160,000); \$4,490.01 for 2012 (\$10,262.88 x \$70,000/\$160,000); and \$4,747.61 for 2013 (\$10,851.68 x \$70,000/\$160,000).

*Example 2.* (i) *Facts*. The facts are the same as in *Example 1*, except that S makes a section 108(i) election for only \$10,000 of the \$30,000 of COD income.

(ii) *Analysis*. The maximum amount of P's deferred OID deductions under section 108(i)(2)(A) is \$10,000 rather than \$17,500 because S made a section 108(i) election for only \$10,000 of the \$30,000 of COD income. Under section 108(i)(2)(A), because the amount of OID that accrues prior to 2014 attributable to the portion of the debt instrument issued to indirectly reacquire S's applicable debt instrument under paragraph (b) of this section (\$17,500) exceeds

the amount of deferred COD income under section 108(i) (\$10,000), P's deferred OID deductions are the following amounts: \$4,015.99 for 2010; \$4,246.39 for 2011; \$1,737.62 for 2012; and \$0 for 2013.

*Example 3.* (i) *Facts*. The facts are the same as in *Example 1*, except that P pays \$200,000 in cash to the lenders/holders on December 31, 2012, to retire the debt instrument. P did not directly or indirectly obtain the funds to retire the debt instrument from the issuance of another debt instrument with OID.

(ii) *Analysis*. Under paragraph (c)(1) of this section, the retirement of P's debt instrument is not an acceleration event for the deferred OID deductions of \$4,015.99 for 2010, \$4,246.39 for 2011, and \$4,490.01 for 2012. Except as provided in §1.108(i)-1T(b)(4), these amounts will be taken into account during the inclusion period. P, however, paid a repurchase premium of \$10,851.68 in 2012 (\$200,000 minus the adjusted issue price of \$189,148.32) to retire the debt instrument. If otherwise allowable, P may deduct this amount in 2012 under §1.163-7(c).

(e) *Effective/applicability dates*. For *effective/applicability dates*, see §1.108(i)-0T(b).

(f) *Expiration date*. This section expires August 9, 2013.

Part 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 5. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805

Par. 6. In §602.101, paragraph (b) is amended by adding the following 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.
* * * * * 1.108(i)-1T * * * * *	1545-2147

\* \* \* \* \*  
Steven T. Miller,  
Deputy Commissioner for  
Services and Enforcement.

Michael Mundaca,  
Assistant Secretary of  
the Treasury (Tax Policy).

**Section 163.—Interest.**

**Limitations on qualified residence interest.** This ruling holds that indebtedness in excess of \$1 million that a taxpayer incurs to acquire, construct, or substantially improve a qualified residence may constitute home equity indebtedness within the

(Filed by the Office of the Federal Register on August 11, 2010, 11:15 a.m., and published in the issue of the Federal Register for August 13, 2010, 75 F.R.)

Approved August 6, 2010.

meaning of section 163(h)(3)(C) of the Code.

## Rev. Rul. 2010-25

### ISSUE

Whether indebtedness that is incurred by a taxpayer to acquire, construct, or substantially improve a qualified residence can constitute “home equity indebtedness” (within the meaning of § 163(h)(3)(C) of the Internal Revenue Code) to the extent it exceeds \$1 million.

### FACTS

In 2009, an unmarried individual (Taxpayer) purchased a principal residence for its fair market value of \$1,500,000. Taxpayer paid \$300,000 and financed the remainder by borrowing \$1,200,000 through a loan that is secured by the residence. In 2009, Taxpayer paid interest that accrued on the indebtedness during that year. Taxpayer has no other debt secured by the residence.

### LAW

Section 163(a) allows as a deduction all interest paid or accrued within the taxable year on indebtedness. However, for individuals § 163(h)(1) disallows a deduction for personal interest. Under § 163(h)(2)(D), qualified residence interest is not personal interest. Section 163(h)(3)(A) defines qualified residence interest as interest paid or accrued during the taxable year on acquisition indebtedness or home equity indebtedness secured by any qualified residence of the taxpayer. Under § 163(h)(4)(A), “qualified residence” means a taxpayer’s principal residence, within the meaning of § 121, and one other residence selected and used by the taxpayer as a residence.

Section 163(h)(3)(B)(i) provides that acquisition indebtedness is any indebtedness that is incurred in acquiring, constructing, or substantially improving a qualified residence and is secured by the residence. However, § 163(h)(3)(B)(ii) limits the amount of indebtedness treated as acquisition indebtedness to \$1,000,000 (\$500,000 for a married individual filing separately). Accordingly, any indebtedness described in § 163(h)(3)(B)(i) in excess of \$1,000,000 is, by definition, not

acquisition indebtedness for purposes of § 163(h)(3).

Section 163(h)(3)(C)(i) provides that home equity indebtedness is any indebtedness secured by a qualified residence other than acquisition indebtedness, to the extent the fair market value of the qualified residence exceeds the amount of acquisition indebtedness on the residence. However, § 163(h)(3)(C)(ii) limits the amount of indebtedness treated as home equity indebtedness to \$100,000 (\$50,000 for a married individual filing separately). Accordingly, any indebtedness described in § 163(h)(3)(C)(i) in excess of \$100,000 is, by definition, not home equity indebtedness for purposes of § 163(h)(3).

In *Pau v. Commissioner*, T.C. Memo. 1997-43, the Tax Court limited the taxpayers’ deduction for qualified residence interest to the interest paid on \$1 million of the \$1.33 million indebtedness incurred to purchase their residence. The court stated that § 163(h) restricts home mortgage interest deductions to interest paid on \$1 million of acquisition indebtedness and \$100,000 of home equity indebtedness. Citing § 163(h)(3)(B), the court stated that acquisition indebtedness is defined as indebtedness that is incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer, and is secured by the residence. Citing § 163(h)(3)(C), the court further stated that home equity indebtedness is defined as any indebtedness (other than acquisition indebtedness) secured by a qualified residence. The court concluded that the taxpayers failed to demonstrate that any of their debt was not incurred in acquiring, constructing, or substantially improving their residence and thus was not acquisition indebtedness. However, the court did not address the effect of the \$1 million limitation in § 163(h)(3)(B)(ii) on the definition of acquisition indebtedness for purposes of § 163(h)(3). The Tax Court followed *Pau* in *Catalano v. Commissioner*, T.C. Memo. 2000-82.

### ANALYSIS

Taxpayer may deduct, as interest on acquisition indebtedness under § 163(h)(3)(B), interest paid in 2009 on \$1,000,000 of the \$1,200,000 indebtedness used to acquire the principal residence. The \$1,200,000 indebtedness was

incurred in acquiring a qualified residence of Taxpayer and was secured by the residence. Thus, indebtedness of \$1,000,000 is treated as acquisition indebtedness under § 163(h)(3)(B).

Taxpayer also may deduct, as interest on home equity indebtedness under § 163(h)(3)(C), interest paid in 2009 on \$100,000 of the remaining indebtedness of \$200,000. The \$200,000 is secured by the qualified residence, is not acquisition indebtedness under § 163(h)(3)(B), and does not exceed the fair market value of the residence reduced by the acquisition indebtedness secured by the residence. Thus, \$100,000 of the \$200,000 is treated as home equity indebtedness under § 163(h)(3)(C).

Under § 163(h)(3)(A), the interest on both acquisition indebtedness and home equity indebtedness is qualified residence interest. Therefore, for 2009 Taxpayer may deduct interest paid on indebtedness of \$1,100,000 as qualified residence interest. Any interest Taxpayer paid on the remaining indebtedness of \$100,000 is nondeductible personal interest under § 163(h).

The Internal Revenue Service will not follow the decisions in *Pau v. Commissioner* and *Catalano v. Commissioner*. The holding in *Pau* was based on the incorrect assertion that taxpayers must demonstrate that debt treated as home equity indebtedness “was not incurred in acquiring, constructing or substantially improving their residence.” The definition of home equity indebtedness in § 163(h)(3)(C) contains no such restrictions, and accordingly the Service will determine home equity indebtedness consistent with the provisions of this revenue ruling, notwithstanding the decisions in *Pau* and *Catalano*.

### HOLDING

Indebtedness incurred by a taxpayer to acquire, construct, or substantially improve a qualified residence can constitute home equity indebtedness to the extent it exceeds \$1 million (subject to the applicable dollar and fair market value limitations imposed on home equity indebtedness by § 163(h)(3)(C)).

### DRAFTING INFORMATION

The principal author of this revenue ruling is Sharon Hall of the Office of Asso-

ciate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue ruling, contact Ms. Hall at (202) 622-4950 (not a toll-free call).

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## Section 280G.—Golden Parachute Payments

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted applicable federal long-term rate is set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 412.—Minimum Funding Standards

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 467.—Certain Payments for the Use of Property or Services

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month

of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 482.—Allocation of Income and Deductions Among Taxpayers

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 483.—Interest on Certain Deferred Payments

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 642.—Special Rules for Credits and Deductions

Federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 807.—Rules for Certain Reserves

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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## Section 846.—Discounted Unpaid Losses Defined

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

## Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 42, 280G, 382, 412, 467, 468, 482, 483, 642, 807, 846, 1288, 7520, 7872.)

**Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate.** For purposes of sections 382, 642, 1274, 1288, and other sections of the Code, tables set forth the rates for November 2010.

## Rev. Rul. 2010-26

This revenue ruling provides various prescribed rates for federal income tax purposes for November 2010 (the current month). Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section 1288(b). Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropriate percentages for determining the low-income housing credit described in section 42(b)(1) for buildings placed in service during the current month. However, under section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, and before December 31, 2013, shall not be less than 9%. Finally, Table 5 contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 2010-26 TABLE 1  
Applicable Federal Rates (AFR) for November 2010

	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
<i>Short-term</i>				
AFR	.35%	.35%	.35%	.35%
110% AFR	.39%	.39%	.39%	.39%
120% AFR	.42%	.42%	.42%	.42%
130% AFR	.46%	.46%	.46%	.46%
<i>Mid-term</i>				
AFR	1.59%	1.58%	1.58%	1.57%
110% AFR	1.75%	1.74%	1.74%	1.73%
120% AFR	1.91%	1.90%	1.90%	1.89%
130% AFR	2.06%	2.05%	2.04%	2.04%
150% AFR	2.38%	2.37%	2.36%	2.36%
175% AFR	2.79%	2.77%	2.76%	2.75%
<i>Long-term</i>				
AFR	3.35%	3.32%	3.31%	3.30%
110% AFR	3.68%	3.65%	3.63%	3.62%
120% AFR	4.02%	3.98%	3.96%	3.95%
130% AFR	4.37%	4.32%	4.30%	4.28%

REV. RUL. 2010-26 TABLE 2  
Adjusted AFR for November 2010

	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
Short-term adjusted AFR	.49%	.49%	.49%	.49%
Mid-term adjusted AFR	1.53%	1.52%	1.52%	1.52%
Long-term adjusted AFR	3.54%	3.51%	3.49%	3.48%

REV. RUL. 2010-26 TABLE 3  
Rates Under Section 382 for November 2010

Adjusted federal long-term rate for the current month	3.54%
Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.)	3.86%

REV. RUL. 2010-26 TABLE 4

Appropriate Percentages Under Section 42(b)(1) for November 2010

Note: Under Section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, and before December 31, 2013, shall not be less than 9%.

Appropriate percentage for the 70% present value low-income housing credit	7.57%
Appropriate percentage for the 30% present value low-income housing credit	3.24%

REV. RUL. 2010-26 TABLE 5

Rate Under Section 7520 for November 2010

Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest	2.0%
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**Section 1288.—Treatment of Original Issue Discount on Tax-Exempt Obligations**

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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**Section 7520.—Valuation Tables**

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

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**Section 7872.—Treatment of Loans With Below-Market Interest Rates**

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2010. See Rev. Rul. 2010-26, page 573.

## Part III. Administrative, Procedural, and Miscellaneous

### Dyed Diesel Fuel and Kerosene: Nontaxable Use; Alaska

#### Notice 2010-68

This notice provides that undyed diesel fuel and undyed kerosene (undyed fuel) may continue to be removed, entered, and sold for nontaxable uses in the entire state of Alaska under the existing procedures in § 48.4082-5 of the Manufacturers and Retailers Excise Tax Regulations. These regulations generally allow tax-free removals of diesel fuel from approved terminals and tax-free sales of undyed fuel between registered dealers and between registered dealers and nontaxable users.

This notice clarifies that recent changes in Environmental Protection Agency (EPA) rules relating to Alaskan diesel fuel do not affect existing Internal Revenue Service (IRS) procedures relating to undyed fuel transactions in Alaska. Section 48.4082-5(b) provides that these existing IRS procedures apply only to areas of Alaska in which the sulfur content requirements for diesel fuel (see § 211(i) of the Clean Air Act, 42 U.S.C. 7545(i)) do not apply because the Administrator of the EPA has granted an exemption under § 211(i)(4) of that Act.

When § 48.4082-5 was issued in 1996, the entire state of Alaska was exempt from both EPA's sulfur content requirement and its requirement for dyeing high sulfur diesel fuel and kerosene. The EPA is now phasing out Alaska's exemption from the EPA sulfur content requirement but has retained its rule that exempts Alaska from the EPA fuel dyeing requirement.

Because § 4082(c) of the Internal Revenue Code provides an exemption from the dyeing requirements of § 4082(a)(2) of the Code for areas that are exempt from the EPA fuel dyeing requirement, diesel fuel and kerosene in Alaska will continue to be exempt from the dyeing requirements of the Internal Revenue Code. In addition, the current system of fuel distribution and nontaxable use in Alaska will remain in effect until the Administrator of the EPA eliminates part or all of Alaska's exemption from the dyeing requirements of the Clean Air Act. The IRS expects to amend

§ 48.4082-5(b) to reflect the provisions of this notice.

Taxpayers are reminded that the \$0.001 per gallon tax for the Leaking Underground Storage Tank Trust Fund financing rate generally applies to sales of undyed fuel for nontaxable uses including off-highway and heating oil uses.

The principal author of this notice is Charles J. Langley, Jr. of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice, contact Charles J. Langley, Jr. at (202) 622-3130 (not a toll-free call).

### Interim Relief with Respect to Form W-2 Reporting of the Cost of Coverage of Group Health Insurance Under § 6051(a)(14)

#### Notice 2010-69

This notice provides interim relief to employers with respect to reporting the cost of coverage under an employer-sponsored group health plan on Form W-2, *Wage and Tax Statement*, pursuant to § 6051(a)(14) of the Code. Specifically, this notice provides that reporting the cost of such coverage will not be mandatory for 2011 Forms W-2. The Treasury Department and the IRS have determined that this relief is appropriate to provide employers with additional time to make any necessary changes to their payroll systems or procedures in preparation for compliance with the reporting requirement.

#### BACKGROUND

Section 6051(a)(14) was added to the Code by § 9002 of the Patient Protection and Affordable Care Act of 2010, Public Law 111-148, enacted March 23, 2010. Section 6051(a)(14) provides generally that the aggregate cost of applicable employer-sponsored coverage (as defined in § 4980I(d)(1)) must be reported on Form W-2. Section 6051(a)(14) further provides that, for this purpose, the aggregate cost is to be determined under rules similar to the rules of § 4980B(f)(4), referring to the

definition of the "applicable premium" under the rules providing for COBRA continuation coverage. Section 6051(a)(14) is effective for taxable years beginning on or after January 1, 2011.

#### INTERIM RELIEF

Pursuant to this notice, the reporting requirement set forth in § 6051(a)(14) is not mandatory for 2011 Forms W-2. Accordingly, an employer will not be treated as failing to meet the requirements of § 6051 for 2011, and will not be subject to any penalties for failure to meet such requirements, merely because it does not report the aggregate cost of employer-sponsored coverage (as defined in § 4980I(d)(1)) on 2011 Forms W-2. The Treasury Department and the IRS anticipate issuing guidance on the reporting requirement set forth in § 6051(a)(14) before the end of this year.

#### DRAFTING INFORMATION

The principal author of this notice is Leslie Paul of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities) though other Treasury Department and IRS officials participated in its development. For further information on the provisions of this notice, contact Leslie Paul at (202) 622-6080 (not a toll-free number).

### Update for Weighted Average Interest Rates, Yield Curves, and Segment Rates

#### Notice 2010-70

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 as in effect for plan years beginning before 2008. It also provides guidance on the corporate bond monthly yield curve (and the corresponding spot segment rates), the 24-month average segment rates, and the funding transitional segment rates under § 430(h)(2). In addition, this notice provides guidance as to the interest

rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning before 2008, the 30-year Treasury weighted average rate under § 431(c)(6)(E)(ii)(I), and the minimum present value segment rates under § 417(e)(3)(D) as in effect for plan years beginning after 2007.

#### 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 and by the Pension Protection Act of 2006 (PPA), provide that the interest rates used to cal-

culate current liability and to determine the required contribution under § 412(l) for plan years beginning in 2004 through 2007 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, 2004-1 C.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 methodology for determining the monthly composite corporate bond rate as set forth in Notice 2004-34 continues to apply in determining that rate. See Notice 2006-75, 2006-2 C.B. 366.

The composite corporate bond rate for September 2010 is 5.17 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.

For Plan Years Beginning in		Corporate Bond Weighted Average	Permissible Range		
<i>Month</i>	<i>Year</i>		90%	to	100%
October	2010	6.21	5.59		6.21

#### YIELD CURVE AND SEGMENT RATES

Generally for plan years beginning after 2007 (except for delayed effective dates for certain plans under sections 104, 105, and 106 of PPA), § 430 of the Code specifies the minimum funding requirements that apply to single employer plans pursuant to § 412. Section 430(h)(2) specifies the interest rates that must be used to determine a plan's target normal cost and funding target. Under this provision, present value is generally determined using three 24-month average interest rates

("segment rates"), each of which applies to cash flows during specified periods. However, an election may be made under § 430(h)(2)(D)(ii) to use the monthly yield curve in place of the segment rates. For plan years beginning in 2008 and 2009, a transitional rule under § 430(h)(2)(G) provides that the segment rates are blended with the corporate bond weighted average as specified above. An election may be made under § 430(h)(2)(G)(iv) to use the segment rates without applying the transitional rule.

Notice 2007-81, 2007-2 C.B. 899, provides guidelines for determining the

monthly corporate bond yield curve, the 24-month average corporate bond segment rates, and the funding transitional segment rates used to compute the target normal cost and the funding target. Pursuant to Notice 2007-81, the monthly corporate bond yield curve derived from September 2010 data is in Table I at the end of this notice. The spot first, second, and third segment rates for the month of September 2010 are, respectively, 1.74, 4.75, and 6.03. The three 24-month average corporate bond segment rates applicable for October 2010 under the election of § 430(h)(2)(G)(iv) are as follows:

First Segment	Second Segment	Third Segment
3.61	6.20	6.53

The transitional segment rates under § 430(h)(2)(G) applicable for October 2010, taking into account the corporate bond

weighted average of 6.21 stated above, are as follows:

For Plan Years Beginning in	First Segment	Second Segment	Third Segment
2009	4.48	6.20	6.42

The transitional rule of § 430(h)(2)(G) does not apply to plan years starting in

2010. Therefore, for a plan year starting in 2010 with a lookback month to Octo-

ber 2010, the funding segment rates are the three 24-month average corporate bond



segment rates applicable for October 2010, listed above without blending for the transitional period.

### 30-YEAR TREASURY SECURITIES INTEREST RATES

Section 417(e)(3)(A)(ii)(II) (prior to amendment by PPA) 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 rate of interest 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.

The rate of interest on 30-year Treasury securities for September 2010 is 3.77 percent. The Service has determined this rate as the average of the daily determinations of yield on the 30-year Treasury bond maturing in August 2040.

Generally for plan years beginning after 2007, § 431 specifies the minimum funding requirements that apply to multiemployer plans pursuant to § 412.

Section 431(c)(6)(B) specifies a minimum amount for the full-funding limitation described in section 431(c)(6)(A), based on the plan's current liability. Section 431(c)(6)(E)(ii)(I) provides that the interest rate used to calculate current liability for this purpose must be no more than 5 percent above and no more than 10 percent below the weighted average of the rates of interest on 30-year Treasury securities during the four-year period ending on the last day before the beginning of the plan year. Notice 88-73, 1988-2 C.B. 383, provides guidelines for determining the weighted average interest rate. The following rates were determined for plan years beginning in the month shown below.

For Plan Years Beginning in		30-Year Treasury Weighted Average	Permissible Range		
<i>Month</i>	<i>Year</i>		90%	to	105%
October	2010	4.28	3.85		4.49

### MINIMUM PRESENT VALUE SEGMENT RATES

Generally for plan years beginning after December 31, 2007, the applicable interest rates under § 417(e)(3)(D) are segment rates computed without regard

to a 24-month average. For plan years beginning in 2008 through 2011, the applicable interest rates are the monthly spot segment rates blended with the applicable rate under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning in 2007. Notice 2007-81 provides guidelines for

determining the minimum present value segment rates. Pursuant to that notice, the minimum present value transitional segment rates determined for September 2010, taking into account the September 2010 30-year Treasury rate of 3.77 stated above, are as follows:

For Plan Years Beginning in	First Segment	Second Segment	Third Segment
2009	2.96	4.16	4.67
2010	2.55	4.36	5.13
2011	2.15	4.55	5.58

### DRAFTING INFORMATION

The principal author of this notice is Tony Montanaro of the Employee Plans,

Tax Exempt and Government Entities Division. Mr. Montanaro may be e-mailed at [RetirementPlanQuestions@irs.gov](mailto:RetirementPlanQuestions@irs.gov).

**Table I**

Monthly Yield Curve for September 2010  
 Derived from September 2010 Data

<i>Maturity</i>	<i>Yield</i>	<i>Maturity</i>	<i>Yield</i>	<i>Maturity</i>	<i>Yield</i>	<i>Maturity</i>	<i>Yield</i>	<i>Maturity</i>	<i>Yield</i>
0.5	0.73	20.5	5.59	40.5	6.09	60.5	6.26	80.5	6.34
1.0	0.88	21.0	5.61	41.0	6.09	61.0	6.26	81.0	6.34
1.5	1.06	21.5	5.63	41.5	6.10	61.5	6.26	81.5	6.34
2.0	1.28	22.0	5.66	42.0	6.10	62.0	6.26	82.0	6.35
2.5	1.54	22.5	5.68	42.5	6.11	62.5	6.27	82.5	6.35
3.0	1.82	23.0	5.70	43.0	6.12	63.0	6.27	83.0	6.35
3.5	2.11	23.5	5.71	43.5	6.12	63.5	6.27	83.5	6.35
4.0	2.40	24.0	5.73	44.0	6.13	64.0	6.27	84.0	6.35
4.5	2.66	24.5	5.75	44.5	6.13	64.5	6.28	84.5	6.35
5.0	2.91	25.0	5.77	45.0	6.14	65.0	6.28	85.0	6.36
5.5	3.14	25.5	5.78	45.5	6.14	65.5	6.28	85.5	6.36
6.0	3.35	26.0	5.80	46.0	6.15	66.0	6.28	86.0	6.36
6.5	3.55	26.5	5.81	46.5	6.15	66.5	6.29	86.5	6.36
7.0	3.72	27.0	5.83	47.0	6.16	67.0	6.29	87.0	6.36
7.5	3.88	27.5	5.84	47.5	6.16	67.5	6.29	87.5	6.36
8.0	4.03	28.0	5.86	48.0	6.17	68.0	6.29	88.0	6.36
8.5	4.16	28.5	5.87	48.5	6.17	68.5	6.30	88.5	6.36
9.0	4.29	29.0	5.88	49.0	6.17	69.0	6.30	89.0	6.37
9.5	4.40	29.5	5.89	49.5	6.18	69.5	6.30	89.5	6.37
10.0	4.51	30.0	5.91	50.0	6.18	70.0	6.30	90.0	6.37
10.5	4.60	30.5	5.92	50.5	6.19	70.5	6.30	90.5	6.37
11.0	4.70	31.0	5.93	51.0	6.19	71.0	6.31	91.0	6.37
11.5	4.78	31.5	5.94	51.5	6.20	71.5	6.31	91.5	6.37
12.0	4.86	32.0	5.95	52.0	6.20	72.0	6.31	92.0	6.37
12.5	4.93	32.5	5.96	52.5	6.20	72.5	6.31	92.5	6.38
13.0	4.99	33.0	5.97	53.0	6.21	73.0	6.31	93.0	6.38
13.5	5.05	33.5	5.98	53.5	6.21	73.5	6.32	93.5	6.38
14.0	5.11	34.0	5.99	54.0	6.21	74.0	6.32	94.0	6.38
14.5	5.16	34.5	6.00	54.5	6.22	74.5	6.32	94.5	6.38
15.0	5.21	35.0	6.00	55.0	6.22	75.0	6.32	95.0	6.38
15.5	5.26	35.5	6.01	55.5	6.22	75.5	6.32	95.5	6.38
16.0	5.30	36.0	6.02	56.0	6.23	76.0	6.33	96.0	6.38
16.5	5.34	36.5	6.03	56.5	6.23	76.5	6.33	96.5	6.38
17.0	5.38	37.0	6.04	57.0	6.23	77.0	6.33	97.0	6.39
17.5	5.41	37.5	6.04	57.5	6.24	77.5	6.33	97.5	6.39
18.0	5.45	38.0	6.05	58.0	6.24	78.0	6.33	98.0	6.39
18.5	5.48	38.5	6.06	58.5	6.24	78.5	6.33	98.5	6.39
19.0	5.51	39.0	6.07	59.0	6.25	79.0	6.34	99.0	6.39
19.5	5.53	39.5	6.07	59.5	6.25	79.5	6.34	99.5	6.39
20.0	5.56	40.0	6.08	60.0	6.25	80.0	6.34	100.0	6.39

## Part IV. Items of General Interest

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

### Guidance Regarding Deferred Discharge of Indebtedness Income of Corporations and Deferred Original Issue Discount Deductions

#### REG-142800-09

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 and the Treasury Department are issuing temporary regulations (T.D. 9497) under section 108(i) of the Internal Revenue Code (Code). These regulations primarily affect C corporations regarding the acceleration of deferred discharge of indebtedness (COD) income (deferred COD income) and deferred original issue discount (OID) deductions (deferred OID deductions) under section 108(i)(5)(D), and the calculation of earnings and profits as a result of an election under section 108(i). In addition, these regulations provide rules applicable to all taxpayers regarding deferred OID deductions under section 108(i) as a result of a reacquisition of an applicable debt instrument by an issuer or related party. The text of the temporary regulations also serves as the text of these proposed regulations.

DATES: Written or electronic comments and request for a public hearing must be received by November 12, 2010.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-142800-09), 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-142800-09),

Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-142800-09).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Robert M. Rhyne (202) 622-7790 and Rubin B. Ranat (202) 622-7530; concerning submissions of comments and/or requests for a public hearing, Richard Hurst (202) 622-7180 (not toll-free numbers), or [Richard.a.hurst@irs.counsel.treas.gov](mailto:Richard.a.hurst@irs.counsel.treas.gov).

#### 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 in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507) under control number 1545-2147. 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 November 12, 2010. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the functions of the Internal Revenue Service, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection 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 collections 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 of operation, maintenance, and purchase of service to provide information.

The collection of information in this proposed regulation is in §1.108(i)-1(b)(3). This information is required by the IRS to allow members of a consolidated group to make an election to accelerate the inclusion of deferred COD income under section 108(i). The likely recordkeepers are corporations filing consolidated income tax returns (electing members). The IRS and Treasury Department believe that an electing member's election under §1.108(i)-1(b)(3) reduces the member's overall reporting burden under section 108(i).

Estimated total annual reporting burden: 0 hours.

Estimated average annual burden per respondent: 0 hours.

Estimated number of respondents: 5,000.

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 26 U.S.C. 6103.

##### Background and Explanation of Provisions

The temporary regulations published in this issue of the Bulletin amend the Income Tax Regulations (26 CFR parts 1 and 602) relating to section 108(i). The temporary regulations set forth rules for applying section 108(i) to C corporations. The text of those temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

## 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. This certification is based upon the fact that these regulations merely provide more specific guidance for the timing of the inclusion of deferred COD income that is otherwise includible under the Code. 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, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

## Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. In addition to the specific requests for comments made elsewhere in this preamble or the preamble to the temporary regulations, the IRS and Treasury Department request comments on the clarity of the proposed rules and how they can 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 who timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place of the hearing will be published in the **Federal Register**.

## Drafting Information

The principal authors of these proposed regulations are Robert M. Rhyne and Ruben B. Ranat of the Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and Treasury Department participated in their development.

\* \* \* \* \*

## Proposed Amendment 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 is amended by adding entries in numerical order to read as follows:

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

Section 1.108(i)-0T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Section 1.108(i)-1T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Section 1.108(i)-3T also issued under 26 U.S.C. 108(i)(7) and 1502. \* \* \*

Par. 2. Section 1.108(i)-0 is added to read as follows:

#### *§1.108(i)-0 Definitions.*

[The text of proposed §1.108(i)-0 is the same as the text of §1.108(i)-0T published elsewhere in this issue of the Bulletin].

Par. 3. Section 1.108(i)-1 is added to read as follows:

#### *§1.108(i)-1 Deferred discharge of indebtedness income and deferred original issue discount deductions of C corporations.*

[The text of proposed §1.108(i)-1 is the same as the text of §1.108(i)-1T published elsewhere in this issue of the Bulletin].

Par. 4. Section 1.108(i)-3 is added to read as follows:

#### *§1.108(i)-3 Rules for the deduction of OID.*

[The text of proposed §1.108(i)-3 is the same as the text of §1.108(i)-3T published elsewhere in this issue of the Bulletin].

Steven T. Miller,  
*Deputy Commissioner for  
Services and Enforcement.*

(Filed by the Office of the Federal Register on August 11, 2010, 11:15 p.m., and published in the issue of the Federal Register for August 13, 2010, 75 F.R.)

## Notice of Proposed Rulemaking

### Regulations Governing Practice Before the Internal Revenue Service

#### REG-138637-07

AGENCY: Office of the Secretary, Treasury.

ACTION: Withdrawal of notice of proposed rulemaking, notice of proposed rulemaking, and notice of public hearing.

SUMMARY: This document contains proposed modifications revising the regulations governing practice before the Internal Revenue Service (IRS). The proposed regulations affect individuals who practice before the IRS and providers of continuing education programs. The proposed regulations modify the general standards of practice before the IRS and the standards with respect to tax returns. This document also provides notice of a public hearing on these proposed regulations and withdraws the notice of proposed rulemaking published on September 26, 2007.

DATES: Written or electronic comments must be received by Thursday, October 7, 2010. Outlines of topics to be discussed at the public hearing scheduled for Friday, October 8, 2010 at 10 am must be received by Monday, September 27, 2010. ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-138637-07), room 5205, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, D.C. 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-138637-07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, D.C., or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-138637-07). The public hearing will be held in IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, D.C.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed

regulations, Matthew D. Lucey or Matthew S. Cooper at (202) 622-4940; concerning submissions of comments, the public hearing, and/or to be placed on the building access list to attend the public hearing, Regina Johnson 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 these proposed regulations was previously 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 1545-1726. 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, D.C. 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, D.C. 20224. Comments on the collection of information should be received by October 22, 2010. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the Internal Revenue Service, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proper collection of information;

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

How the burden of complying with the proposed collection 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 §§10.6 and 10.9. The total annual burden of this collection of information is an increase from the burden in the current regulations.

Section 10.6 requires a registered tax return preparer to maintain records and educational materials regarding the completion of the required qualifying continuing education credits. Section 10.9 also requires providers of qualifying continuing education programs to maintain records and educational material concerning these programs and the individuals who attend them. Continuing education providers also obtain approval of each program as a qualified continuing education program. The collection of this material helps to ensure that individuals authorized to prepare tax returns are informed of the latest developments in Federal tax practice.

Currently, there are approximately 46,000 enrolled agents and 300 enrolled retirement plan agents who are required to maintain records and educational materials regarding the completion of the required continuing education credits. There are approximately 350 continuing education providers of qualifying continuing education programs required to maintain records and educational material concerning these programs and the individuals who attend them. It is expected that there will be an additional 600,000 registered tax return preparers and 1,900 continuing education providers who will be affected by the collection of information requirements in these proposed regulations. The IRS and the Treasury Department estimate that the total annual costs resulting from these requirements will be \$9,880,000 for all affected practitioners and \$38,632,500 for all affected continuing education providers.

This collection of information is mandatory. The likely respondents and record keepers are individuals and businesses.

Estimated total annual recordkeeping and reporting burden is 1,710,000 hours.

Estimated annual burden per practitioner varies from 30 minutes to one hour, depending on individual circumstances, with an estimated average of 54 minutes.

Estimated annual burden per continuing education provider varies from five hours to 5,000 hours, depending on individual circumstances, with an estimated average of 500 hours.

Estimated number of affected practitioners is 650,000.

Estimated number of affected continuing education providers is 2,250.

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.

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.

##### **Background**

Section 330 of title 31 of the United States Code authorizes the Secretary of the Treasury (the Secretary) to regulate the practice of representatives before the Treasury Department. The Secretary is authorized, after notice and an opportunity for a proceeding, to censure, suspend, or disbar from practice before the Treasury Department those representatives who are incompetent, disreputable, or who violate regulations prescribed under section 330 of title 31. The Secretary also is authorized to impose a monetary penalty against these individuals and the individuals' firms or other entities that employ them. Additionally, the Secretary may seek an injunction against these individuals under section 7408 of the Internal Revenue Code (Code).

The Secretary has published regulations governing the practice of representatives before the IRS in 31 CFR part 10 and reprinted the regulations as Treasury Department Circular No. 230 (Circular 230). These regulations authorize the Director of the Office of Professional Responsibility (OPR) to act upon applications for enrollment to practice before the IRS, to make inquiries with respect to matters under OPR's jurisdiction, to institute proceedings to impose a monetary penalty or to censure, suspend, or disbar a practitioner from practice before the IRS, to institute proceedings to disqualify appraisers, and to perform other duties necessary to carry out these functions.

Circular 230 has been amended periodically. The regulations were amended most recently on September 26, 2007 (T.D. 9359, 2007-2 C.B. 931 [72 FR 54540]), to modify various provisions relating to the general standards of practice. For example, the 2007 regulations established an enrolled retirement plan agent designation, modified the conflict of interest rules, lim-

ited the use of contingent fees by practitioners, and required public disclosure of OPR disciplinary decisions after the decisions become final.

Those final regulations, however, did not finalize the standards with respect to tax returns under §10.34(a) and the definitions under §10.34(e) because of the amendments to section 6694(a) of the Code made by the Small Business and Work Opportunity Tax Act of 2007, Public Law 110-28, 121 Stat. 190. Rather, the IRS and the Treasury Department reserved §10.34(a) and (e) in those final regulations and also simultaneously issued a notice of proposed rulemaking (REG-138637-07, 2007-2 C.B. 977) in the Federal Register (72 FR 54621) proposing to conform the professional standards under §10.34 of Circular 230 with the civil penalty standards under section 6694(a) as amended by the 2007 Act.

On October 3, 2008, the Tax Extenders and Alternative Minimum Tax Relief Act of 2008, Div. C. of Public Law 110-343, 122 Stat. 3765, again amended the standard of conduct that must be met to avoid imposition of the tax return preparer penalty under section 6694(a). The IRS and the Treasury Department published final regulations (T.D. 9436, 2009-3 I.R.B. 268) in the Federal Register (73 FR 78430) implementing amendments to the tax return preparer penalties on December 22, 2008. This document proposes modifications to the standards with respect to tax returns and also withdraws the proposed amendments to §10.34 published in the Federal Register on September 26, 2007.

The proposed regulations also provide new rules governing the oversight of tax return preparers. Currently, an individual tax return preparer generally is not subject to the provisions in Circular 230 unless the tax return preparer is an attorney, certified public accountant, enrolled agent, or other type of practitioner identified in Circular 230. Under current law, any individual may prepare tax returns and claims for refund without meeting any qualifications or competency standards. A tax return preparer also may exercise the privilege of limited practice before the IRS pursuant to the rules in §10.7(c)(1)(viii) of Circular 230 and Revenue Procedure 81-38, 1981-2 C.B. 592. See §601.601(d)(2)(ii)(b).

In June 2009, the IRS launched a review of tax return preparers with the intent to propose a comprehensive set of recommendations to ensure uniform and high ethical standards of conduct for all tax return preparers and to increase taxpayer compliance. As part of this effort, the IRS received input from a large and diverse community through numerous channels, including public forums, solicitation of written comments, and meetings with advisory groups.

The IRS made findings and recommendations in Publication 4832, “*Return Preparer Review*” (the Report), which was published on January 4, 2010. The Report recommends increased oversight of the tax return preparer industry through the issuance of regulations.

This document proposes amendments to Circular 230 based upon certain of the recommendations in the Report. Specifically, the proposed regulations establish “registered tax return preparers,” as a new class of practitioners. Sections 10.3 through 10.6 of the proposed regulations describe the process for becoming a registered tax return preparer and the limitations on a registered tax return preparer’s practice before the IRS. In general, practice by registered tax return preparers is limited to preparing tax returns, claims for refund, and other documents for submission to the IRS. A registered tax return preparer may prepare all or substantially all of a tax return or claim for refund, and sign a tax return or claim for refund, commensurate with the registered tax return preparer’s level of competence as demonstrated by written examination. The proposed regulations also revise §10.30 regarding solicitation, §10.36 regarding procedures to ensure compliance, and §10.51 regarding incompetence and disreputable conduct.

Proposed regulations under section 6109 of the Code (REG-134235-08, 2010-16 I.R.B. 596) published in the **Federal Register** (75 FR 14539) on March 26, 2010, also implement certain recommendations in the Report. The proposed regulations under section 6109 provide that, for returns or claims for refund filed after December 31, 2010, the identifying number of a tax return preparer is the individual’s preparer tax identification number (PTIN) or such other number prescribed by the IRS in

forms, instructions, or other appropriate guidance. The proposed regulations under section 6109 provide that the IRS is authorized to require through other guidance (as well as in forms and instructions) that tax return preparers apply for a PTIN or other prescribed identifying number, the regular renewal of PTINs or other prescribed identifying number, and the payment of user fees.

## Explanation of Provisions

The scope of these proposed regulations is limited to practice before the IRS. The Director of OPR has general oversight responsibilities for the rules in these proposed regulations, but specific duties related to the administration of certain procedural aspects of these rules (for example, test administration, issuance of enrollment or registration certificates or cards) may be delegated to employees of other IRS functions or third party vendors if the Commissioner determines that the performance of these duties by these organizations will aid tax administration. These proposed regulations do not change the existing authority of attorneys, certified public accountants, and enrolled agents to practice before the IRS under Circular 230. These proposed regulations also do not alter or supplant ethical standards that might otherwise be applicable to practitioners.

### *Definitions — Practice Before the Internal Revenue Service and Tax Return Preparer*

“Practice before the Internal Revenue Service” under §10.2(a)(4) comprehends all matters connected with a presentation to the IRS or any of its officers or employees relating to a taxpayer’s rights, privileges, or liabilities under laws or regulations administered by the IRS. Under the current definition of practice, preparing a tax return or claim for refund (even if the tax return or claim for refund is filed by another person) is practice before the IRS. Similarly, an individual who files a tax return or claim for refund prepared by someone else also is engaged in practice before the IRS. The IRS and the Treasury Department are aware that some tax professionals have suggested that they are not engaged in practice before the IRS unless they both prepare and file a tax return, claim for refund, or other document. Accordingly, §10.2(a)(4) of the proposed regulations is

revised to eliminate this misunderstanding, and specifically clarifies that either preparing a document or filing a document may constitute practice before the IRS. Section 10.2(a)(8) of the proposed regulations also clarifies that the definition of “tax return preparer” in Circular 230 is the same as the meaning in section 7701(a)(36) of the Code and 26 CFR 301.7701-15.

#### *Who May Practice*

Section 10.3(f) of the proposed regulations establishes a new “registered tax return preparer” designation. A registered tax return preparer is any individual so designated under §10.4(c) who is not currently under suspension or disbarment from practice before the IRS. An individual who is a registered tax return preparer pursuant to this part is a practitioner authorized to practice before the IRS, subject to the limitations identified in these proposed regulations.

These proposed regulations generally limit practice as a registered tax return preparer to preparing tax returns, claims for refund, and other documents for submission to the IRS. Pursuant to §10.3(f)(2) of these proposed regulations, a registered tax return preparer may only prepare, or assist in the preparation of, all or substantially all of a tax return or claim for refund that is commensurate with the level of competence that the registered tax return preparer has demonstrated by written examination. Registered tax return preparers also are permitted to sign tax returns, claims for refund, and other documents as the preparer provided the document is commensurate with the level of competence demonstrated, and may represent taxpayers before revenue agents, customer service representatives or similar officers and employees of the IRS (including the Taxpayer Advocate Service) during an examination if the registered tax return preparer signed the tax return or claim for refund for the taxable year or period under examination. Consistent with the limited practice rights currently available to unenrolled return preparers under §10.7(c)(1)(viii), registered tax return preparers are not permitted to represent taxpayers, regardless of the circumstances requiring representation, before appeals officers, revenue officers, Counsel or similar officers or employees of the IRS or

the Treasury Department. A registered tax return preparer’s authorization to practice under this part also does not include the authority to provide tax advice to a client or another person except as necessary to prepare a tax return, claim for refund, or other document intended to be submitted to the IRS.

The conduct of the registered tax return preparer in connection with the preparation of the return, claim for refund, or other document, as well as any representation of the client during an examination, will be subject to the standards of conduct in Circular 230. Inquiries into possible misconduct and disciplinary proceedings relating to registered tax return preparer misconduct will be conducted under the provisions in Circular 230.

#### *Eligibility to Become a Registered Tax Return Preparer*

An individual must pass a minimum competency examination and possess a current or otherwise valid PTIN or other prescribed identifying number to become a registered tax return preparer. The examination will be administered by, or administered under the oversight of, the IRS, similar to the special enrollment examinations for enrolled agents and enrolled retirement plan agents. After completing competency testing, tax return preparers will be subject to suitability checks to determine whether the tax return preparer has engaged in disreputable conduct which, at the time the application is filed with OPR, could result in suspension or disbarment under Circular 230. An individual who has engaged in disreputable conduct is not eligible to become a registered tax return preparer.

Consistent with the recommendations made in the Report, these proposed regulations do not exempt a tax return preparer from the competency testing requirements based upon the individual’s past tax return preparation experience. Initially, the IRS will offer two competency examinations. One examination will cover wage and nonbusiness income Form 1040 series returns, while another examination will cover wage and small business income Form 1040 series returns. An individual must successfully complete an examination prior to becoming a registered tax return preparer and obtaining a PTIN. The

IRS will prescribe by forms, instructions, or other appropriate guidance the tax returns and claims for refund, including the schedules and forms, that a registered tax return preparer may prepare based upon the written examination successfully completed under §10.4(c). The registered tax return preparer who passes the wage and small business income Form 1040 series examination, however, will be able to prepare any Form 1040 series returns. The IRS and the Treasury Department request comments on whether a tax return preparer who solely prepares tax returns other than Form 1040 series returns (for example, Form 941, *Employer’s QUARTERLY Federal Tax Return*, or Form 706, *U.S. Estate Tax Return*) should be permitted to prepare these other tax returns without successfully completing any examination.

It is currently anticipated that the examination to become a registered tax return preparer will not be available until after the effective date of these regulations. The IRS and the Treasury Department will provide published guidance establishing transition rules that explain the steps individuals must take to prepare all or substantially all of a tax return or claim for refund while awaiting full implementation of the examination process.

#### *Application and Renewal Procedures*

Section 10.5 of the regulations sets forth the applicable procedures relating to the application to become a registered tax return preparer, which generally are consistent with the procedures currently utilized for enrolled agents and enrolled retirement plan agents. The proposed regulations provide that applicants must utilize forms and comply with the procedures established and published by the IRS. The proposed regulations permit the IRS to change the procedures to apply to become a registered tax return preparer.

As a condition for consideration of an application, the IRS may conduct a Federal tax compliance check and suitability check. The tax compliance check will be limited to an inquiry regarding whether an applicant has filed all required individual or business tax returns (such as employment tax returns that might have been required to be filed by the applicant) and whether the applicant has failed to pay, or make proper arrangement with the IRS for

payment of, any Federal tax debts. The suitability check will be limited to an inquiry regarding whether an applicant has engaged in any conduct that would justify suspension or disbarment of any practitioner under the provisions of this part, including whether the applicant has engaged in disreputable conduct.

The IRS may deny an application only if the results of the tax compliance or suitability check are sufficient to establish that the practitioner engaged in conduct subject to sanctions under Circular 230 at the time the application is filed or the applicant does not pass the required competency examination. If the applicant does not pass the competency examination or the tax compliance or suitability check, the applicant will not be issued an enrollment or registration card or certificate, and will be provided information regarding the denial of the application and the rules on appealing the denial. An applicant who is initially denied enrollment or registration for failure to pass a tax compliance check may reapply after the initial denial if the applicant becomes current with respect to the applicant's tax liabilities.

Once an application to become a registered tax return preparer is approved, the IRS will issue a registration card or certificate to each individual and each card or certificate will be valid for the period stated on the card or certificate. The card or certificate will be in addition to any certificate that may be issued to an attorney, certified public accountant, enrolled agent, or registered tax return preparer who obtains a PTIN. Registered tax return preparers must have both a current and valid registration card or certificate and a current and valid PTIN certificate to practice before the IRS.

Section 10.6 of the proposed regulations sets forth the procedures for renewal of application to practice before the IRS as a registered tax return preparer. A registered tax return preparer must apply for renewal as prescribed in forms, instructions, or other appropriate guidance. A condition of renewal, as recommended in the Report, is the completion of continuing education requirements by registered tax return preparers. A registered tax return preparer must complete 15 hours of continuing education during each registration year, with a minimum of three hours of Federal tax law updates, two hours of

tax-related ethics and 10 hours of Federal tax law topics. The registration year is defined as each 12-month period that the registered tax return preparer is authorized to practice before the IRS. Registered tax return preparers will be required to maintain records with respect to the completion of the continuing education credit hours and to self-certify the completion of the continuing education credit at the time of renewal. The proposed regulations require that a qualifying continuing education course enhance professional knowledge in Federal taxation or Federal tax related matters and be consistent with the Code and effective tax administration.

Section 10.6(f)(2)(iii) and (f)(2)(iv) of the current regulations authorizes continuing education credit to be awarded for hours relating to work as an instructor, discussion leader, or speaker at an education program, as well as hours for authoring articles, books, or other publications on Federal taxation or Federal tax-related matters. The maximum credit for instruction and preparation currently may not exceed 50 percent of the continuing education requirement for an enrollment cycle. After further consideration, the IRS and the Treasury Department believe that the maximum credit for instruction and preparation should be reduced to encourage a more diverse educational program. These proposed regulations, therefore, reduce the maximum credit for instruction and preparation to four hours annually of the continuing education requirement. These proposed regulations also remove the ability to receive hours for authoring articles, books, or other publications.

Section 10.5(b) and §10.6(d)(6) of the proposed regulations are revised to reflect that the IRS will charge a reasonable non-refundable fee for each initial application and application for renewal as a registered tax return preparer filed with OPR. Separate regulation projects under 26 CFR part 300 will provide further details on the amounts of those user fees in the near future.

#### *Continuing Education Providers*

The rules regarding continuing education providers that currently are in §10.6 of Circular 230 are moved to new §10.9. Under §10.9 of the proposed regulations, providers of continuing education

courses are required to maintain records and educational material concerning these programs and the individuals who attend them, as well as obtain approval of each program to be qualified as a qualified continuing education program. Section 10.9(a)(6) also states that the IRS may charge a reasonable nonrefundable fee for each application for qualification as a qualified continuing education program. A separate regulation project under 26 CFR part 300 will provide further details on the amounts of the user fee in the near future.

#### *Limited Practice Before the IRS, Return Preparation, and Application to Other Individuals*

Section 10.7(c)(1)(viii) currently authorizes an individual, who is not otherwise a practitioner, to represent a taxpayer during an examination if that individual prepared the return for the taxable period under examination. The proposed regulations remove this limited practice authorization from §10.7(c) because of the addition to §10.3(f) regarding registered tax return preparers. Additionally, these proposed regulations remove current §10.8 regarding customhouse brokers from Circular 230 and move the language in current §10.7(e) to new §10.8(a). Section 10.8(a) of the proposed regulations provides that any individual, whether or not the individual is a practitioner, may assist with the preparation of a tax return or claim for refund (provided the individual prepares less than substantially all of the tax return or claim for refund). This revision is consistent with the inclusion of registered tax return preparers as practitioners authorized to practice before the IRS and the practice rights available to these practitioners.

These proposed regulations also establish a new §10.8(b) regarding other individuals. Any individual who prepares for compensation all or a substantial portion of a document pertaining to a taxpayer's tax liability for submission to the IRS is subject to the duties and restrictions relating to practice before the IRS and may be sanctioned, after notice and opportunity for a conference, for any conduct that would justify a sanction under §10.50. An individual described in 26 CFR 301.7701-15(f) is not treated



as having prepared all or a substantial portion of the document by reason of such assistance. For example, an individual who only furnishes typing, reproducing, or other mechanical assistance with respect to a document is not subject to the duties and restrictions relating to practice before the IRS. Only an attorney, certified public accountant, enrolled agent, or registered tax return preparer may prepare for compensation all or substantially all of a tax return or claim for refund, or sign as a preparer tax returns and claims for refund.

An individual who is not an attorney, certified public accountant, enrolled agent, or registered tax return preparer who nevertheless prepares for compensation all or a substantial portion of a document (including tax returns and claims for refund) for submission to the IRS is engaged in practice before the IRS, and subject to the rules and standards of Circular 230.

#### *Solicitation*

Section 10.30(a)(1) of these proposed regulations provides that a practitioner may not, with respect to any IRS matter, in any way use or participate in the use of any form of public communication or private solicitation containing a false, fraudulent, coercive, misleading, or deceptive statement or claim. In describing their professional designation, registered tax return preparers may not utilize the term “certified” or imply an employer/employee relationship with the IRS. An example of an acceptable description for registered tax return preparers under §10.4(c), in describing their professional designation, is “designated as a registered tax return preparer with the Internal Revenue Service.”

#### *Standards With Respect to Tax Returns and Documents, Affidavits and Other Papers*

After careful consideration, the IRS and the Treasury Department continue to conclude that the professional standards in §10.34(a) generally should be consistent with the civil penalty standards in section 6694 for tax return preparers. As discussed in this preamble, the limited differences between the proposed standards in §10.34 and section 6694 arise from the different purposes served by those provisions and the different manner in which the two standards will be administered.

The standards with respect to tax returns in §10.34(a) are being repropoed to provide broader guidelines that are more appropriate for professional ethics standards. Under §10.34(a)(1)(i) of these proposed regulations, a practitioner may not willfully, recklessly, or through gross incompetence, sign a tax return or claim for refund that the practitioner knows or reasonably should know contains a position that: (A) lacks a reasonable basis; (B) is an unreasonable position as described in section 6694(a)(2) (including the related regulations and other published guidance); or (C) is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard of rules or regulations by the practitioner as described in section 6694(b)(2) (including the related regulations and other published guidance).

Under §10.34(a)(1)(ii) of these proposed regulations, a practitioner may not willfully, recklessly, or through gross incompetence, advise a client to take a position on a tax return or claim for refund, or prepare a portion of a tax return or claim for refund containing a position, that: (A) lacks a reasonable basis; (B) is an unreasonable position as described in section 6694(a)(2) (including the related regulations and other published guidance); or (C) is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard of rules or regulations by the practitioner as described in section 6694(b)(2) (including the related regulations and other published guidance).

These proposed ethical guidelines under §10.34 closely mirror the civil penalty standards in section 6694 with only a few minor differences. First, these proposed regulations specifically provide that a position on a return or claim for refund must always meet the minimum threshold standard of reasonable basis. Because Circular 230 establishes minimum standards for practitioners, these proposed regulations provide that a practitioner acts unethically when the practitioner advises a taxpayer to take a return position that lacks a reasonable basis. The proposed regulations do not provide an exception to §10.34(a) merely because there is a final determination that no understatement of liability for tax exists. This differs from section 6694(d), which provides that the IRS must abate (or refund) a preparer penalty any

time there is a final administrative determination or a final judicial decision that there was no understatement of liability by the taxpayer. A practitioner, therefore, may still be subject to discipline under §10.34(a) for a position on a tax return or claim for refund even if other positions on the same tax return or claim for refund eliminate the understatement of liability.

Second, these proposed regulations provide that a practitioner is subject to discipline under §10.34(a) only after willful, reckless, or grossly incompetent conduct. Under section 6694, a single, unintentional error that is not willful, reckless, or grossly incompetent may result in a section 6694(a) penalty. Similarly, a return preparer may claim a reasonable cause defense to the imposition of penalties under section 6694, while Circular 230 does not provide such a defense but rather relies on the requirement that a practitioner must have acted willfully, recklessly, or through gross incompetence to ensure that sanctions are not imposed on a practitioner who acts reasonably and in good faith. If the IRS imposes a penalty against a practitioner under section 6694 and also refers the practitioner for possible discipline under Circular 230, OPR will make an independent determination as to whether the practitioner engaged in willful, reckless, or grossly incompetent conduct subject to discipline under §10.34(a) before any disciplinary proceedings are instituted or any sanctions are imposed. Thus, a practitioner liable for a penalty under section 6694 is not automatically subject to discipline under §10.34(a).

Third, multiple practitioners from the same firm may be disciplined if their conduct in connection with the same act(s) does not comply with the standard of conduct required under §10.34. Under the provisions in the regulations under section 6694, only one person within a firm is subject to the penalty under section 6694. The provisions of section 6694 prevent unwarranted duplication of civil penalties, but in the Circular 230 context, it may be critical that each practitioner engaged in misconduct be subject to appropriate sanctions.

Finally, §10.34(a)(2) of these proposed regulations expressly provides that a pattern of conduct is a factor that will be taken into account in determining whether a practitioner acted willfully, recklessly, or through gross incompetence for purposes

of §10.34. This differs from section 6694, which imposes a penalty based upon a single act in violation of the applicable provisions.

With these revisions, the definitions previously proposed under §10.34(e) are withdrawn because the well-established definitions under the section 6662 and section 6694 penalty regulations and other published guidance will control for purposes of §10.34.

#### *Procedures to Ensure Compliance*

Section 10.36 currently provides procedures to ensure that tax practitioners with responsibility for overseeing a firm's practice before the IRS 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 regarding covered opinions. The procedures to ensure compliance have produced great successes in encouraging firms to self-regulate, while at the same time doing so in a flexible way that is not a rigid one-size-fits-all regulatory burden. Firm responsibility is a critical factor in ensuring high quality advice and representation for taxpayers. Accordingly, the IRS and the Treasury Department conclude that the procedures to ensure compliance should be expanded to include practice involving tax return preparation activities. Section 10.36 of the proposed regulations provides that firm management with principal authority and responsibility for overseeing a firm's practice of preparing tax returns, claims for refunds and other documents filed with the IRS must take reasonable steps to ensure that the firm has adequate procedures in effect for purposes of complying with Circular 230.

#### *Incompetence and Disreputable Conduct*

Section 10.51 of Circular 230 defines disreputable conduct for which a practitioner may be sanctioned. Section 6011(e)(3) of the Code, enacted by section 17 of the Worker, Homeownership, and Business Assistance Act of 2009, Public Law 111-92 (123 Stat. 2984, 2996) (Nov. 6, 2009), requires certain specified tax return preparers to file individual income tax returns electronically. Because the IRS and the Treasury Department believe that the failure to comply with

this requirement is disreputable conduct, these proposed regulations are amended to add a new paragraph in §10.51 to address practitioners who fail to comply with this requirement. Under §10.51(a)(16) of the proposed regulations, disreputable conduct includes willfully failing to file on magnetic or other electronic media a tax return prepared by the practitioner when the practitioner is required to do so by the Federal tax laws (unless the failure is due to reasonable cause and not due to willful neglect).

Under §10.51(a)(17) of the proposed regulations, disreputable conduct also includes willfully preparing all or substantially all of, or signing as a compensated tax return preparer, a tax return or claim for refund when the practitioner does not possess a current or otherwise valid PTIN or other prescribed identifying number. Section 10.51(a)(18) states that it is disreputable conduct for a practitioner to willfully represent a taxpayer before an officer or employee of the IRS unless the practitioner is authorized to do so pursuant to Circular 230. These changes are consistent with the other revisions in these proposed regulations and under section 6109.

#### *Records*

Under §10.90 of the current regulations, OPR must maintain and may make available for public inspection in the time and manner prescribed by the Secretary a roster of enrolled agents, including those who are active, inactive, and sanctioned. These proposed regulations clarify that the roster requirements also pertain to registered tax return preparers and qualified continuing education programs.

#### **Proposed Effective Date**

These regulations are generally proposed to apply 60 days after the date that final regulations are published in the Federal Register.

#### **Special Analyses**

Executive Order 12866 requires certain regulatory assessments and procedures for a significant regulatory action, defined as adversely affecting in a material way the economy, a sector of the economy, productivity, competition, or jobs. This rule has been designated as significant and has

been reviewed by the Office of Management and Budget as required under the provisions of E.O. 12866. The Regulatory Assessment prepared for this regulation is provided below under the heading "Regulatory Assessment under E.O. 12866."

It has been determined that an initial regulatory flexibility analysis is required for this notice of proposed rulemaking under 5 U.S.C. 603. This analysis is set forth later in this preamble under the heading "Initial Regulatory Flexibility Analysis."

Pursuant to section 7805(f) of the Internal Revenue Code (Code), this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

#### *A. Regulatory Assessment under E.O. 12866*

##### *1. Description of need for the regulatory action*

Although the IRS has exercised its authority to regulate for attorneys, certified public accountants, and other specified tax professionals, regulations under Circular 230 currently do not apply to a critical group of tax professionals: tax return preparers. As discussed in the Report, taxpayers' reliance on tax return preparers has grown steadily in recent decades. The number of taxpayers who prepared their own tax returns without assistance fell by more than two-thirds between 1993 and 2005. In fact, today, tax return preparers assist a majority of U.S. taxpayers in meeting their Federal tax filing obligations. In 2008 and 2009, for example, tax return preparers prepared almost 60 percent of all federal tax returns filed, including approximately 87 million federal individual income tax returns. The IRS expects these numbers to increase in 2010 and the coming years.

Tax return preparers are not only responsible for assisting taxpayers in filing complete, timely, and accurate returns, but also help educate taxpayers about the tax laws, and facilitate electronic filing. Tax return preparers provide advice to taxpayers, identify items or issues for which the law or guidance is unclear, and inform taxpayers of the benefits and risks of positions taken on a tax return, and the tax treatment or reporting of items and transactions. The

IRS and the Treasury Department recognize that the majority of tax return preparers serve the interests of their clients and the tax system by preparing complete and accurate returns.

The tax system is best served by tax return preparers who are ethical, provide good service, and are qualified. Recent government studies, including studies from the Government Accountability Office and the Treasury Inspector General for Tax Administration, *see, e.g., Government Accountability Office, Paid Tax Return Preparers: In a limited Study, Chain Preparers Made Serious Errors*, GAO-06-563T (Apr. 4, 2006); Treasury Inspector General for Tax Administration, *Most Tax Returns Prepared by a Limited Sample of Unenrolled Preparers Contained Significant Errors*, Rept. # 2008-40-171 (Sept. 3, 2008), illustrate the losses incurred by both taxpayers and the system of Federal tax administration when tax return preparers fail to properly prepare tax returns. Additionally, many of the more than 500 public comments received by the IRS during the agency's review of the return preparer industry expressed concern for taxpayers, tax administration and the return preparer industry, all of whom are hurt when tax returns are not accurately prepared.

An overwhelming number of commentators (98 percent of the persons who offered comments on oversight and enforcement) supported increased government oversight of tax return preparers, particularly for individuals who are not attorneys, certified public accountants or others currently authorized to practice before the IRS. These commentators argued that taxpayers, the IRS and tax administration generally would benefit from the registration of tax return preparers. Eighty-eight percent of the persons who expressed an opinion on registering paid tax return preparers favor registration. Ninety percent of the persons who commented on testing and education favor minimum education or testing requirements for paid tax return preparers. And 98 percent of the persons who commented on quality and ethics favor establishment of quality and ethics standards for paid tax return preparers.

Because the IRS has not adopted a uniform set of regulations for tax return preparers, the amount of oversight of tax return professionals varies greatly depend-

ing on professional affiliations and the geographic area in which they practice. Most tax return preparers do not have to pass any government or professionally mandated competency requirement. Most tax return preparers are not required to participate in a specified program of continuing professional education. And the ethical rules found in Circular 230 currently are not applicable to all tax return preparers.

As such, the IRS recognizes the need to apply a uniform set of rules to offer taxpayers some assurance that their tax returns are prepared completely and accurately. Increasing the completeness and accuracy of returns would necessarily lead to increase compliance with tax obligations by taxpayers.

## 2. Potentially affected tax returns

These proposed regulations generally extend current regulations that apply to attorneys, certified public accountants and other specified tax professionals to all tax return preparers, including currently unenrolled tax return preparers, who prepare all or substantially all of a tax return or claim for refund for compensation. The rules apply to all returns prepared by tax return preparers regardless of the taxpayer. The rule is not limited by the type of return or claim for refund. For example, the rule applies to self-employed tax return preparers who prepare primarily individual tax returns for persons who have only wage and interest income. The rule also applies to tax return preparers employed by large accounting firms who prepare primarily corporate and large partnership returns. It also applies to those tax returns preparers who prepare only estate or excise tax returns. These examples are nonexclusive and the application of these rules is not limited to only those tax return preparers covered by the examples.

The IRS and the Treasury Department believe that the expansion of these regulations to currently unenrolled tax return preparers may impact individual taxpayers more than large corporate taxpayers because the IRS and the Treasury Department believe that large corporate taxpayers more likely employ the services of those who are currently regulated than those who are currently unenrolled to prepare their tax returns. The IRS and the Treasury

Department are seeking comments on the types of returns (for example: individual versus corporate tax returns) currently being prepared by currently unenrolled tax return preparers.

## 3. An assessment of benefits anticipated from the regulatory action

The primary benefit anticipated from these regulations is that they will improve the accuracy, completeness, and timeliness of tax returns prepared by tax return preparers. As illustrated in the recent government studies, including the IRS's recent review of the tax return preparer industry, inaccurate tax returns are costly both to taxpayers and the government. Inaccurate returns may affect the finances of taxpayers, who might overpay their respective share of taxes or fail to take advantage of available tax benefits. Inaccurate tax returns may also affect the U.S. government because of underpayments and increased costs of enforcement and collection.

The regulations are expected to improve the accuracy, completeness, and timeliness of tax returns in a number of ways. First, requiring tax return preparers to demonstrate the necessary qualifications to provide a valuable service by successfully completing a government or professionally mandated competency examination and continued competence by completing the specified continuing education credits annually will result in more competent and ethical tax return preparers who are well educated in the rules and subject matter. A more competent and ethical tax return preparer community will prevent costly errors, potentially saving taxpayers from unwanted problems and relieving the IRS from expending valuable examination and collection resources. Thus, these proposed regulations are critical to assisting the IRS curtail the activities of noncompliant and unethical tax return preparers.

Second, these regulations, in association with new and separate regulations under section 6109 requiring all individuals who prepare all or substantially all of a tax return for compensation to obtain a PTIN, are expected to improve the accuracy, completeness and timeliness of tax returns because they will help the IRS identify tax return preparers and the tax returns and claims for refund that they

prepare, which will aid the IRS's oversight of tax return preparers, and to administer requirements intended to ensure that tax return preparers are competent, trained, and conform to rules of practice. Individuals who prepare all or substantially all of a tax return or claim for refund will be required to obtain a PTIN prescribed by the IRS and furnish the PTIN when the tax return preparer signs (as the tax return preparer) a tax return or claim for refund. These individuals who are currently not attorneys, certified public accountants, or enrolled agents will apply for status as a registered tax return preparer and regularly renew that status. Given the important role that tax return preparers play in Federal tax administration, the IRS has a significant interest in being able to accurately identify tax return preparers and monitor the tax return preparation activities of these individuals. These regulations, in conjunction with the final PTIN regulations, will enable the IRS to more accurately identify tax return preparers and improve the IRS's ability to associate filed tax returns and refund claims with the responsible tax return preparer.

Third, the proposed regulations are expected to improve the accuracy of tax returns by providing that all registered tax return preparers are practicing before the IRS and, therefore, are practitioners subject to the ethical standards of conduct in Circular 230. This change will authorize OPR to inquire into possible misconduct and institute disciplinary proceedings relating to paid preparer misconduct under

the provisions of Circular 230. A paid preparer who is shown to be incompetent or disreputable, fails to comply with the provisions in Circular 230, or with intent to defraud, willfully and knowingly misleads or threatens a client or prospective client, is subject to censure, suspension, or disbarment from practice before the IRS, as well as a monetary penalty.

The availability of these sanctions will act as a deterrent to paid preparers engaging in misconduct because disreputable or incompetent paid preparers who are suspended or disbarred from practice will no longer be able to prepare tax returns, claims for refund, and other documents submitted to the IRS. Competent and ethical tax return preparers who are well educated in the rules and subject matter of their field can prevent costly errors, potentially saving a taxpayer from unwanted problems later on and relieving the IRS from expending valuable examination and collection resources.

Because these regulations apply to all tax return preparers, the IRS and the Treasury Department anticipate that they will improve the accuracy of tax returns prepared by all types of tax professionals. The IRS and the Treasury Department expect that the largest marginal improvements in accuracy will be with regard to tax returns prepared by tax return preparers who previously were unregulated through the Circular 230 requirements. Unlike certified public accountants, attorneys, and enrolled agents, unenrolled tax return preparers generally are not subject to any form

of testing, continuing professional education, or uniform ethical standards. The tax returns prepared by unenrolled tax return preparers may involve tax issues that are less complicated and smaller in amount than issues in tax returns prepared by other types of tax professionals. In addition, individual taxpayers may face a variety of complex tax issues, for which the advice of a qualified tax advisor will improve the accuracy on the return. Finally, by requiring registration of all tax return preparers, these regulations will allow the IRS to better monitor the relative accuracy of tax returns prepared by various types of tax professionals.

Comments are requested on whether these proposed regulations will improve overall tax administration. In particular, comments are specifically requested regarding the extent to which the improved accuracy of tax returns will be achieved through these regulations and whether the testing and continuing education provisions of these regulations are properly focused on currently unregulated tax return preparers.

*4. An assessment of costs anticipated from the regulatory action*

There are various costs anticipated from this regulatory action.

Cost Category	Preliminary Cost Estimate
<b>COMPETENCY EXAMINATION</b>	
<ul style="list-style-type: none"> <li>Costs to registered tax preparers: costs associated with taking a minimum competency examination (including costs of examination, amount of time required to study for the exam, and any associated travel)</li> </ul>	<p><u>Costs to Registered Tax Preparers</u></p> <p>The costs associated with competency examinations for registered tax preparers are currently unknown. The competency examination has not been developed and an examination vendor has not been selected. The cost of the examination and amount of time required to study for it, therefore, are unknown. The costs for any associated travel will depend on what locations the test is offered in and how close the applicant lives to those locations. While there is currently no vendor for the examination, it is expected that the vendor will offer the test in many locations across the United States and several locations outside the United States.</p>

<ul style="list-style-type: none"> <li>• Costs to vendors: user fee costs IRS will charge to recover the costs to third-party vendors who administer the registered tax return preparer competency examination</li> <li>• Costs to government: costs associated with creating, administering, and reviewing competency exams</li> </ul>	<p><u>Costs to Vendors</u> The vendor for the examination has not been selected so these fees cannot yet be determined. This vendor fee will include the cost associated with fingerprinting every applicant.</p> <p><u>Costs to Government</u> These costs are currently unknown. The costs to the government will depend, in part, on which functions will be performed by a vendor. Also, the vendor may recover the vendor's associated costs through a separate fee charged by the vendor. We therefore seek comment from the public on the costs related to competency examination faced by both individuals and the government.</p>
<b>PTIN</b>	
<ul style="list-style-type: none"> <li>• Costs to registered tax preparers: user fees for applying for a PTIN and renewing a PTIN</li> <li>• Costs to vendors: user fee assessed by third-party vendor to administer the PTIN application and renewal process</li> <li>• Costs to government: administration of PTIN registration program</li> </ul>	<p><u>Costs to Registered Tax Preparers</u> The fees registered tax preparers will face for applying for a PTIN and renewing a PTIN is \$50 annually. Given that there are an estimated 800,000 to 1,200,000 individuals who will apply for a PTIN, we estimate that the PTIN registration costs registered tax preparers face will be from \$40 million to \$60 million.</p> <p><u>Costs to Vendors</u> These fees are currently unknown because the selected vendor has not yet determined the fee.</p> <p><u>Costs to Government</u> The \$50 annual fee is expected to recover the \$59,427,633 annual costs the government will face in its administration of the PTIN registration program. This fee includes: (1) the costs the government faces in administering registration cards or certificates for each registered tax preparer, (2) costs associated with prescribing by forms, instructions, or other guidance which forms and schedules registered tax preparers can sign for, and (3) tax compliance and suitability checks conducted by the government. The \$50 fee does not include the cost of fingerprinting which we expect will be covered in the examination fee.</p>
<b>RECORDKEEPING</b>	
<ul style="list-style-type: none"> <li>• Costs to continuing education providers: recordkeeping requirements on continuing education providers to maintain records and educational material concerning these programs and the individuals who attend them.</li> <li>• Costs to registered tax preparers: recordkeeping requirements on registered tax preparers to maintain records and educational materials regarding the completion of the required qualifying continuing education credits.</li> </ul>	<p><u>Costs to Continuing education providers</u> \$38,632,500 annual costs</p> <p><u>Costs to Registered Tax Preparers</u> \$9,880,000 annual costs</p>

CONTINUING EDUCATION	
<ul style="list-style-type: none"> <li>Costs to registered tax preparers: completing continuing education coursework requirement</li> <li>Costs to government: user fee for costs to government for review, approval and oversight of continuing education, and fee for IRS recovering these costs.</li> </ul>	<p><u>Costs to registered tax preparers</u></p> <p>We do not have a cost estimate available for continuing education costs borne by the tax preparers. We seek comment on the cost of continuing education.</p> <p><u>Costs to government</u></p> <p>We do not have a cost estimate available for continuing education costs borne by the government for its review, approval and oversight of continuing education requirements imposed by the rule, which will be recovered by a user fee (in a future rulemaking) assessed on continuing education providers. We therefore seek comment from the public on the cost the government will incur.</p>

Tax return preparers will incur costs associated with taking a minimum competency examination, including the cost of the examination, the amount of time required to study for the examination, and any associated travel depending on the proximity of tax return preparer to the test site location. Although it is anticipated that the vendor will offer the test at several locations in the United States and outside the United States, the vendor and the test locations have not been selected at this time. Future regulations will be proposed that address the costs to the government for creating, administering, and reviewing the examination and the user fee the IRS will charge to recover these costs. The third-party vendor who helps administer the registered tax return preparer competency examination also will charge a reasonable fee to take the registered tax return preparer examination. Comments are specifically requested on the costs associated with the examination and the impact these costs may have on tax return preparers, entities that employ them or taxpayers who use their services.

Additionally, preparers will be subject to user fees for applying for a PTIN and renewing the PTIN. Proposed regulations published in the Federal Register on July 23, 2010, establish a \$50 fee to apply for a PTIN. A third party vendor will administer the PTIN application and renewal process and will charge a fee that is independent of the user fee charged by the government. Comments are specifically requested on the costs associated with applying for and renewing a PTIN and the impact these costs may have on tax return preparers and entities that employ them.

Tax return preparers will incur record-keeping and other costs associated with taking continuing education classes and any associated travel. Section 10.6 of these proposed regulations requires a registered tax return preparer to maintain records and educational materials regarding the completion of the required qualifying continuing education credits. The IRS and the Treasury Department estimate that there are 650,000 practitioners who will be affected by these recordkeeping requirements and the estimated annual burden per practitioner will vary from 30 minutes to one hour, depending on individual circumstances, with an estimated average of 54 minutes. The total annual costs resulting from these recordkeeping requirements will be \$9,880,000 for all affected practitioners. Comments are specifically requested on the other costs associated with taking continuing education classes.

Continuing education providers will be subject to recordkeeping costs and user fees for each application for qualification as a qualified continuing education program. Section 10.9 of these proposed regulations requires providers of qualifying continuing education programs to maintain records and educational material concerning these programs and the individuals who attend them. Continuing education providers also obtain approval of each program as a qualified continuing education program. Approximately 500 continuing education providers are currently approved to provide continuing education programs for the approximately 50,000 enrolled agents, enrolled actuaries and enrolled retirement plan agents who must complete continuing education currently, but the IRS and the Treasury Department

estimate that there are 2,250 continuing education providers who will be affected by these recordkeeping requirements and the estimated annual burden per continuing education provider will vary from 5 hours to 5,000 hours, depending on individual circumstances, with an estimated average of 500 hours. The estimated total annual costs resulting from these requirements will be \$38,632,500 for all affected continuing education providers.

The amounts of the user fee for providing continuing education programs are still to be determined and another regulation addressing user fees will be proposed. These future regulations will address the costs to the government for the review, approval, and oversight of continuing education providers to ensure their compliance with program design and maintenance for continuing education programs and the user fee to be charged by the IRS to recover these costs.

Currently, the cost to the tax return preparer of any particular continuing education course can vary greatly from free to hundreds of dollars. Many tax return preparation firms either provide continuing education courses at the firm to its employees for no charge or sponsor the cost of external courses for its employees. Other tax return preparers, however, will have to personally pay the cost of each continuing education course, which generally ranges anywhere from \$20 to \$300 per course depending on whether the continuing education provider offers the course in person, online, or over the phone. After the publication of this regulatory action, continuing education providers may increase the costs of the courses in response to the new user fee on continuing education providers. Tax return preparers also

may incur additional costs if they travel to attend continuing education programs. These costs may include the time to travel to the program, transportation, lodging and incidentals.

Entities may be directly affected by the competency examination, PTIN and continuing education costs if they choose to pay any or all of the user fees or expenses for their employees. Some individuals and entities also may lose sales and profits while preparers are studying and sitting for the examination or taking the continuing education courses. Finally, individual tax return preparers and entities that employ individuals who prepare tax returns may need to close or change their business model if all, or a majority, of their employees cannot satisfy the necessary qualifications and competency requirements. The IRS and the Treasury Department believe that only a small percentage of tax return preparers will need to close or change their business model based upon these proposed rules. Comments are specifically requested on the costs associated with continuing education and the impact these costs may have on tax return preparers, continuing education providers, entities that employ tax return preparers or taxpayers who use the services of a tax return preparer.

#### 5. *An assessment of costs and benefits of potential alternatives*

The IRS and the Treasury Department considered various alternatives in determining the best ways to implement proposed changes to the regulation of tax return preparers. In order to place the costs and benefits of the proposed rule in context, E.O. 12866 requires a comparison between the proposed rule, a baseline of what the world would look like without the proposed rule, and reasonable alternatives to the proposed rule.

##### i. *Baseline scenario*

Under a baseline scenario, the current ethical standards in Circular 230 would continue to apply only to attorneys, certified public accountants, enrolled agents, and other practitioners who prepare tax returns and claims for refund, but not to unenrolled tax return preparers. Also, any unenrolled tax return preparer under this

baseline scenario would be able to prepare and sign tax returns and claims for refund without passing an examination to establish competence or satisfying continuing education requirements.

Remaining under the current rules regarding tax return preparers would eliminate the benefits of the proposed rule described in section A2 of this preamble. For example, under the baseline, OPR would not be authorized to institute disciplinary proceedings seeking sanctions against unenrolled tax return preparers.

Continuing to authorize any individual to prepare tax returns and claims for refund for compensation without passing an examination or taking continuing education courses also would eliminate any costs associated with the proposed rule described in section A3 of this preamble. Tax return preparers, however, would still potentially be subject to user fees for obtaining a PTIN and renewing the PTIN if other Treasury Department and IRS regulations specifically prescribed those fees.

##### ii. *Alternative one*

The first alternative that was considered is to require all tax return preparers to comply with the ethical standards in Circular 230, but not to require any tax return preparer to pass an examination and complete continuing education courses. Under this alternative, the provisions of the proposed rule clarifying that tax return preparers are subject to the ethical rules in Circular 230 would remain intact, but all of the other changes would not be adopted.

The benefits resulting from this alternative would likely be less than the rules in the proposed regulations because tax return preparers would not need to meet a minimum competency level and keep educated and up-to-date on Federal tax issues. The most significant drawback to this alternative is the potential loss of these benefits and the benefits that result from monitoring the return preparation activities of tax return preparers generally. Under this alternative, however, tax return preparers would not incur the majority of costs that exist under the proposed regulations.

##### iii. *Alternative two*

A second alternative is to require tax return preparers who are not currently authorized to practice before the IRS to apply

for such authorization with the IRS, satisfy annual continuing education requirements, and meet certain ethical standards, but not to pass a minimum competency examination. This alternative is identical to the proposed regulations other than requiring certain preparers to successfully pass an examination administered by, or under the oversight of, the IRS.

The benefits resulting from this alternative are more comparable to the benefits in the proposed regulations than under alternative one. Nevertheless, the lack of an examination probably would not be as effective in ensuring that tax return preparers are qualified to obtain professional credentials and practice before the IRS. Tax return preparers under this alternative would incur all of the same costs that are in the proposed regulations other than the costs associated with taking the examination.

##### iv. *Alternative three*

A third alternative is to “grandfather in” unenrolled tax return preparers who have accurately and competently prepared tax returns for a certain amount of years. This alternative is the same as the rules in the proposed regulations other than authorizing some unenrolled return preparers who have a specified amount of prior experience preparing tax returns and claims for refund to continue to prepare and sign returns without passing a minimum competency examination.

The benefits resulting from this alternative would likely be less than the rules in the proposed regulations because the IRS and the Treasury Department believe a minimum level of competency needs to be assured through examination. Additionally, this alternative is not as likely to promote the same taxpayer confidence in the tax return preparation community as the proposed regulations, which may, in turn, influence taxpayers when choosing a tax return preparer. Tax return preparers under this alternative would incur all of the same costs that are in the proposed regulations except certain unenrolled preparers would avoid the costs associated with taking the examination.

Comments are specifically requested on the benefits and costs of these alternatives compared to the approach taken in the proposed regulations.

## B. Initial Regulatory Flexibility Analysis

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act (5 U.S.C. chapter 6) (RFA) requires the agency “to prepare and make available for public comment an initial regulatory flexibility analysis” that will “describe the impact of the proposed rule on small entities.” See 5 U.S.C. 603(a). Section 605 of the RFA provides an exception to this requirement if the agency certifies that the proposed rulemaking will not have a significant economic impact on a substantial number of small entities. A small entity is defined as a small business, small non-profit organization, or small governmental jurisdiction. See 5 U.S.C. 601(3) through (6). The IRS and the Treasury Department conclude that the proposed regulations, if promulgated, will impact a substantial number of small entities and the economic impact will be significant. As a result, an initial regulatory flexibility analysis is required.

### 1. Description of the reasons why the agency action is being considered

As discussed in more detail in section A1 of this preamble, tax return preparers are critical to ensuring compliance with the Federal tax laws and are an important component in the IRS’s administration of those laws. More than eighty percent of U.S. taxpayers use a tax return preparer or consumer tax return preparation software to help prepare and file tax returns. Most tax return preparers are currently not subject to the ethical rules governing practice before the IRS and do not have to pass any competency requirement established by the government or a professional organization. After completing a comprehensive six-month review of tax return preparers, which included receiving input through public forums, solicitation of written comments, and meetings with advisory groups, the IRS concluded that there was a need for increased oversight of the tax return preparer industry. These proposed regulations implement higher standards for the tax return preparer community with the goal of significantly enhancing protections and service for taxpayers, increasing confidence in the tax system, and resulting in greater long-term compliance with the tax laws.

### 2. Statement of the objectives of, and legal basis for, the proposed rule

The principal objective of the proposed regulations is to increase oversight of all tax return preparers and to provide guidance to tax return preparers about the new requirements imposed on them under Circular 230. Specifically, the proposed regulations clarify that any registered tax return preparer is a practitioner practicing before the IRS and thereby is subject to the ethical rules in Circular 230. The proposed regulations require a tax return preparer to demonstrate the necessary qualifications and competency to advise and assist other persons in the preparation of all or substantially all of a tax return or claim for refund. The legal basis for these requirements is contained in section 330 of title 31.

### 3. Description and estimate (where feasible) of the number of small entities subject to the proposed rule

The proposed regulations affect all individuals currently working as paid preparers, individuals who want to become designated as a registered tax return preparer under the new oversight rules in Circular 230, and those small entities that are owned by or employ paid preparers. Only individuals, not businesses, can practice before the IRS or become a registered tax return preparer. Thus, the economic impact of these regulations on any small entity generally will be a result of an unenrolled individual owning a small business or on a small business that otherwise employs unenrolled paid return preparers. These regulations also will economically affect any small entity that is a provider of qualifying continuing education programs.

The appropriate NAICS codes for tax return preparers relate to tax preparation services (NAICS code 541213) and other accounting services (NAICS code 541219). Entities identified under these codes are considered small under the Small Business Administration size standards (13 CFR 121.201) if their annual revenue is less than \$7 million or \$8.5 million, respectively. The IRS estimates that approximately seventy to eighty percent of the individuals subject to these proposed regulations are paid preparers operating as or employed by small entities. The IRS

estimates that there will be 2,250 providers of qualifying continuing education programs.

### 4. Description of the projected reporting, recordkeeping and related requirements of the proposed rule, including an estimate of the classes of small entities that will be subject to the requirements and the type of professional skills necessary for preparation of the report or record

The IRS estimates that there are approximately 600,000 to 700,000 unenrolled tax return preparers who are currently not attorneys, certified public accountants, or enrolled agents and who will apply for status as a registered tax return preparer if these proposed rules are adopted. Under the proposed regulations, tax return preparers who become registered tax return preparers are subject to a recordkeeping requirement within the meaning of the PRA because they are required to maintain records and educational materials regarding the satisfaction of their qualifying continuing education requirements. These recordkeeping requirements do not require any specific professional skills other than general recordkeeping skills already needed to own and operate a small business or to competently act as a tax return preparer. It is estimated that practitioners will annually spend approximately 30 minutes to one hour in maintaining the required records, depending on individual circumstances.

The estimated 2,250 providers of qualifying continuing education programs will be required to maintain records and educational material concerning these programs and the persons who attended them. These entities will need to obtain approval of the program as a qualified continuing education program from OPR. These continuing education providers will annually spend approximately 5 minutes per attendee maintaining the required records and approximately 30 minutes to one hour per program completing and filing the application for approval as a qualified continuing education program.

As previously discussed in section A3 of this preamble, the proposed rule contains a number of other compliance requirements not subject to the PRA. These include the costs tax return preparers incur to take a competency examination, costs



for continuing education classes, and other incidental costs and user fees. Small entities may be directly affected by these costs if they choose to pay any or all of these fees for their employees. In some cases, small entities may lose sales and profits while their employees prepare for and take the examination or participate in continuing education courses. Finally, some small entities that employ individuals who prepare tax returns may need to alter their business model if a significant number of their employees cannot satisfy the necessary qualifications and competency requirements. The IRS and the Treasury Department believe that only a small percentage of small entities, if any, may need to cease doing business or radically change their business model due to these proposed rules.

*5. Identification, to the extent practicable, of all relevant Federal rules that may duplicate, overlap or conflict with the proposed rule*

All tax return preparers currently are subject to various civil and criminal penalties under the Code. For example, section 6694 imposes civil penalties on tax return preparers for conduct giving rise to certain understatements of liability on a return, while section 6695 imposes civil penalties for, among other acts, failing to sign or provide an identification number on a return they prepare. Tax return preparers who demonstrate a pattern of misconduct may be enjoined from preparing further returns under section 7407. Additionally, the IRS, under its broad authority to regulate the filing of electronic returns, requires any tax return preparer who files returns electronically to comply with certain rules, including requiring the electronic return originator to pass background and credit history checks. The IRS and the Treasury Department believe that the proposed rules complement these existing rules with a resulting comprehensive enforcement strategy that ensures that all tax return preparers are assisting clients appropriately.

*6. Description of any significant alternatives to the proposed rule that accomplish the stated objectives of applicable statutes and which minimize any significant economic impact on small entities*

The IRS received a large volume of comments, through the Return Preparer Review, on the oversight and enforcement of tax return preparers from all interested parties, including tax professional groups representing large and small entities, Federal and state organizations, IRS advisory groups, software vendors, individual return preparers, and the public. The input received from this large and diverse community overwhelmingly expressed support for efforts to increase the oversight of tax return preparers, particularly for those who are not attorneys, certified public accountants, or other individuals currently authorized to practice before the IRS.

In concert with this tremendous public support for increased IRS oversight of tax return preparers, the IRS and the Treasury Department considered various alternatives in determining the best ways to implement proposed changes to the regulation of paid preparers. As discussed in more detail in section A4 of this preamble, these alternatives included:

(1) Requiring all tax return preparers to comply with the ethical standards in Circular 230 or a code of ethics similar to Circular 230, but not requiring any tax return preparers to demonstrate their qualifications and competency;

(2) Requiring tax return preparers who are not currently authorized to practice before the IRS to apply for authorization with the IRS, satisfy annual continuing education requirements, and meet certain ethical standards, but not to pass a minimum competency examination; and

(3) Requiring all tax return preparers who are not currently authorized to practice before the IRS to pass a minimum competency examination and meet other requirements, but “grandfather in” tax return preparers who have accurately and competently prepared tax returns for a certain number of years.

After consideration of these and other alternatives and all of the input provided through the public comment process, the IRS and the Treasury Department concluded that the provisions of the proposed regulations are necessary for sound tax administration and are the best way to increase oversight of all paid preparers. The testing requirements in the proposed rules will ensure that tax return preparers pass a minimum competency examination to obtain their professional credentials, while

the continuing education requirements will help ensure that tax return preparers remain current on Federal tax law and continue to expand their tax knowledge. The extension of the rules in Circular 230 to registered tax return preparers will require all practitioners to meet certain ethical standards and allow the IRS to suspend or otherwise discipline tax return preparers who engage in unethical or disreputable conduct. Accordingly, the implementation of the qualification and competency standards in these proposed rules is expected to increase taxpayer compliance and ensure uniform and high ethical standards of conduct for tax return preparers. The public comments submitted during the Return Preparer Review overwhelmingly supported the provisions in these proposed rules.

### **Comments and Requests For Public Hearing**

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

A public hearing has been scheduled for Friday, October 8, 2010, beginning at 10:00 am in Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, D.C. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. All visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 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

an outline of the topics to be discussed and the time to be devoted to each topic by Monday, September 27, 2010. 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 author of these regulations is Matthew S. Cooper of the Office of the Associate Chief Counsel (Procedure and Administration).

\* \* \* \* \*

### Withdrawal of Notice of Proposed Rulemaking

Accordingly, under the authority of 31 U.S.C. 330, the notice of proposed rulemaking (REG-138637-07, 2007-2 C.B. 977) that was published in the **Federal Register** on September 26, 2007 (72 FR 54621) is withdrawn.

### Proposed Amendments to the Regulations

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

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

Paragraph 1. The authority citation for 31 CFR part 10 is revised 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. 321; 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 10.0 is revised to read as follows:

##### *§10.0 Scope of part.*

This part contains rules governing the recognition of attorneys, certified public accountants, enrolled agents, enrolled retirement plan agents, registered tax return preparers, and other persons representing taxpayers before the Internal Revenue Service. Subpart A of this part sets forth rules

relating to the authority to practice before the Internal Revenue Service; Subpart B of this part prescribes the duties and restrictions relating to such practice; Subpart C of this part prescribes the sanctions for violating the regulations; Subpart D of this part contains the rules applicable to disciplinary proceedings; and Subpart E of this part contains general provisions relating to the availability of official records.

Par. 3. Section 10.2 is amended by revising paragraphs (a)(4), (a)(5), and (b) and adding paragraph (a)(8) to read as follows:

##### *§10.2 Definitions.*

(a) \* \* \*

(4) *Practice before the Internal Revenue Service* comprehends all matters connected with a presentation to the Internal Revenue Service or any of its officers or employees relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service. Such presentations include, but are not limited to, preparing documents; filing documents; corresponding and communicating with the Internal Revenue Service; rendering written advice with respect to any entity, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion; and representing a client at conferences, hearings, and meetings.

(5) *Practitioner* means any individual described in paragraphs (a), (b), (c), (d), (e), or (f) of §10.3.

\* \* \* \* \*

(8) *Tax return preparer* means any individual within the meaning of section 7701(a)(36) and 26 CFR 301.7701-15.

(b) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 4. Section 10.3 is amended by:

1. Redesignating paragraphs (f), (g), (h), and (i) as paragraphs (g), (h), (i), and (j) respectively.

2. Adding new paragraph (f).

3. Revising paragraphs (d)(3) and (e)(3), and newly designated paragraph (j).

The revisions and additions read as follows:

##### *§10.3 Who may practice.*

\* \* \* \* \*

(d) \* \* \*

(3) An individual who practices before the Internal Revenue Service pursuant to paragraph (d)(1) of this section is subject to the provisions of this part in the same manner as attorneys, certified public accountants, enrolled agents, enrolled retirement plan agents, and registered tax return preparers.

(e) \* \* \*

(3) An individual who practices before the Internal Revenue Service pursuant to paragraph (e)(1) of this section is subject to the provisions of this part in the same manner as attorneys, certified public accountants, enrolled agents, enrolled actuaries, and registered tax return preparers.

(f) *Registered tax return preparers.* (1) Any individual who is designated as a registered tax return preparer pursuant to §10.4(c) of this part who is not currently under suspension or disbarment from practice before the Internal Revenue Service may practice before the Internal Revenue Service.

(2) Practice as a registered tax return preparer is limited to preparing tax returns, claims for refund, and other documents for submission to the Internal Revenue Service. A registered tax return preparer may prepare, or assist in preparing, all or substantially all of a tax return or claim for refund for which the registered tax return preparer has passed the requisite written examination. A registered tax return preparer also may sign tax returns, claims for refund, or other documents for which the registered tax return preparer has passed the requisite written examination. The Internal Revenue Service will prescribe by forms, instructions, or other appropriate guidance the tax returns and claims for refund, including the schedules and forms, that a registered tax return preparer may prepare or sign based on the written examination that the registered tax return preparer has successfully completed. A registered tax return preparer may represent taxpayers before revenue agents, customer service representatives, or similar officers and employees of the Internal Revenue Service during an examination if the registered tax return preparer signed the tax return or claim for refund for the taxable year or period under examination. Unless otherwise prescribed by regulation or notice, this right does not permit such indi-

vidual to represent the taxpayer, regardless of the circumstances requiring representation, before appeals officers, revenue officers, Counsel or similar officers or employees of the Internal Revenue Service or the Treasury Department. A registered tax return preparer's authorization to practice under this part also does not include the authority to provide tax advice to a client or another person except as necessary to prepare a tax return, claim for refund, or other document intended to be submitted to the Internal Revenue Service.

(3) An individual who practices before the Internal Revenue Service pursuant to paragraph (f)(1) of this section is subject to the provisions of this part in the same manner as attorneys, certified public accountants, enrolled agents, enrolled retirement plan agents, and enrolled actuaries.

\* \* \* \* \*

(j) *Effective/applicability date.* This section is generally applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 5. Section 10.4 is revised to read as follows:

*§10.4 Eligibility to become an enrolled agent, enrolled retirement plan agent, or registered tax return preparer.*

(a) *Enrollment as an enrolled agent upon examination.* The Director of the Office of Professional Responsibility may grant enrollment as an enrolled agent to an applicant who demonstrates special competence in tax matters by written examination administered by, or administered under the oversight of, the Director of the Office of Professional Responsibility and who has not engaged in any conduct that would justify the suspension or disbarment of any practitioner under the provisions of this part on the date the application is submitted.

(b) *Enrollment as a retirement plan agent upon examination.* The Director of the Office of Professional Responsibility may grant enrollment as an enrolled retirement plan agent to an applicant who demonstrates special competence in qualified retirement plan matters by written examination administered by, or administered under the oversight of, the Director of the Office of Professional Responsibility and who has not engaged in any conduct that would justify the suspension

or disbarment of any practitioner under the provisions of this part.

(c) *Designation as a registered tax return preparer.* The Director of the Office of Professional Responsibility may designate an individual as a registered tax return preparer provided an applicant demonstrates competence in Federal tax return preparation matters by written examination administered by, or administered under the oversight of, the Internal Revenue Service, possesses a current or otherwise valid PTIN or other prescribed identifying number, and has not engaged in any conduct that would justify the suspension or disbarment of any practitioner under the provisions of this part on the date the application is submitted.

(d) *Enrollment of former Internal Revenue Service employees.* The Director of the Office of Professional Responsibility may grant enrollment as an enrolled agent or enrolled retirement plan agent to an applicant who, by virtue of past service and technical experience in the Internal Revenue Service, has qualified for such enrollment and who has not engaged in any conduct that would justify the suspension or disbarment of any practitioner under the provisions of this part, under the following circumstances—

(1) The former employee applies for enrollment to the Director of the Office of Professional Responsibility on a form supplied by the Director of the Office of Professional Responsibility and supplies the information requested on the form and such other information regarding the experience and training of the applicant as may be relevant.

(2) An appropriate office of the Internal Revenue Service, at the request of the Director of the Office of Professional Responsibility, will provide the Director of the Office of Professional Responsibility with a detailed report of the nature and rating of the applicant's work while employed by the Internal Revenue Service and a recommendation whether such employment qualifies the applicant technically or otherwise for the desired authorization.

(3) Enrollment as an enrolled agent based on an applicant's former employment with the Internal Revenue Service may be of unlimited scope or it may be limited to permit the presentation of matters only of the particular specialty or only

before the particular unit or division of the Internal Revenue Service for which the applicant's former employment has qualified the applicant. Enrollment as an enrolled retirement plan agent based on an applicant's former employment with the Internal Revenue Service will be limited to permit the presentation of matters only with respect to qualified retirement plan matters.

(4) Application for enrollment as an enrolled agent or enrolled retirement plan agent based on an applicant's former employment with the Internal Revenue Service must be made within three years from the date of separation from such employment.

(5) An applicant for enrollment as an enrolled agent who is requesting such enrollment based on former employment with the Internal Revenue Service must have had a minimum of five years continuous employment with the Internal Revenue Service during which the applicant must have been regularly engaged in applying and interpreting the provisions of the Internal Revenue Code and the regulations relating to income, estate, gift, employment, or excise taxes.

(6) An applicant for enrollment as an enrolled retirement plan agent who is requesting such enrollment based on former employment with the Internal Revenue Service must have had a minimum of five years continuous employment with the Internal Revenue Service during which the applicant must have been regularly engaged in applying and interpreting the provisions of the Internal Revenue Code and the regulations relating to qualified retirement plan matters.

(7) For the purposes of paragraphs (d)(5) and (d)(6) of this section, an aggregate of 10 or more years of employment in positions involving the application and interpretation of the provisions of the Internal Revenue Code, at least three of which occurred within the five years preceding the date of application, is the equivalent of five years continuous employment.

(e) *Natural persons.* Enrollment or authorization to practice may be granted only to natural persons.

(f) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 6. Section 10.5 is revised to read as follows:

*§10.5 Application to become an enrolled agent, enrolled retirement plan agent, or registered tax return preparer.*

(a) *Form; address.* An applicant to become an enrolled agent, enrolled retirement plan agent, or registered tax return preparer must apply as required by forms or procedures established and published by the Internal Revenue Service, including proper execution of required forms under oath or affirmation. The address on the application will be the address under which a successful applicant is enrolled or registered and is the address to which all correspondence concerning enrollment or registration will be sent.

(b) *Fee.* A reasonable nonrefundable fee will be charged for each application filed with the Director of the Office of Professional Responsibility. See 26 CFR part 300.

(c) *Additional information; examination.* The Director of the Office of Professional Responsibility, as a condition to consideration of an application, may require the applicant to file additional information and to submit to any written or oral examination under oath or otherwise. The Director of the Office of Professional Responsibility will, on written request filed by the applicant, afford such applicant the opportunity to be heard with respect to his or her application for enrollment.

(d) *Compliance and suitability checks.*  
(1) As a condition to consideration of an application, the Internal Revenue Service may conduct a Federal tax compliance check and suitability check. The tax compliance check will be limited to an inquiry regarding whether an applicant has filed all required individual or business tax returns and whether the applicant has failed to pay, or make proper arrangement with the Internal Revenue Service for payment of, any Federal tax debts. The suitability check will be limited to an inquiry regarding whether an applicant has engaged in any conduct that would justify suspension or disbarment of any practitioner under the provisions of this part on the date the application is submitted, including whether the applicant has engaged in disreputable conduct as defined in §10.51. The application will be denied only if the results

of the compliance or suitability check are sufficient to establish that the practitioner engaged in conduct subject to sanctions under §10.51 and §10.52.

(2) If the applicant does not pass the tax compliance or suitability check, the applicant will not be issued an enrollment or registration card or certificate pursuant to §10.6(b) of this part, and will be provided information regarding the denial of the application and the rules on appealing the denial. An applicant who is initially denied enrollment or registration for failure to pass a tax compliance check may reapply after the initial denial if the applicant becomes current with respect to the applicant's tax liabilities.

(e) *Temporary recognition.* On receipt of a properly executed application, the Director of the Office of Professional Responsibility may grant the applicant temporary recognition to practice pending a determination as to whether status as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer should be granted. Temporary recognition will be granted only in unusual circumstances and it will not be granted, in any circumstance, if the application is not regular on its face, if the information stated in the application, if true, is not sufficient to warrant granting the application to practice, or if there is any information before the Director of the Office of Professional Responsibility indicating that the statements in the application are untrue or that the applicant would not otherwise qualify to become an enrolled agent, enrolled retirement plan agent, or registered tax return preparer. Issuance of temporary recognition does not constitute either a designation or a finding of eligibility as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer, and the temporary recognition may be withdrawn at any time by the Director of the Office of Professional Responsibility.

(f) *Appeal from denial of application.* The Director of the Office of Professional Responsibility must inform the applicant in writing as to the reason(s) for any denial of an application. The applicant may, within 30 days after receipt of the notice of denial of the application, file a written appeal of the denial with the Secretary of the Treasury or delegate. A decision on the appeal will be rendered by the Secretary, or delegate, as soon as practicable.

(g) *Effective/applicability date.* This section is applicable to applications received 60 days after the date that final regulations are published in the Federal Register.

Par. 7. Section 10.6 is revised to read as follows:

*§10.6 Term and renewal of status as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer.*

(a) *Term.* Each individual authorized to practice before the Internal Revenue Service as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer will be accorded active enrollment or registration status subject to renewal of enrollment or registration as provided in this part.

(b) *Enrollment or registration card or certificate.* The Director of the Office of Professional Responsibility will issue an enrollment or registration card or certificate to each individual whose application to practice before the Internal Revenue Service is approved. Each card or certificate will be valid for the period stated on the card or certificate. An enrolled agent or registered tax return preparer may not practice before the Internal Revenue Service if the card or certificate is not current or otherwise valid. The card or certificate is in addition to any certificate that may be issued to each attorney, certified public accountant, enrolled agent, or registered tax return preparer who obtains a preparer tax identification number.

(c) *Change of address.* An enrolled agent, enrolled retirement plan agent, or registered tax return preparer must send notification of any change of address to the address specified by the Director of the Office of Professional Responsibility within 60 days of the change of address. This notification must include the enrolled agent's, enrolled retirement plan agent's, or registered tax return preparer's name, prior address, new address, tax identification number(s) (including preparer tax identification number), and the date the change of address became effective. Unless this notification is sent, the address for purposes of any correspondence from the Director of the Office of Professional Responsibility shall be the address as reflected on the practitioner's most recent application for enrollment or registration,

or application for renewal of enrollment or registration.

(d) *Renewal*—(1) *In general*. Designation as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer must be renewed periodically to maintain active status to practice before the Internal Revenue Service. Failure to receive notification from the Director of the Office of Professional Responsibility of the renewal requirement will not be justification for the individual's failure to satisfy this requirement.

(2) *Renewal period for enrolled agents*.

(i) All individuals enrolled to practice before the Internal Revenue Service who have a social security number or tax identification number that ends with the numbers 0, 1, 2, or 3, except for those individuals who received their initial enrollment after November 1, 2003, must apply for renewal between November 1, 2003, and January 31, 2004. The renewal will be effective April 1, 2004.

(ii) All individuals enrolled to practice before the Internal Revenue Service who have a social security number or tax identification number that ends with the numbers 4, 5, or 6, except for those individuals who received their initial enrollment after November 1, 2004, must apply for renewal between November 1, 2004, and January 31, 2005. The renewal will be effective April 1, 2005.

(iii) All individuals enrolled to practice before the Internal Revenue Service who have a social security number or tax identification number that ends with the numbers 7, 8, or 9, except for those individuals who received their initial enrollment after November 1, 2005, must apply for renewal between November 1, 2005, and January 31, 2006. The renewal will be effective April 1, 2006.

(iv) Thereafter, applications for renewal as an enrolled agent will be required between November 1 and January 31 of every subsequent third year as specified in paragraph (d)(2)(i), (d)(2)(ii), or (d)(2)(iii) of this section according to the last number of the individual's social security number or tax identification number. Those individuals who receive initial enrollment as an enrolled agent after November 1 and before April 2 of the applicable renewal period will not be required to renew their enrollment before the first full renewal pe-

riod following the receipt of their initial enrollment.

(3) *Renewal period for enrolled retirement plan agents*. Applications for renewal as an enrolled retirement plan agent will be required of all enrolled retirement plan agents between April 1 and June 30 of every third year period subsequent to their initial enrollment.

(4) *Renewal period for registered tax return preparers*. Applications for renewal as a registered tax return preparer will be required of all registered tax return preparers as prescribed in forms, instructions, or other appropriate guidance.

(5) *Notification of renewal*. After review and approval, the Director of the Office of Professional Responsibility will notify the individual of the renewal and will issue the individual a card or certificate evidencing current status as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer.

(6) *Fee*. A reasonable nonrefundable fee will be charged for each application for renewal filed with the Director of the Office of Professional Responsibility. See 26 CFR part 300.

(7) *Forms*. Forms required for renewal may be obtained by sending a written request to the Director of the Office of Professional Responsibility, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20224 or from such other source as the Internal Revenue Service will publish in the Internal Revenue Bulletin (see 26 CFR 601.601(d)(2)(ii)(b)) and on the Internal Revenue Service website ([www.irs.gov](http://www.irs.gov)).

(e) *Condition for renewal: continuing education*. In order to qualify for renewal as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer, an individual must certify, in the manner prescribed by the Internal Revenue Service, that the individual has satisfied the required continuing education requirements.

(1) *Definitions*. For purposes of this section—

(i) *Enrollment year* means January 1 to December 31 of each year of an enrollment cycle.

(ii) *Enrollment cycle* means the three successive enrollment years preceding the effective date of renewal.

(iii) *Registration year* means each 12-month period the registered tax return

preparer is authorized to practice before the Internal Revenue Service.

(iv) The *effective date of renewal* is the first day of the fourth month following the close of the period for renewal described in paragraph (d) of this section.

(2) *For renewed enrollment as an enrolled agent or enrolled retirement plan agent*—(i) *Requirements for enrollment cycle*. A minimum of 72 hours of continuing education credit, including six hours of ethics or professional conduct, must be completed during each enrollment cycle.

(ii) *Requirements for enrollment year*. A minimum of 16 hours of continuing education credit, including two hours of ethics or professional conduct, must be completed during each enrollment year of an enrollment cycle.

(iii) *Enrollment during enrollment cycle*—(A) *In general*. Subject to paragraph (e)(2)(iii)(B) of this section, an individual who receives initial enrollment during an enrollment cycle must complete two hours of qualifying continuing education credit for each month enrolled during the enrollment cycle. Enrollment for any part of a month is considered enrollment for the entire month.

(B) *Ethics*. An individual who receives initial enrollment during an enrollment cycle must complete two hours of ethics or professional conduct for each enrollment year during the enrollment cycle. Enrollment for any part of an enrollment year is considered enrollment for the entire year.

(3) *Requirements for renewal as a registered tax return preparer*. A minimum of 15 hours of continuing education credit, including two hours of ethics or professional conduct, three hours of Federal tax law updates, and 10 hours of Federal tax law topics, must be completed during each registration year.

(f) *Qualifying continuing education*—(1) *General*—(i) *Enrolled agents*. To qualify for continuing education credit for an enrolled agent, a course of learning must—

(A) Be a qualifying continuing education program designed to enhance professional knowledge in Federal taxation or Federal tax related matters (programs comprised of current subject matter in Federal taxation or Federal tax related matters, including accounting, tax return preparation software, taxation, or ethics); and

(B) Be a qualifying continuing education program consistent with the Internal Revenue Code and effective tax administration.

(ii) *Enrolled retirement plan agents.* To qualify for continuing education credit for an enrolled retirement plan agent, a course of learning must—

(A) Be a qualifying continuing education program designed to enhance professional knowledge in qualified retirement plan matters; and

(B) Be a qualifying continuing education program consistent with the Internal Revenue Code and effective tax administration.

(iii) *Registered tax return preparers.* To qualify for continuing education credit for a registered tax return preparer, a course of learning must—

(A) Be a qualifying continuing education program designed to enhance professional knowledge in Federal taxation or Federal tax related matters (programs comprised of current subject matter in Federal taxation or Federal tax related matters, including accounting, tax return preparation software, taxation, or ethics); and

(B) Be a qualifying continuing education program consistent with the Internal Revenue Code and effective tax administration.

(2) *Qualifying programs*—(i) *Formal programs.* A formal program qualifies as a continuing education program if it—

(A) Requires attendance and provides each attendee with a certificate of attendance;

(B) Requires that the program be conducted by a qualified instructor, discussion leader, or speaker (in other words, a person whose background, training, education, and experience is appropriate for instructing or leading a discussion on the subject matter of the particular program);

(C) Provides or requires a written outline, textbook, or suitable electronic educational materials; and

(D) Is approved as a qualified continuing education program by the Director of the Office of Professional Responsibility pursuant to §10.9.

(ii) *Correspondence or individual study programs (including taped programs).* Qualifying continuing education programs include correspondence or individual study programs that are conducted by con-

tinuing education providers and completed on an individual basis by the enrolled individual. The allowable credit hours for such programs will be measured on a basis comparable to the measurement of a seminar or course for credit in an accredited educational institution. Such programs qualify as continuing education programs only if they—

(A) Require registration of the participants by the continuing education provider;

(B) Provide a means for measuring successful completion by the participants (for example, a written examination), including the issuance of a certificate of completion by the continuing education provider;

(C) Provide a written outline, textbook, or suitable electronic educational materials; and

(D) Are approved as a qualified continuing education program by the Director of the Office of Professional Responsibility pursuant to §10.9.

(iii) *Serving as an instructor, discussion leader or speaker.* (A) One hour of continuing education credit will be awarded for each contact hour completed as an instructor, discussion leader, or speaker at an educational program that meets the continuing education requirements of paragraph (f) of this section.

(B) A maximum of two hours of continuing education credit will be awarded for actual subject preparation time for each contact hour completed as an instructor, discussion leader, or speaker at such programs. It is the responsibility of the individual claiming such credit to maintain records to verify preparation time.

(C) The maximum credit for instruction and preparation may not exceed four hours annually of the continuing education requirement.

(D) An instructor, discussion leader, or speaker who makes more than one presentation on the same subject matter during an enrollment cycle or registration year, will receive continuing education credit for only one such presentation for the enrollment cycle or registration year.

(3) *Periodic examination.* (i) Enrolled individuals may establish eligibility for renewal of enrollment for any enrollment cycle by—

(A) Achieving a passing score on each part of the Special Enrollment Examina-

tion administered under this part during the three year period prior to renewal; and

(B) Completing a minimum of 16 hours of qualifying continuing education during the last year of an enrollment cycle.

(ii) Courses designed to help an applicant prepare for the examination specified in §10.4 are considered basic in nature and are not qualifying continuing education.

(g) *Measurement of continuing education coursework.* (1) All continuing education programs will be measured in terms of contact hours. The shortest recognized program will be one contact hour.

(2) A contact hour is 50 minutes of continuous participation in a program. Credit is granted only for a full contact hour, which is 50 minutes or multiples thereof. For example, a program lasting more than 50 minutes but less than 100 minutes will count as only one contact hour.

(3) Individual segments at continuous conferences, conventions and the like will be considered one total program. For example, two 90-minute segments (180 minutes) at a continuous conference will count as three contact hours.

(4) For university or college courses, each semester hour credit will equal 15 contact hours and a quarter hour credit will equal 10 contact hours.

(h) *Recordkeeping requirements.* (1) Each individual applying for renewal must retain for a period of four years following the date of renewal the information required with regard to qualifying continuing education credit hours. Such information includes—

(i) The name of the sponsoring organization;

(ii) The location of the program;

(iii) The title of the program, qualified program number, and description of its content;

(iv) Written outlines, course syllabi, textbook, and/or electronic materials provided or required for the course;

(v) The dates attended;

(vi) The credit hours claimed;

(vii) The name(s) of the instructor(s), discussion leader(s), or speaker(s), if appropriate; and

(viii) The certificate of completion and/or signed statement of the hours of attendance obtained from the continuing education provider.

(2) To receive continuing education credit for service completed as an in-

structor, discussion leader, or speaker, the following information must be maintained for a period of four years following the date of renewal —

(i) The name of the sponsoring organization;

(ii) The location of the program;

(iii) The title of the program and copy of its content;

(iv) The dates of the program; and

(v) The credit hours claimed.

(i) *Waivers.* (1) Waiver from the continuing education requirements for a given period may be granted by the Director of the Office of Professional Responsibility for the following reasons—

(i) Health, which prevented compliance with the continuing education requirements;

(ii) Extended active military duty;

(iii) Absence from the United States for an extended period of time due to employment or other reasons, provided the individual does not practice before the Internal Revenue Service during such absence; and

(iv) Other compelling reasons, which will be considered on a case-by-case basis.

(2) A request for waiver must be accompanied by appropriate documentation. The individual is required to furnish any additional documentation or explanation deemed necessary by the Director of the Office of Professional Responsibility. Examples of appropriate documentation could be a medical certificate or military orders.

(3) A request for waiver must be filed no later than the last day of the renewal application period.

(4) If a request for waiver is not approved, the individual will be placed in inactive status, so notified by the Director of the Office of Professional Responsibility, and placed on a roster of inactive enrolled agents, enrolled retirement plan agents, or registered tax return preparers.

(5) If a request for waiver is approved, the individual will be notified and issued a card or certificate evidencing renewal.

(6) Those who are granted waivers are required to file timely applications for renewal of enrollment or registration.

(j) *Failure to comply.* (1) Compliance by an individual with the requirements of this part is determined by the Director of the Office of Professional Responsibility. An individual who fails to meet the continuing education and fee requirements of el-

igibility for renewal will be notified by the Director of the Office of Professional Responsibility. The notice will state the basis for the determination of noncompliance and will provide the individual an opportunity to furnish the requested information in writing relating to the matter within 60 days of the date of the notice. Such information will be considered by the Director of the Office of Professional Responsibility in making a final determination as to eligibility for renewal. The Director of the Office of Professional Responsibility must inform the individual as to the reason(s) for any denial of a renewal. The individual may, within 30 days after receipt of the notice of denial of renewal, file a written appeal of the denial with the Secretary or delegate. A decision on the appeal will be rendered by the Secretary, or delegate, as soon as practicable.

(2) The Director of the Office of Professional Responsibility may require any individual to provide copies of any records required to be maintained under this part. The Director of the Office of Professional Responsibility may disallow any continuing education hours claimed if the individual fails to comply with this requirement.

(3) An individual who has not filed a timely application for renewal, who has not made a timely response to the notice of noncompliance with the renewal requirements, or who has not satisfied the requirements of eligibility for renewal will be placed on a roster of inactive enrolled individuals or inactive registered individuals. During this time, the individual will be ineligible to practice before the Internal Revenue Service.

(4) Individuals placed in inactive status and individuals ineligible to practice before the Internal Revenue Service may not state or imply that they are eligible to practice before the Internal Revenue Service, or use the terms enrolled agent, enrolled retirement plan agent, or registered tax return preparer, the designations “EA” or “ERPA” or other form of reference to eligibility to practice before the Internal Revenue Service.

(5) An individual placed in inactive status may be reinstated to an active status by filing an application for renewal and providing evidence of the completion of all required continuing education hours for the enrollment cycle or registration year. Continuing education credit under this para-

graph (k)(5) may not be used to satisfy the requirements of the enrollment cycle or registration year in which the individual has been placed back on the active roster.

(6) An individual placed in inactive status must file an application for renewal and satisfy the requirements for renewal as set forth in this section within three years of being placed in inactive status. Otherwise, the name of such individual will be removed from the inactive status roster and the individual’s status as an enrolled agent, enrolled retirement plan agent, or registered tax return preparer will terminate. Future eligibility for active status must then be reestablished by the individual as provided in this section.

(7) Inactive status is not available to an individual who is the subject of a pending disciplinary matter before the Office of Professional Responsibility.

(k) *Inactive retirement status.* An individual who no longer practices before the Internal Revenue Service may request to be placed in an inactive retirement status at any time and such individual will be placed in an inactive retirement status. The individual will be ineligible to practice before the Internal Revenue Service. An individual who is placed in an inactive retirement status may be reinstated to an active status by filing an application for renewal and providing evidence of the completion of the required continuing education hours for the enrollment cycle or registration year. Inactive retirement status is not available to an individual who is ineligible to practice before the Internal Revenue Service or who is the subject of a disciplinary matter in the Office of Professional Responsibility.

(l) *Renewal while under suspension or disbarment.* An individual who is ineligible to practice before the Internal Revenue Service by virtue of disciplinary action by the Director of the Office of Professional Responsibility is required to conform to the requirements for renewal of enrollment or registration before the individual’s eligibility is restored.

(m) *Verification.* The Director of the Office of Professional Responsibility may review the continuing education records of an enrolled agent, enrolled retirement plan agent, or registered tax return preparer in any manner deemed appropriate to determine compliance with the requirements

and standards for renewal as provided in paragraph (f) of this section.

(n) *Enrolled actuaries.* The enrollment and renewal of enrollment of actuaries authorized to practice under paragraph (d) of §10.3 are governed by the regulations of the Joint Board for the Enrollment of Actuaries at 20 CFR 901.1 through 901.72.

(o) *Effective/applicability date.* This section is applicable to enrollment or registration effective 60 days after the date that final regulations are published in the Federal Register.

Par. 8. Section 10.7 is amended by:

1. Revising the section heading.
2. Removing paragraphs (c)(1)(viii) and (e).
3. Redesignating paragraphs (f) and (g) as paragraphs (e) and (f).
4. Revising newly designated paragraphs (e) and (f).

The revisions read as follows:

*§10.7 Representing oneself; participating in rulemaking; limited practice; and special appearances.*

\* \* \* \* \*

(e) *Fiduciaries.* For purposes of this part, a fiduciary (for example, a trustee, receiver, guardian, personal representative, administrator, or executor) is considered to be the taxpayer and not a representative of the taxpayer.

(f) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 9. Section 10.8 is revised to read as follows:

*§10.8 Return preparation and application of rules to other individuals.*

(a) *Preparing tax returns and furnishing information.* Any individual may prepare or assist with the preparation of a tax return or claim for refund (provided the individual prepares less than substantially all of the tax return or claim for refund), appear as a witness for the taxpayer before the Internal Revenue Service, or furnish information at the request of the Internal Revenue Service or any of its officers or employees.

(b) *Application of rules to other individuals.* Any individual who for compensation prepares, or assists in the preparation of, all or a substantial portion of a docu-

ment pertaining to any taxpayer's tax liability for submission to the Internal Revenue Service is subject to the duties and restrictions relating to practice in subpart B, as well as subject to the sanctions for violation of the regulations in subpart C. Unless otherwise a practitioner, however, an individual may not prepare, or assist in the preparation of, all or substantially all of a tax return or claim for refund, or sign tax returns and claims for refund. For purposes of this paragraph, an individual described in 26 CFR 301.7701-15(f) is not treated as having prepared all or a substantial portion of the document by reason of such assistance.

(c) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 10. Section 10.9 is added to subpart A to read as follows:

*§10.9 Continuing education programs.*

(a) *Continuing education providers—(1) In general.* Continuing education providers are those responsible for presenting continuing education programs. A continuing education provider must—

(i) Be an accredited educational institution;

(ii) Be recognized for continuing education purposes by the licensing body of any State, territory, or possession of the United States, including a Commonwealth, or the District of Columbia; or

(iii) Be recognized by the Director of the Office of Professional Responsibility as one who offers a qualified continuing education program.

(2) *Qualification of continuing education program.* A continuing education provider must obtain the approval of the Director of the Office of Professional Responsibility for each program to be qualified as a qualified continuing education program in the time and manner required by forms or procedures established and published by the Internal Revenue Service.

(3) *Requirements for qualified continuing education program.* A continuing education provider must ensure the qualified continuing education program complies with all the following requirements—

(i) Programs must be developed by individual(s) qualified in the subject matter;

(ii) Program subject matter must be current;

(iii) Instructors, discussion leaders, and speakers must be qualified with respect to program content;

(iv) Programs must include some means for evaluation by the Director of the Office of Professional Responsibility of technical content and presentation;

(v) Certificates of completion bearing a current qualified continuing education program number issued by the Director of the Office of Professional Responsibility must be provided to the participants who successfully complete the program; and

(vi) Records must be maintained by the continuing education provider to verify the participants who attended and completed the program for a period of four years following completion of the program. In the case of continuous conferences, conventions, and the like, records must be maintained to verify completion of the program and attendance by each participant at each segment of the program.

(4) *Fees.* Reasonable nonrefundable fees may be charged for each qualification of a qualified continuing education program. See 26 CFR part 300.

(b) *Failure to comply.* Compliance by a continuing education provider with the requirements of this part is determined by the Director of the Office of Professional Responsibility. A continuing education provider who fails to meet the requirements of this part will be notified by the Director of the Office of Professional Responsibility. The notice will state the basis for the determination of noncompliance and will provide the continuing education provider an opportunity to furnish the requested information in writing relating to the matter within 60 days of the date of the notice. Such information will be considered by the Director of the Office of Professional Responsibility in making a determination as to the qualification of a program as a qualified continuing education program. The Director of the Office of Professional Responsibility must inform the continuing education provider as to the reason(s) for any denial of a program as a qualified continuing education program. The continuing education provider may, within 30 days after receipt of the notice of denial, file a written appeal with the Secre-



tary or delegate. A decision on the appeal will be rendered by the Secretary or delegate, as soon as practicable.

(c) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 11. Section 10.30 is amended by revising paragraphs (a)(1) and (e) to read as follows:

*§10.30 Solicitation.*

(a) *Advertising and solicitation restrictions.* (1) A practitioner may not, with respect to any Internal Revenue Service matter, in any way use or participate in the use of any form or public communication or private solicitation containing a false, fraudulent, or coercive statement or claim; or a misleading or deceptive statement or claim. Enrolled agents, enrolled retirement plan agents, or registered tax return preparers, in describing their professional designation, may not utilize the term “certified” or imply an employer/employee relationship with the Internal Revenue Service. Examples of acceptable descriptions for enrolled agents are “enrolled to represent taxpayers before the Internal Revenue Service,” “enrolled to practice before the Internal Revenue Service,” and “admitted to practice before the Internal Revenue Service.” Similarly, examples of acceptable descriptions for enrolled retirement plan agents are “enrolled to represent taxpayers before the Internal Revenue Service as a retirement plan agent” and “enrolled to practice before the Internal Revenue Service as a retirement plan agent.” An example of an acceptable description for registered tax return preparers is “designated as a registered tax return preparer with the Internal Revenue Service.”

\* \* \* \* \*

(e) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 12. Section 10.34 is amended by:

1. Adding paragraph (a).
2. Redesignating paragraph (f) as paragraph (e).
3. Revising newly designated paragraph (e).

The revisions read as follows:

*§10.34 Standards with respect to tax returns and documents, affidavits and other papers.*

(a) *Tax returns.* (1) A practitioner may not willfully, recklessly, or through gross incompetence—

(i) Sign a tax return or claim for refund that the practitioner knows or reasonably should know contains a position that—

- (A) Lacks a reasonable basis;
- (B) Is an unreasonable position as described in section 6694(a)(2) of the Internal Revenue Code (Code) (including the related regulations and other published guidance); or
- (C) Is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard of rules or regulations by the practitioner as described in section 6694(b)(2) of the Code (including the related regulations and other published guidance).

(ii) Advise a client to take a position on a tax return or claim for refund, or prepare a portion of a tax return or claim for refund containing a position, that—

- (A) Lacks a reasonable basis;
- (B) Is an unreasonable position as described in section 6694(a)(2) of the Code (including the related regulations and other published guidance); or
- (C) Is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard of rules or regulations by the practitioner as described in section 6694(b)(2) of the Code (including the related regulations and other published guidance).

(2) A pattern of conduct is a factor that will be taken into account in determining whether a practitioner acted willfully, recklessly, or through gross incompetence.

\* \* \* \* \*

(e) *Effective/applicability date.* Paragraph (a) of this section is applicable for returns or claims for refund filed, or advice provided, 60 days after the date that final regulations are published in the Federal Register. Paragraphs (b) through (d) of this section are applicable to tax returns, documents, affidavits, and other papers filed on or after September 26, 2007.

Par. 13. Section 10.36 is amended by:

1. Redesignating paragraph (b) as paragraph (c).
2. Adding new paragraph (b).

3. Revising newly designated paragraph (c).

The addition and revisions read as follows:

*§10.36 Procedures to ensure compliance.*

\* \* \* \* \*

(b) *Requirements for tax returns and other documents.* Any practitioner who has (or practitioners who have or share) principal authority and responsibility for overseeing a firm’s practice of preparing tax returns, claims for refunds, or other documents for submission to the Internal Revenue Service 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 Circular 230. Any practitioner who has (or practitioners who have or share) this principal authority 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 Circular 230, 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 Circular 230; 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, who does not comply with Circular 230, and the practitioner, through willfulness, recklessness, or gross incompetence fails to take prompt action to correct the noncompliance.

(c) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the Federal Register.

Par. 14. Section 10.51 is amended by adding paragraphs (a)(16), (a)(17), and (a)(18) and revising paragraph (b) to read as follows:

*§10.51 Incompetence and disreputable conduct.*

(a) \* \* \*

(16) Willfully failing to file on magnetic or other electronic media a tax return prepared by the practitioner when the practitioner is required to do so by the Federal tax laws unless the failure is due to reasonable cause and not due to willful neglect.

(17) Willfully preparing all or substantially all of, or signing, a tax return or claim for refund when the practitioner does not possess a current or otherwise valid preparer tax identification number or other prescribed identifying number.

(18) Willfully representing a taxpayer before an officer or employee of the Internal Revenue Service unless the practitioner is authorized to do so pursuant to this part.

(b) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the **Federal Register**.

Par. 15. Section 10.90 is amended by:

1. Revising paragraph (a).
2. Redesignating the second paragraph (b) as paragraph (c).
3. Revising newly designated paragraph (c).

The revisions read as follows:

#### *§10.90 Records.*

(a) *Roster.* The Director of the Office of Professional Responsibility will maintain, and may make available for public inspection in the time and manner prescribed by the Secretary, or delegate, rosters of—

(1) Individuals (and employers, firms, or other entities, if applicable) censured, suspended, or disbarred from practice before the Internal Revenue Service or upon whom a monetary penalty was imposed.

(2) Enrolled agents, including individuals—

(i) Granted active enrollment to practice;

(ii) Whose enrollment has been placed in inactive status for failure to meet the requirements for renewal of enrollment;

(iii) Whose enrollment has been placed in inactive retirement status; and

(iv) Whose offer of consent to resign from enrollment has been accepted by the Director of the Office of Professional Responsibility under §10.61.

(3) Enrolled retirement plan agents, including individuals—

(i) Granted active enrollment to practice;

(ii) Whose enrollment has been placed in inactive status for failure to meet the requirements for renewal of enrollment;

(iii) Whose enrollment has been placed in inactive retirement status; and

(iv) Whose offer of consent to resign from enrollment has been accepted by the Director of the Office of Professional Responsibility under §10.61.

(4) Registered tax return preparers, including individuals—

(i) Authorized to prepare all or substantially all of a tax return or claim for refund;

(ii) Who have been placed in inactive status for failure to meet the requirements for renewal;

(iii) Who have been placed in inactive retirement status; and

(iv) Whose offer of consent to resign from their status as a registered tax return preparer has been accepted by the Director of the Office of Professional Responsibility under §10.61.

(5) Disqualified appraisers.

(6) Programs granted status as a qualified continuing education program.

\* \* \* \* \*

(c) *Effective/applicability date.* This section is applicable 60 days after the date that final regulations are published in the **Federal Register**.

Christopher Wagner,  
*Acting Deputy Commissioner  
for Services and Enforcement.*

(Filed by the Office of the Federal Register on August 19, 2010, 11:15 a.m., and published in the issue of the Federal Register for August 23, 2010, 75 F.R. 51713)

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

### **Announcement 2010–84**

The Internal Revenue Service has revoked its determination that the organizations listed below qualify as organizations described in sections 501(c)(3) and 170(c)(2) of the Internal Revenue Code of 1986.

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 November 1, 2010, 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.

American Children's Safety Source  
Michigan Center, MI

Anna Foundation, Inc.,  
Melville, NY

California Consumer Credit  
Los Angeles, CA

Interpreter Referral Service dba Chicago  
Area Interpreter Referral Service  
Chicago, IL

Consumer Counseling Centers of America  
Washington, DC

The Cruffel Foundation  
Jackson, WY

Debicated Consumer Counseling, Inc.,  
Centerport, NY

Museum of Military History  
Chandler, AZ

United Children's Fund  
Michigan Center, MI

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

### Announcement 2010-85

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 organizations 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.

Xelan Foundation AKA Significance  
Foundation  
Tampa, FL

Exegetical Institute, Inc.  
Kingsland, GA

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## IRS and the George Washington University Law School to Sponsor Institute on International Tax Issues

### Announcement 2010-86

The Internal Revenue Service announces the Twenty-Third Annual Institute on Current Issues in International Taxation, jointly sponsored by the Internal Revenue Service and The George Washington University Law School, to be held on December 9 and 10, 2010, at the J.W. Marriott Hotel in Washington, DC. Registration is currently underway for the Institute.

The program, which is intended for international tax professionals, will present a unique opportunity for top IRS and Treasury officials and tax experts, foreign government tax authorities, and leading private sector specialists, to address breaking issues and present key perspectives on new developments.

The first day will also feature sessions on:

- Competent Authority
- Transfer Pricing and Intellectual Property Transfers

- Foreign Tax Credit Developments
- Inbound and Outbound Update: What's New and What's Coming?
- New Reporting and Withholding Tax Rules: Sections 1471-1474
- Evolving Reporting Requirements for Uncertain Tax Positions

The second day will focus on:

- Welcome Address by William J. Wilkins, Chief Counsel of the Internal Revenue Service
- PFICs: Searching for Answers, Looking for Guidance
- Managing International Tax Issues: Cooperation or Controversy?
- Financing the Global Corporation: Working With Section 956
- Ethics Issues in International Tax Practice

On the first day, Douglas H. Shulman, Commissioner, Internal Revenue Service, will deliver the luncheon address. On the second day, Michael F. Mundaca, Assistant Secretary of the Treasury for Tax Policy, will deliver the luncheon address. The second day will also include an "Ask the IRS" panel featuring senior officials from the Service.

Those interested in attending or obtaining more information should contact The George Washington University Law School, at <http://docs.law.gwu.edu/ciit/>. The principal author of this announcement is Patricia A. Bray of the Office of Associate Chief Counsel (International). For further information regarding this announcement, contact Patricia A. Bray at 202-622-5871 (not a toll-free call).

# 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.

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