

# INTERNAL REVENUE BULLETIN



## HIGHLIGHTS OF THIS ISSUE

**Bulletin No. 2019-23**  
**June 3, 2019**

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.

### EMPLOYEE PLANS

#### **NOT 2019-35, page 1277.**

This notice sets forth updates on the corporate bond monthly yield curve, the corresponding spot segment rates for May 2019 used under § 417(e)(3)(D), the 24-month average segment rates applicable for May 2019, and the 30-year Treasury rates, as reflected by the application of § 430(h)(2)(C)(iv).

### INCOME TAX

#### **REV RUL 2019-14, page 1275.**

Federal rates; adjusted federal rates; adjusted federal long-term rate, the long-term exempt rate, and the blended annual rate. For purposes of sections 382, 1274, 1288, 7872 and other sections of the Code, tables set forth the rates for June 2019.

#### **NOT 2019-36, page 1280.**

The notice announces the inflation adjustment factor and phase-out amount for the enhanced oil recovery credit for taxable years beginning in the 2019 calendar year. The notice concludes that because the reference price for the 2019 calendar year (\$61.41) exceeds \$28 multiplied by the inflation adjustment factor for the 2018 calendar year (\$28 multiplied by 1.7334 = \$12.88), the enhanced oil recovery credit for qualified costs paid or incurred in 2019 is phased out completely by using a particular ratio.

#### **NOT 2019-37, page 1283.**

The Notice publishes Treasury's estimate of the annual average wellhead price per 1000 cubic feet for all domestic natural gas. This estimate is the "reference price" for purposes of the credit in § 45l. The Treasury Department estimate, for calendar year 2018, is \$2.68 per 1000 cubic feet, meaning the § 45l credit is \$0.00 per 1,000 cubic feet of qualified natural gas produced from marginal wells

#### **NOT 2019-38, page 1284.**

The notice announces that under § 613A(c)(6)(C) of the Internal Revenue Code, the applicable percentage for purposes of determining percentage depletion on marginal properties for calendar year 2019 is 15 percent. The format of the notice is identical to the format of notices previously published on this issue.

#### **REG-125135-15, page 1286.**

These proposed regulations provide rules regarding attribution for purposes of determining whether a person is a related person with respect to a controlled foreign corporation. They also provide rules for determining whether rents are derived in the active conduct of a trade or business for purposes of computing foreign personal holding company income. The regulations would affect United States persons with direct or indirect ownership interests in certain foreign corporations.

# The IRS Mission

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

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

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

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

against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

### **Part I.—1986 Code.**

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

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

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

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

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

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

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

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

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

# Part I.

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

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

### Rev. Rul. 2019-14

This revenue ruling provides various prescribed rates for federal income

tax purposes for June 2019 (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 ap-

propriate 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, 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. 2019-14 TABLE 1				
Applicable Federal Rates (AFR) for June 2019				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
		<i>Short-term</i>		
AFR	2.37%	2.36%	2.35%	2.35%
110% AFR	2.62%	2.60%	2.59%	2.59%
120% AFR	2.85%	2.83%	2.82%	2.81%
130% AFR	3.09%	3.07%	3.06%	3.05%
		<i>Mid-term</i>		
AFR	2.38%	2.37%	2.36%	2.36%
110% AFR	2.63%	2.61%	2.60%	2.60%
120% AFR	2.86%	2.84%	2.83%	2.82%
130% AFR	3.10%	3.08%	3.07%	3.06%
150% AFR	3.59%	3.56%	3.54%	3.53%
175% AFR	4.19%	4.15%	4.13%	4.11%
		<i>Long-term</i>		
AFR	2.76%	2.74%	2.73%	2.72%
110% AFR	3.03%	3.01%	3.00%	2.99%
120% AFR	3.32%	3.29%	3.28%	3.27%
130% AFR	3.59%	3.56%	3.54%	3.53%

REV. RUL. 2019-14 TABLE 2				
Adjusted AFR for June 2019				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
Short-term adjusted AFR	1.80%	1.79%	1.79%	1.78%
Mid-term adjusted AFR	1.81%	1.80%	1.80%	1.79%
Long-term adjusted AFR	2.09%	2.08%	2.07%	2.07%

REV. RUL. 2019-14 TABLE 3  
Rates Under Section 382 for June 2019

Adjusted federal long-term rate for the current month	2.09%
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.)	2.19%

REV. RUL. 2019-14 TABLE 4

Appropriate Percentages Under Section 42(b)(1) for June 2019

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

Appropriate percentage for the 70% present value low-income housing credit	7.59%
Appropriate percentage for the 30% present value low-income housing credit	3.25%

REV. RUL. 2019-14 TABLE 5

Rate Under Section 7520 for June 2019

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	2.8%
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### Section 42.—Low-Income Housing Credit

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

### Section 280G.—Golden Parachute Payments

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

### 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 June 2019. See Rev. Rul. 2019-14, page 1275.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

### Section 483.—Interest on Certain Deferred Payments

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

### 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 June 2019. See Rev. Rul. 2019-14, page 1275.

### Section 7520.—Valuation Tables

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2019. See Rev. Rul. 2019-14, page 1275.

## Part III.

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

#### Notice 2019-35

This notice provides guidance on the corporate bond monthly yield curve, the corresponding spot segment rates used under § 417(e)(3), and the 24-month average segment rates under § 430(h)(2) of the Internal Revenue Code. 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 and the 30-year Treasury weighted average rate under § 431(c)(6)(E)(ii)(I).

#### YIELD CURVE AND SEGMENT RATES

Section 430 specifies the minimum funding requirements that apply to single-employer plans (except for CSEC plans under § 414(y)) 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. To the extent provided under § 430(h)(2)(C)(iv), these segment rates are adjusted by the applicable percentage of the 25-year average segment rates for the period ending September 30 of the year preceding the calendar year in which the plan year begins.<sup>1</sup> However, an election may be made under § 430(h)(2)(D)(ii) to use the monthly yield curve in place of the segment rates.

Notice 2007-81, 2007-44 I.R.B. 899, provides guidelines for determining the monthly corporate bond yield curve, and the 24-month average corporate bond segment rates used to compute the target normal cost and the funding target. Consistent with the methodology specified in Notice 2007-81, the monthly corporate bond yield curve derived from April 2019

data is in Table 2019-4 at the end of this notice. The spot first, second, and third segment rates for the month of April 2019 are, respectively, 2.79, 3.88, and 4.33.

The 24-month average segment rates determined under § 430(h)(2)(C)(i) through (iii) must be adjusted pursuant to § 430(h)(2)(C)(iv) to be within the applicable minimum and maximum percentages of the corresponding 25-year average segment rates. For plan years beginning before 2021, the applicable minimum percentage is 90% and the applicable maximum percentage is 110%. The 25-year average segment rates for plan years beginning in 2018 and 2019 were published in Notice 2017-50, 2017-41 I.R.B. 280, and Notice 2018-73, 2018-40 I.R.B. 526, respectively.

#### 24-MONTH AVERAGE CORPORATE BOND SEGMENT RATES

The three 24-month average corporate bond segment rates applicable for May 2019 without adjustment for the 25-year average segment rate limits are as follows:

<i>24-Month Average Segment Rates Without 25-Year Average Adjustment</i>			
<b>Applicable Month</b>	<b>First Segment</b>	<b>Second Segment</b>	<b>Third Segment</b>
May 2019	2.71	3.96	4.45

Based on § 430(h)(2)(C)(iv), the 2019, adjusted to be within the applicable the corresponding 25-year average segment rates, are as follows:

<i>Adjusted 24-Month Average Segment Rates</i>				
<b>For Plan Years Beginning In</b>	<b>Applicable Month</b>	<b>First Segment</b>	<b>Second Segment</b>	<b>Third Segment</b>
2018	May 2019	3.92	5.52	6.29
2019	May 2019	3.74	5.35	6.11

#### 30-YEAR TREASURY SECURITIES INTEREST RATES

Section 431 specifies the minimum funding requirements that apply to multi-employer plans pursuant to § 412. Section 431(c)(6)(B) specifies a minimum amount

for the full-funding limitation described in § 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 aver-

age 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 rate of interest on 30-year Treasury securities

<sup>1</sup>Pursuant to § 433(h)(3)(A), the 3<sup>rd</sup> segment rate determined under § 430(h)(2)(C) is used to determine the current liability of a CSEC plan (which is used to calculate the minimum amount of the full funding limitation under § 433(c)(7)(C)).

for April 2019 is 2.94 percent. The Service determined this rate as the average of the daily determinations of yield on the 30-year

Treasury bond maturing in February 2049. For plan years beginning in May 2019, the weighted average of the rates of interest on

30-year Treasury securities and the permissible range of rates used to calculate current liability are as follows:

<i>Treasury Weighted Average Rates</i>		
<b>For Plan Years Beginning In</b>	<b>30-Year Treasury Weighted Average</b>	<b>Permissible Range</b>
May 2019	2.94	90% to 105% 2.65 to 3.09

**MINIMUM PRESENT VALUE SEGMENT RATES**

In general, the applicable interest rates

under § 417(e)(3)(D) are segment rates computed without regard to a 24-month average. Notice 2007-81 provides guidelines for determining the minimum pres-

ent value segment rates. Pursuant to that notice, the minimum present value segment rates determined for April 2019 are as follows:

<i>Minimum Present Value Segment Rates</i>			
<b>Month</b>	<b>First Segment</b>	<b>Second Segment</b>	<b>Third Segment</b>
April 2019	2.79	3.88	4.33

**DRAFTING INFORMATION**

The principal author of this notice is Tom Morgan of the Office of the Asso-

ciate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the IRS participated in the development

of this guidance. For further information regarding this notice, contact Mr. Morgan at 202-317-6700 or Paul Stern at 202-317-8702 (not toll-free numbers).

**Table 2019-4**  
 Monthly Yield Curve for April 2019  
 Derived from April 2019 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	2.65	20.5	4.26	40.5	4.34	60.5	4.37	80.5	4.39
1.0	2.70	21.0	4.26	41.0	4.34	61.0	4.37	81.0	4.39
1.5	2.74	21.5	4.26	41.5	4.34	61.5	4.37	81.5	4.39
2.0	2.77	22.0	4.27	42.0	4.34	62.0	4.37	82.0	4.39
2.5	2.79	22.5	4.27	42.5	4.34	62.5	4.38	82.5	4.39
3.0	2.80	23.0	4.27	43.0	4.35	63.0	4.38	83.0	4.39
3.5	2.82	23.5	4.27	43.5	4.35	63.5	4.38	83.5	4.39
4.0	2.84	24.0	4.28	44.0	4.35	64.0	4.38	84.0	4.39
4.5	2.89	24.5	4.28	44.5	4.35	64.5	4.38	84.5	4.39
5.0	2.94	25.0	4.28	45.0	4.35	65.0	4.38	85.0	4.39
5.5	3.01	25.5	4.28	45.5	4.35	65.5	4.38	85.5	4.39
6.0	3.08	26.0	4.28	46.0	4.35	66.0	4.38	86.0	4.39
6.5	3.17	26.5	4.29	46.5	4.35	66.5	4.38	86.5	4.39
7.0	3.26	27.0	4.29	47.0	4.35	67.0	4.38	87.0	4.39
7.5	3.34	27.5	4.29	47.5	4.35	67.5	4.38	87.5	4.39
8.0	3.43	28.0	4.29	48.0	4.36	68.0	4.38	88.0	4.39
8.5	3.52	28.5	4.30	48.5	4.36	68.5	4.38	88.5	4.39
9.0	3.60	29.0	4.30	49.0	4.36	69.0	4.38	89.0	4.40
9.5	3.68	29.5	4.30	49.5	4.36	69.5	4.38	89.5	4.40
10.0	3.75	30.0	4.30	50.0	4.36	70.0	4.38	90.0	4.40
10.5	3.82	30.5	4.31	50.5	4.36	70.5	4.38	90.5	4.40
11.0	3.88	31.0	4.31	51.0	4.36	71.0	4.38	91.0	4.40
11.5	3.93	31.5	4.31	51.5	4.36	71.5	4.38	91.5	4.40
12.0	3.98	32.0	4.31	52.0	4.36	72.0	4.38	92.0	4.40
12.5	4.02	32.5	4.31	52.5	4.36	72.5	4.38	92.5	4.40
13.0	4.06	33.0	4.32	53.0	4.36	73.0	4.39	93.0	4.40
13.5	4.09	33.5	4.32	53.5	4.36	73.5	4.39	93.5	4.40
14.0	4.12	34.0	4.32	54.0	4.37	74.0	4.39	94.0	4.40
14.5	4.15	34.5	4.32	54.5	4.37	74.5	4.39	94.5	4.40
15.0	4.17	35.0	4.32	55.0	4.37	75.0	4.39	95.0	4.40
15.5	4.18	35.5	4.33	55.5	4.37	75.5	4.39	95.5	4.40
16.0	4.20	36.0	4.33	56.0	4.37	76.0	4.39	96.0	4.40
16.5	4.21	36.5	4.33	56.5	4.37	76.5	4.39	96.5	4.40
17.0	4.22	37.0	4.33	57.0	4.37	77.0	4.39	97.0	4.40
17.5	4.23	37.5	4.33	57.5	4.37	77.5	4.39	97.5	4.40
18.0	4.24	38.0	4.33	58.0	4.37	78.0	4.39	98.0	4.40
18.5	4.24	38.5	4.33	58.5	4.37	78.5	4.39	98.5	4.40
19.0	4.25	39.0	4.34	59.0	4.37	79.0	4.39	99.0	4.40
19.5	4.25	39.5	4.34	59.5	4.37	79.5	4.39	99.5	4.40
20.0	4.26	40.0	4.34	60.0	4.37	80.0	4.39	100.0	4.40

## 2019 Section 43 Inflation Adjustment

### Notice 2019-36

Section 43(a) provides that for purposes of section 38, the enhanced oil recovery credit for any taxable year is an amount equal to 15 percent of the taxpayer's qualified enhanced oil recovery costs for such taxable year.

Section 43(b)(1) provides that the amount of the credit determined under subsection (a) for any taxable year shall be reduced by an amount which bears the same ratio to the amount of such credit (determined without regard to this para-

graph) as – (A) the amount by which the reference price for the calendar year preceding the calendar year in which the taxable year begins exceeds \$28, bears to (B) \$6.

Section 43(b)(3)(B) of the Internal Revenue Code requires the Secretary to publish an inflation adjustment factor. The enhanced oil recovery credit under § 43 for any taxable year is reduced if the “reference price,” determined under § 45K(d)(2)(C), for the calendar year preceding the calendar year in which the taxable year begins is greater than \$28 multiplied by the inflation adjustment factor for that year.

The term “inflation adjustment factor” means, with respect to any calendar year,

a fraction the numerator of which is the GNP implicit price deflator for the preceding calendar year and the denominator of which is the GNP implicit price deflator for 1990.

Because the reference price for the 2018 calendar year (\$61.41) exceeds \$28 multiplied by the inflation adjustment factor for the 2018 calendar year (\$28 multiplied by 1.7334 = \$48.5352) by \$12.88, the enhanced oil recovery credit for qualified costs paid or incurred in 2019 is phased out completely.

Table 1 contains the GNP implicit price deflator used for the 2019 calendar year, as well as the previously published GNP implicit price deflators used for the 1991 through 2018 calendar years.



Notice 2019-36 TABLE 1  
GNP IMPLICIT PRICE DEFLATORS

<i>Calendar Year</i>	<i>GNP Implicit Price Deflator</i>
1990	112.9 (used for 1991)
1991	117.0 (used for 1992)
1992	120.9 (used for 1993)
1993	124.1 (used for 1994)
1994	126.0 (used for 1995)*
1995	107.5 (used for 1996)
1996	109.7 (used for 1997)**
1997	112.35 (used for 1998)
1998	112.64 (used for 1999)***
1999	104.59 (used for 2000)
2000	106.89 (used for 2001)
2001	109.31 (used for 2002)
2002	110.63 (used for 2003)
2003	105.67 (used for 2004)****
2004	108.23 (used for 2005)
2005	112.129 (used for 2006)
2006	116.036 (used for 2007)
2007	119.656 (used for 2008)
2008	122.407 (used for 2009)
2009	109.764 (used for 2010)*****
2010	110.654 (used for 2011)
2011	113.347 (used for 2012)*****
2012	115.387 (used for 2013)
2013	106.710 (used for 2014)*****
2014	108.407 (used for 2015)*****
2015	109.868 (used for 2016)
2016	111.528 (used for 2017)
2017	113.500 (used for 2018)
2018	110.308 (used for 2019)

- \* Beginning in 1995, the GNP implicit price deflator was rebased relative to 1992. The 1990 GNP implicit price deflator used to compute the 1996 § 43 inflation adjustment factor is 93.6.
- \*\* Beginning in 1997, two digits follow the decimal point in the GNP implicit price deflator. The 1990 GNP price deflator used to compute the 1998 § 43 inflation adjustment factor is 93.63.
- \*\*\* Beginning in 1999, the GNP implicit price deflator was rebased relative to 1996. The 1990 GNP implicit price deflator used to compute the 2000 § 43 inflation adjustment factor is 86.53.
- \*\*\*\* Beginning in 2003, the GNP implicit price deflator was rebased, and the 1990 GNP implicit price deflator used to compute the 2004 § 43 inflation adjustment factor is 81.589.
- \*\*\*\*\* Beginning in 2009, the GNP implicit price deflator was rebased, and the 1990 GNP implicit price deflator used to compute the 2010 § 43 inflation adjustment factor is 72.199.
- \*\*\*\*\* Beginning in 2011, the 1990 GNP implicit price deflator used to compute the 2012 § 43 inflation adjustment factor is 72.260.
- \*\*\*\*\* Beginning in 2013, the GNP implicit price deflator was rebased, and the 1990 GNP implicit price deflator used to compute the 2014 § 43 inflation adjustment factor is 66.803.
- \*\*\*\*\* Beginning in 2014, the 1990 GNP implicit price deflator used to compute the 2015 § 43 inflation adjustment factor is 66.732.

Table 2 contains the inflation adjustment factor and the phase-out amount for taxable years beginning in the 2019 calendar year as well as the previously published inflation adjustment factors and phase-out amounts for taxable years beginning in the 1991 through 2018 calendar years.

DRAFTING INFORMATION

Notice 2019-36 TABLE 2 INFLATION ADJUSTMENT FACTORS AND PHASE-OUT AMOUNTS		
<i>Calendar Year</i>	<i>Inflation Adjustment Factor</i>	<i>Phase-out Amount</i>
1991	1.0000	0
1992	1.0363	0
1993	1.0708	0
1994	1.0992	0
1995	1.1160	0
1996	1.1485	0
1997	1.1720	0
1998	1.1999	0
1999	1.2030	0
2000	1.2087	0
2001	1.2353	0
2002	1.2633	0
2003	1.2785	0
2004	1.2952	0
2005	1.3266	0
2006	1.3743	100 percent
2007	1.4222	100 percent
2008	1.4666	100 percent
2009	1.5003	100 percent
2010	1.5203	100 percent
2011	1.5326	100 percent
2012	1.5686	100 percent
2013	1.5968	100 percent
2014	1.5974	100 percent
2015	1.6245	100 percent
2016	1.6464	0
2017	1.6713	0
2018	1.7008	1.069 percent
2019	1.7334	100 percent

The principal author of this notice is Phil Tiegerman of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, contact Phil Tiegerman at (202) 317-6853

# Reference Price for Section 45I Credit for Production of Natural Gas from Marginal Wells During Taxable Years Beginning in Calendar Year 2018

## Notice 2019-37

### SECTION 1. PURPOSE

This notice provides the applicable reference price for qualified natural gas production from qualified marginal wells during taxable years beginning in calendar year 2018 for the purpose of determining the marginal well production credit (MWC) under § 45I of the Internal Revenue Code. The applicable reference price for taxable years beginning in calendar year 2018 is \$2.68 per 1,000 cubic feet (mcf).

This notice also provides the credit amount used for the purpose of determining the MWC for taxable years beginning in calendar year 2018. The credit amount is determined using the 2018 inflation adjustment factor of 1.2739 and the applicable reference price of \$2.68 per mcf. The credit amount for taxable years beginning in calendar year 2018 is \$0. per mcf.

### SECTION 2. BACKGROUND

Section 45I(a), as it relates to qualified natural gas production, provides that, for purposes of § 38, the MWC for any taxable year is an amount equal to the product of (1) the credit amount and (2) the qualified natural gas production that is attributable to the taxpayer.

Section 45I(c)(1) provides that “qualified natural gas production” means domestic natural gas produced from a qualified marginal well. Section 45I(c)(3)(A) provides that a qualified marginal well is a domestic well (i) the production from which during the taxable year is treated as marginal production under § 613A(c)(6), or (ii) which during the taxable year (I) has average production of not more than 25 barrel-of-oil equivalents per day,

and (II) produces water at a rate of not less than 95 percent of total well effluent.

Section 613A(c)(6)(D) and (E) provide that “marginal production” means domestic natural gas produced during any taxable year from a property that is a stripper well property for the calendar year in which the taxable year begins. A “stripper well property” is, with respect to any calendar year, any property producing not more than 15 barrel equivalents per day, determined by dividing the average daily production of domestic crude oil and domestic natural gas from producing wells on the property for such calendar year by the number of such wells on the property.

Section 45I(c)(2)(A) provides that generally only the first 1,095 barrels or barrel-of-oil-equivalents (as defined in § 45K(d)(5)) produced during the taxable year qualify for the MWC. This limitation is proportionately reduced in the case of a short taxable year or in the case of a well that is not capable of production each day of a taxable year.

See § 45I(c)(2)(B). The number of wells on which a taxpayer can claim the MWC is not limited.

Section 45I(d)(2) provides that to claim the credit a taxpayer must hold an operating interest in the qualified marginal well producing the natural gas to which the credit relates. Under § 45I(d)(1) if a well is owned by more than one owner and the natural gas production exceeds the limitation under § 45I(c)(2), the qualifying natural gas production attributable to the taxpayer is determined on the basis of the ratio the taxpayer’s revenue interest in the production bears to the aggregate of the revenue interests of all operating interest owners in the production. Finally, § 45I(d)(3) provides that the MWC is not allowable if the taxpayer is also eligible to claim the § 45K nonconventional sources credit for the taxable year, unless the taxpayer elects not to claim the credit under § 45K for the well.

For purposes of § 45I(a)(1), the credit amount is 50 cents (adjusted for inflation) per mcf of qualified natural gas production (tentative credit amount). See § 45I(b)(1)(B) and (b)(2)(B).

Section 45I(b)(2)(A) and (B) provide that the tentative credit amount (adjusted

for inflation) is reduced (but not below zero) to the extent that the applicable reference price exceeds \$1.67 (adjusted for inflation). More specifically, § 45I(b)(2)(A) provides that the tentative credit amount (adjusted for inflation) is reduced by an amount that bears the same ratio to such amount as the excess (if any) of the applicable reference price over \$1.67 (adjusted for inflation), bears to \$0.33 (adjusted for inflation). As a result, the MWC is not available if the applicable reference price for qualified natural gas production exceeds \$2 (adjusted for inflation).

Section 45I(b)(2)(A) also provides that the applicable reference price for a taxable year is the reference price for the calendar year preceding the calendar year in which the taxable year begins. Section 45I(b)(2)(C)(ii) provides the term “reference price” means, with respect to any calendar year, in the case of qualified natural gas production, the Secretary’s estimate of the annual average wellhead price per mcf for all domestic natural gas.

Section 45I(b)(2)(B) provides that in the case of any taxable year beginning in a calendar year after 2005, each of the dollar amounts contained in § 45I(b)(2)(A) will be increased to an amount equal to such dollar amount multiplied by the inflation adjustment factor for such calendar year (determined under § 43(b)(3)(B) by substituting “2004” for “1990”).

### SECTION 3. INFLATION ADJUSTMENT FACTOR AND REFERENCE PRICE

1 *Inflation Adjustment.* The inflation adjustment factor under § 45I(b)(2)(B) for calendar year 2018 is 1.2739

2 *Reference Price.* The Secretary’s estimate of the calendar year 2017 annual average wellhead price per mcf for all domestic natural gas under § 45I(b)(2)(C)(ii) was calculated by applying the Producer Price Index commodity index for “Natural Gas from the Wellhead” (WPU053101051)<sup>1</sup> published by the Bureau of Labor Statistics (BLS) as part of its Producer Price Index program, to the 2016 annual average wellhead price (\$2.17) published in Notice 2018-52, 2018-22 I.R.B. 629. The annual Produc-

<sup>1</sup> <https://data.bls.gov/cgi-bin/srgate>. BLS publishes indexes and not actual or average prices.

er Price Index commodity index for natural gas published by the BLS was 67.5 in 2016 and 83.4 in 2017, which implies a ratio of 2017 to 2016 average wellhead prices of 1.236 (83.4/67.5). Therefore, the Secretary's estimate of the calendar year 2017 annual average wellhead price per mcf for all domestic natural gas is \$2.68 per mcf (1.236 x \$2.17 per mcf).

For years after 2017, the Secretary intends to continue calculating the reference price by application of the Producer Price Index commodity index for "Natural Gas from the Wellhead" (WPU053101051)

published by the BLS to the previous year's reference price.

#### SECTION 4. CALCULATION OF CREDIT AMOUNT

Under § 451(b)(1)(B) and(2)(B), the tentative credit amount used to calculate the MWC for taxable years beginning in calendar year 2018 is 64 cents per mcf (\$0.50 x 1.2739 inflation adjustment factor). However, in order to determine the credit amount for purposes of § 451(a)(1),

the tentative credit amount must be reduced as provided by § 451(b)(2)(A).

Pursuant to § 451(b)(2)(A), the tentative credit amount for taxable years beginning in calendar year 2018 is reduced (but not below zero) by an amount (§ 451(b)(2) Reduction Amount) which bears the same ratio to such amount as (i) the excess (if any) of the applicable reference price over \$2.09 (\$1.67 x 1.2739 inflation adjustment factor), bears to (ii) \$0.44 (\$0.33 x 1.2739 adjustment factor). Accordingly, the § 451(b)(2) Reduction Amount (as adjusted for inflation) is computed as follows:

$$\frac{\$ 451(b)(2) \text{ Red. Amount}}{0.64} = \frac{\text{App. Ref. Price} - 2.09}{0.42}$$

*Solving for the § 451(b)(2) Red. Amount yields the following formula:*

$$\$ 451(b)(2) \text{ Red. Amount} = \frac{0.64 \times \text{App. Ref. Price} - 2.13}{0.42}$$

Using the applicable reference price of \$2.68, the § 451(b)(2) Reduction Amount is \$0.84. Therefore, the credit amount used to calculate the MWC for taxable years beginning in calendar year 2018 is \$0. per mcf (\$0.64 - \$0.84).

#### SECTION 5. EFFECTIVE DATE

This notice is effective for qualified natural gas production during taxable years beginning in calendar year 2018.

#### SECTION 6. DRAFTING AND CONTACT INFORMATION

The principal author of this notice is Philip Tiegerman of the Office of Associate Chief Counsel (Passthroughs & Spe-

cial Industries). For further information regarding this notice contact Philip Tiegerman at (202) 317-6853 (not a toll-free number).

## 2019 Marginal Production Rates

### Notice 2019-38

This notice announces the applicable percentage under § 613A of the Internal Revenue Code to be used in determining percentage depletion for marginal properties for the 2019 calendar year.

Section 613A(c)(6)(C) defines the term "applicable percentage" for purposes of determining percentage depletion for oil and gas produced from marginal properties. The applicable percentage is the percentage (not greater than 25 percent) equal to the sum of 15 percent, plus one percentage point for each whole dollar by which \$20 exceeds the reference price (determined under § 45K(d)(2)(C)) for crude oil for the calendar year preceding the calendar year in which the taxable year begins. The reference price determined under § 45K(d)(2)(C) for the 2018 calendar year is \$61.41.

The following table contains the applicable percentages for marginal production for taxable years beginning in calendar years 1991 through 2019.

Notice 2019-  
APPLICABLE PERCENTAGE FOR MARGINAL PRODUCTION

<i>Calendar Year</i>	<i>Applicable Percentage</i>
1991	15 percent
1992	18 percent
1993	19 percent
1994	20 percent
1995	21 percent
1996	20 percent
1997	16 percent
1998	17 percent
1999	24 percent
2000	19 percent
2001	15 percent
2002	15 percent
2003	15 percent
2004	15 percent
2005	15 percent
2006	15 percent
2007	15 percent
2008	15 percent
2009	15 percent
2010	15 percent
2011	15 percent
2012	15 percent
2013	15 percent
2014	15 percent
2015	15 percent
2016	15 percent
2017	15 percent
2018	15 percent
2019	15 percent

The principal author of this notice is Phil Tiegerman of the Office of Associate Chief Counsel (Passthroughs and Special Indus

## Part IV.

### Notice of Proposed Rulemaking

REG-125135-15

### Ownership Attribution for Purposes of Determining Whether a Person Is Related to a Controlled Foreign Corporation; Rents Derived in the Active Conduct of a Trade or Business

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that provide rules regarding the attribution of ownership of stock or other interests for purposes of determining whether a person is a related person with respect to a controlled foreign corporation (CFC) under section 954(d)(3). In addition, the proposed regulations provide rules for determining whether a CFC is considered to derive rents in the active conduct of a trade or business for purposes of computing foreign personal holding company income (FPHCI). The regulations would affect United States persons with direct or indirect ownership interests in certain foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by July 19, 2019.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-125135-15), 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-125135-15), Courier's Desk, Internal Revenue Service,

1111 Constitution Avenue, NW, Washington, DC 20224, or sent electronically via the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov) (indicate IRS and REG-125135-15).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Rose E. Jenkins at (202) 317-6934; concerning submissions of comments and requests for a public hearing, Regina L. Johnson at 202-317-6901 (not toll-free numbers).

#### SUPPLEMENTARY INFORMATION:

##### Background

This document contains proposed amendments to 26 CFR part 1 under sections 954 and 958 of the Internal Revenue Code (Code). Section 954(a) defines foreign base company income (FBCI), which is a category of subpart F income. Subpart F income generally is income earned by a CFC that is taken into account in computing the amount that a United States shareholder (as defined in section 951(b)) of the CFC must include in income under section 951(a)(1)(A). FBCI includes foreign personal holding company income, as defined in section 954(c), as well as certain types of income from sales and services. The determination of whether certain types of sales and services income constitute FBCI depends, in part, on whether the income is earned from a transaction that involves a related person, as defined under section 954(d)(3). See section 954(d) and (e). The definition of related person under section 954(d)(3) is also relevant in determining whether certain income qualifies for an exception to FPHCI. See, for example, sections 954(c)(2)(A), 954(c)(3), and 954(c)(6). As provided in section 952(a)(2), subpart F income also includes insurance income (as defined under section 953), and the rules in section 953 similarly reference the definition of related person in section 954(d)(3). The definition of related person under section 954(d)(3) is also relevant in deter-

mining whether an exception to the definition of United States property applies for purposes of section 956. See section 956(c)(2)(L)(ii)(II). Additionally, certain provisions outside of subpart F<sup>1</sup> reference the definition of related person in section 954(d)(3). See, for example, sections 267A, 904(d)(2)(I), 988(a)(3)(C), 1297(b)(2), and 1471(e)(2).

Section 954(d)(3) provides that a person is a related person with respect to a CFC if the person is (i) an individual who controls the CFC; (ii) a corporation, a partnership, a trust, or an estate that controls or is controlled by the CFC; or (iii) a corporation, a partnership, a trust, or an estate that is controlled by the same person or persons that control the CFC. With respect to a corporation, control means the ownership, directly or indirectly, of stock possessing more than 50 percent of (i) the total voting power of all classes of stock entitled to vote or (ii) the total value of stock of the corporation. With respect to a partnership, trust, or estate, control means the ownership, directly or indirectly, of more than 50 percent (by value) of the beneficial interests in the partnership, trust, or estate. Section 954(d)(3) states that “rules similar to the rules of section 958 shall apply” for purposes of determining ownership. Section 958 provides rules for determining direct, indirect, and constructive stock ownership and states that such rules “shall apply” for purposes of section 954(d)(3) to the extent that the effect is to treat a person as a related person within the meaning of section 954(d)(3). See section 958(b). Sections 954(d)(3) and 958 were added to the Code in 1962, as part of the legislation that enacted the subpart F regime, and section 954(d)(3) provided as originally enacted that “the rules for determining ownership of stock prescribed by section 958 shall apply.” Revenue Act of 1962 (Public Law 87-834, 76 Stat. 960). The change in the language of section 954(d)(3) to provide for the application of rules “similar to the rules of” section 958 was made in 1986, but no corresponding change was made to the language in section 958. Tax Reform

<sup>1</sup>References in this preamble to subpart F are references to subpart F, part III, subchapter N, chapter 1 of the Code.

Act of 1986 (Public Law 99-514, 100 Stat. 2085).

Final regulations published in the **Federal Register** on May 15, 1964 (T.D. 6734, 29 FR 6385), cross-referenced section 958 and the regulations thereunder for purposes of determining ownership under section 954(d)(3) as then in effect. Final regulations published in the **Federal Register** on September 7, 1995 (T.D. 8618, 60 FR 46500), and corrected on December 4, 1995 (60 FR 62024), revised the regulations, in part to provide that the principles of section 958, modified to apply to domestic as well as foreign entities, applied for purposes of determining direct and indirect ownership under section 954(d)(3). Thus, under current §1.954-1(f)(2)(iv), the principles of section 958(a) and (b) apply, without regard to whether an entity is foreign or domestic, to determine direct and indirect ownership for section 954(d)(3) purposes. The existing regulations do not provide any additional guidance beyond this general statement. These proposed regulations would revise the existing regulations under section 954(d)(3) to provide some specific guidance on the application of principles similar to the constructive ownership rules in section 958(b).

This document also proposes to revise rules under section 954(c). FPHCI, as defined in section 954(c), generally includes rents. Section 954(c)(1)(A). However, rents are excluded from FPHCI if they are received from a person other than a related person and derived in the active conduct of a trade or business within the meaning of section 954(c)(2)(A) and §1.954-2(c) (the active rents exception). These regulations propose to revise the rules under section 954(c) to provide guidance on the treatment of amounts (including royalties) paid or incurred by a CFC in connection with the CFC's rental income for purposes of the active rents exception.

## Explanation of Provisions

### 1. *Definition of Related Person in Section 954(d)(3)*

Section 1.954-1(f)(1), like section 954(d)(3), provides that a person is a related person with respect to a CFC if the person is (i) an individual who controls

the CFC; (ii) a corporation, a partnership, a trust, or an estate that controls or is controlled by the CFC; or (iii) a corporation, a partnership, a trust, or an estate that is controlled by the same person or persons that control the CFC. Section 1.954-1(f)(2) provides that, with respect to a corporation, control means the ownership, directly or indirectly, of stock possessing more than 50 percent of the total voting power of all classes of stock entitled to vote or the total value of stock of the corporation. With respect to a trust or estate, control means the ownership, directly or indirectly, of more than 50 percent (by value) of the beneficial interests of the trust or estate. With respect to a partnership, control means the ownership, directly or indirectly, of more than 50 percent (by value) of the capital or profits interest in the partnership.

Section 954(d)(3) provides that rules similar to the rules of section 958 apply for purposes of determining whether a person is a related person. Similarly, current §1.954-1(f)(2)(iv) states that the principles of section 958 apply to determine direct or indirect ownership for purposes of §1.954-1(f) and further provides that the principles of section 958 apply without regard to whether a corporation, partnership, trust, or estate is foreign or domestic or whether an individual is a citizen or resident of the United States.

Under section 958(a)(1), stock is considered owned by a person if it is owned directly or indirectly through certain foreign entities under section 958(a)(2). In relevant part, section 958(b) provides that section 318(a) (relating to the constructive ownership of stock) applies for purposes of section 954(d)(3), subject to certain modifications, to the extent that the effect is to treat a person as a related person within the meaning of section 954(d)(3). Section §1.958-2 sets forth the rules in section 318(a) as modified by section 958(b).

Section 318 provides rules that attribute the ownership of stock to certain family members, between certain entities and their owners, and to holders of options to acquire stock. Section 318(a)(1) provides rules attributing stock ownership among members of a family, and section 318(a)(2) provides rules attributing stock ownership "upward" from an entity to the

owner of an entity. In addition, section 318(a)(3) provides specific rules that attribute the ownership of stock "downward" from the owner of an entity to the entity. In particular, section 318(a)(3)(A) provides that stock owned, directly or indirectly, by or for a partner in a partnership or a beneficiary of an estate is considered owned by the partnership or estate. This provision applies to all partners and beneficiaries without regard to the size of their interest in the partnership or estate. See also §1.958-2(d)(1)(i). Section 318(a)(3)(B) similarly provides, subject to certain exceptions, that stock owned, directly or indirectly, by or for a beneficiary of a trust (or a person who is considered an owner of a trust) is considered owned by the trust. See also §1.958-2(d)(1)(ii). In comparison, section 318(a)(3)(C) attributes stock owned, directly or indirectly, by or for a person to a corporation only if 50 percent or more in value of the stock in the corporation is owned, directly or indirectly, by the person. See also §1.958-2(d)(1)(iii). Section 318(a)(4) provides that a person that has an option to acquire stock is considered to own the stock. See also §1.958-2(e).

The Department of the Treasury (Treasury Department) and the IRS are concerned that, in certain situations, the application of the section 318(a)(3)(A) and (B) constructive ownership rules, if incorporated into §1.954-1(f) by the reference to section 958, could produce inappropriate results when defining related person for purposes of section 954(d)(3). For example, if two otherwise unrelated domestic corporations each owned interests in a partnership, the partnership would be treated under section 318(a)(3)(A) as owning any stock owned directly or indirectly by the unrelated domestic corporations. Thus, for purposes of section 954(d)(3), the partnership would be treated as controlling any corporations, including CFCs, in which one of the domestic corporations owned more than 50 percent of the stock, regardless of the size of the domestic corporation's ownership interest in the partnership, such that a CFC of one of the domestic corporations would be treated as related to a CFC of the other domestic corporation.

Treatment of the domestic corporations' CFCs as related persons with re-

spect to one another under section 954(d)(3) could be relied upon by taxpayers, for example, to treat payments of interest between the otherwise unrelated CFCs as interest that is eligible for the exception from FPHCI in section 954(c)(6). Similarly, a sale of personal property between a CFC of one domestic corporation and a CFC of the other domestic corporation could give rise to foreign base company sales income under section 954(d). The Treasury Department and the IRS do not believe that either of these results is appropriate when the domestic corporations each own 50 percent or less of the partnership because the domestic corporations (and thus their CFCs) do not have a significant relationship to each other, for purposes of section 954(d)(3), which itself refers to ownership of “more than 50 percent” of stock or other ownership interests, and subpart F more generally.

Similarly, when two unrelated domestic corporations each own exactly 50 percent of the stock of a joint venture corporation, that joint venture corporation would be treated under section 318(a)(3)(C) as owning other stock owned by the domestic corporations (including stock of CFCs) and, accordingly, could be treated as controlling the domestic corporations’ CFCs, such that a CFC of one of the domestic corporations would be treated as related to a CFC of the other domestic corporation. The Treasury Department and the IRS do not believe that section 954(d)(3) was intended to treat the CFCs of the domestic corporations as related persons with respect to each other or with respect to the joint venture corporation in these circumstances, given that no person owns more than 50 percent of both the joint venture corporation and one of the CFCs directly or indirectly, as directly or indirectly would commonly be understood. Accordingly, the Treasury Department and the IRS interpret section 954(d)(3) to qualify the application of the constructive ownership rules in section 318(a)(3).

Concerns about the application of the downward attribution rules of section 318(a)(3) similar to those discussed in this Part 1 were raised in connection with proposed regulations under section 385 (REG-108060-15) (the section 385 proposed regulations) published by the Treasury Department and the IRS in the

**Federal Register** on April 8, 2016 (81 FR 20912), as discussed in the preamble to the final regulations under section 385 (TD 9790) (the section 385 final regulations) published by the Treasury Department and the IRS in the **Federal Register** on October 21, 2016 (81 FR 72858). See Part III.B.2.c.v of the Summary of Comments and Explanation of Revisions (81 FR 72866-72867). Accordingly, the section 385 final regulations revised the rules in the section 385 proposed regulations concerning the definition of an expanded group to provide that section 318(a)(3) generally does not apply for such purpose. See §1.385-1(c)(4)(iii)(A).

As noted in the Background section of this preamble, until 1986, section 954(d)(3) and section 958(b) both provided for the rules in section 958(b) to apply for purposes of section 954(d)(3). Although section 958(b) was not changed in 1986, when section 954(d)(3) was amended to provide that rules “similar to” those in section 958 would apply, the change to section 954(d)(3) indicates that Congress intended for the Treasury Department and the IRS to prescribe rules regarding the incorporation of section 958(b) into the definition of a related person under section 954(d)(3) with such modifications as may be appropriate. For the foregoing reasons, and consistent with the section 385 final regulations, the Treasury Department and the IRS propose, pursuant to the grant of regulatory authority to the Secretary under section 7805(a), to revise §1.954-1(f) to provide that the rules of section 318(a)(3) and §1.958-2(d) do not apply for purposes of section 954(d)(3) and §1.954-1(f). Section 1.958-2 is also proposed to be revised to cross-reference the limitations on its applicability in §1.954-1(f). However, the revision to §1.954-1(f) does not preclude a corporation, partnership, trust, or estate from being treated as controlled by the same person or persons that control the CFC under the other rules that remain applicable for purposes of section 954(d)(3) and §1.954-1(f). For example, if one domestic corporation (USP1) held 51 percent of the stock of a joint venture corporation, while an unrelated domestic corporation (USP2) held 49 percent of its stock, the joint venture corporation would continue to be a related person with respect to a CFC in which USP1 owned 51

percent of the stock (CFC1) as a result of USP1’s direct ownership of more than 50 percent of both entities, notwithstanding the fact that the joint venture corporation would no longer be treated as owning the stock of CFC1 owned by USP1.

The Treasury Department and the IRS also are concerned that the application of the option attribution rule in section 318(a)(4) in the context of section 954(d)(3) could lead to inappropriate results. If, for example, two otherwise unrelated domestic corporations owned 51 percent and 49 percent, respectively, of the total value of the stock of a joint venture CFC, and the 49-percent owner also held an option to acquire an additional 2 percent of the corporation, the 49-percent owner could take the position that it, as well as the 51-percent owner, controlled the CFC for purposes of section 954(d)(3). Based on this position, payments of interest between the joint venture CFC and another CFC of the 49-percent owner would be eligible for the exception from FPHCI in section 954(c)(6). The Treasury Department and the IRS have determined that it would be inappropriate to allow taxpayers to effectively elect related person status using options in this manner. Accordingly, these proposed regulations provide that section 318(a)(4) does not apply to treat a person that has an option to acquire stock or an equity interest, or an interest similar to such an option, as owning the stock or equity interest for purposes of the section 954(d) related person definition if a principal purpose for the use of the option or similar interest is to cause a person to be treated as a related person with respect to a CFC (the option anti-abuse rule).

Section 7(d) of Notice 2007-9, 2007-1 C.B. 401, stated that regulations containing a similar rule would be issued, providing that if a principal purpose for the use of the option or similar interest is to qualify dividends, interest, rents, or royalties paid by a foreign corporation for the section 954(c)(6) exception, the dividends, interest, rents, or royalties received or accrued from such foreign corporation will not be treated as being received or accrued from a CFC payor and, therefore, will not be eligible for the section 954(c)(6) exception. Notice 2007-9 indicated that section 7(d) would



be effective for taxable years of foreign corporations beginning after December 31, 2006. Accordingly, these proposed regulations also contain, pursuant to the grant of regulatory authority to the Secretary under section 954(c)(6), the rule described in Notice 2007-9 (the Notice 2007-9 option anti-abuse rule), which is proposed to apply for taxable years of CFCs beginning after December 31, 2006, and ending before the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and for the taxable years of United States shareholders in which or with which such years end. Section 7(d) of Notice 2007-9 will be obsolete upon finalization of these proposed regulations.

Comments with respect to the section 385 proposed regulations also raised concerns regarding the application of section 318(a)(4) to options in a joint venture corporation. See Part III.B.2.c.vi of the Summary of Comments and Explanation of Revisions (81 FR 72867). The section 385 final regulations address those comments by providing that section 318(a)(4) applies only to options that are reasonably certain to be exercised as described in §1.1504-4(g). See §1.385-1(c)(4)(iii)(C). Comments are requested as to whether the concerns of the Treasury Department and the IRS concerning the application of section 318(a)(4) for purposes of the definition of related person in section 954(d)(3) would be better addressed by the proposed option anti-abuse rule or a rule similar to §1.385-1(c)(4)(iii)(C).

## 2. Active Rent Exception to FPHCI

Although rents generally are included in FPHCI under section 954(c)(1)(A), rents derived in the active conduct of a trade or business and received from a person that is not a related person are excluded from FPHCI under the active rents exception in section 954(c)(2)(A) and §1.954-2(b)(6). The section 954 regulations provide the exclusive rules for determining whether rents are derived in the active conduct of a trade or business for purposes of section 954(c)(2)(A). Specifically, §1.954-2(c) provides four alternative ways for rents to be derived in the active conduct of a trade or business, one

of which applies to rents derived by a CFC from leasing property as a result of performing marketing activities. Under this rule, the CFC derives rents in the active conduct of a trade or business when the CFC satisfies an “active marketing” test, which, among other things, requires the CFC to operate in a foreign country or countries an organization that is regularly engaged in the business of marketing, or marketing and servicing, the leased property, and that is “substantial” in relation to the amount of rents derived from the property. See §1.954-2(c)(1)(iv). Pursuant to a safe harbor in the regulations, an organization is “substantial” if its active leasing expenses equal or exceed 25 percent of the adjusted leasing profit. See §1.954-2(c)(2)(ii). The regulations generally define active leasing expenses to mean, subject to certain exceptions, deductions that are properly allocable to rental income and that would be allowable under section 162 if the CFC were a domestic corporation. See §1.954-2(c)(2)(iii). The regulations generally define adjusted leasing profit to mean the gross income of the lessor from rents, reduced by certain items. See §1.954-2(c)(2)(iv).

A CFC may derive rent from leasing property that it does not own. In that case, the CFC likely will make payments to the owner of the property, which may be characterized as rent. For purposes of applying the safe harbor, the regulations provide that rents paid or incurred by the CFC with respect to the rental income (i) are not taken into account in determining active leasing expenses (in other words, are excluded from the definition of active leasing expenses); and (ii) are taken into account for purposes of determining adjusted leasing profit (in other words, reduce the CFC’s gross income for purposes of determining adjusted leasing profit). Section 1.954-2(c)(2)(iii)(B) and (iv)(A). These rules reflect the principle that when a lessor CFC derives rents from property that it does not own, the substantiality of the CFC’s marketing organization should be determined under the safe harbor on the basis of the CFC’s income and expenses net of any payments that it makes for the use of the property.

The Treasury Department and the IRS are aware that in cases in which a lessor CFC derives rent from leasing property

that it does not own, the CFC may make payments to the owner of the property that are characterized as royalties rather than rent. For purposes of the safe harbor, there is no reason to distinguish between payments made by the CFC for the use of property based on their characterization as rents or royalties. For example, if a CFC pays \$100 for the transfer of a computer program, and in turn transfers the computer program to an unrelated person for \$150 in a transaction that is treated as a lease under §1.861-18, the determination of whether the CFC satisfies the safe harbor in §1.954-2(c)(2)(ii) should not depend on whether the transaction pursuant to which the CFC received the computer program is characterized under §1.861-18 as a license, under which the CFC pays royalties, or a lease, under which the CFC pays rents. In both cases, the CFC’s \$100 payment for use of the computer program should be excluded from active leasing expenses and reduce the CFC’s adjusted leasing profit, in order to ensure that only expenses related to the marketing organization are taken into account in assessing its substantiality. Accordingly, the Treasury Department and the IRS propose to revise §1.954-2(c)(2)(iii)(B) and §1.954-2(c)(2)(iv)(A) to apply generally to amounts paid or incurred, including both rents and royalties, by the lessor CFC for the right to use the property (or a component thereof) that generated the rental income.

## 3. Proposed Applicability Dates

These regulations generally are proposed to apply for taxable years of CFCs ending on or after the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and for the taxable years of United States shareholders in which or with which such taxable years end. However, pursuant to the authority under section 7805(b)(1)(C), the Notice 2007-9 option anti-abuse rule is proposed to apply for taxable years of CFCs beginning after December 31, 2006, and ending before the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and for the taxable years of United States shareholders in which or with which

such years end. Furthermore, pursuant to the authority under section 7805(b)(1)(B), the rules in proposed §1.954-1(f)(2)(iv)(B)(I) and (3) will apply to taxable years of CFCs ending on or after May 17, 2019, and to taxable years of United States shareholders in which or with which such taxable years end, with respect to amounts that are received or accrued by a CFC on or after May 17, 2019 to the extent the amounts are received or accrued by the CFC in advance of the period to which such amounts are attributable with a principal purpose of avoiding the application of §1.954-1(f)(2)(iv)(B)(I) or (3) with respect to such amounts. As discussed in Part 1 of this Explanation of Provisions, these rules would prevent taxpayers from effectively electing related person status in inappropriate situations, including to qualify payments for the exception from FPHCI in section 954(c)(6). Accordingly, the Treasury Department and the IRS have determined that an immediate applicability date for these rules is appropriate to address the possibility of acceleration of payments to a period before these rules are adopted as final regulations. Until the effective date of the final regulations, CFCs may rely on the rules in proposed §1.954-1(f)(2)(iv) for taxable years ending on or after May 17, 2019, provided that they consistently apply the rules in §§1.954-1(f)(2)(iv) and 1.958-2(d) and (e) for all such taxable years.

### Special Analyses

Executive Orders 13563 and 12866 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility.

The Treasury Department will submit the final regulations to the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA) for Executive Order 12866 review consider-

ation. The Treasury Department requests comment and any potential data regarding the expected impacts of this proposed regulation, including whether the impacts of this proposed regulation will have an annual effect on the economy of \$100 million or more.

Because this rulemaking is an interpretive rule and does not impose a collection of information on small entities, under 5 U.S.C. 603(a) the provisions of the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply. Accordingly, a regulatory flexibility analysis under the Regulatory Flexibility Act is not required.

Pursuant to section 7805(f), 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. The Treasury Department requests comment on the impacts of this proposed regulation on small entities and businesses.

### Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any comments that are submitted timely to the IRS as prescribed in this preamble under the "ADDRESS-ES" heading. The Treasury Department and the IRS request comments on all aspects of the proposed rules, as well as whether modifications to the attribution rules similar to those proposed to be made to §1.954-1(f) should apply for purposes other than the definition of related person under section 954(d)(3) and §1.954-1(f). All comments will be available at [www.regulations.gov](http://www.regulations.gov) or upon request. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

### Drafting Information

The principal author of these proposed regulations is Rose E. Jenkins of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS par-

ticipated in the development of these proposed regulations.

\* \* \* \* \*

### Proposed Amendments to the Regulations

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

#### PART 1—INCOME TAXES

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

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

Section 1.954-1 also issued under 26 U.S.C. 954(b) and (c).

Section 1.954-2 also issued under 26 U.S.C. 954(b) and (c).

\* \* \* \* \*

Par. 2. Section 1.954-0 is amended in paragraph (b) by adding entries for §§1.954-1(f)(3), (f)(3)(i) through (iii), (g), and (g)(1) through (4) and 1.954-2(c)(2)(v) through (viii), (d)(2)(v), (i), and (i)(1) through (3) to read as follows:

*§1.954-0 Introduction.*

\* \* \* \* \*

(b) \* \* \*

*§1.954-1 Foreign base company income.*

\* \* \* \* \*

(f) \* \* \*

(3) Applicability dates.

(i) General rule.

(ii) Option rule in paragraph (f)(2)(iv)(B)(2) of this section.

(iii) Anti-abuse rule.

(g) Distributive share of partnership income.

(1) Application of related person and country of organization tests.

(2) Application of related person test for sales and purchase transactions between a partnership and its controlled foreign corporation partner.

(3) Examples.

(4) Effective date.

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

\* \* \* \* \*

(c) \* \* \*

(2) \* \* \*

(v) Leased in foreign commerce.

(vi) Leases acquired by the CFC lessor.

(vii) Marketing of leases.

(viii) Cost sharing arrangements (CSAs).

\*\*\*\*\*

(d)\*\*\*

(2)\*\*\*

(v) Cost sharing arrangements (CSAs).

\*\*\*\*\*

(i) Applicability dates.

(1) Paragraphs (c)(2)(v) through (vii).

(2) Paragraphs (c)(2)(iii)(B) and (c)(2)(iv)(A) of this section.

(3) Other paragraphs.

Par. 3. Section 1.954-1 is amended by revising paragraph (f)(2)(iv) and adding paragraph (f)(3) to read as follows:

*§1.954-1 Foreign base company income.*

\*\*\*\*\*

(f)\*\*\*

(2)\*\*\*

(iv) *Direct or indirect ownership.* For purposes of section 954(d)(3) and this paragraph (f), to determine direct or indirect ownership--

(A) The principles of §1.958-1 and section 958(a) apply without regard to whether a corporation, partnership, trust, or estate is foreign or domestic or whether an individual is a citizen or resident of the United States; and

(B) The principles of §1.958-2 and section 958(b) apply, except that--

(1) Neither section 318(a)(3), nor §1.958-2(d) or the principles thereof, applies to attribute stock or other interests to a corporation, partnership, estate, or trust; and

(2) Neither section 318(a)(4), nor §1.958-2(e) or the principles thereof, applies to treat dividends, interest, rents, or royalties received or accrued from a foreign corporation as received or accrued from a controlled foreign corporation payor if a principal purpose of the use of an option to acquire stock or an equity interest, or an interest similar to such an option, that causes the foreign corporation to be a controlled foreign corporation payor is to qualify dividends, interest, rents, or royalties paid by the foreign corporation for the section 954(c)(6) exception. For purposes of this paragraph (f)(2)(iv)(B) (2), an interest that is similar to an option to acquire stock or an equity interest includes, but is not limited to, a warrant, a convertible debt instrument, an instrument

other than debt that is convertible into stock or an equity interest, a put, a stock or equity interest subject to risk of forfeiture, and a contract to acquire or sell stock or an equity interest.

(3) Neither section 318(a)(4), nor §1.958-2(e) or the principles thereof, applies to treat a person that has an option to acquire stock or an equity interest, or an interest similar to such an option, as owning the stock or equity interest if a principal purpose for the use of the option or similar interest is to treat a person as a related person with respect to a controlled foreign corporation under this paragraph (f). For purposes of this paragraph (f)(2)(iv)(B)(3), an interest that is similar to an option to acquire stock or an equity interest includes, but is not limited to, a warrant, a convertible debt instrument, an instrument other than debt that is convertible into stock or an equity interest, a put, a stock or equity interest subject to risk of forfeiture, and a contract to acquire or sell stock or an equity interest.

(3) *Applicability dates--(i) General rule.* Except as otherwise provided in this paragraph (f)(3), paragraph (f)(2)(iv) of this section applies to taxable years of controlled foreign corporations ending on or after the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and taxable years of United States shareholders in which or with which such taxable years end.

(ii) *Option rule in paragraph (f)(2)(iv)(B)(2) of this section.* Paragraph (f)(2)(iv)(B)(2) of this section applies to taxable years of controlled foreign corporations beginning after December 31, 2006, and ending before the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and taxable years of United States shareholders in which or with which such taxable years end.

(iii) *Anti-abuse rule.* Paragraphs (f)(2)(iv)(B)(1) and (3) of this section apply to taxable years of controlled foreign corporations ending on or after May 17, 2019, and to taxable years of United States shareholders in which or with which such taxable years end, with respect to amounts that are received or accrued by a controlled foreign corporation on or after

May 17, 2019 to the extent the amounts are received or accrued in advance of the period to which such amounts are attributable with a principal purpose of avoiding the application of paragraph (f)(2)(iv)(B) (1) or (3) of this section with respect to such amounts.

\*\*\*\*\*

Par. 4. Section 1.954-2 is amended by:

1. Revising paragraphs (c)(2)(iii)(B) and (c)(2)(iv)(A).

2. Revising the heading of paragraph (i).

3. Redesignating paragraph (i)(2) as paragraph (i)(3).

2. Adding new paragraph (i)(2).

The revisions and addition read as follows:

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

\*\*\*\*\*

(c)\*\*\*

(2)\*\*\*

(iii)\*\*\*

(B) Deductions for amounts (including rents and royalties) paid or incurred by the lessor for the right to use the property (or a component thereof) that generated the rental income;

\*\*\*\*\*

(iv)\*\*\*

(A) Amounts (including rents and royalties) paid or incurred by the lessor for the right to use the property (or a component thereof) that generated the rental income;

\*\*\*\*\*

(i) *Applicability dates.*\*\*\*

(2) *Paragraphs (c)(2)(iii)(B) and (c)(2)(iv)(A) of this section.* Paragraphs (c)(2)(iii)(B) and (c)(2)(iv)(A) of this section apply for taxable years of controlled foreign corporations ending on or after the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and for the taxable years of United States shareholders in which or with which such taxable years end.

\*\*\*\*\*

Par. 5. Section 1.958-2 is amended by revising paragraph (d)(1) introductory text and the first sentence of paragraph (e) and adding paragraph (h) to read as follows:

*§1.958-2 Constructive ownership of stock.*

\*\*\*\*\*

(d) \* \* \*

(1) \* \* \* Except as otherwise provided in paragraph (d)(2) of this section and §1.954-1(f)--

\* \* \* \* \*

(e) \* \* \* Except as otherwise provided in §1.954-1(f), if any person has an option to acquire stock, such stock shall be considered as owned by such person. \* \* \*

\* \* \* \* \*

(h) *Applicability date.* Paragraphs (d) (1) and (e) of this section apply for taxable years of controlled foreign corporations ending on or after the date of publication in the **Federal Register** of the Treasury decision adopting these rules as final regulations, and for the taxable years of United States shareholders in

which or with which such taxable years end.

Kirsten Wielobob,  
*Deputy Commissioner for Services  
and Enforcement.*

(Filed by the Office of the Federal Register on May 17, 2019, 8:45 a.m., and published in the issue of the Federal Register for May 20, 2019, 84 F.R. 22751)

# 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.  
FR.—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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<sup>1</sup>A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2018–27 through 2018–52 is in Internal Revenue Bulletin 2018–52, dated December 27, 2018.

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

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<sup>1</sup>A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2018–27 through 2018–52 is in Internal Revenue Bulletin 2018–52, dated December 27, 2018.

# **Internal Revenue Service**

## **Washington, DC 20224**

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## **INTERNAL REVENUE BULLETIN**

The Introduction at the beginning of this issue describes the purpose and content of this publication. The weekly Internal Revenue Bulletins are available at [www.irs.gov/irb/](http://www.irs.gov/irb/).

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## **We Welcome Comments About the Internal Revenue Bulletin**

If you have comments concerning the format or production of the Internal Revenue Bulletin or suggestions for improving it, we would be pleased to hear from you. You can email us your suggestions or comments through the IRS Internet Home Page ([www.irs.gov](http://www.irs.gov)) or write to the Internal Revenue Service, Publishing Division, IRB Publishing Program Desk, 1111 Constitution Ave. NW, IR-6230 Washington, DC 20224.