

HIGHLIGHTS OF THIS ISSUE

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

INCOME TAX

T.D. 8664, page 7.

Final regulations under section 6049 of the Code provide rules regarding the reporting on Form 1042-S of certain bank deposit interest paid to a U.S. bank account for an individual who is a nonresident alien of the U.S. and a Canadian resident.

T.D. 8667, page 4.

Final regulations under section 168 of the Code relate to the lease term of tax-exempt use property. These regulations also provide guidance regarding certain like-kind exchanges among related parties involving tax-exempt use property.

EXEMPT ORGANIZATIONS

Notice 96-30, page 11.

This notice provides relief from filing Form 3115, Application for Change in Accounting Method, for 501(c) organizations that are changing their federal tax accounting methods to comply with the provisions of Statement of Financial Accounting Standards, No. 116, Accounting for Contributions Received and Contributions Made (SFAS 116). This notice also discusses how a not-for-profit organization that changes its federal tax accounting methods to conform to SFAS 116 should report any adjustment required by section 481(a).

Rev. Proc. 96-32, page 14.

Low-income housing guidelines. Guidance on qualifica-

tion for tax-exemption under section 501(c)(3) is provided for organizations that provide low-income housing. The guidance includes a safe-harbor procedure to determine qualification.

Announcement 96-43, page 18.

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

ADMINISTRATIVE

Rev. Proc. 96-31, page 11.

Changes in computing depreciation or amortization. An automatic consent procedure is provided for taxpayers changing their method of accounting for depreciation or amortization for property for which less than the allowable depreciation or amortization is claimed. Rev. Proc. 92-20 modified.

Announcement 96-41, page 18.

The 1996 Form W-4, Employee's Withholding Allowance Certificate, is now available.

Announcement 96-42, page 18.

Form 8807, Certain Manufacturers and Retailers Excise Taxes, and Form 8645, Soil and Water Conservation Plan Certificate, are obsolete. The IRS has determined that taxpayers may meet the reporting and certification requirements of these forms by reporting the required information on other forms.

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the

quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, efficiency and fairness.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

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 of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

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

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

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

With the exception of the Notice of Proposed Rulemaking and the disbarment and suspension list included in this part, none of these announcements are consolidated in the Cumulative Bulletins.

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

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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.

For sale by the Superintendent of Documents U.S. Government Printing Office, Washington, D.C. 20402.

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

Section 167.—Depreciation

If a taxpayer changes from claiming less than the allowable depreciation to claiming the allowable depreciation for property subject to section 167, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

26 CFR 1.167(e)-1: Change in method.

If a taxpayer changes from claiming less than the allowable depreciation to claiming the allowable depreciation, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

Section 168.—Accelerated Cost Recovery System

26 CFR 1.168(h)(1): Like-kind exchanges involving tax-exempt use property.

T.D. 8667

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Lease Term; Exchanges of Tax-Exempt Use Property

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the lease term of tax-exempt use property. The final regulations also provide guidance regarding certain like-kind exchanges among related parties involving tax-exempt use property.

DATES: These regulations are effective April 29, 1996.

For dates of applicability see “Effective dates” section under the “SUPPLEMENTARY INFORMATION” portion of the preamble and §§1.168(h)-1(e) and 1.168(i)-2(g).

FOR FURTHER INFORMATION CONTACT: John M. Aramburu of the Office of Assistant Chief Counsel (Income Tax and Accounting) at (202) 622-4960 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains final regulations under section 168 of the Internal Revenue Code of 1986 (Code). The regulations provide guidance relating to certain exchanges of tax-exempt use property among related parties and the determination of lease term under certain circumstances. Proposed regulations (IA-18-95 [1995-1 C.B. 955]) were published in the Federal Register on April 21, 1995 (60 FR 19868). The IRS received a number of comments on the proposed regulations. A scheduled public hearing was cancelled because there were no requests to testify. After consideration of all the comments, the regulations proposed by IA-18-95 are adopted as revised by this Treasury decision. The revisions are discussed below.

Overview

Under section 168, property used in a trade or business, or held for the production of income, generally may be depreciated under the general depreciation system (GDS) using accelerated methods over relatively short recovery periods. However, certain property, including “tax-exempt use property,” must be depreciated under the alternative depreciation system (ADS) described in section 168(g). Section 168(h)(1)(A) generally defines tax-exempt use property to include tangible property (other than nonresidential real property) leased to a tax-exempt entity. For this purpose, certain foreign entities and persons are considered tax-exempt entities.

Congress subjected tax-exempt use property to a slower depreciation system than GDS to prevent tax-exempt entities from indirectly claiming tax benefits (in the form of reduced rentals) “from investment incentives for which they [would] not qualify directly, and effectively gain[ing] the advantage of taking income tax deductions and credits while having no corresponding liability to pay any tax on income from the property.” S. Rep. No. 169 (Vol. 1), 98th Cong., 2d Sess. 123 (1984).

In particular, section 168(g)(3)(A) provides that tax-exempt use property

subject to a lease must be depreciated using the straight-line method over a period equal to the greater of the property’s class life or 125 percent of the lease term. Under section 168(i)(3), options to renew generally must be taken into account in determining the lease term and the periods of certain successive leases must be aggregated with the period of an original lease.

Lease term

The proposed regulations generally include an additional period of time during which a lessee may not continue to be the lessee in the lease term if the lessee (or a related person) has agreed that one or both of them will or could be obligated to make a payment of rent, or a payment in the nature of rent, with respect to such period. The arrangements described in the proposed regulations are frequently referred to as “replacement leases.” One commentator requested that the portion of the proposed regulations dealing with replacement leases be withdrawn. The commentator argued that Congress would not have intended that the term of the replacement lease be taken into account in determining lease term. The IRS and Treasury believe that the proposed regulations are consistent with Congressional intent, and thus the final regulations retain this portion of the proposed regulations.

Another commentator indicated that application of the proposed regulations was unclear where property is subject to multiple leases, possibly involving multiple parties. The final regulations clarify that if property is subject to more than one lease (including any sublease) entered into as part of a single transaction (or a series of related transactions), the lease term shall include all periods described in one or more of such leases. Thus, for example, if one taxable corporation leases property to another taxable corporation for a 20-year term and, as part of the same transaction, the lessee subleases the property to a tax-exempt entity for a 10-year term, then the lease term of the property is 20 years, and during the period of tax-exempt use it must be depreciated using the straight line method over the greater of its class life or 25 years.

Finally, the final regulations provide that lease term also includes any period

during which the lessee (or a related party) has assumed or retained any risk of loss with respect to the property (including, for example, by holding a note secured by the property). The IRS and Treasury believe that such an arrangement is generally similar to the replacement leases described in the proposed regulations. As in the case of a replacement lease, the lessee is assuming risk with respect to the value of the property at the termination of the initial lease term. In addition, the term of the debt provides an objective indication that the useful life of the property exceeds the original term of the lease, in which case failure to include the term of the debt in the lease term could allow a tax-exempt lessee to benefit from depreciation deductions that exceed economic depreciation, which would be contrary to Congressional intent.

Like-kind exchanges

The proposed regulations also address certain transactions between related persons that are designed to circumvent the tax-exempt use property rules through the use of a like-kind exchange described in section 1031. The proposed regulations provide that property (tainted property) transferred directly or indirectly to the taxpayer by a related person (the related party) as part of, or in connection with, a transaction described in section 1031 where the related party receives tax-exempt use property (related tax-exempt use property) will, if the tainted property is subject to an allowance for depreciation, be treated in the same manner as the related tax-exempt use property for purposes of determining the allowable depreciation deduction under section 167(a). Under this rule, the tainted property is depreciated by the taxpayer over the remaining recovery period of, and using the same depreciation method and convention as that of, the related tax-exempt use property.

The rule applies only with respect to direct or indirect transfers of property involving related persons where (1) section 1031 applies to any party, and (2) a principal purpose of the transfer is to avoid or limit the application of ADS. For purposes of this rule, a person is related to another person if they bear a relationship specified in section 267(b) or section 707(b)(1). An exchange between members of a con-

solidated group in a taxable year beginning on or after July 12, 1995, will not be subject to this provision because section 1031 does not apply to intercompany transactions. See §1.1502-80(f).

No comments were received with respect to the treatment of like-kind exchanges under the proposed regulations. Accordingly, these provisions of the proposed regulations are adopted without modification by this Treasury decision.

Effective dates

The definition of lease term is generally applicable to leases entered into on or after April 20, 1995. The changes made by the final regulations apply to leases entered into after April 26, 1996. The treatment of like-kind exchanges is applicable to transfers made on or after April 20, 1995. No inference is intended by these effective dates as to the treatment of any transaction under prior law. The regulations do not preclude the application of common law doctrines (such as the substance over form or step transaction doctrines) and other authorities to transactions described in the regulations (e.g., as to whether a particular transaction should be characterized as a lease or a conditional sale for federal income tax purposes).

Special analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is John M. Aramburu of the Office of Assistant Chief Counsel

(Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

Section 1.168(h)-1 also issued under 26 U.S.C. 168. * * *

Section 1.168(i)-2 also issued under 26 U.S.C. 168. * * *

Par. 2. Sections 1.168(h)-1 and 1.168(i)-2 are added to read as follows:

§1.168(h)-1 Like-kind exchanges involving tax-exempt use property.

(a) *Scope.* (1) This section applies with respect to a direct or indirect transfer of property among related persons, including transfers made through a qualified intermediary (as defined in §1.1031(k)-1(g)(4)) or other unrelated person, (a transfer) if—

(i) Section 1031 applies to any party to the transfer or to any related transaction; and

(ii) A principal purpose of the transfer or any related transaction is to avoid or limit the application of the alternative depreciation system (within the meaning of section 168(g)).

(2) For purposes of this section, a person is related to another person if they bear a relationship specified in section 267(b) or section 707(b)(1).

(b) *Allowable depreciation deduction for property subject to this section—(1) In general.* Property (tainted property) transferred directly or indirectly to a taxpayer by a related person (related party) as part of, or in connection with, a transaction in which the related party receives tax-exempt use property (related tax-exempt use property) will, if the tainted property is subject to an allowance for depreciation, be treated in the same manner as the related tax-exempt use property for purposes of determining the allowable depreciation

deduction under section 167(a). Under this paragraph (b), the tainted property is depreciated by the taxpayer over the remaining recovery period of, and using the same depreciation method and convention as that of, the related tax-exempt use property.

(2) *Limitations*—(i) *Taxpayer's basis in related tax-exempt use property.* The rules of this paragraph (b) apply only with respect to so much of the taxpayer's basis in the tainted property as does not exceed the taxpayer's adjusted basis in the related tax-exempt use property prior to the transfer. Any excess of the taxpayer's basis in the tainted property over its adjusted basis in the related tax-exempt use property prior to the transfer is treated as property to which this section does not apply. This paragraph (b)(2)(i) does not apply if the related tax-exempt use property is not acquired from the taxpayer (e.g., if the taxpayer acquires the tainted property for cash but section 1031 nevertheless applies to the related party because the transfer involves a qualified intermediary).

(ii) *Application of section 168(i)(7).* This section does not apply to so much of the taxpayer's basis in the tainted property as is subject to section 168(i)(7).

(c) *Related tax-exempt use property.*

(1) For purposes of paragraph (b) of this section, related tax-exempt use property includes—

(i) Property that is tax-exempt use property (as defined in section 168(h)) at the time of the transfer; and

(ii) Property that does not become tax-exempt use property until after the transfer if, at the time of the transfer, it was intended that the property become tax-exempt use property.

(2) For purposes of determining the remaining recovery period of the related tax-exempt use property in the circumstances described in paragraph (c)(1)(ii) of this section, the related tax-exempt use property will be treated as having, prior to the transfer, a lease term equal to the term of any lease that causes such property to become tax-exempt use property.

(d) *Examples.* The following examples illustrate the application of this section. The examples do not address common law doctrines or other authorities that may apply to recharacterize or alter the effects of the transactions described therein. Unless otherwise indicated, parties to the

transactions are not related to one another.

Example 1. (i) X owns all of the stock of two subsidiaries, B and Z. X, B and Z do not file a consolidated federal income tax return. On May 5, 1995, B purchases an aircraft (FA) for \$1 million and leases it to a foreign airline whose income is not subject to United States taxation and which is a tax-exempt entity as defined in section 168(h)(2). On the same date, Z owns an aircraft (DA) with a fair market value of \$1 million, which has been, and continues to be, leased to an airline that is a United States taxpayer. Z's adjusted basis in DA is \$0. The next day, at a time when each aircraft is still worth \$1 million, B transfers FA to Z (subject to the lease to the foreign airline) in exchange for DA (subject to the lease to the airline that is a United States taxpayer). Z realizes gain of \$1 million on the exchange, but that gain is not recognized pursuant to section 1031(a) because the exchange is of like-kind properties. Assume that a principal purpose of the transfer of DA to B or of FA to Z is to avoid the application of the alternative depreciation system. Following the exchange, Z has a \$0 basis in FA pursuant to section 1031(d). B has a \$1 million basis in DA.

(ii) B has acquired property from Z, a related person; Z's gain is not recognized pursuant to section 1031(a); Z has received tax-exempt use property as part of the transaction; and a principal purpose of the transfer of DA to B or of FA to Z is to avoid the application of the alternative depreciation system. Accordingly, the transaction is within the scope of this section. Pursuant to paragraph (b) of this section, B must recover its \$1 million basis in DA over the remaining recovery period of, and using the same depreciation method and convention as that of, FA, the related tax-exempt use property.

(iii) If FA did not become tax-exempt use property until after the exchange, it would still be related tax-exempt use property and paragraph (b) of this section would apply if, at the time of the exchange, it was intended that FA become tax-exempt use property.

Example 2. (i) X owns all of the stock of two subsidiaries, B and Z. X, B and Z do not file a consolidated federal income tax return. B and Z each own identical aircraft. B's aircraft (FA) is leased to a tax-exempt entity as defined in section 168(h)(2) and has a fair market value of \$1 million and an adjusted basis of \$500,000. Z's aircraft (DA) is leased to a United States taxpayer and has a fair market value of \$1 million and an adjusted basis of \$10,000. On May 1, 1995, B and Z exchange aircraft, subject to their respective leases. B realizes gain of \$500,000 and Z realizes gain of \$990,000, but neither person recognizes gain because of the operation of section 1031(a). Moreover, assume that a principal purpose of the transfer of DA to B or of FA to Z is to avoid the application of the alternative depreciation system.

(ii) As in *Example 1*, B has acquired property from Z, a related person; Z's gain is not recognized pursuant to section 1031(a); Z has received tax-exempt use property as part of the transaction; and a principal purpose of the transfer of DA to B or of FA to Z is to avoid the application of the alternative depreciation system. Thus, the transaction is within the scope of this section even though B has held tax-exempt use property for a period of time and, during that time, has used the alternative depreciation system with respect to such property. Pursuant to

paragraph (b) of this section, B, which has a substituted basis determined pursuant to section 1031(d) of \$500,000 in DA, must depreciate the aircraft over the remaining recovery period of FA, using the same depreciation method and convention. Z holds tax-exempt use property with a basis of \$10,000, which must be depreciated under the alternative depreciation system.

(iii) Assume the same facts as in paragraph (i) of this *Example 2*, except that B and Z are members of an affiliated group that files a consolidated federal income tax return. Of B's \$500,000 basis in DA, \$10,000 is subject to section 168(i)(7) and therefore not subject to this section. The remaining \$490,000 of basis is subject to this section. But see §1.1502-80(f) making section 1031 inapplicable to intercompany transactions occurring in consolidated return years beginning on or after July 12, 1995.

(e) *Effective date.* This section applies to transfers made on or after April 20, 1995.

§1.168(i)-2 *Lease term.*

(a) *In general.* For purposes of section 168, a lease term is determined under all the facts and circumstances. Paragraph (b) of this section and §1.168(j)-1T, Q&A 17, describe certain circumstances that will result in a period of time not included in the stated duration of an original lease (additional period) nevertheless being included in the lease term. These rules do not prevent the inclusion of an additional period in the lease term in other circumstances.

(b) *Lessee retains financial obligation*—(1) *In general.* An additional period of time during which a lessee may not continue to be the lessee will nevertheless be included in the lease term if the lessee (or a related person)—

(i) Has agreed that one or both of them will or could be obligated to make a payment of rent or a payment in the nature of rent with respect to such period; or

(ii) Has assumed or retained any risk of loss with respect to the property for such period (including, for example, by holding a note secured by the property).

(2) *Payments in the nature of rent.* For purposes of paragraph (b)(1)(i) of this section, a payment in the nature of rent includes a payment intended to substitute for rent or to fund or supplement the rental payments of another. For example, a payment in the nature of rent includes a payment of any kind (whether denominated as supplemental

rent, as liquidated damages, or otherwise) that is required to be made in the event that—

(i) The leased property is not leased for the additional period;

(ii) The leased property is leased for the additional period under terms that do not satisfy specified terms and conditions;

(iii) There is a failure to make a payment of rent with respect to such additional period; or

(iv) Circumstances similar to those described in paragraph (b)(2)(i), (ii), or (iii) of this section occur.

(3) *De minimis rule.* For the purposes of this paragraph (b), obligations to make de minimis payments will be disregarded.

(c) *Multiple leases or subleases.* If property is subject to more than one lease (including any sublease) entered into as part of a single transaction (or a series of related transactions), the lease term includes all periods described in one or more of such leases. For example, if one taxable corporation leases property to another taxable corporation for a 20-year term and, as part of the same transaction, the lessee subleases the property to a tax-exempt entity for a 10-year term, then the lease term of the property for purposes of section 168 is 20 years. During the period of tax-exempt use, the property must be depreciated under the alternative depreciation system using the straight line method over the greater of its class life or 25 years (125 percent of the 20-year lease term).

(d) *Related person.* For purposes of paragraph (b) of this section, a person is related to the lessee if such person is described in section 168(h)(4).

(e) *Changes in status.* Section 168(i)(5) (changes in status) applies if an additional period is included in a lease term under this section and the leased property ceases to be tax-exempt use property for such additional period.

(f) *Example.* The following example illustrates the principles of this section. The example does not address common law doctrines or other authorities that may apply to cause an additional period to be included in the lease term or to recharacterize a lease as a conditional sale or otherwise for federal income tax purposes. Unless otherwise indicated, parties to the transactions are not related to one another.

Example. Financial obligation with respect to an additional period—(i) Facts. X, a taxable

corporation, and Y, a foreign airline whose income is not subject to United States taxation, enter into a lease agreement under which X agrees to lease an aircraft to Y for a period of 10 years. The lease agreement provides that, at the end of the lease period, Y is obligated to find a subsequent lessee (replacement lessee) to enter into a subsequent lease (replacement lease) of the aircraft from X for an additional 10-year period. The provisions of the lease agreement require that any replacement lessee be unrelated to Y and that it not be a tax-exempt entity as defined in section 168(h)(2). The provisions of the lease agreement also set forth the basic terms and conditions of the replacement lease, including its duration and the required rental payments. In the event Y fails to secure a replacement lease, the lease agreement requires Y to make a payment to X in an amount determined under the lease agreement.

(ii) *Application of this section.* The lease agreement between X and Y obligates Y to make a payment in the event the aircraft is not leased for the period commencing after the initial 10-year lease period and ending on the date the replacement lease is scheduled to end. Accordingly, pursuant to paragraph (b) of this section, the term of the lease between X and Y includes such additional period, and the lease term is 20 years for purposes of section 168.

(iii) *Facts modified.* Assume the same facts as in paragraph (i) of this *Example*, except that Y is required to guarantee the payment of rentals under the 10-year replacement lease and to make a payment to X equal to the present value of any excess of the replacement lease rental payments specified in the lease agreement between X and Y, over the rental payments actually agreed to be paid by the replacement lessee. Pursuant to paragraph (b) of this section, the term of the lease between X and Y includes the additional period, and the lease term is 20 years for purposes of section 168.

(iv) *Changes in status.* If, upon the conclusion of the stated duration of the lease between X and Y, the aircraft either is returned to X or leased to a replacement lessee that is not a tax-exempt entity as defined in section 168(h)(2), the subsequent method of depreciation will be determined pursuant to section 168(i)(5).

(g) *Effective date—(1) In general.* Except as provided in paragraph (g)(2) of this section, this section applies to leases entered into on or after April 20, 1995.

(2) *Special rules.* Paragraphs (b)(1)-(ii) and (c) of this section apply to leases entered into after April 26, 1996.

Margaret Milner Richardson,
Commissioner of Internal Revenue

Approved March 26, 1996.

Leslie Samuels,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on April 26, 1996, 8:45 a.m., and published in the issue of the Federal Register for April 29, 1996, 61 F.R. 18675)

Section 168.—Accelerated Cost Recovery System

If a taxpayer changes from claiming less than the allowable depreciation to claiming the allowable depreciation for property subject to section 168, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

Section 197.—Amortization of Goodwill and Certain Other Intangibles

If a taxpayer changes from claiming less than the allowable amortization to claiming the allowable amortization for an amortizable section 197 intangible, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

Section 446.—General Rule for Methods of Accounting

If a taxpayer changes from claiming less than the allowable depreciation or amortization to claiming the allowable depreciation or amortization, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

26 CFR 1.446-1: General rule for methods of accounting.

If a taxpayer changes from claiming less than the allowable depreciation or amortization to claiming the allowable depreciation or amortization, is this change a change in method of accounting. See Rev. Proc. 96-31, page 11.

Section 6049.—Returns Regarding Payments of Interest

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

T.D. 8664

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1, 31 and 602

Information Reporting and Backup Withholding

Agency: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide rules

regarding the reporting on Form 1042-S of certain bank deposit interest paid with respect to a United States bank account to an individual who is a nonresident alien of the United States and a resident of Canada. The IRS has determined that information concerning those deposits would be of significant use in furthering its compliance efforts, which include exchange of tax information with Canada.

EFFECTIVE DATE: January 1, 1997.

FOR FURTHER INFORMATION CONTACT: Teresa Burrige Hughes, (202) 622-3880 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this final regulation has been reviewed and approved by the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-0096. Responses to this collection of information are mandatory.

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

The estimated annual burden per respondent/recordkeeper is approximately .10 hour, depending on individual circumstances.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be directed to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, PC:FP, Washington DC 20224, and the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

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

Background

This document contains final regulations to be added to the Income Tax Regulations (26 CFR part 1) under section 6049 of the Internal Revenue Code (Code). The final regulations provide rules regarding reporting on Form 1042-S of certain bank deposit interest paid with respect to a United States bank account to a nonresident alien individual who is a resident of Canada.

Proposed regulations on this subject were set forth, at §§1.6049-5(e)(2), 1.6049-6(e)(6), and 31.3406(a)-3(b)(1), in a notice of proposed rulemaking published in the Federal Register (53 FR 5991) on February 29, 1988 [INTL-52-86 (1988-1 C.B. 892)]. The IRS received comments on the proposed regulations and held a public hearing on June 15, 1989. Having considered the comments and the statements made at the hearing, the IRS and the Treasury Department adopt the proposed regulations as modified by this Treasury decision.

Explanation of Provisions

A. Reporting of payments to Canadians

This Treasury decision requires reporting on a Form 1042-S of certain interest paid on deposits maintained at a bank's office within the United States when paid to a nonresident alien individual who is a resident of Canada. However, interest on certain bearer certificates of deposit targeted to foreign persons is excepted from the reporting requirement if the interest is paid outside the United States. This final regulation makes an exception to the current rule, based on §1.6049-5(b), that certain interest amounts paid to non-U.S. persons is not subject to reporting if a statement certifying non-U.S. status is furnished to the payor or middleman on a Form W-8 (Certificate of Foreign Status), as described in §1.6049-5(b)(2)(iv). However, although bank deposit interest paid to Canadians is made subject to reporting under this final regulation, backup withholding under section 3406 is not required. Further, in response to suggestions from commentators that segregating interest amounts on the basis of residence would be burdensome, this final regulation allows payors volun-

tarily to report on a Form 1042-S payments to all foreign persons receiving bank deposit interest without segregating on the basis of residency.

The payor determines whether a payee is a Canadian resident based on the address in the country of permanent residence required to be provided on the Form W-8. However, if the payor has actual knowledge that the payee is a U.S. person, Form 1099 reporting provisions apply.

See proposed regulations published elsewhere in this issue of the Federal Register regarding proposed changes to the notice of proposed rulemaking published in the Federal Register on February 29, 1988.

B. Comments on Canadian reporting provisions

Commentors stated that imposing information reporting with respect to deposits of nonresident aliens may undercut the competitiveness of U.S. banks. The IRS and Treasury considered these comments but, in light of our obligations under the United States-Canada income tax treaty and the reporting by Canadian banks of U.S. depositor interest to Canadian tax authorities, have decided to finalize these proposed regulations.

In response to comments that the reporting requirement be delayed, or at least that a transition period be allowed, because of the time required to identify Canadian account holders and to modify processing systems for reporting purposes, the new reporting requirement will be phased in over a three-year period, starting with payments made on or after January 1, 1997. On or after that date, payors will identify Canadian account holders as Forms W-8 are received from new depositors or renewed by existing depositors. Upon identifying account holders as Canadians, payors must begin reporting bank deposit interest paid to those persons.

Commentors also requested that the IRS develop and permit Form 1042-S reporting on magnetic diskette, as is allowed for Form 1099 filings; permit the Form 1042-S to be the transmittal document for the Form 1042-S filing; and allow financial institutions to file separate tapes or diskettes for each area of the bank, rather than bank-wide. These filing changes have previously been made by the IRS and require no further action.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required.

Drafting Information

The principal author of these regulations is Teresa Burridge Hughes, Office of Associate Chief Counsel (International). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1, 31 and 602 are amended as follows:

PART 1—INCOME TAXES

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

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

Sections 1.6049-4 also issued under 26 U.S.C. 6049(a), (b), (c), and (d).

Section 1.6049-5 also issued under 26 U.S.C. 6049(a), (b), (c), and (d). * * *

Par. 2. Section 1.6049-4 is amended by:

1. Removing the reference “(b)(3)” and adding “(b)(3) and (b)(5)” in its place in the first sentence of paragraphs (b)(1) and (b)(2) introductory text.
2. Revising the first sentence of paragraphs (b)(3) and (b)(4).
3. Adding paragraph (b)(5).
4. Removing the authority citation at the end of the section.

The revisions and addition read as follows:

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

* * * * *

(b) * * *

(3) * * * Except as provided in paragraph (b)(5) of this section, every person acting as a middleman (as defined in paragraph (f)(4) of this section) shall make an information return on Forms 1096 and 1099 for the calendar year. * * *

(4) * * * Except as provided in paragraph (b)(5) of this section, every person carrying on the banking business who makes payments of interest to another person (whether or not aggregating \$10 or more) during a calendar year with respect to a certificate of deposit issued in bearer form shall make an information return on Forms 1096 and 1099. * * *

(5) *Interest payments to Canadian nonresident alien individuals*—(i) *General rule.* In the case of interest paid to a Canadian nonresident alien individual (as described in §1.6049-8(a)), the payor or middleman shall make an information return on Form 1042-S for the calendar year in which the interest is paid. The payor or middleman shall prepare and transmit Form 1042-S at the time and in the manner prescribed by section 1461 and the regulations under that section and by the form and its accompanying instructions. See §1.6049-6(e)(4) for furnishing a copy of the Form 1042-S to the payee. To determine whether an information return is required for original issue discount, see §§1.6049-5(c) and 1.6049-8(a).

(ii) *Effective date.* Paragraph (b)(5)(i) of this section shall be effective for payments made after December 31, 1996 with respect to a Form W-8 (Certificate of Foreign Status) furnished to the payor or middleman after that date.

* * * * *

Par. 3. Section 1.6049-5 is amended by:

1. Revising the introductory text of paragraph (b)(1).
2. Revising the last sentence in paragraph (c).
3. Removing authority citation at the end of the section.

The revisions read as follows:

§1.6049-5 Interest and original issue discount subject to reporting after December 31, 1982.

* * * * *

(b) * * * (1) * * * Subject to the provisions of §1.6049-8, the term *interest* does not include:

* * * * *

(c) * * * Original issue discount on an obligation (including an obligation with a maturity of not more than 6 months from the date of original issue) held by a nonresident alien individual or foreign corporation is interest described in paragraph (b)(1)(vi)(A) or (B) of this section and, therefore is not interest subject to reporting under section 6049 unless it is described in §1.6049-8(a) (relating to bank deposit interest paid to a Canadian nonresident alien individual).

Par. 4. Section 1.6049-6 is amended by:

1. Redesignating paragraph (e)(4) as paragraph (e)(5).
 2. Adding new paragraph (e)(4).
- The addition reads as follows:

§1.6049-6 Statements to recipients of interest payments and holders of obligations for attributed original issue discount.

* * * * *

(e) * * *

(4) *Special rule for amounts described in §1.6049-8(a) paid after December 31, 1996.* In the case of amounts described in §1.6049-8(a) (relating to payments of interest to Canadian nonresident alien individuals) paid after December 31, 1996, any person who makes a Form 1042-S under section 6049(a) and §1.6049-4(b)(5) shall furnish a statement to the recipient. The statement shall include a copy of the Form 1042-S required to be prepared pursuant to §1.6049-4(b)(5) and a statement to the effect that the information on the Form is being furnished to the United States Internal Revenue Service and may be furnished to Canada.

* * * * *

Par. 5. Section 1.6049-8 is added to read as follows:

§1.6049-8 Interest and original issue discount paid to residents of Canada.

(a) *Interest subject to reporting requirement.* For purposes of §§1.6049-4, 1.6049-6 and this section and except as provided in paragraph (b) of this

section, the term *interest* means interest paid to a Canadian nonresident alien individual after December 31, 1996, where the interest is described in section 871(i)(2)(A) with respect to a deposit maintained at an office within the United States. For purposes of the regulations under section 6049, a Canadian nonresident alien individual is an individual who resides in Canada and is not a United States citizen. The payor or middleman may rely upon the permanent residence address (as defined in section 1441 and the regulations under that section) as stated on the Form W-8 (described in section 6049 and the regulations under that section) in order to determine whether the payment is made to a Canadian nonresident alien individual. Amounts described in this paragraph (a) are not subject to backup withholding under section 3406. See §31.3406(g)-1(d) of this chapter.

(b) *Interest excluded from reporting requirement.* The term *interest* does not include an amount that is paid by the issuer or its agent outside the United States with respect to an obligation that is described in paragraph (b)(1) or (2) of this section.

(1)(i) The obligation is not in registered form (within the meaning of section 163(f) and the regulations thereunder); is part of a larger single public offering of securities; and is described in section 163(f)(2)(B).

(ii) Unless it has actual knowledge to the contrary, a middleman may treat an obligation as if it is described in section 163(f)(2)(B) if the obligation or coupon therefrom, whichever is presented for payment, contains the statement described in section 163(f)(2)(B)(ii)(II) and the regulations thereunder.

(2)(i) The obligation has a face or principal amount of not less than \$500,000, and satisfies the requirements described in paragraphs (b)(2)(i)(A), (B), and (C) of this section.

(A) The obligation satisfies the requirements of sections 163(f)(2)(B)(i) and (ii)(I) and the regulations thereunder (as if it were a registration-required obligation within the meaning of section 163(f)(2)(A)) and is issued in accordance with the procedures of §1.163-5(c)(2)(i)(D)).

(B) If the obligation is in registered form, it is registered in the name of an exempt recipient described in §1.6049-4(c)(1)(ii).

(C) The obligation has on its face and on any detachable coupons the following statement (or a similar statement having the same effect): “By accepting this obligation or coupon, the holder represents and warrants that it is not a United States person (other than an exempt recipient described in the regulations under section 6049(b)(4) of the Internal Revenue Code and the regulations thereunder) and that it is not acting for or on behalf of a United States person (other than an exempt recipient described in the regulations under section 6049(b)(4) of the Internal Revenue Code and the regulations thereunder).”

(ii) Unless the middleman has actual knowledge to the contrary, it may treat an obligation as satisfying the requirements of sections 163(f)(2)(B)(i) and (ii)(I) and the regulations thereunder if the obligation or a coupon therefrom, whichever is presented for payment, contains the statement in paragraph (b)(2)(i)(C) of this section.

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

Par. 6. The authority for part 31 continues to read in part as follows:

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

Par. 7. Section 31.3406(g)-1 is amended by adding paragraph (d) to read as follows:

§31.3406(g)-1 Exception for payments to certain payees and certain other payments.

* * * * *

(d) *Reportable payments made to Canadian nonresident alien individuals.* A payment of interest made to a Canadian nonresident alien individual under §1.6049-8(a) of this chapter is not subject to withholding under section 3406.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 8. The authority for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 9. Section 602.101, paragraph (c) is amended by removing the entry “§31.3406(a)-1 – §31.3406(i)-1” and adding entries to the table in numerical order to read as follows:

§602.101 OMB Control numbers.

* * * * *

(c) * * *

CFR part or section where identified and described	Current OMB control number
* * * * *	
1.6049-6	1545-0096
* * * * *	
31.3406(a)-1	1545-0112
31.3406(a)-2	1545-0112
31.3406(a)-3	1545-0112
31.3406(a)-4	1545-0112
31.3406(b)(2)-1	1545-0112
31.3406(b)(2)-2	1545-0112
31.3406(b)(2)-3	1545-0112
31.3406(b)(2)-4	1545-0112
31.3406(b)(2)-5	1545-0112
31.3406(b)(3)-1	1545-0112
31.3406(b)(3)-2	1545-0112
31.3406(b)(3)-3	1545-0112
31.3406(b)(3)-4	1545-0112
31.3406(b)(4)-1	1545-0112
31.3406(c)-1	1545-0112
31.3406(d)-1	1545-0112
31.3406(d)-2	1545-0112
31.3406(d)-3	1545-0112
31.3406(d)-4	1545-0112
31.3406(e)-1	1545-0112
31.3406(f)-1	1545-0112
31.3406(g)-1	1545-0096
	1545-0112
31.3406(g)-2	1545-0112
31.3406(g)-3	1545-0112
31.3406(h)-1	1545-0112
31.3406(h)-2	1545-0112
31.3406(h)-3	1545-0112
31.3406(i)-1	1545-0112
* * * * *	

Margaret Milner Richardson,
Commissioner of Internal Revenue.

Approved March 27, 1996.

Leslie Samuels,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on April 15, 1996, 10:24 a.m., and published in the issue of the Federal Register for April 22, 1996, 61 F.R. 17572)

Part III. Administrative, Procedural, and Miscellaneous

Relief from Filing Form 3115 for a Change in Methods of Accounting Required by Statement of Financial Accounting Standards No. 116

Notice 96-30

The purpose of this Notice is to provide relief from filing Form 3115, Application for Change in Accounting Method, to organizations described in section 501(c) of the Internal Revenue Code that are changing their methods of accounting for federal income tax purposes to comply with the provisions of Statement of Financial Accounting Standards No. 116, Accounting for Contributions Received and Contributions Made (SFAS 116).

In SFAS 116 the Financial Accounting Standards Board revised certain generally accepted accounting principles relating to contributions received and contributions awarded by not-for-profit organizations. Not-for-profit organizations described in section 501(c) of the Code that change to the methods of accounting provided in SFAS 116 for federal income tax purposes, will not be required, in this situation, to file Form 3115, Application for Change in Accounting Method.

Not-for-profit organizations described in section 501(c) may change to the methods provided in SFAS 116 for federal income tax purposes for any tax year beginning after December 15, 1994, by properly reflecting the effect of the change, in the manner described below, on a timely filed (including extensions) Form 990-series return for the tax year of the change. Any not-for-profit organization described in section 501(c) that is not required to file a Form 990-series information return for the tax year of the change may change to the methods provided in SFAS 116 for federal income tax purposes without notifying the Service of the change.

A not-for-profit organization that changes its methods of accounting for federal income tax purposes to conform to the methods provided in SFAS 116 should report any adjustment required by section 481(a) on line 20 of Form 990 or 990-EZ or in Part III of Form 990-PF as a net asset adjustment made during the year the change is made. The adjustment should be identified as the effect of changing to the methods

provided in SFAS 116. The beginning of year statement of financial position (balance sheet) should not be restated to reflect any prior period adjustments. If the adjustment reflects contributions not reported under the old methods for year(s) preceding the year of change and not reported under the new methods in the year of change or any subsequent year, any contributor of an amount included in the adjustment who meets the criteria described in the instructions to line 1 of Form 990 or 990-EZ or line 1 of Part 1 of Form 990-PF should be included in the list of contributors required to be attached to Form 990, 990-EZ or 990-PF for the year of the change.

For further information regarding this notice, contact John Roman Faron at (202) 622-7645 (not a toll free call).

26 CFR 601.204: Changes in accounting periods and in methods of accounting. (Also Part I, §§ 167, 168, 197, 446; 1.167(e)-1, 1.446-1)

Rev. Proc. 96-31

SECTION 1. PURPOSE

This revenue procedure provides an automatic consent procedure that permits a taxpayer who has claimed less than the depreciation or amortization allowable to change the taxpayer's method of accounting to claim allowable depreciation or amortization. The omitted depreciation or amortization from years prior to the year of change will be taken into account through a § 481(a) adjustment. The taxpayer has the option of either making the method change under this revenue procedure or requesting permission to make the method change under Rev. Proc. 92-20, 1992-1 C.B. 685 (or any successor).

SECTION 2. BACKGROUND

.01 A change from not claiming the depreciation or amortization allowable (hereafter, depreciation means depreciation or amortization) to claiming the depreciation allowable is a change in method of accounting for which the consent of the Commissioner of Internal Revenue is required. Sections

1.167(e)-1(a) and 1.446-1(e)(2)(ii)(b) of the Income Tax Regulations.

.02 To obtain this consent, a Form 3115, Application for Change in Accounting Method, generally must be filed within 180 days after the beginning of the taxable year in which the proposed change is to be made. Section 1.446-1(e)(3)(i).

.03 The Commissioner is authorized to prescribe administrative procedures setting forth the limitations, terms, and conditions as the Commissioner deems necessary to obtain consent for effecting a change in method of accounting and to prevent amounts from being duplicated or omitted, including the taxable year or years in which the § 481(a) adjustment is to be taken into account. Section 1.446-1(e)(3)(ii).

.04 In computing taxable income, § 481(a) of the Internal Revenue Code requires a taxpayer to take into account those adjustments necessary to prevent amounts from being duplicated or omitted when the taxpayer's taxable income is computed under a method of accounting different from the method used to compute taxable income for the preceding taxable year.

.05 The basis of depreciable property is reduced by the amount of the depreciation allowed or allowable, whichever is greater. Section 1016(a)(2).

.06 Unless otherwise provided in this revenue procedure, the terms "taxpayer", "year of change", and "filed" have the meaning given to them by sections 3.01, 3.03, and 3.04 of Rev. Proc. 92-20 (or any successor), respectively.

SECTION 3. SCOPE

.01 *Application of this revenue procedure.* Except as provided in sections 3.02 and 3.03 of this revenue procedure, this revenue procedure applies to any taxpayer changing to a permissible method of accounting for depreciation for any item of property that: (1) under the taxpayer's present method of accounting, the taxpayer has not taken into account any depreciation allowance or has taken into account some depreciation but less than the depreciation allowable (hereafter, referred to as claimed less than the depreciation allowable); (2) is subject to § 167,

§ 168, § 197, or § 168 prior to its amendment in 1986 (former § 168); and (3) is held by the taxpayer as of the beginning of the year of change.

.02 *Non-application of this revenue procedure.* This revenue procedure does not apply to:

(1) Any property to which § 1016(a)(3) (generally relating to property held by a tax-exempt organization) applies;

(2) Any intangible property subject to § 167, except for property subject to § 167(f) (pertaining to certain property excluded from § 197);

(3) Any property for which a taxpayer is seeking either to revoke a timely election, or to make a late election, under § 167, § 168, former § 168, or § 13261(g)(2) or (3) of the Revenue Reconciliation Act of 1993 (the "1993 Act"), 1993-3 C.B. 1, 128 (relating to amortizable § 197 intangibles). A taxpayer may request consent to revoke or make the election by submitting a request for a letter ruling under Rev. Proc. 96-1, 1996-1 I.R.B. 8 (or any successor);

(4) Except for property subject to § 167(f), any property subject to § 167 for which a taxpayer is changing only the estimated useful life of the property. A change in the estimated useful life of property subject to § 167 must be made prospectively. *See, e.g.,* § 1.167(b)-2(c);

(5) Any depreciable property that changes use but continues to be owned by the same taxpayer. *See, e.g.,* § 168(i)(5);

(6) Any property for which a taxpayer has claimed depreciation in excess of the depreciation allowable;

(7) Any change in method of accounting involving a change from deducting the cost or other basis of any property as an expense to capitalizing and depreciating the cost or other basis;

(8) Any change in method of accounting involving a change from one permissible method of accounting for the property to another permissible method of accounting for the property. For example, a:

(a) Change from the straight-line method of depreciation to the income forecast method of depreciation for videocassettes. *See* Rev. Rul. 89-62, 1989-1 C.B. 78; or

(b) Change from charging the depreciation reserve with costs of removal and crediting the depreciation

reserve with salvage proceeds to deducting costs of removal as an expense and including salvage proceeds in taxable income. *See* Rev. Rul. 74-455, 1974-2 C.B. 63; or

(9) Any change in method of accounting for an item of income or deduction other than depreciation even if a taxpayer's present method of accounting may have resulted in the taxpayer claiming less than the depreciation allowable. For example, a change in accounting method involving a:

(a) Change in inventory costs (for example, when property is reclassified from inventory property to depreciable property); or

(b) Change in the character of a transaction from sale to lease.

.03 *Taxpayer under criminal investigation or proceeding.* If a criminal investigation or proceeding is pending concerning (1) any issue directly or indirectly related to a taxpayer's federal tax liability for any taxable year, or (2) the possibility of false or fraudulent statements made by the taxpayer regarding any issue related to the taxpayer's federal tax liability for any taxable year, this revenue procedure does not apply to the taxpayer.

.04 *Procedures available when a method change may not be made under this revenue procedure.* If a change in accounting method is not permitted under this revenue procedure solely by reason of section 3.02(1), 3.02(2), 3.02(6), 3.02(7), 3.02(8), or 3.02(9) of this revenue procedure, a taxpayer must file a Form 3115 in accordance with the requirements of either Rev. Proc. 92-20 (or any successor) or any other applicable revenue procedure pertaining to the method change. Thus, for example, if a taxpayer wants to change from claiming more than the depreciation allowable on some items of property but also opts to use this revenue procedure to change from claiming less than the depreciation allowable on other items of property, the taxpayer must file two Forms 3115—one Form 3115 under Rev. Proc. 92-20 (or any successor) for the over-depreciated property and one Form 3115 under this revenue procedure for the under-depreciated property. The taxpayer, however, files one Form 3115 if the taxpayer uses Rev. Proc. 92-20 (or any successor) to change the method of accounting for both the under- and over-depreciated properties.

SECTION 4. CONSENT TO CHANGE

.01 *Consent granted.* The consent of the Commissioner under § 1.446-1(e)-(2)(i) is granted to any taxpayer within the scope of this revenue procedure to make a method change to a permissible method of accounting for depreciation for any item of property within the scope of this revenue procedure. This consent is granted, however, only if the taxpayer complies with section 5 of this revenue procedure. If the taxpayer does not comply with section 5 of this revenue procedure, the taxpayer will be deemed to have initiated a change in method of accounting without obtaining the consent of the Commissioner required under § 446(e).

.02 *Effect of consent.* The consent that is granted under this revenue procedure does not constitute an opinion of the Commissioner regarding the propriety of a taxpayer's proposed method of accounting. Consequently, if the proposed method of accounting is an impermissible method of accounting, the Service may change the taxpayer's proposed method of accounting to a permissible method of accounting in any open year.

SECTION 5. MANNER OF EFFECTING AUTOMATIC CHANGE

.01 *General procedure.*

(1) *Complete and file a current Form 3115.* A taxpayer makes a change in method of accounting under this revenue procedure by completing and filing a current Form 3115 in duplicate. The original of the Form 3115 must be filed with the Office of Associate Chief Counsel (Domestic) (national office) on or before 180 days after the beginning of the year of change and addressed to the Commissioner of Internal Revenue, Attn: CC:DOM:P&SI:6, Room 5112, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. In addition, a copy of the Form 3115 must be attached to the taxpayer's timely filed (including extensions) federal income tax return for the year of change.

The 180-day filing period begins on the first day of any taxable year. If the taxable year is a short taxable year (less than 12 full months), the original of the Form 3115 must be filed with the national office no later than 180

days after the beginning of the short taxable year or, if earlier, no later than the last day of the short taxable year.

In completing the current Form 3115 (Rev. February 1996), the taxpayer must complete Schedule D, Part II, Change in Depreciation or Amortization (page 7 of the Form 3115), and any other applicable schedule. With respect to Parts I through III on pages 1 and 2 of the current Form 3115, the taxpayer must provide only the information requested on the following lines:

(a) Part I, Eligibility To Request Change (page 1)-lines 1, 2a and b, and 6;

(b) Part II, Description of Change (page 2)-line 8 and to the extent not provided elsewhere on the Form 3115, lines 10, 11, 12, 13, 17, 18a and b, and 19; and

(c) Part III, Section 481(a) Adjustment (page 2)-lines 20, 22, 23, and 25.

(2) *Label.* The taxpayer should type or legibly print at the top of the Form 3115: "AUTOMATIC METHOD CHANGE UNDER REV. PROC. 96-31."

(3) *No user fee and acknowledgment.* No user fee is required for a Form 3115 filed under this revenue procedure and a Form 3115 filed pursuant to this revenue procedure will not be acknowledged.

.02 *Permissible method of accounting for depreciation must be used.* A taxpayer must change to a permissible method of accounting for depreciation for the item of property. This method is the same method that determines the depreciation allowable for the item of property (as determined under section 7 of this revenue procedure).

.03 *Year of change.* The year of change is the taxable year for which the original of the Form 3115 is considered timely filed with the national office under section 5.01(1) of this revenue procedure.

.04 *Section 481(a) adjustment.*

(1) *In general.* A change in method of accounting under this revenue procedure is treated as a voluntary change in method of accounting that is initiated by the taxpayer and, therefore, the § 481(a) adjustment is not restricted to post-1953 items.

(2) *Amount of § 481(a) adjustment.* The § 481(a) adjustment is a negative § 481(a) adjustment (decrease in taxable income) to prevent the

omission of the allowable but unclaimed depreciation for open and closed years prior to the year of change. This negative § 481(a) adjustment equals the difference between the total amount of depreciation taken into account in computing taxable income for the property under the taxpayer's present method of accounting, and the total amount of depreciation allowable for the property under the taxpayer's proposed method of accounting (as determined under section 7 of this revenue procedure), for any taxable year prior to the year of change. The amount of the negative § 481(a) adjustment, however, must be offset by any allowable but unclaimed depreciation that is required to be capitalized under any provision of the Code (for example, § 263A) as of the beginning of the year of change.

(3) *Section 481(a) adjustment period.* A taxpayer must take the entire negative § 481(a) adjustment into account in computing the taxable income in the year of change.

.05 *Basis adjustment.* The basis of depreciable property to which this revenue procedure applies must reflect the reductions required by § 1016(a)(2) for the depreciation allowable for the property (as determined under section 7 of this revenue procedure).

SECTION 6. REVIEW OF FORM 3115

The Form 3115 will be subject to review by the national office. In addition, the facts underlying the method change, including the amount of any § 481(a) adjustment and any § 1016(a)(2) adjustment to the basis of the property, will be subject to verification by the district director. If the Form 3115 is reviewed and the taxpayer's proposed method of accounting appears to be an impermissible method of accounting for depreciation or the taxpayer or property appears to be outside the scope of this revenue procedure, the national office or the district director will notify the taxpayer, in writing, that consent is not granted under this revenue procedure. The taxpayer then may complete and file a new Form 3115 under this revenue procedure or Rev. Proc. 92-20 (or any successor), as applicable. The year of change for this new Form 3115 will be determined in accordance with the requirements of such revenue procedure.

SECTION 7. MEANING OF DEPRECIATION ALLOWABLE

.01 *In general.* This section 7 discusses the amount of the depreciation allowable determined under § 167, § 168, § 197, or former § 168. This amount, however, may be limited under other provisions of the Code (for example, § 280F).

.02 *Section 167 property.* Generally, for any taxable year, the depreciation allowable for property subject to § 167 is determined either: (1) under the depreciation method adopted by a taxpayer for the property; or (2) if this depreciation method does not result in a reasonable allowance for depreciation or a taxpayer has not adopted a depreciation method for the property, under the straight-line depreciation method. For determining the estimated useful life and salvage value of the property, see § 1.167(a)-1(b) and (c), respectively. The depreciation allowable for any taxable year for property subject to § 167(f) (pertaining to certain property excluded from § 197) is determined by using the depreciation method and useful life prescribed in § 167(f).

.03 *Section 168 property.* The depreciation allowable for any taxable year for property subject to § 168 is determined by using either: (1) the general depreciation system in § 168(a); or (2) the alternative depreciation system in § 168(g) if the property is required to be depreciated under the alternative depreciation system pursuant to § 168(g)(1) or other provisions of the Code (for example, property described in § 263A(e)(2)(A) or § 280F(b)(1)). Property required to be depreciated under the alternative depreciation system pursuant to § 168(g)(1) includes property in a class for which the taxpayer made a timely election under § 168(g)(7).

.04 *Section 197 property.* The depreciation allowable for any taxable year for an amortizable § 197 intangible (including any property for which a timely election under § 13261(g)(2) of the 1993 Act was made) is determined by using the straight-line method over a 15-year period.

.05 *Former § 168 property.* The depreciation allowable for any taxable year for property subject to former § 168 is determined by using either: (1) the accelerated method of cost recovery applicable to the property (for example,

for 5-year property, the recovery method under former § 168(b)(1)); or (2) the straight-line method applicable to the property if the property is required to be depreciated under the straight-line method (for example, property described in former § 168(f)(12) or former § 280F(b)(2)) or if the taxpayer elected to determine the depreciation allowance under the optional straight-line percentage (for example, the straight-line method in former § 168(b)(3)).

SECTION 8. EFFECTIVE DATE

.01 *In general.* This revenue procedure is effective May 13, 1996.

.02 *Form 3115 already pending with the Service.*

(1) *In general.* The provisions of this revenue procedure apply to a taxpayer with a Form 3115 (including a Form 3115 filed under the early application provision of section 5.01(3) of Rev. Proc. 92-20) timely filed with the Service as of May 13, 1996, for a method change for depreciation to which this revenue procedure applies. Therefore, the taxpayer has the option to make the method change under this revenue procedure or to request permission to make the method change under Rev. Proc. 92-20 (or any successor). In this regard, the taxpayer must notify the national office, in writing, on or before August 15, 1996, as to the taxpayer's decision. If the national office is not notified by August 15, 1996, the Form 3115 will be treated as filed under Rev. Proc. 92-20.

(2) *Manner of effecting automatic change.* If the taxpayer makes the method change under this revenue procedure, the taxpayer's Form 3115 timely filed as of May 13, 1996, will be treated as being timely filed with the national office under this revenue procedure. The original of the Form 3115 will be retained by the national office. The national office will return a copy of the Form 3115 to the taxpayer so that, as required, the taxpayer can attach the copy to the taxpayer's timely filed (including extensions) original federal income tax return, or to an amended return, for the year of change. The receipt of this copy is not an opinion of the Commissioner regarding the propriety of the taxpayer's proposed method of accounting. See section 4.02 of this revenue procedure.

If all of the property subject to the Form 3115 appears to be within the

scope of this revenue procedure and the taxpayer notifies the national office in a timely manner that the taxpayer is making the method change under this revenue procedure, any user fee submitted with the Form 3115 will be returned to the taxpayer.

(3) *Year of change.* For a taxpayer with a Form 3115 timely filed as of May 13, 1996, the taxpayer may make the method change under this revenue procedure either for the year of change originally requested on the Form 3115 (or if this year is a closed year, for the first subsequent open year) or for the taxpayer's taxable year beginning in 1995 or 1996. If the taxpayer modifies the year of change, the taxpayer must submit a letter to the national office, stating the new year of change and any revised information on the taxpayer's Form 3115 to reflect the new year of change (for example, the revised § 481(a) adjustment for the year of change). This letter must be submitted on or before August 15, 1996, to the national office. If the national office is not notified by August 15, 1996, the year of change is the one originally requested on the taxpayer's Form 3115 (or if this year is a closed year, the first subsequent open year).

If the taxpayer makes the method change under this revenue procedure for under-depreciated property but the Form 3115 also includes items of property for which the taxpayer, under the taxpayer's present method of accounting, claimed more than the depreciation allowable, the year of change for the over-depreciated property will be the same as the year of change for the under-depreciated property.

(4) *Submission of additional information.* The additional information requested in section 8.02(1) and (3) of this revenue procedure must be accompanied by the following penalties of perjury statement: "Under penalties of perjury, I declare that I have examined this request, including accompanying documents, and to the best of my knowledge and belief, the facts presented in support of the requested Form 3115 are true, correct, and complete." This penalties of perjury statement must be signed and dated by the taxpayer, not the taxpayer's representative. Also, a stamped signature is not permitted.

The additional information (including the penalties of perjury statement) must

be addressed to the Commissioner of Internal Revenue, Attn: CC:DOM: P&SI:6, Room 5112, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

SECTION 9. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 92-20 is modified.

DRAFTING INFORMATION

The principal author of this revenue procedure is Kathleen Reed of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Ms. Reed at (202) 622-3110 (not a toll-free number).

26 CFR 601.201: Rulings and determination letters.

(Also Part I, §§ 501(c)(3); 1.501(c)(3)-1.)

Rev. Proc. 96-32

SECTION 1. PURPOSE

.01 This revenue procedure sets forth a safe harbor under which organizations that provide low-income housing will be considered charitable as described in § 501(c)(3) of the Internal Revenue Code because they relieve the poor and distressed as described in § 1.501(c)(3)-1(d)(2) of the Income Tax Regulations. This revenue procedure also describes the facts and circumstances test that will apply to determine whether organizations that fall outside the safe harbor relieve the poor and distressed such that they will be considered charitable organizations described in § 501(c)(3). It also clarifies that housing organizations may rely on other charitable purposes to qualify for recognition of exemption from federal income tax as organizations described in § 501(c)(3). These other charitable purposes are described in § 1.501(c)(3)-1(d)(2). This revenue procedure supersedes the application referral described in Notice 93-1, 1993-1 C.B. 290.

.02 This revenue procedure does not alter the standards that have long been applied to determine whether low-income housing organizations qualify for tax-exempt status under § 501(c)(3). Rather, it is intended to expedite

the consideration of applications for tax-exempt status filed by such organizations by providing a safe harbor and by accumulating relevant information on the existing standards for exemption in a single document. Low-income housing organizations that have ruling or determination letters and have not materially changed their organizations or operations from how they were described in their applications can continue to rely on those letters.

SEC. 2. BACKGROUND OF SAFE HARBOR

.01 Rev. Rul. 67-138, 1967-1 C.B. 129, Rev. Rul. 70-585, 1970-2 C.B. 115, and Rev. Rul. 76-408, 1976-2 C.B. 145, hold that the provision of housing for low-income persons accomplishes charitable purposes by relieving the poor and distressed. The Service has long held that poor and distressed beneficiaries must be needy in the sense that they cannot afford the necessities of life. Rev. Ruls. 67-138, 70-585, and 76-408 refer to the needs of housing recipients and to their inability to secure adequate housing under all the facts and circumstances to determine whether they are poor and distressed.

.02 The existence of a national housing policy to maintain a commitment to provide decent, safe, and sanitary housing for every American family is reflected in several federal housing acts. See, for example, § 2 of the United States Housing Act of 1937, 42 U.S.C. § 1437; § 2 of the Housing Act of 1949, 42 U.S.C. § 1441; § 2 of the Housing and Urban Development Act of 1968, 12 U.S.C. § 1701t; and §§ 101, 102, and 202 of the Cranston-Gonzalez National Affordable Housing Act, 42 U.S.C. §§ 12701, 12702, and 12721. Not all beneficiaries of these housing acts, however, are necessarily poor and distressed within the meaning of § 1.501(c)(3)-1(d)(2).

.03 In order to support national housing policy, the safe harbor contained in this revenue procedure identifies those low-income housing organizations that will, with certainty, be considered to relieve the poor and distressed. The safe harbor permits a limited number of units occupied by residents with incomes above the low-income limits in order to assist in the social and economic integration of the poorer residents and, thereby, further

the organization's charitable purposes. To avoid giving undue assistance to those who can otherwise afford safe, decent, and sanitary housing, the safe harbor requires occupancy by significant levels of both very low-income and low-income families.

.04 Low-income housing organizations that fall outside the safe harbor may still be considered organizations that offer relief to the poor and distressed based on all the surrounding facts and circumstances. Some of the facts and circumstances that will be taken into consideration in determining whether a low-income housing organization will be so considered are set forth in section 4.

.05 Low-income housing organizations may also qualify for tax-exempt status because they serve a charitable purpose described in § 501(c)(3) other than relief of the poor and distressed. Exempt purposes other than relief of the poor and distressed are discussed in section 6.

.06 To be recognized as exempt from income tax under § 501(c)(3), a low-income housing organization must not only serve a charitable purpose but also meet the other requirements of that section, including the prohibitions against inurement and private benefit. Specific concerns with respect to these prohibitions are set forth in section 7.

SEC. 3. SAFE HARBOR FOR RELIEVING THE POOR AND DISTRESSED

.01 An organization will be considered charitable as described in § 501(c)(3) if it satisfies the following requirements:

(1) The organization establishes for each project that (a) at least 75 percent of the units are occupied by residents that qualify as low-income; and (b) either at least 20 percent of the units are occupied by residents that also meet the very low-income limit for the area or 40 percent of the units are occupied by residents that also do not exceed 120 percent of the area's very low-income limit. Up to 25 percent of the units may be provided at market rates to persons who have incomes in excess of the low-income limit.

(2) The project is actually occupied by poor and distressed residents. For projects requiring construction or rehabilitation, a reasonable transition period is allowed for an organization to

place the project in service. Whether an organization's transition period is reasonable is determined by reference to all relevant facts and circumstances. For projects that do not require substantial construction or substantial rehabilitation, a one-year transition period to satisfy the actual occupancy requirement will generally be considered to be reasonable. If a project operates under a government program that allows a longer transition period, this longer period will be used to determine reasonableness.

(3) The housing is affordable to the charitable beneficiaries. In the case of rental housing, this requirement will ordinarily be satisfied by the adoption of a rental policy that complies with government-imposed rental restrictions or otherwise provides for the limitation of the tenant's portion of the rent charged to ensure that the housing is affordable to low-income and very low-income residents. In the case of homeownership programs, this requirement will ordinarily be satisfied by the adoption of a mortgage policy that complies with government-imposed mortgage limitations or otherwise makes the initial and continuing costs of purchasing a home affordable to low and very low-income residents.

(4) If a project consists of multiple buildings and each building does not separately meet the requirements of sections 3.01(1), (2), and (3), then the buildings must share the same grounds. This requirement does not apply to organizations that provide individual homes or individual apartment units located at scattered sites in the community exclusively to families with incomes at or below 80 percent of the area's median income.

.02 In applying this safe harbor, the Service will follow the provisions listed below:

(1) Low-income families and very low-income families will be identified in accordance with the income limits computed and published by the Department of Housing and Urban Development ("HUD") in *Income Limits for Low and Very Low-Income Families Under the Housing Act of 1937*. The term "very low-income" is defined by the relevant housing statute as 50 percent of an area's median income. The term "low-income" is defined by the same statute as 80 percent of an area's median income. However, these income limits may be adjusted by HUD

to reflect economic differences, such as high housing costs, in each area. The income limits are then tailored to reflect different family sizes. If HUD's program terminates, the Service will use income limits computed under such program as is in effect immediately before such termination. Copies of all or part of HUD's publication may be obtained by calling HUD at (800) 245-2691 (HUD charges a small fee to cover costs of reproduction).

(2) The retention of the right to evict tenants for failure to pay rent or other misconduct, or the right to foreclose on homeowners for defaulting on loans will not, in and of itself, cause the organization to fail to meet the safe harbor.

(3) An organization originally meeting the safe harbor will continue to satisfy the requirements of the safe harbor if a resident's income increases and causes the organization to fail the safe harbor, provided that the resident's income does not exceed 140 percent of the applicable income limit under the safe harbor. If the resident's income exceeds 140 percent of the qualifying income limit, the organization will not fail to meet the safe harbor if it rents the next comparable non-qualifying unit to someone under the income limits.

(4) To be considered charitable, an organization that provides assistance to the aged or physically handicapped who are not poor must satisfy the requirements set forth in Rev. Rul. 72124, 1972-1 C.B. 145, Rev. Rul. 79-18, 1979-1 C.B. 194, and Rev. Rul. 79-19, 1979-1 C.B. 195. If an organization meets the safe harbor, then it does not need to meet the requirements of these rulings even if all of its residents are elderly or handicapped residents. However, an organization may not use a combination of elderly or handicapped persons and low-income persons to establish the 75-percent occupancy requirement of the safe harbor. An organization with a mix of elderly or handicapped residents and low-income residents may still qualify for tax-exempt status under the facts and circumstances test set forth in section 4.

SEC. 4. FACTS AND CIRCUMSTANCES TEST FOR RELIEVING THE POOR AND DISTRESSED

.01 If the safe harbor contained in section 3 is not satisfied, an organiza-

tion may demonstrate that it relieves the poor and distressed by reference to all the surrounding facts and circumstances.

.02 Facts and circumstances that demonstrate relief of the poor may include, but are not limited to, the following:

(1) A substantially greater percentage of residents than required by the safe harbor with incomes up to 120 percent of the area's very low-income limit.

(2) Limited degree of deviation from the safe harbor percentages.

(3) Limitation of a resident's portion of rent or mortgage payment to ensure that the housing is affordable to low-income and very low-income residents.

(4) Participation in a government housing program designed to provide affordable housing.

(5) Operation through a community-based board of directors, particularly if the selection process demonstrates that community groups have input into the organization's operations.

(6) The provision of additional social services affordable to the poor residents.

(7) Relationship with an existing 501(c)(3) organization active in low-income housing for at least five years if the existing organization demonstrates control.

(8) Acceptance of residents who, when considered individually, have unusual burdens such as extremely high medical costs which cause them to be in a condition similar to persons within the qualifying income limits in spite of their higher incomes.

(9) Participation in a homeownership program designed to provide homeownership opportunities for families that cannot otherwise afford to purchase safe and decent housing.

(10) Existence of affordability covenants or restrictions running with the property.

SEC. 5. EXAMPLES

.01 Application of the safe harbor and the facts and circumstances test is illustrated by the following examples:

(1) Organization *N* operates pursuant to a government program to provide low and moderate income housing projects. Seventy percent of

N's residents have incomes that do not exceed the area's low-income limit. Fifty percent of *N*'s residents have incomes that are at or below the area's very low-income limit. Under the program, *N* restricts rents charged to residents below the income limits to no more than 30 percent of the applicable low or very low-income limits for *N*'s area. *N* is close to meeting the safe harbor. *N* has a substantially greater percentage of very low-income residents than required by the safe harbor; it participates in a federal housing program; and it restricts its rents pursuant to an established government program. Although *N* does not meet the safe harbor, the facts and circumstances demonstrate that *N* relieves the poor and distressed.

(2) Organization *O* will finance a housing project using tax-exempt bonds pursuant to § 145(d). *O* will meet the 20-50 test under § 142(d)(1)(A). Another 45 percent of the residents will have incomes at or below 80 percent of the area's median income. The final 35 percent of the residents will have incomes above 80 percent of the area's median income. *O* will restrict rents charged to residents below the income limits to no more than 30 percent of the residents' incomes. *O* will provide social services to project residents and to other low-income residents in the neighborhood. Also, *O* will purchase its project through a government program designed to retain low-income housing stock. *O* does not meet the safe harbor. However, the facts and circumstances demonstrate that *O* relieves the poor and distressed.

(3) Organization *R* provides affordable homeownership opportunities to purchasers determined to be low-income under a federal housing program. The homes are scattered throughout a section of *R*'s community. Beneficiaries under the program cannot afford to purchase housing without assistance. *R*'s program makes the initial and continuing costs of mortgages affordable to the home buyers by providing assistance with down payments and closing costs. Homeowners assisted by *R* will have the following composition: 40 percent will not exceed 140 percent of the very low-income limit for the area, 25 percent will not exceed the low-income limit, and 35 percent will exceed the low-income limit but will not exceed 115 percent of the area's median income. *R* does not satisfy the safe harbor. How-

ever, the facts and circumstances demonstrate that *R* relieves the poor and distressed.

(4) Organization *U* will purchase existing residential rental housing financed using tax-exempt bonds issued in accordance with § 145(d). *U* will meet the minimum requirements of the 40–60 test of § 142(d)(1)(B). It will provide the balance of its units to residents with incomes at or above area median income levels. *U* has a community-based board of directors. *U* does not satisfy the safe harbor. Moreover, the facts and circumstances do not demonstrate that *U* relieves the poor and distressed.

(5) Organization *V* provides rental housing in a section of the city where income levels are well below the other parts of the city. All of *V*'s residents are below the very low-income limits for the area, yet they pay rents that are above 50 percent of the area's very low-income limits. *V* has not otherwise demonstrated that the housing is affordable to its residents. Although the residents are all considered poor and distressed under the safe harbor, *V* does not relieve the poverty of the residents.

(6) Organization *W* provides homeownership opportunities to purchasers with incomes up to 115 percent of the area's median income. *W* does not meet the income levels required under the safe harbor. *W*'s board of directors is representative of community interests, and *W* provides classes and counseling services for its residents. The facts and circumstances do not demonstrate that *W* relieves the poor and distressed.

SEC. 6. EXEMPT PURPOSES OTHER THAN RELIEVING THE POOR AND DISTRESSED

.01 Relief of the poor and distressed, whether demonstrated by satisfaction of the safe harbor described in section 3 of this Revenue Procedure or by reference to the facts and circumstances test described in section 4, does not

constitute the only exempt purpose that a housing organization may have. Such organizations may qualify for exemption without having to satisfy the standards for relief of the poor and distressed by providing housing in a way that accomplishes any of the purposes set forth in § 501(c)(3) or § 1.501(c)(3)–1(d)(2). Those purposes include, but are not limited to, the following:

(1) Combatting community deterioration is an exempt purpose, as illustrated by Rev. Rul. 68–17, 1968–1 C.B. 247, Rev. Rul. 68–655, 1968–2 C.B. 213, Rev. Rul. 70–585, 1970–2 C.B. 115 (Situation 3), and Rev. Rul. 76–147, 1976–1 C.B. 151. An organization that combats community deterioration must (1) operate in an area with actual or potential deterioration, and (2) directly prevent or relieve that deterioration. Constructing or rehabilitating housing has the potential to combat community deterioration.

(2) Lessening the burdens of government is an exempt purpose, as illustrated by Rev. Ruls. 85–1 and 85–2, 1985–1 C.B. 178. An organization lessens the burdens of government if (a) there is an objective manifestation by the governmental unit that it considers the activities of the organization to be the government's burdens, and (b) the organization actually lessens the government's burdens.

(3) Elimination of discrimination and prejudice is an exempt purpose, as illustrated by Rev. Rul. 68–655, 1968–2 C.B. 213, and Rev. Rul. 70–585, 1970–2 C.B. 115 (Situation 2). These rulings describe organizations that further charitable purposes by assisting persons in specific racial groups to acquire housing for the purpose of stabilizing neighborhoods or reducing racial imbalances.

(4) Lessening neighborhood tensions is an exempt purpose, as illustrated by Rev. Rul. 68–655, 1968–2 C.B. 213, and Rev. Rul. 70–585, 1970–2 C.B. 115 (Situation 2). It is generally

identified as an additional charitable purpose by organizations that fight poverty and community deterioration associated with overcrowding in lower income areas in which ethnic or racial tensions are high.

(5) Relief of the distress of the elderly or physically handicapped is an exempt purpose, as illustrated by Rev. Rul. 72–124, 1972–1 C.B. 145, Rev. Rul. 79–18, 1979–1 C.B. 194, and Rev. Rul. 79–19, 1979–1 C.B. 195. An organization may further a charitable purpose by meeting the special needs of the elderly or physically handicapped.

SEC. 7. OTHER CONSIDERATIONS

If an organization furthers a charitable purpose such as relieving the poor and distressed, it nevertheless may fail to qualify for exemption because private interests of individuals with a financial stake in the project are furthered. For example, the role of a private developer or management company in the organization's activities must be carefully scrutinized to ensure the absence of inurement or impermissible private benefit resulting from real property sales, development fees, or management contracts.

SEC. 8. EFFECT ON OTHER DOCUMENTS

Notice 93–1 is superseded.

SEC. 9. EFFECTIVE DATE

This revenue procedure is effective on [date of publication].

DRAFTING INFORMATION

The principal authors of this revenue procedure are Lynn Kawecky and Marvin Friedlander. For further information regarding this revenue procedure, contact Mr. Kawecky at (202) 622-7305 (not a toll free number).

Part IV. Items of General Interest

Announcement 96-41

1996 Form W-4

The IRS has approved the 1996 **Form W-4**, Employee's Withholding Allowance Certificate, for printing. The form should be available for distribution by May 1996. Employers may order Form W-4 by telephone or they may use other IRS electronic information services to get copies.

Request by—	Number or Address
Telephone	1-800-TAX-FORM (1-800-829-3676)
Computer and modem	703-321-8020 (modem settings are N, 8, 1)
Internet: World Wide Web FTP Telnet	www.irs.ustreas.gov ftp.irs.ustreas.gov iris.irs.ustreas.gov
Fax	703-487-4160

Employers should remind employees to check their withholding to see if it is sufficient. Employees may use Publication 919, "Is My Withholding Correct?," for assistance. If an employee submitted a 1995 Form W-4 for 1996, he or she is not required to submit a 1996 Form W-4 but should if the withholding is not adequate.

Obsolete Federal Tax Forms

Announcement 96-42

Form 8807 and Form 8645 are obsolete. The IRS has determined that taxpayers may meet the reporting and certification requirements of these forms by reporting the required information on other forms, as noted below.

Form 8807, Certain Manufacturers and Retailers Excise Taxes. Beginning with the second quarter of 1996, taxpayers must only summarize these taxes on **Form 720**, Quarterly Federal Excise Tax Return. Rates and other information on these taxes are included

on Form 720 and in the Instructions for Form 720.

Form 8645, Soil and Water Conservation Plan Certificate. For tax years beginning after 1995, taxpayers will no longer need to file Form 8645. However, the soil and water conversation expenses reported on the following forms must be consistent with an approved plan: **Schedule F (Form 1040)**, Farming Expenses; **Form 4835**, Farm Rental Income and Expenses; **Form 1040-SS**, U.S. Self-Employment Tax Return (Virgin Islands, Guam, American Samoa, and the Northern Mariana Islands); and **Form 1040-PR**, Planilla Para La Declaracion De La Contribucion Federal Sobre El Trabajo Por Cuenta Propia-Puerto Rico.

Foundations Status of Certain Organizations

Announcement 96-43

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

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

A G Cox Orchestra Booster Club Inc., Winterville, NC
 Ahoskie Civic Association Inc., Ahoskie, NC
 Aid To Inmate Mothers, Montgomery, AL
 AIDS Service Agency of Orange County, Chapel Hill, NC
 Alabama Rural Heritage Foundation Inc., Thomaston, AL
 Alabamians for Quality Education Inc., Birmingham, AL

Arcadia Wildlife Preserve Inc., Atlanta, GA
 Arkansas Housing Partnership Inc., Little Rock, AR
 Athens Peace Coalition Inc., Athens, GA
 Barefoot Ballet Inc., Atlanta, GA
 Bethesda, Oneonta, AL
 Black Swan Center, The, Black Mountain, NC
 Bokwes Cultural Group, Durham, NC
 Boys and Girls Club of Putnam County, Cookeville, TN
 Calvin Peete Golf Foundation Inc., Atlanta, GA
 Care-ag Inc., Charlotte, NC
 Carolina Hispanic Community Inc., Wilmington, NC
 Cars for Kids-Southern Style Inc., Selmer, TN
 Catholic Education Foundation for Northwest Arkansas Inc., Fayetteville, AR
 Central Arkansas Fund for Veterans Inc., North Little Rock, AR
 Central Carolinas Citizens Forum, Charlotte, NC
 Chain of Hope Ministries, Clarksville, TN
 Chapel Hill-Carrboro Community Foundation, Chapel Hill, NC
 Charlotte Philharmonic Society-Orchestra, Charlotte, NC
 Chatom Dixie Youth Baseball Inc., Chatom, AL
 Chelsea Farms Inc., Memphis, TN
 Childrens Rights of America National Fund Inc., Atlanta, GA
 Coastal Georgia Soccer Association Inc., Savannah, GA
 Committee for Public Art Inc., Hickory, NC
 Committee to Feed the Hungry Inc., Atlanta, GA
 Community Apartments Corporation of Rutherford City, Raleigh, NC
 Community Housing Development Services Inc., Nashville, TN
 Comprehensive Learning Laboratory Corp., Fayetteville, NC
 Confederate Brass Inc., The, Athens, GA
 Conyers Cherry Blossom Festival Foundation Inc., Conyers, GA
 Cornerstone Foundation, The, Memphis, TN
 Creative Childrens Learning Center Inc., Birmingham, AL

Creative Educational Consulting Services Inc., Reidsville, GA

Credit Wise Company Inc., The, Memphis, TN

Crime Stoppers of Lexington Inc., Lexington, TN

Culturally Specific Treatment Enhancement Programs Inc., Atlanta, GA

David Gries Memorial Foundation Inc., Montgomery, AL

Decatur County Families in Action, Parsons, TN

Doulos Fellowship Inc., Hertford, NC

Drug Awareness of Newton County Inc., Covington, GA

Easley Place Inc., Millington, TN

Eastern Correctional Institution Community Resource, Maury, NC

Easy Riders Therapeutic Horsemanship Inc., McCalla, AL

Echo 1 Community Outreach Services, Roanoke, AL

Economic Development Learning Center, The, Chocowinity, NC

Ecumenical Consulting Associates Inc., Atlanta, GA

Ed Care Inc., Brentwood, TN

E H Wilbourn Scholarship Fund of Huntsville-Madison, Gurley, AL

Em-Art Inc., Kennesaw, GA

End of the Line Inc., The, Memphis, TN

Envistas Corporation, Blue Ridge, GA

Euclid Arts Collective Inc., Decatur, GA

Exeter Association of Georgia Inc., The, Atlanta, GA

Faith & Culture Society Inc., Grand Rapids, MI

Family Management Inc., Montgomery, AL

First Amazing Grace Ministries Inc., Atlanta, GA

Flotilla 17-08 Inc., Charlotte, NC

Forrcce Inc., Hamlet, NC

Frayser-Raleigh Community Theatre Inc., Memphis, TN

Friends of Grandfather Mountain, Sugar Grove, NC

Friends of Gravette Medical Center Hospital Inc., The, Gravette, AR

Friends of Jazz Inc., Chattanooga, TN

Frye Regional Medical Center Auxiliary, Hickory, NC

Georgia Rails Into Trails Society Inc., Marietta, GA

Georgia Sentencing Alternatives Inc., Marietta, GA

Girls Traveling Softball Association of Georgia, Douglasville, GA

Gospel Team Outreach International Ministries Inc., Renoldsburg, OH

Granville Residents Opposed to Waste Inc., Oxford, NC

Great 100 Inc., The, Laurel Hill, NC

Greater Hamilton County Soccer Council Inc., Chattanooga, TN

Green Hill Church of Christ Child Care Center Inc., Mount Juliet, TN

Guardian Ad Litem Volunteer Association Inc., Jacksonville, NC

Healthcare Transportation Foundation Inc., Birmingham, AL

Help Our Planet Earth Inc., Atlanta, GA

Hendersonville Filmmakers Club Inc., Hendersville, TN

Henry County Horsemen Assoc., McDonough, GA

Hickorys Committee for a Secure Tomorrow Inc., Hickory, NC

Higher Education Addiction Prevention Prof of NC Inc., Greensboro, NC

H O P E in Cobb Inc., Marietta, GA

Hospice of Johnston County Inc., Selma, NC

Hospice of Peach County Inc., Fort Valley, GA

Host Christian Ministries Inc., The, Gainesville, GA

House of Sunshine Inc., Asheville, NC

Huntsville Academy and Forum, Huntsville, TN

Hunstville Folk Dancers, Huntsville, AL

In Time Ministries Inc., Memphis, TN

Institute for Advanced Studies in Life Support Inc., Huntsville, AL

Institute for Urological Research Inc., Nashville, TN

Institute for Wholistic Education Inc., Raleigh, NC

Jack Fowler Park, Dr., Walnut Cove, NC

Jackson Community Housing Resource Board Inc. Community Counsel, Jackson, TN

Jobs for Stars Inc., Memphis, TN

Keep Saying No Inc., Fayette, AL

Kentucky-Tennessee Water Pollution Control Assoc., Nashville, TN

Knox County Task Force Against Domestic Violence, Knoxville, TN

Knoxville Smokies Baseball Team, Knoxville, TN

Kurt Einstein Foundation Inc., Cary, NC

L Anguille Arts Council, Forrest City, AR

LA Sociedad Panamena De Atlanta Georgia Inc., Stone Mountain, GA

Leadership Lowdes Inc., Valdosta, GA

Lebanon High School Blue Devil Booster Club Inc., The, Lebanon, TN

Life Way Ministries, Hayden, AL

Main Street Camden Inc., Camden, AR

Masters Place Inc., The, Atlanta, GA

Maury County Public Education Foundation, Columbia, TN

Mental Health Association of Columbus Georgia Inc., Columbus, GA

Mobile Area African American Summit, Mobile, AL

Mobile Area Teen Resource Center, Inc., Mobile, AL

Municipal Park Youth Football Assoc. Inc., Mobile, AL

Music City Endurance Athletes Inc., Nashville, TN

National Committee for Drug Awareness Inc., Atlanta, GA

NC Association of Plumbing, Heating, Cooling Contractors Education FDN Inc., Raleigh, NC

Newborns in Need Foundation Inc., Auburn, GA

North Carolina Arboretum Society, The, Asheville, NC

North Carolina Hunger Network, Raleigh, NC

North Carolina Partners for Democracy Foundation, Raleigh, NC

North Fayette County Volunteer Fire Department, Mason, TN

North Raleigh Athletic Association Inc., Raleigh, NC

Northwest Flight Attendants Emergency Fund, Cordova, TN

Northwestern Carolina Education & Development Association Inc., Boone, NC

Old Fort Community Club, Old Fort, NC

Orleans Care Home, Memphis, TN

Ozark Therapeutic Weight Training Center Inc., Marby, AR

Percussionistic Corporation, Durham,
NC

Persian Community Center Inc.,
Atlanta, GA

Phoenix House of Raleigh Inc.,
Raleigh, NC

Pickens Respite Inc., Fairfield, AL

Piedmont Aid Corp., High Point, NC

Pinnacle Ministries, Gatlinburg, TN

Police Athletic League of
Chattanooga Inc., Chattanooga, TN

Power Over Panic Inc., Atlanta, GA

Predator Control and Conservation,
Mobile, AL

Progressive Southeast Arkansas
Housing Development Corp., Pine
Bluff, AR

PWA Inc., Ranger, GA

Radio Reading Services Corp.,
Kingsport, TN

Ralph David Abernathy Foundation
Inc., Atlanta, GA

RE Builders Action Council, Little
Rock, AR

Red Carpet Industry FDN Inc.,
Dalton, GA

Reduce Infant Deaths Foundation,
Winston Salem, NC

Region 1 Football Officials
Scholarship Endowment Bowl,
Johnson City, TN

Ricky Fountain Educational
Foundation Inc., Wilmington, NC

R K Enterprise Child Care Food
Program Inc., Decatur, GA

Robeson County Dispute Resolution
Center, Lumberton, NC

ROHI Inc., Buford, GA

Rolling Hills Lakes Volunteer Fire
Department, Montgomery, AL

Rowan Environmental Action
Partners—REAP, Salisbury, NC

Roy Bolton Patton JR Scholarship
Endowment Fund, Athens, AL

Royal Pavilions of Creedmoor Inc.,
Creedmoor, NC

Ruth Faison Shaw Memorial
Committee, Chapel Hill, NC

Savannah State College Community
Booster Club Inc., Savannah, GA

Serenity Thru Recovery of
Fayetteville Inc., Fayetteville, NC

Shambhala Institute and Foundation
Inc., Asheville, NC

Society for the Advancement of
Social Psychology Inc., Macon, GA

Society of Parrot Breeders and
Exhibitors Inc., Marietta, GA

South Arkansas County Fine Arts
Council Inc., The, Dewitt, AR

Spavinaw Valley Boy Scout Boosters
Inc., Gravette, AR

Spavinaw Valley United Way,
Gravette, AR

SSS Band Backers Inc., Smithfield,
NC

Stiles Foundation, Statesville, NC

Student Awareness for Environment
in North Carolina, Wrightsville
Beach, NC

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

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 law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

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

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

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

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

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

Abbreviations

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

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

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

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

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