

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. 9443, page 564.

Final regulations under section 7508A of the Code relate to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster.

REG-143686-07, page 579.

Proposed regulations under section 358 of the Code provide guidance relating to the allocation and recovery of stock basis in distributions under section 301 and transactions under sections 302, 304, 354, 355, and 356. The regulations also provide guidance regarding qualification of a transaction under section 368, the determination of gain under section 351(b), and adjustments to basis in certain capital contributions.

Notice 2009-17, page 575.

This notice invites public comments regarding guidance to be provided to brokers, transferors, issuers, customers, and other affected persons concerning new requirements with respect to the reporting of a customer's basis in securities transactions and new rules for determining the basis of certain securities subject to the new reporting requirements. These new requirements and rules generally begin to take effect on January 1, 2011. Interested parties are invited to submit comments on this notice by Monday, March 2, 2009.

EMPLOYEE PLANS

Notice 2009-16, page 572.

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

This notice contains updates for the corporate bond weighted

average interest rate for plan years beginning in February 2009; the 24-month average segment rates; the funding transitional segment rates applicable for February 2009; and the minimum present value transitional rates for January 2009.

ESTATE TAX

T.D. 9443, page 564.

Final regulations under section 7508A of the Code relate to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster.

GIFT TAX

T.D. 9443, page 564.

Final regulations under section 7508A of the Code relate to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster.

EMPLOYMENT TAX

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Final regulations under section 7508A of the Code relate to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster.

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Announcements of Disbarments and Suspensions begin on page 598.
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EXCISE TAX

T.D. 9443, page 564.

Final regulations under section 7508A of the Code relate to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster.

TAX CONVENTIONS

Announcement 2009–5, page 569.

This announcement provides the tax rates for various types of income under new tax treaties with Bulgaria and Iceland and a new protocol with Canada. The tables in this announcement provide supplemental withholding tax rates and exempt personal service income for Publication 515, *Withholding of Tax on Nonresident Aliens and Foreign Entities (For Withholding in 2008)*, and Publication 901, *U.S. Tax Treaties (Rev. April 2008)*.

ADMINISTRATIVE

Notice 2009–17, page 575.

This notice invites public comments regarding guidance to be provided to brokers, transferors, issuers, customers, and other affected persons concerning new requirements with respect to the reporting of a customer's basis in securities transactions and new rules for determining the basis of certain securities subject to the new reporting requirements. These new requirements and rules generally begin to take effect on January 1, 2011. Interested parties are invited to submit comments on this notice by Monday, March 2, 2009.

Announcement 2009–4, page 597.

This document withdraws proposed regulations (REG–149519–03, 2004–2 C.B. 1009) under section 707 of the Code regarding the treatment of transactions between a partnership and its partners as disguised sales of partnership interests between the partners under section 707(a)(2)(B). The withdrawal affects partnerships and their partners.

The IRS Mission

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

the tax law with integrity and fairness to all.

Introduction

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

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

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

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

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

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.

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

Part II.—Treaties and Tax Legislation.

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

Part III.—Administrative, Procedural, and Miscellaneous.

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

Part IV.—Items of General Interest.

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

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

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

Section 301.—Distributions of Property

A proposed regulation describes that a dividend distribution is made pro rata with respect to the class of stock upon which the distribution is made. See REG-143686-07, page 579.

Section 302.—Distributions in Redemption of Stock

26 CFR 1.302-5: Redemptions taxable as dividends.

A proposed regulation describes the timing and effect on shareholders in dividend equivalent redemptions, including the treatment of unrecovered basis. See REG-143686-07, page 579.

Section 304.—Redemption Through Use of Related Corporations

26 CFR 1.304-2: Acquisition by related corporation (other than a subsidiary).

A proposed regulation describes the timing and effect on shareholders in dividend equivalent redemptions involving related corporations that are not subsidiaries. A proposed regulation also describes the applicability of section 318(a) to determine control. See REG-143686-07, page 579.

Section 351.—Transfer to Corporation Controlled by Transferor

26 CFR 1.351-2: Receipt of property.

A proposed regulation describes the way to allocate consideration received for purposes of determining gain under section 351(b). See REG-143686-07, page 579.

Section 354.—Exchanges of Stock and Securities in Certain Reorganizations

26 CFR 1.354-1: Exchanges of stock and securities in certain reorganizations.

A proposed regulation describes the treatment of consideration received for shares of stock or securities that are exchanged solely or partly for money or other property. See REG-143686-07, page 579.

Section 355.—Distribution of Stock and Securities of a Controlled Corporation

26 CFR 1.355-1: Distribution of stock and securities of a controlled corporation.

A proposed regulation describes that a shareholder's exchange of all of the shareholders shares of stock within a class solely for cash is not an exchange described in section 355. See REG-143686-07, page 579.

Section 356.—Receipt of Additional Consideration

26 CFR 1.356-1: Receipt of additional consideration in connecting with an exchange.

A proposed regulation describes how consideration received must be allocated if the distribution of other property or money has the effect of a distribution of a dividend for purposes of determining gain under section 356. See REG-143686-07, page 579.

Section 358.—Basis to Distributees

26 CFR 1.358-2: Allocation of basis among non-recognition property in certain exchanges or distributions.

A proposed regulation describes how consideration received must be allocated if the distribution of other property or money has the effect of a distribution of a dividend for purposes of determining basis under section 358. A proposed regulation describes the section 351 transactions and the manner in which the basis in stock transferred is traced to shares received. See REG-143686-07, page 579.

Section 368.—Definitions Relating to Corporate Reorganizations

26 CFR 1.368-1: Purpose and scope of exception of reorganization exchanges.

A proposed regulation describes when the terms of an exchange can determine whether a transaction qualifies as a reorganization. See REG-143686-07, page 579.

Section 1001.—Determination of Amount of and Recognition of Gain or Loss

26 CFR 1.1001-6: Sales or exchanges.

A proposed regulation reflects the repeal of section 1002 and describes when the terms of an exchange can determine whether sections 354 or 361 (as opposed to section 1001) apply to an exchange. See REG-143686-07, page 579.

Section 7508A.—Authority to Postpone Certain Deadlines by Reason of Presidially Declared Disaster or Terroristic or Military Actions

26 CFR 301.7508A-1: Postponement of certain tax-related deadlines by reasons of a federally declared disaster or terroristic or military action.

T.D. 9443

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 301

Postponement of Certain Tax-Related Deadlines by Reason of a Federally Declared Disaster or Terroristic or Military Action

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains final regulations relating to postponement of certain tax-related deadlines either due to service in a combat zone or due to a federally declared disaster. The regulations reflect changes in the law made by the Victims of Terrorism Tax Relief Act of 2001, the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 (TEAMTRA), and current IRS practice. The regulations affect taxpayers serving

in a combat zone and taxpayers affected by a federally declared disaster.

DATES: *Effective Date:* These regulations are effective on January 15, 2009.

Applicability Dates: For dates of applicability, see §301.7508A-1(g).

FOR FURTHER INFORMATION CONTACT: Mary Ellen Keys, (202) 622-4570 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Procedure and Administration Regulations (26 CFR part 301). Section 7508A of the Internal Revenue Code (Code) relates to the postponement of certain tax-related acts by reason of a federally declared disaster or terroristic or military action. Section 7508A was added by section 911(a) of the Taxpayer Relief Act of 1997, Public Law 105-34 (111 Stat. 788, 877-78 (1997)) (the 1997 Act), which was effective for any period for performing an act that had not expired before December 5, 1997.

A notice of proposed rulemaking (REG-142680-06, 2008-35 I.R.B. 565) was published in the **Federal Register** (73 FR 40471-01) on July 15, 2008. No comments were received from the public in response to the notice of proposed rulemaking, and no public hearing was requested or held. In this Treasury decision, the proposed regulations are adopted as revised.

Explanation of Revisions

Section 301.7508A-1 of these final regulations is revised throughout to use the term “federally declared disaster” instead of the term “Presidentially declared disaster” when referring to any disaster determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, 42 U.S.C. §§5121, *et seq.* (the “Stafford Act”). Prior versions of these regulations and the proposed regulations included the term “Presidentially declared disaster” as defined in former Code section 1033(h)(3). Sec. 706(a) of TEAMTRA, Div. C of Public Law

110-343 (122 Stat. 3765, 3920), amended Code section 1033(h)(3) by replacing the term “Presidentially declared disaster” with “federally declared disaster” and providing that the term shall have the meaning given such term by section 165(h)(3)(C). Section 165(h)(3)(C), added by section 706(a) of TEAMTRA, defines the term “federally declared disaster” to mean any disaster subsequently determined by the President of the United States to warrant assistance by the Federal Government under the Stafford Act. This definition is substantially the same as the definition of “Presidentially declared disaster” under former section 1033(h)(C). Thus, these statutory changes in terminology do not materially impact the meaning of either the proposed or final regulations.

Section 301.7508A-1(d)(1) of the final regulations is revised to expand the definition of “affected taxpayer” to include any individual, business entity, or sole proprietorship not located in a covered disaster area, but whose records necessary to meet a deadline for an act specified in paragraph (c) of §301.7508A-1 are located in the covered disaster area. Section 301.7508A-1(d)(1) of the final regulations further expands the definition of *affected taxpayer* to include any individual visiting the covered disaster area who was killed or injured as a result of the disaster. These changes reflect current IRS practice of broadly defining the term “affected taxpayer.”

Section 301.7508A-1(f) of the final regulations is revised to include a new *Example 9*. *Example 9*, which reflects current IRS practice, explains the impact of disaster relief on installment agreement payments that become due during the postponement period. *Example 9* explains that the affected taxpayer’s obligation to make installment agreement payments is suspended during the postponement period. *Example 9* further explains that, because installment agreement payments pertain to pre-existing tax liabilities, interest and penalties continue to accrue during the postponement period.

Special Analyses

It has been determined that these final regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment

is not required. It has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. The regulations do not impose a collection of information requirement on small business entities, thus the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these final regulations is Mary Ellen Keys of the Office of the Associate Chief Counsel (Procedure and Administration).

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

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

Par. 2. Section 301.7508A-1 is amended by:

1. Revising the section heading and paragraphs (b), (d)(1)(vii), (d)(2), and (e).
2. Adding paragraphs (d)(1)(viii) and (d)(1)(ix), and (d)(3).
3. Removing paragraph (f), redesignating paragraphs (g) and (h) as paragraphs (f) and (g), respectively, and revising them.

The revisions and additions read as follows:

§301.7508A-1 Postponement of certain tax-related deadlines by reasons of a federally declared disaster or terroristic or military action.

* * * * *

(b) *Postponed deadlines*—(1) *In general.* In the case of a taxpayer determined by the Secretary to be affected by a federally declared disaster (as defined in section

1033(h)(3)) or a terroristic or military action (as defined in section 692(c)(2)), the Secretary may specify a postponement period (as defined in paragraph (d)(1) of this section) of up to one year that may be disregarded in determining under the internal revenue laws, in respect of any tax liability of the affected taxpayer (as defined in paragraph (d)(1) of this section)—

(i) Whether any or all of the acts described in paragraph (c) of this section were performed within the time prescribed;

(ii) The amount of interest, penalty, additional amount, or addition to the tax; and

(iii) The amount of credit or refund.

(2) *Effect of postponement period.*

When an affected taxpayer is required to perform a tax-related act by a due date that falls within the postponement period, the affected taxpayer is eligible for postponement of time to perform the act until the last day of the period. The affected taxpayer is eligible for relief from interest, penalties, additional amounts, or additions to tax during the postponement period.

(3) *Interaction between postponement period and extensions of time to file or pay—(i) In general.* The postponement period under section 7508A runs concurrently with extensions of time to file and pay, if any, under other sections of the Internal Revenue Code.

(ii) *Original due date prior to, but extended due date within, the postponement period.* When the original due date precedes the first day of the postponement period and the extended due date falls within the postponement period, the following rules apply. If an affected taxpayer received an extension of time to file, filing will be timely on or before the last day of the postponement period, and the taxpayer is eligible for relief from penalties or additions to tax related to the failure to file during the postponement period. Similarly, if an affected taxpayer received an extension of time to pay, payment will be timely on or before the last day of the postponement period, and the taxpayer is eligible for relief from interest, penalties, additions to tax, or additional amounts related to the failure to pay during the postponement period.

(4) *Due date not extended.* The postponement of the deadline of a tax-related act does not extend the due date for the act, but merely allows the IRS to disregard a

time period of up to one year for performance of the act. To the extent that other statutes may rely on the date a return is due to be filed, the postponement period will not change the due date of the return.

(5) *Additional relief.* The rules of this paragraph (b) demonstrate how the IRS generally implements section 7508A. The IRS may determine, however, that additional relief to taxpayers is appropriate and may provide additional relief to the extent allowed under section 7508A. To the extent that the IRS grants additional relief, the IRS will provide specific guidance on the scope of relief in the manner provided in paragraph (e) of this section.

* * * * *

(d) * * *(1) * * *

(vii) Any individual, business entity, or sole proprietorship not located in a covered disaster area, but whose records necessary to meet a deadline for an act specified in paragraph (c) of this section are located in the covered disaster area;

(viii) Any individual visiting the covered disaster area who was killed or injured as a result of the disaster; or

(ix) Any other person determined by the IRS to be affected by a federally declared disaster (within the meaning of section 1033(h)(3)).

(2) *Covered disaster area* means an area of a federally declared disaster (within the meaning of section 1033(h)(3)) to which the IRS has determined paragraph (b) of this section applies.

(3) *Postponement period* means the period of time (up to one year) that the IRS postpones deadlines for performing tax-related acts under section 7508A.

(e) *Notice of postponement of certain acts.* If a tax-related deadline is postponed under section 7508A and this section, the IRS will publish a revenue ruling, revenue procedure, notice, announcement, news release, or other guidance (see §601.601(d)(2) of this chapter) describing the acts postponed, the postponement period, and the location of the covered disaster area. Guidance under this paragraph (e) will be published as soon as practicable after the occurrence of a terroristic or military action or declaration of a federally declared disaster.

(f) *Examples.* The rules of this section are illustrated by the following examples:

Example 1. (i) Corporation X, a calendar year taxpayer, has its principal place of business in County

M in State W. Pursuant to a timely filed request for extension of time to file, Corporation X's 2008 Form 1120, "U.S. Corporation Income Tax Return," is due on September 15, 2009. Also due on September 15, 2009, is Corporation X's third quarter estimated tax payment for 2009. Corporation X's 2009 third quarter Form 720, "Quarterly Federal Excise Tax Return," and third quarter Form 941, "Employer's QUARTERLY Federal Tax Return," are due on October 31, 2009. In addition, Corporation X has an employment tax deposit due on September 15, 2009.

(ii) On September 1, 2009, a hurricane strikes County M in State W. On September 7, 2009, certain counties in State W (including County M) are determined to be disaster areas within the meaning of section 1033(h)(3) that are eligible for assistance by the Federal government under the Stafford Act. Also on September 7, 2009, the IRS determines that County M in State W is a covered disaster area and publishes guidance announcing that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after September 1, 2009, and on or before November 30, 2009, has been postponed to November 30, 2009, pursuant to section 7508A.

(iii) Because Corporation X's principal place of business is in County M, Corporation X is an affected taxpayer. Accordingly, Corporation X's 2008 Form 1120 will be timely if filed on or before November 30, 2009. Corporation X's 2009 third quarter estimated tax payment will be timely if made on or before November 30, 2009. In addition, pursuant to paragraph (c) of this section, Corporation X's 2009 third quarter Form 720 and third quarter Form 941 will be timely if filed on or before November 30, 2009. However, because deposits of taxes are excluded from the scope of paragraph (c) of this section, Corporation X's employment tax deposit is due on September 15, 2009. In addition, Corporation X's deposits relating to the third quarter Form 720 are not postponed. Absent reasonable cause, Corporation X is subject to the failure to deposit penalty under section 6656 and accrual of interest.

Example 2. The facts are the same as in *Example 1*, except that because of the severity of the hurricane, the IRS determines that postponement of government acts is necessary. During 2009, Corporation X's 2005 Form 1120 is being examined by the IRS. Pursuant to a timely filed request for extension of time to file, Corporation X timely filed its 2005 Form 1120 on September 15, 2006. Without application of this section, the statute of limitation on assessment for the 2005 income tax year will expire on September 15, 2009. However, pursuant to paragraph (c) of this section, assessment of tax is one of the government acts for which up to one year may be disregarded. Because September 15, 2009, falls within the period in which government acts are postponed, the statute of limitation on assessment for Corporation X's 2005 income tax will expire on November 30, 2009. Because Corporation X did not timely file an extension of time to pay, payment of its 2005 income tax was due on March 15, 2006. As such, Corporation X will be subject to the failure to pay penalty and related interest beginning on March 15, 2006. The due date for payment of Corporation X's 2005 income tax preceded the postponement period. Therefore, Corporation X is not entitled to the suspension of interest or penal-

ties during the disaster period with respect to its 2005 income tax liability.

Example 3. The facts are the same as in *Example 2*, except that the examination of the 2005 taxable year was completed earlier in 2009, and on July 28, 2009, the IRS mailed a statutory notice of deficiency to Corporation X. Without application of this section, Corporation X has 90 days (or until October 26, 2009) to file a petition with the Tax Court. However, pursuant to paragraph (c) of this section, filing a petition with the Tax Court is one of the taxpayer acts for which a period of up to one year may be disregarded. Because Corporation X is an affected taxpayer, Corporation X's petition to the Tax Court will be timely if filed on or before November 30, 2009, the last day of the postponement period.

Example 4. (i) H and W, individual calendar year taxpayers, intend to file a joint Form 1040, "U.S. Individual Income Tax Return," for the 2008 taxable year and are required to file a Schedule H, "Household Employment Taxes." The joint return is due on April 15, 2009. H and W's principal residence is in County M in State Q.

(ii) On April 2, 2009, a severe ice storm strikes County M. On April 5, 2009, certain counties in State Q (including County M) are determined to be disaster areas within the meaning of section 1033(h)(3) that are eligible for assistance by the Federal government under the Stafford Act. Also on April 5, 2009, the IRS determines that County M in State Q is a covered disaster area and publishes guidance announcing that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after April 2, 2009, and on or before June 2, 2009, has been postponed to June 2, 2009.

(iii) Because H and W's principal residence is in County M, H and W are affected taxpayers. April 15, 2009, the due date for the filing of H and W's 2008 Form 1040 and Schedule H, falls within the postponement period described in the IRS published guidance. Thus, H and W's return will be timely if filed on or before June 2, 2009. If H and W request an extension of time to file under section 6081 on or before June 2, 2009, the extension is deemed to have been filed by April 15, 2009. Thus, H and W's return will be timely if filed on or before October 15, 2009.

(iv) April 15, 2009, is also the due date for the payment due on the return. This date falls within the postponement period described in the IRS published guidance. Thus, the payment of tax due with the return will be timely if paid on or before June 2, 2009, the last day of the postponement period. If H and W fail to pay the tax due on the 2008 Form 1040 by June 2, 2009, and do not receive an extension of time to pay under section 6161, H and W will be subject to failure to pay penalties and accrual of interest beginning on June 3, 2009.

Example 5. (i) H and W, residents of County D in State G, intend to file an amended return to request a refund of 2008 taxes. H and W timely filed their 2008 income tax return on April 15, 2009. Under section 6511(a), H and W's amended 2008 tax return must be filed on or before April 16, 2012 (because April 15, 2012, falls on a Sunday, H and W's amended return was due to be filed on April 16, 2012).

(ii) On April 2, 2012, an earthquake strikes County D. On April 6, 2012, certain counties in State G (including County D) are determined to be disaster areas within the meaning of section 1033(h)(3) that

are eligible for assistance by the Federal government under the Stafford Act. Also on April 6, 2012, the IRS determines that County D in State G is a covered disaster area and publishes guidance announcing that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after April 2, 2012, and on or before October 2, 2012, has been postponed to October 2, 2012.

(iii) Under paragraph (c) of this section, filing a claim for refund of tax is one of the taxpayer acts for which the IRS may disregard a period of up to one year. The postponement period for this disaster begins on April 2, 2012, and ends on October 2, 2012. Accordingly, H and W's claim for refund for 2008 taxes will be timely if filed on or before October 2, 2012. Moreover, in applying the lookback period in section 6511(b)(2)(A), which limits the amount of the allowable refund, the period from October 2, 2012, back to April 2, 2012, is disregarded under paragraph (b)(1)(iii) of this section. Thus, if the claim is filed on or before October 2, 2012, amounts deemed paid on April 15, 2009, under section 6513(b), such as estimated tax and tax withheld from wages, will have been paid within the lookback period of section 6511(b)(2)(A).

Example 6. (i) A is an unmarried, calendar year taxpayer whose principal residence is located in County W in State Q. A intends to file a Form 1040 for the 2008 taxable year. The return is due on April 15, 2009. A timely files Form 4868, "Application for Automatic Extension of Time To File U.S. Individual Income Tax Return." Due to A's timely filing of Form 4868, the extended filing deadline for A's 2008 tax return is October 15, 2009. Because A timely requested an extension of time to file, A will not be subject to the failure to file penalty under section 6651(a)(1), if A files the 2008 Form 1040 on or before October 15, 2009. However, A failed to pay the tax due on the return by April 15, 2009, and did not receive an extension of time to pay under section 6161. Absent reasonable cause, A is subject to the failure to pay penalty under section 6651(a)(2) and accrual of interest.

(ii) On September 30, 2009, a blizzard strikes County W. On October 5, 2009, certain counties in State Q (including County W) are determined to be disaster areas within the meaning of section 1033(h)(3) that are eligible for assistance by the Federal government under the Stafford Act. Also on October 5, 2009, the IRS determines that County W in State Q is a covered disaster area and announces that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after September 30, 2009, and on or before December 2, 2009, has been postponed to December 2, 2009.

(iii) Because A's principal residence is in County W, A is an affected taxpayer. Because October 15, 2009, the extended due date to file A's 2008 Form 1040, falls within the postponement period described in the IRS's published guidance, A's return is timely if filed on or before December 2, 2009. However, the payment due date, April 15, 2009, preceded the postponement period. Thus, A will continue to be subject to failure to pay penalties and accrual of interest during the postponement period.

Example 7. (i) H and W, individual calendar year taxpayers, intend to file a joint Form 1040 for the

2008 taxable year. The joint return is due on April 15, 2009. After credits for taxes withheld on wages and estimated tax payments, H and W owe tax for the 2008 taxable year. H and W's principal residence is in County J in State W.

(ii) On March 3, 2009, severe flooding strikes County J. On March 6, 2009, certain counties in State W (including County J) are determined to be disaster areas within the meaning of section 1033(h)(3) that are eligible for assistance by the Federal government under the Stafford Act. Also on March 6, 2009, the IRS determines that County J in State W is a covered disaster area and publishes guidance announcing that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after March 3, 2009, and on or before June 1, 2009, has been postponed to June 1, 2009.

(iii) Because H and W's principal residence is in County J, H and W are affected taxpayers. April 15, 2009, the due date for filing the 2008 joint return, falls within the postponement period described in the IRS published guidance. Therefore, H and W's joint return without extension will be timely if filed on or before June 1, 2009. Similarly, H and W's 2008 income taxes will be timely paid if paid on or before June 1, 2009.

(iv) On April 30, 2009, H and W timely file Form 4868, "Application for Automatic Extension of Time To File U.S. Individual Income Tax Return." H and W's extension will be deemed to have been filed on April 15, 2009. Thus, H and W's 2008 income tax return will be timely if filed on or before October 15, 2009.

(v) H and W did not request or receive an extension of time to pay. Therefore, the payment of tax due with the 2008 joint return will be timely if paid on or before June 1, 2009. If H and W fail to pay the tax due on the 2008 joint return by June 1, 2009, H and W will be subject to failure to pay penalties and accrual of interest beginning on June 2, 2009.

Example 8. The facts are the same as in *Example 7* except that H and W file the joint 2008 return and pay the tax due on April 15, 2009. Later, H and W discover additional deductions that would lower their taxable income for 2008. On June 1, 2012, H and W file a claim for refund under section 6511(a). The amount of H and W's overpayment exceeds the amount of taxes paid on April 15, 2009. Section 6511(a) generally requires that a claim for refund be filed within three years from the time the return was filed or two years from the time the tax was paid, whichever period expires later. Section 6511(b)(2)(A) includes within the lookback period the period of an extension of time to file. Thus, payments that H and W made on or after June 1, 2009, would be eligible to be refunded. Because the period from April 15, 2009, to June 1, 2009, is disregarded, the payments H and W made on April 15, 2009 (including withholding or estimated tax payments deemed to have been made on April 15, 2009) would also be included in the section 6511(b)(2)(A) lookback period. Thus, H and W are entitled to a full refund in the amount of their overpayment.

Example 9. (i) H and W, individual calendar year taxpayers, entered into an installment agreement with respect to their 2006 tax liabilities. H and W's installment agreement required H and W to make regularly scheduled installment payments on the 15th day of the

month for the next 60 months. H and W's principal residence is in County K in State X.

(ii) On May 1, 2009, severe flooding strikes County K. On May 5, 2009, certain counties in State X including County K) are determined by the Federal government to be disaster areas within the meaning of section 1033(h)(3), and are eligible for assistance under the Stafford Act. Also on May 5, 2009, the IRS determines that County K in State X is a covered disaster area and publishes guidance announcing that the time period for affected taxpayers to file returns, pay taxes, and perform other time-sensitive acts falling on or after May 1, 2009, and on or before July 1, 2009, has been postponed to July 1, 2009.

(iii) Because H and W's principal residence is in County K, H and W are affected taxpayers. Pursuant to the IRS's grant of relief under section 7508A,

H and W's installment agreement payments that become due during the postponement period are suspended until after the postponement period has ended. H and W will be required to resume payments no later than August 15, 2009. Skipped payments will be tacked on at the end of the installment payment period. Because the installment agreement pertains to prior year tax liabilities, interest and penalties will continue to accrue. H and W may, however, be entitled to abatement of the failure to pay penalties incurred during the postponement period upon establishing reasonable cause.

(g) *Effective/applicability date.* This section applies to disasters declared after January 15, 2009.

Linda E. Stiff,
*Deputy Commissioner for
Services and Enforcement.*

Approved January 6, 2009.

Eric Solomon,
*Assistant Secretary of
the Treasury (Tax Policy).*

(Filed by the Office of the Federal Register on January 14, 2009, 8:45 a.m., and published in the issue of the Federal Register for January 15, 2009, 74 F.R. 2370)

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions and Other Related Items

Supplemental Tables of Income Tax Rates Under New Income Tax Conventions

Announcement 2009–5

The United States recently exchanged instruments of ratification for new income tax treaties with Bulgaria and Iceland and a new protocol to the income tax treaty with Canada. The effective dates are as follows:

Bulgaria. The provisions for withholding tax at source are effective for amounts paid or credited on or after January 1, 2009. For other taxes, the treaty is effective for tax periods beginning on or after January 1, 2009.

Canada. The provisions for withholding tax at source are generally effective for

amounts paid or credited on or after February 1, 2009. For other taxes, the protocol is effective for tax periods beginning on or after January 1, 2009. Certain provisions, none of which are discussed in this announcement, have different effective dates.

Iceland. The provisions for withholding tax at source are effective for amounts derived on or after January 1, 2009. For other taxes, the new treaty is effective for tax years beginning on or after January 1, 2009.

An individual who was otherwise entitled to benefits under Article 21 (Teachers) of the former treaty can continue to apply those provisions. A person entitled to benefits under the former treaty can elect to have that treaty apply in its entirety for

a twelve-month period following the date the new treaty would otherwise apply.

Tables 1 and 2. The following tables can be used to supplement Tables 1 and 2 in Publication 515, *Withholding of Tax on Nonresident Aliens and Foreign Entities (For Withholding in 2008)*, and Publication 901, *U.S. Tax Treaties*. The footnotes in those publications that relate to the column headings in these tables generally apply to these entries. These tables are intended only as a summary, and the full text of the relevant income tax treaty and protocol should be consulted.

The complete texts of the Bulgaria and Iceland treaties and the Canada protocol are available on the IRS website at www.irs.gov.

Table 1. Withholding Tax Rates on Income Other Than Personal Service Income

| Income code number | | 1 | 2 | 3 | 6 | 7 | 9 | 10 | 11 | 12 | 13 | 14 | 21 |
|--------------------|----|------------|--------------|------------|-------------|------------|--------|----------|---------|--------|----|----------|----|
| Country/Code | | | | | | | | | | | | | |
| Bulgaria | BU | 5 a,b,c | 5 a,b,c,d | 5 a,b,c | 10 a,c,e | 5 a,c,e | 0 a | 5 a | 5 a | 5 a | 30 | 0 f,g | 30 |
| Canada | CA | 0 a,b,k | 0 a,b,d,k | 0 a,b,k | 15 a,e | 5 a,e | 0 i | 0 a | 10 a | 0 a | 30 | 15 | 0 |
| Iceland | IC | 0 a,j | 0 a,d,j | 0 a,j | 15 a,c,e | 5 a,c,e | 0 a | 0 a,h | 5 a | 0 a | 30 | 0 g | 30 |

Income Codes

- | | |
|---|---|
| 1 Interest paid by U.S. obligors — General | 10 Industrial royalties |
| 2 Interest on real property mortgages | 11 Copyright royalties — Motion pictures and Television |
| 3 Interest paid to controlling foreign corporations | 12 Copyright royalties — Other |
| 6 Dividends paid by U.S. corporations — General | 13 Real property income and Natural resources royalties |
| 7 Dividends qualifying for direct dividend rate | 14 Pensions and annuities |
| 9 Capital gains | 21 Social security payments |

Footnotes

- a The exemption or reduction in rate does not apply if the recipient has a permanent establishment in the United States and the income paid is attributable to this permanent establishment.
- b The rate is 10% (15% for Canada) for contingent interest that does not qualify as portfolio interest. Generally, this is interest based on receipts, sales, income, or changes in the value of property.
- c Amounts paid to a pension fund that are not derived from the carrying on of a business by the pension fund are exempt. For Bulgaria, interest paid to a financial institution is exempt.
- d The exemption or reduced rate does not apply to an excess inclusion for a residual interest in a real estate mortgage investment conduit (REMIC).

- e The rate in column 6 applies to dividends paid by a regulated investment company (RIC) or real estate investment trust (REIT). However, that rate applies to dividends paid by a REIT only if the beneficial owner of the dividends is (a) an individual (and for Bulgaria, a pension fund) holding not more than a 10% interest in the REIT, (b) a person holding not more than 5% of any class of the REIT's stock and the dividends are paid on stock that is publicly traded, or (c) a person holding not more than a 10% interest in the REIT and the REIT is diversified. For Bulgaria, dividends paid to pension fund from a RIC, or a REIT that meets the above conditions, are exempt.
- f Includes alimony.
- g A 30% rate applies to U.S. government pensions (federal, state, or local); however, pensions paid to an individual who is both a resident and national of the treaty country are exempt from U.S. tax.
- h The rate is 5% for trademarks and any information for rentals of industrial, commercial, or scientific equipment.
- i Generally, if the property was owned by the Canadian resident on September 26, 1980, not as part of the business property of a permanent establishment in the U.S., the taxable gain is limited to the appreciation after 1984. Capital gains on personal property not belonging to a permanent establishment of the taxpayer in the U.S. are exempt.
- j The rate is 15% for interest determined with reference to (a) receipts, sales, income, profits or other cash flow of the debtor or a related person, (b) any change in the value of any property of the debtor or a related person, or (c) any dividend, partnership distribution, or similar payment made by the debtor or related person.
- k If the payor and the beneficial owner are related, the rate for interest paid or credited in 2009 is 4%.

Table 2. Compensation for Personal Services Performed in United States Exempt from Withholding and U.S. Income Tax Under Income Tax Treaties

| Country | Code | Category of personal services | Maximum presence in U.S. | Required Employer or Payer | Maximum Amount of Compensation | Article No. |
|----------|------|--|--------------------------|---|--------------------------------|-------------|
| | | Purpose | | | | |
| Bulgaria | 16 | Independent personal services ¹ | No limit | Any contractor | No limit | 7 |
| | 17 | Dependent personal services ^{4,5} | 183 days | Any foreign resident | No limit | 14 |
| | 20 | Public entertainment | No limit | Any U.S. or foreign resident | \$15,000 p.a. ⁶ | 16 |
| | 18 | Teaching ² | 2 years | U.S. educational or research institution | No limit | 19(2) |
| | 19 | Studying and training: ⁸ Remittances or allowances | No limit ³ | Any foreign resident | No limit | 19(1)(a) |
| | | Compensation during study or training | No limit ³ | Any U.S. or foreign resident ⁹ | \$9,000 p.a. | 19(1)(b) |

| Country | Code | Category of personal services | Maximum presence in U.S. | Required Employer or Payer | Maximum Amount of Compensation | Article No. |
|---------|------|---|--------------------------|--|--------------------------------|-------------|
| | | Purpose | | | | |
| Canada | 16 | Independent personal services ¹ | No limit | Any contractor | No limit | VII |
| | 20 | Public entertainment | No limit | Any contractor | \$15,000 p.a. ⁶ | XVI |
| | 17 | Dependent personal services | No limit | Any U.S. or foreign resident | \$10,000 | XV |
| | | | 183 days | Any foreign resident ⁵ | No limit ⁷ | XV |
| | 20 | Public entertainment | No limit | Any U.S. or foreign resident | \$15,000 p.a. ⁶ | XVI |
| | 19 | Studying and training: Remittances or allowances ⁸ | No limit ³ | Any foreign resident | No limit | XX |
| Iceland | 15 | Scholarship or fellowship grant | 5 years | Any U.S. or foreign resident ¹⁰ | No limit | 19(1) |
| | 16 | Independent personal services ¹ | No limit | Any contractor | No limit | 7 |
| | 17 | Dependent personal services ^{4,5} | 183 days | Any foreign resident | No limit | 14 |
| | 20 | Public entertainment | No limit | Any U.S. or foreign resident | \$20,000 p.a. ⁶ | 16 |
| | 19 | Studying and training: Remittances or allowances | 5 years | Any foreign resident | No limit | 19(1) |
| | | | 5 years | Any U.S. or foreign resident | \$9,000 p.a. | 19(1) |
| | | | 12 consec. mo. | Any U.S. or foreign resident ⁹ | \$9,000 | 19(2) |
| | | | 1 year | U.S. Government or its contractor | \$9,000 | 19(3) |

Footnotes

- 1 The exemption does not apply to any amounts attributable to a permanent establishment in the United States.
- 2 Does not apply to income from research work primarily for private benefit.
- 3 Exemption applies to a business apprentice (trainee) only for a period not exceeding 2 years (1 year for Canada) from the date of arrival in the United States.
- 4 The exemption does not apply to fees paid to a director of a U.S. corporation.
- 5 The exemption does not apply if the employee's compensation is borne by a permanent establishment that the employer has in the United States.
- 6 The exemption does not apply if gross receipts (including reimbursements) exceed this amount during the year.
- 7 Does not apply to compensation paid to public entertainers.
- 8 Applies only to full-time student or trainee.
- 9 Applies only if training or experience is received from a person other than the alien's employer.
- 10 Grant must be from nonprofit organization.

Part III. Administrative, Procedural, and Miscellaneous

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

Notice 2009-16

This notice provides guidance as to the corporate bond weighted average interest rate and the permissible range of interest rates specified under § 412(b)(5)(B)(ii)(II) of the Internal Revenue Code as in effect for plan years beginning before 2008. It also provides guidance on the corporate bond monthly yield curve (and the corresponding spot segment rates), the 24-month average segment rates, and the funding transitional segment rates under § 430(h)(2). In addition, this notice provides guidance as to the interest rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning before 2008, the 30-year Treasury weighted average rate under § 431(c)(6)(E)(ii)(I), and the min-

imum present value segment rates under § 417(e)(3)(D) as in effect for plan years beginning after 2007.

CORPORATE BOND WEIGHTED AVERAGE INTEREST RATE

Sections 412(b)(5)(B)(ii) and 412(l)(7)(C)(i), as amended by the Pension Funding Equity Act of 2004 and by the Pension Protection Act of 2006 (PPA), provide that the interest rates used to calculate current liability and to determine the required contribution under § 412(l) for plan years beginning in 2004 through 2007 must be within a permissible range based on the weighted average of the rates of interest on amounts invested conservatively in long term investment grade corporate bonds during the 4-year period ending on the last day before the beginning of the plan year.

Notice 2004-34, 2004-1 C.B. 848, provides guidelines for determining the corporate bond weighted average interest rate

and the resulting permissible range of interest rates used to calculate current liability. That notice establishes that the corporate bond weighted average is based on the monthly composite corporate bond rate derived from designated corporate bond indices. The methodology for determining the monthly composite corporate bond rate as set forth in Notice 2004-34 continues to apply in determining that rate. See Notice 2006-75, 2006-2 C.B. 366.

The composite corporate bond rate for January 2009 is 6.47 percent. Pursuant to Notice 2004-34, the Service has determined this rate as the average of the monthly yields for the included corporate bond indices for that month.

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

| For Plan Years Beginning in | | Corporate Bond Weighted Average | Permissible Range | |
|-----------------------------|------|---------------------------------|-------------------|------|
| Month | Year | | 90% | 100% |
| February | 2009 | 6.32 | 5.69 | 6.32 |

YIELD CURVE AND SEGMENT RATES

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

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

Notice 2007-81, 2007-44 I.R.B. 899, provides guidelines for determining the

monthly corporate bond yield curve, the 24-month average corporate bond segment rates, and the funding transitional segment rates used to compute the target normal cost and the funding target. Pursuant to Notice 2007-81, the monthly corporate bond yield curve derived from January 2009 data is in Table I at the end of this notice. The spot first, second, and third segment rates for the month of January 2009 are, respectively, 5.20, 6.80, and 6.31. The three 24-month average corporate bond segment rates applicable for February 2009 under the election of § 430(h)(2)(G)(iv) are as follows:

| First Segment | Second Segment | Third Segment |
|---------------|----------------|---------------|
| 5.31 | 6.49 | 6.69 |

The transitional segment rates under § 430(h)(2)(G) applicable for February 2009, taking into account the corporate

bond weighted average of 6.32 stated above, are as follows:

| For Plan Years Beginning in | First Segment | Second Segment | Third Segment |
|--------------------------------|------------------|-------------------|------------------|
| 2008 | 5.98 | 6.38 | 6.44 |
| 2009 | 5.65 | 6.43 | 6.57 |

30-YEAR TREASURY SECURITIES INTEREST RATES

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

rate of interest on 30-year Treasury securities as specified by the Commissioner for that month in revenue rulings, notices or other guidance published in the Internal Revenue Bulletin.

The rate of interest on 30-year Treasury securities for January 2009 is 3.13 percent. The Service has determined this rate as the monthly average of the daily determination of yield on the 30-year Treasury bond maturing in May 2038.

Generally for plan years beginning after 2007, § 431 specifies the minimum funding requirements that apply to multiemployer plans pursuant to § 412. Section 431(c)(6)(B) specifies a minimum

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

| For Plan Years Beginning in | | 30-Year Treasury Weighted Average | Permissible Range | |
|--------------------------------|------|--|-------------------|------|
| Month | Year | | 90% | 105% |
| February | 2009 | 4.54 | 4.09 | 4.77 |

MINIMUM PRESENT VALUE SEGMENT RATES

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

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

ing the minimum present value segment rates. Pursuant to that notice, the minimum present value transitional segment rates determined for January 2009, taking into account the January 2009 30-year Treasury rate of 3.13 stated above, are as follows:

| For Plan Years Beginning in | First Segment | Second Segment | Third Segment |
|--------------------------------|------------------|-------------------|------------------|
| 2008 | 3.54 | 3.86 | 3.77 |
| 2009 | 3.96 | 4.60 | 4.40 |

DRAFTING INFORMATION

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

Tax Exempt and Government Entities Division. Mr. Montanaro may be e-mailed at RetirementPlanQuestions@irs.gov.

Table I
Monthly Yield Curve for January 2009

| <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> |
|-----------------|--------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|
| 0.5 | 3.90 | 20.5 | 6.76 | 40.5 | 6.26 | 60.5 | 6.11 | 80.5 | 6.03 |
| 1.0 | 4.38 | 21.0 | 6.73 | 41.0 | 6.25 | 61.0 | 6.11 | 81.0 | 6.03 |
| 1.5 | 4.79 | 21.5 | 6.71 | 41.5 | 6.25 | 61.5 | 6.10 | 81.5 | 6.03 |
| 2.0 | 5.11 | 22.0 | 6.68 | 42.0 | 6.24 | 62.0 | 6.10 | 82.0 | 6.03 |
| 2.5 | 5.34 | 22.5 | 6.66 | 42.5 | 6.24 | 62.5 | 6.10 | 82.5 | 6.03 |
| 3.0 | 5.49 | 23.0 | 6.64 | 43.0 | 6.23 | 63.0 | 6.10 | 83.0 | 6.02 |
| 3.5 | 5.61 | 23.5 | 6.61 | 43.5 | 6.23 | 63.5 | 6.09 | 83.5 | 6.02 |
| 4.0 | 5.70 | 24.0 | 6.59 | 44.0 | 6.22 | 64.0 | 6.09 | 84.0 | 6.02 |
| 4.5 | 5.80 | 24.5 | 6.57 | 44.5 | 6.22 | 64.5 | 6.09 | 84.5 | 6.02 |
| 5.0 | 5.90 | 25.0 | 6.56 | 45.0 | 6.21 | 65.0 | 6.09 | 85.0 | 6.02 |
| 5.5 | 6.00 | 25.5 | 6.54 | 45.5 | 6.21 | 65.5 | 6.08 | 85.5 | 6.02 |
| 6.0 | 6.11 | 26.0 | 6.52 | 46.0 | 6.20 | 66.0 | 6.08 | 86.0 | 6.02 |
| 6.5 | 6.22 | 26.5 | 6.51 | 46.5 | 6.20 | 66.5 | 6.08 | 86.5 | 6.02 |
| 7.0 | 6.33 | 27.0 | 6.49 | 47.0 | 6.20 | 67.0 | 6.08 | 87.0 | 6.01 |
| 7.5 | 6.44 | 27.5 | 6.48 | 47.5 | 6.19 | 67.5 | 6.08 | 87.5 | 6.01 |
| 8.0 | 6.54 | 28.0 | 6.47 | 48.0 | 6.19 | 68.0 | 6.07 | 88.0 | 6.01 |
| 8.5 | 6.64 | 28.5 | 6.45 | 48.5 | 6.18 | 68.5 | 6.07 | 88.5 | 6.01 |
| 9.0 | 6.72 | 29.0 | 6.44 | 49.0 | 6.18 | 69.0 | 6.07 | 89.0 | 6.01 |
| 9.5 | 6.80 | 29.5 | 6.43 | 49.5 | 6.18 | 69.5 | 6.07 | 89.5 | 6.01 |
| 10.0 | 6.87 | 30.0 | 6.42 | 50.0 | 6.17 | 70.0 | 6.07 | 90.0 | 6.01 |
| 10.5 | 6.92 | 30.5 | 6.41 | 50.5 | 6.17 | 70.5 | 6.06 | 90.5 | 6.01 |
| 11.0 | 6.97 | 31.0 | 6.40 | 51.0 | 6.16 | 71.0 | 6.06 | 91.0 | 6.00 |
| 11.5 | 7.01 | 31.5 | 6.39 | 51.5 | 6.16 | 71.5 | 6.06 | 91.5 | 6.00 |
| 12.0 | 7.03 | 32.0 | 6.38 | 52.0 | 6.16 | 72.0 | 6.06 | 92.0 | 6.00 |
| 12.5 | 7.05 | 32.5 | 6.37 | 52.5 | 6.15 | 72.5 | 6.06 | 92.5 | 6.00 |
| 13.0 | 7.06 | 33.0 | 6.36 | 53.0 | 6.15 | 73.0 | 6.06 | 93.0 | 6.00 |
| 13.5 | 7.07 | 33.5 | 6.36 | 53.5 | 6.15 | 73.5 | 6.05 | 93.5 | 6.00 |
| 14.0 | 7.06 | 34.0 | 6.35 | 54.0 | 6.14 | 74.0 | 6.05 | 94.0 | 6.00 |
| 14.5 | 7.06 | 34.5 | 6.34 | 54.5 | 6.14 | 74.5 | 6.05 | 94.5 | 6.00 |
| 15.0 | 7.04 | 35.0 | 6.33 | 55.0 | 6.14 | 75.0 | 6.05 | 95.0 | 6.00 |
| 15.5 | 7.02 | 35.5 | 6.32 | 55.5 | 6.14 | 75.5 | 6.05 | 95.5 | 6.00 |
| 16.0 | 7.00 | 36.0 | 6.32 | 56.0 | 6.13 | 76.0 | 6.04 | 96.0 | 5.99 |
| 16.5 | 6.98 | 36.5 | 6.31 | 56.5 | 6.13 | 76.5 | 6.04 | 96.5 | 5.99 |
| 17.0 | 6.95 | 37.0 | 6.30 | 57.0 | 6.13 | 77.0 | 6.04 | 97.0 | 5.99 |
| 17.5 | 6.93 | 37.5 | 6.30 | 57.5 | 6.12 | 77.5 | 6.04 | 97.5 | 5.99 |
| 18.0 | 6.90 | 38.0 | 6.29 | 58.0 | 6.12 | 78.0 | 6.04 | 98.0 | 5.99 |
| 18.5 | 6.87 | 38.5 | 6.28 | 58.5 | 6.12 | 78.5 | 6.04 | 98.5 | 5.99 |
| 19.0 | 6.84 | 39.0 | 6.28 | 59.0 | 6.12 | 79.0 | 6.04 | 99.0 | 5.99 |
| 19.5 | 6.81 | 39.5 | 6.27 | 59.5 | 6.11 | 79.5 | 6.03 | 99.5 | 5.99 |
| 20.0 | 6.79 | 40.0 | 6.27 | 60.0 | 6.11 | 80.0 | 6.03 | 100.0 | 5.99 |

Information Reporting of Customer's Basis in Securities Transactions

Notice 2009-17

PURPOSE

This notice invites public comments regarding guidance to be provided to brokers, transferors, issuers, customers, and other affected persons concerning new requirements with respect to the reporting of a customer's basis in securities transactions. The new reporting requirements are in sections 6045(g) and (h), 6045A, and 6045B of the Internal Revenue Code, which were added by section 403 of the Energy Improvement and Extension Act of 2008, Div. B of Pub. L. No. 110-343, 122 Stat. 3765 (the Act). This portion of the Act also amended section 1012 to provide new rules for determining the basis of certain securities subject to the new reporting requirements. The new reporting requirements and basis rules generally begin to take effect on January 1, 2011.

The Department of the Treasury and Internal Revenue Service propose to issue guidance on compliance with the new reporting requirements and basis rules. To assist them in drafting guidance under the new provisions, they are requesting comments from all affected persons.

BACKGROUND

Section 6045(a) requires brokers to file with the Service annual information returns showing the gross proceeds realized by customers from various sales transactions. Under new section 6045(g), every broker that is required to file a return under section 6045(a) from the sale of a covered security must include in the return the customer's adjusted basis in the security and whether any gain or loss with respect to that security is long-term or short-term.

Section 6045(g)(3)(A) provides that a "covered security" is any specified security acquired on or after the applicable date if the security (1) was acquired through a transaction in the account of which the security was held, or (2) was transferred to that account from an account in which the security was a covered security, but only if the transferee broker received a statement under section 6045A (described be-

low) with respect to the transfer. Section 6045(g)(3)(B) provides that a "specified security" is: (1) any share of stock in a corporation (including stock of a regulated investment company); (2) any note, bond, debenture, or other evidence of indebtedness; (3) any commodity, or a contract or a derivative with respect to the commodity, if the Secretary determines that adjusted basis reporting is appropriate; and (4) any other financial instrument with respect to which the Secretary determines that adjusted basis reporting is appropriate. In the case of a short sale, section 6045(g)(5) provides that gross proceeds and basis reporting under section 6045 generally is required in the year in which the short sale is closed (rather than, as under the present law rule for gross proceeds reporting, the year in which the short sale is entered into). In addition, section 6045(h) provides that gross proceeds and basis reporting is required when there is a lapse of, or a closing transaction with respect to, an option on a specified security or an exercise of a cash-settled option on a specified security.

For stock in a corporation (other than stock in a regulated investment company or stock acquired in connection with a dividend reinvestment plan), section 6045(g)(3)(C)(i) provides that the applicable date is January 1, 2011. For stock in a regulated investment company or stock acquired in connection with a dividend reinvestment plan (for which additional rules are described below), section 6045(g)(3)(C)(ii) provides that the applicable date is January 1, 2012. For any other specified security, section 6045(g)(3)(C)(iii) provides that the applicable date is January 1, 2013, or such later date as determined by the Secretary. The reporting rules related to options transactions apply only to options granted or acquired on or after January 1, 2013, as provided in section 6045(h)(3).

The customer's adjusted basis required to be reported is determined under the following rules. Under section 6045(g)(2)(B)(i)(I), the adjusted basis of any security (other than stock in a regulated investment company or stock acquired in connection with a dividend reinvestment plan) is determined under the first-in first-out method unless the customer notifies the broker by means of making an adequate identification of the stock sold or transferred at the time of

sale. Under section 6045(g)(2)(B)(i)(II), the adjusted basis of stock in a regulated investment company or stock acquired in connection with a dividend reinvestment plan is determined in accordance with the broker's default method under section 1012 unless the customer notifies the broker that the customer elects another permitted method.

For any sale, exchange, or other disposition of a specified security on or after the applicable date, section 1012(c) provides that the conventions prescribed by regulations under section 1012 for determining adjusted basis (the first-in first-out, specific identification, and average basis conventions) apply on an account-by-account basis. Section 1012(c)(2) allows a regulated investment company, however, to elect (at the time and in the form and manner prescribed by the Secretary), on a stockholder-by-stockholder basis, to treat as covered securities all stock in the company held by the stockholder without regard to when the stock was acquired. When this election applies, the average basis of a customer's regulated investment company stock is determined by taking into account shares of stock acquired before, on, and after January 1, 2012. A similar election is allowed for any broker holding stock in a regulated investment company as a nominee of the beneficial owner of the stock.

If stock is acquired on or after January 1, 2011, in connection with a dividend reinvestment plan, section 1012(d)(1) provides that the basis of that stock is determined under one of the basis computation methods permissible for stock in a regulated investment company. Accordingly, an average cost method may be used for determining the basis of stock acquired in connection with a dividend reinvestment plan. Section 1012(d)(4)(A) provides that a dividend reinvestment plan is any arrangement under which dividends on stock are reinvested in stock identical to the stock with respect to which the dividends are paid. Section 1012(d)(4)(B) further provides that stock is treated as acquired in connection with a dividend reinvestment plan if the stock is acquired pursuant to the plan or if the dividends paid on the stock are subject to the plan. Under section 1012(d)(3), in determining basis under this rule, the account-by-account rules of section 1012(c), including

the election available to regulated investment companies, apply. The special rule for stock acquired in connection with a dividend reinvestment plan, however, applies only while the stock is held as part of the plan. If stock to which this rule applies is transferred to another account, section 1012(d)(2) provides that the stock will have a cost basis in that other account equal to its basis in the dividend reinvestment plan immediately before the transfer (with any proper adjustment for charges incurred in connection with the transfer). After the transfer, however, the transferee broker may use the otherwise applicable convention (that is, the first-in first-out method or the specific identification method) for determining which shares are sold when a sale is made of some but not all shares of a particular security.

Section 6045(g)(2)(B)(ii) provides that, unless the Secretary provides otherwise, a customer's adjusted basis in a covered security generally is determined without taking into account the effect on basis of the wash sale rules of section 1091 unless the acquisition and sale transactions resulting in a wash sale occur in the same account and are in identical securities (rather than substantially identical securities).

Section 6045(g)(4) provides that, for purposes of section 6045, an S corporation (other than a financial institution) is treated in the same manner as a partnership. This rule applies to any sale of a covered security acquired by an S corporation (other than a financial institution) after December 31, 2011. It is expected that, when this rule takes effect, brokers generally will be required to report gross proceeds and basis information to customers that are S corporations.

The Act also amended section 6045(b) to extend the deadline from January 31 to February 15 for furnishing certain information statements to customers, effective for statements required to be furnished after December 31, 2008. Section 6045(b) provides that the statements to which the new February 15 deadline applies are (1) statements showing gross proceeds (under section 6045(a)) or substitute payments (under section 6045(d)) and (2) statements with respect to reportable items (including, but not limited to, interest, dividends, and royalties) that are furnished with consolidated reporting statements (as defined in

regulations). See Notice 2009-11, 2009-5 I.R.B. 420 (providing that, with respect to reportable items from calendar year 2008, brokers have until February 17, 2009, to report all items that they customarily report on their annual composite form recipient statements).

Under new section 6045A, a broker and any other person specified in Treasury regulations that transfers to a broker a security that is a covered security when held by that broker or other person must furnish to the transferee broker a written statement that allows the transferee broker to satisfy the basis and holding period reporting requirements of section 6045(g). Section 6045A(c) provides that, unless the Secretary provides otherwise, the statement required by this rule must be furnished to the transferee broker not later than fifteen days after the date of the transfer of the covered security.

Under new section 6045B, an issuer of specified securities must file a return according to forms or regulations prescribed by the Secretary setting forth a description of any organizational action (such as a stock split or a merger or acquisition) that affects the basis of the specified security, the quantitative effect on the basis of that specified security, and any other information required by the Secretary. Section 6045B(b) provides that this return must be filed within forty-five days after the date of the organizational action or, if earlier, by January 15 of the year following the calendar year during which the action occurred.

Additionally, section 6045B(c) provides that the issuer must furnish, according to forms or regulations prescribed by the Secretary, to the nominee with respect to that security (or to a certificate holder if there is no nominee) a written statement showing (1) the name, address, and telephone number of the information contact of the person required to file the return, (2) the information required to be included on the return with respect to the security, and (3) any other information required by the Secretary. This statement must be furnished to the nominee or certificate holder on or before January 15 of the year following the calendar year in which the organizational action took place.

Section 6045B(e) provides that the Secretary may waive the return filing and information statement requirements if the

person to which the requirements apply makes publicly available, in the form and manner determined by the Secretary, the name, address, telephone number, and e-mail address of the information contact of that person, and the information about the organizational action and its effect on basis otherwise required to be included in the return.

REQUEST FOR PUBLIC COMMENTS

The Treasury Department and the Service request comments on issues that should be addressed in guidance implementing the new requirements with respect to the reporting of a customer's basis in securities transactions. The Treasury Department and the Service request specific comments regarding:

Applicability of Reporting Requirements

1. How to determine who is a "middleman" subject to the broker reporting and transfer reporting statement requirements and how to minimize duplication of reporting by multiple brokers;
2. Who, in addition to brokers, should be treated as "applicable persons" subject to the transfer reporting requirements;
3. Whether the issuer's classification of an instrument (e.g., as stock or debt) should determine which effective date applies;

Basis Method Elections

4. How to ensure that customers are adequately informed of the broker's default basis determination method and that brokers are adequately notified of a customer's election of a different acceptable method for an account;
5. How to facilitate customer elections of acceptable basis determination methods, including average cost basis, for an account to maximize customer flexibility and minimize broker burden;
6. Whether and under what circumstances a customer may elect to change from the average cost basis method to the first-in first-out or specific identification method and, if so, what cost basis rules and adjustments should apply;
7. What it means to apply the basis determination conventions on an "account-by-account" basis;

Dividend Reinvestment Plans

8. How to determine what qualifies as an “arrangement under which dividends on any stock are reinvested in stock identical to the stock with respect to which the dividends are paid” (that is, as a “dividend reinvestment plan”);

9. How to determine which stock qualifies as “acquired in connection with” a dividend reinvestment plan, for which the average cost basis method is available beginning in 2011, and to which the later effective date of 2012 for information reporting applies;

10. Whether and to what extent the average cost basis method applies to subsequent additions to dividend reinvestment plan accounts by purchase or transfer;

11. How to maximize the utility of the single-account election for stock acquired in connection with a dividend reinvestment plan or stock held in a regulated investment company, particularly where basis and holding period information for pre-effective date stock is weak or unclear;

Reconciliation with Customer Reporting

12. How to ensure that broker reporting on Form 1099-B and customer reporting on Schedule D of Form 1040 are maximally consistent, including whether brokers should report separately for securities subject to basis reporting or report the basis of securities that are not covered securities, for example, securities purchased by their customers prior to 2011;

13. How to ensure consistency between customers making specific identification of securities sold or transferred and broker reporting;

14. How to ensure that reconciliation is possible if broker reporting should differ from customer reporting;

15. Whether customers, after a sale, may identify or change the identification of specific stock sold and, if so, for what period of time or by what deadline;

Special Rules and Mechanical Issues

16. The scope of the wash sales exception, including the definition of “identical securities” (including identical options), the wash-sale period, and any *de minimis* or other exceptions;

17. How to apply the rules for basis reporting of options;

18. Whether rules, including transition rules, are required to address the change in timing for reporting of short sales from the date the short sale is entered into to the date the short sale closes;

19. How to address mechanical issues relating to the computation of basis, such as adjustments for debt securities (for example, as a result of original issue discount, market discount, acquisition premium, or bond premium), gift-related adjustments, death-related adjustments, section 1043 basis rollovers, regulated investment company and real estate investment trust distributions representing return of capital, regulated investment company load adjustments, and the mark-to-market method of accounting for securities;

20. What, if any, translation conventions or computation adjustments should be allowed when securities are purchased with foreign currency in an account subject to United States taxation at the time of purchase or in an account that later becomes subject to United States taxation, for example, when an owner of securities becomes a United States citizen;

Transfer Reporting

21. What information about the transferring person, the customer, the security transferred, and the underlying lots should be required on the transfer reporting statements;

22. Whether fifteen days is the proper period for furnishing transfer reporting statements, and under what circumstances a different time period, if any, should apply;

23. Whether the basis determination rules and customer elections governing sales of securities should apply equally to transfers of securities, for example, when a customer transfers some, but not all, holdings of a security to another broker;

24. Whether electronic transfer reporting may be appropriate and, if so, whether a common format should apply;

25. Whether brokers and transferring parties may utilize reporting services of third-party intermediaries to meet their transfer reporting requirements;

26. Whether the transferring person should communicate any information or justification to the transferee broker when no transfer reporting statement is required

because the security is not a covered security;

Issuer Reporting

27. What information about the issuer and organizational action should be required on the issuer returns and reporting statements;

28. How to maximize the timeliness of issuer returns and statements and promote public reporting by issuers in lieu of return filing;

29. How to account for basis-changing organizational actions by foreign issuers of securities to the extent that foreign issuers are not subject to the issuer reporting requirements;

30. How to coordinate broker transfer reporting with issuer corporate action reporting to avoid duplicate broker adjustments when accounts are transferred and whether a universal timing standard should apply;

Broker Practices and Procedures

31. To what extent a broker should verify the reasonableness of basis information and what document retention requirements should apply;

32. What procedures a broker should follow if the broker derives basis and holding period information for or from customers with respect to a security that is not a covered security, including potential reporting of such information to either the customer or the Service;

33. What procedures a transferee broker should follow if the broker does not receive a transfer reporting statement;

34. What procedures a transferee broker should follow if the broker receives transfer reporting information with respect to a security that is not a covered security, or from a transferor who is not subject to the transfer reporting requirements;

35. What procedures a broker should follow with respect to basis adjustments if an issuer report on a corporate action is insufficient or untimely; and

36. Under what circumstances penalties may apply to brokers or other reporting entities and when relief from penalties should be available.

Interested parties are invited to submit comments on this notice by Monday, March 2, 2009. Written comments

should be submitted to: Internal Revenue Service, CC:PA:LPD:PR (Notice 2009-17), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Alternatively, comments may be hand delivered between the hours of 8:00 a.m. and 4:00 p.m. Monday to Friday to CC:PA:LPD:PR (Notice 2009-17), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, D.C. Comments

may also be transmitted electronically via the following e-mail address: *Notice.Comments@irs.counsel.treas.gov*. Please include "Notice 2009-17" in the subject line of any electronic communications. All comments will be available for public inspection and copying.

The principal author of this notice is Stephen Schaeffer of the Office of Associate Chief Counsel (Procedure &

Administration). For further information regarding this notice, please contact Stephen Schaeffer at (202) 622-4910 (not a toll-free call).

Part IV. Items of General Interest

Notice of Proposed Rulemaking

The Allocation of Consideration and Allocation and Recovery of Basis in Transactions Involving Corporate Stock or Securities

REG-143686-07

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations under sections 301, 302, 304, 351, 354, 356, 358, 368, 861, 1001, and 1016 of the Internal Revenue Code (Code). The proposed regulations provide guidance regarding the recovery of stock basis in distributions under section 301 and transactions that are treated as dividends to which section 301 applies, as well as guidance regarding the determination of gain and the basis of stock or securities received in exchange for, or with respect to, stock or securities in certain transactions. The proposed regulations affect shareholders and security holders of corporations. These proposed regulations are necessary to provide such shareholders and security holders with guidance regarding the allocation and recovery of basis on distributions of property.

DATES: Written or electronic comments, and a request for a public hearing, must be received by April 21, 2009.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-143686-07), room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-143686-07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the Federal eRulemaking Portal at www.regulations.gov (IRS#REG-143686-07).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations under sections 301, 302, and 304, Theresa M. Kolish, (202) 622-7530; concerning the proposed regulations under sections 351, 354, 356, 358, 368, 1001, and 1016, Rebecca O. Burch, (202) 622-7550; concerning the proposed regulations under section 861, Jeffrey L. Parry, (202) 622-4476; concerning submission of comments or to request a hearing, Richard Hurst (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

The primary objective of these proposed regulations is to provide a single model for stock basis recovery by a shareholder that receives a constructive or actual distribution to which section 301 applies and a single model for sale and exchange transactions to which section 302(a) applies, including certain elements of a reorganization exchange. Further to this objective, these proposed regulations define the scope of the exchange that must be analyzed under particular Code provisions, and provide a methodology for determining gain realized under section 356 and stock basis under section 358.

In addition, these proposed regulations respond to comments received by the IRS and Treasury Department regarding the current section 358 regulations, such as suggestions to expand the tracing rules to stock transfers that are subject to section 351 but do not qualify as reorganizations, questions regarding whether (and, if so, to what extent) shareholder elections constitute terms of an exchange, and whether the terms of an exchange control for purposes of qualifying a transaction as a reorganization under section 368. Finally, these proposed regulations include amendments to the section 304 regulations that import the statutory amendments to that section. See section 226 of the Tax Equity and Fiscal Responsibility Act of 1982, Public Law 97 248 (96 Stat. 325, 490) (September 3, 1982), section 712(l) of the Deficit Reduction Act of 1984, Public Law 98 369 (98 Stat. 494, 953 55) (July 18, 1984), section 1875(b) of the Tax Reform Act of

1986, Public Law 99 514 (100 Stat. 2085, 2894) (October 22, 1986), and section 1013 of the Taxpayer Relief Act of 1997, Public Law 105 34 (111 Stat. 788, 918) (August 5, 1997).

Explanation of Provisions

I. Introduction — Exchanges and Distributions to Which Sections 301 and 302 Apply

Section 301 provides rules for the treatment of a distribution with respect to stock but does not specify how to identify the shares upon which a distribution is made. Furthermore, the tax law does not provide rules concerning whether a shareholder recovers its stock basis in the aggregate, or alternatively, whether a shareholder is required to recover stock basis share-by-share. Finally, the tax law does not provide specifically that transactions treated as section 301 distributions (*i.e.*, redemptions under section 302(d), certain section 304 transactions, and certain reorganizations) should be subject to the same rules as actual section 301 distributions.

In the reorganization context, the Code provides consequences resulting from different types of exchanges, but does not specify whether the exchange is based on a shareholder's aggregate stock holdings, or alternatively, based on particular elements of the overall exchange.

Rules related to stock basis recovery and stock basis determinations have evolved independently over many years on a transactional basis. Ad hoc development of these authorities has led to the possibility of variant treatment of economically similar transactions to which section 301 or 302(a) applies either directly or through the operation of other Code provisions. Moreover, because there has not been a comprehensive review of these issues, many questions lack definitive answers. Prior guidance attempted to address particular areas of uncertainty within the subject matter of basis recovery and basis identification. Without the benefit of addressing all related issues, however, certain of this prior guidance was needed reconsidered. See REG-150313-01. Other guidance built the framework for basis identifica-

tion that has encouraged the development of these proposed regulations.

Building on themes developed in §1.358-2 and comments received from the tax community, this proposal is intended to be a comprehensive approach to stock basis recovery and stock basis identification to produce consistent results among economically similar transactions, regardless of the transaction type or the specific Code provision that results in the application of section 301 or 302(a).

The cornerstone of this proposal is that a share of stock is the basic unit of property that can be disposed of and, accordingly, the results of a transaction should generally derive from the consideration received in respect of that share. This guiding principle has section 1012 as its underpinning and has become fundamental to the tax treatment of shareholders, regardless of the specific nature of a shareholder's exchange. See §1.358-2 and §1.367(b)-13. A corollary to this basic premise is that a reorganization exchange is not an event that justifies alteration of a shareholder's tax position beyond what is necessary to reflect the results of the reorganization.

To harmonize the tax treatment of economically similar transactions, these proposed regulations adopt a single model for section 301 distributions (dividend equivalent transactions) and a single model for sale or exchange transactions to which section 302(a) applies (non-dividend equivalent transactions), regardless of whether section 301 or section 302(a) applies directly or by reason of section 302(d), 304 or 356.

II. Distributions with Respect to Stock and Dividend Equivalent Transactions

A. Section 301 distributions

Consistent with the fundamental notion that a share of stock is the basic unit of property, the results of a section 301 distribution should derive from the consideration received in respect of each share of stock, notwithstanding designations otherwise. *Johnson v. United States*, 435 F.2d 1257 (4th Cir. 1971). Accordingly, these proposed regulations treat a section 301 distribution as received on a *pro rata*, share-by-share basis with respect to the class of stock upon which the distribution is made. Thus, a distribution that is not

a dividend within the meaning of section 301(c)(1) can result in gain with respect to some shares of a class while other shares have unrecovered basis.

B. Dividend equivalent redemptions

To promote consistency among transactions treated as section 301 distributions under the Code, these proposed regulations apply the same basis recovery rules described above to both dividend equivalent redemptions and certain section 304 transactions. Accordingly, under these proposed regulations, a dividend equivalent redemption results in a *pro rata*, share-by-share distribution to all shares of the "redeemed class" held by the redeemed shareholder immediately before the redemption. The proposed regulations define the term "redeemed class" to mean all of the shares of that class held by the redeemed shareholder. Similar to an actual section 301 distribution, the proportional approach to basis recovery in dividend equivalent redemptions can produce gain with respect to some shares while other shares have unrecovered basis.

The constructive section 301 distribution is limited to the shares of the redeemed class (instead of constructing a *pro rata* distribution among all shares of various classes held by the redeemed shareholder) because different classes of stock have distinct legal entitlements that are respected for federal income tax purposes. *H.K. Porter Co.*, 87 T.C. 689 (1986); *Comm'r v. Spaulding Bakeries*, 252 F.2d 693 (2d Cir. 1958). Accordingly, a constructive section 301 distribution is conformed to an actual section 301 distribution by identifying those shares with respect to which an actual section 301 distribution would have been received, and by reducing the basis of only those shares.

i. Basis adjustments in dividend equivalent redemptions if less than all of the shares of a single class held by the taxpayer are redeemed

If less than all of the shares of a class of stock held by the taxpayer are redeemed, the proposed regulations provide that in a hypothetical recapitalization described in section 368(a)(1)(E), the redeemed shareholder is deemed to exchange all its shares

in the class, including the redeemed shares, for the actual number of shares held after the redemption transaction. The tracing rules of the section 358 regulations apply to preserve the basis of the shares exchanged in the recapitalization in the remaining shares of the redeemed class held by the shareholder. Thus, under these proposed regulations, a dividend equivalent redemption is generally treated in the same manner, and its results are the same as, a section 301 distribution in which no shares were cancelled.

ii. Basis recovery in dividend equivalent redemptions in which the taxpayer surrenders all of its shares in a single class

Under current law, if all of the shares of a single class held by a shareholder are redeemed in a dividend equivalent redemption, any unrecovered basis in the redeemed shares is permitted to shift to other shares in certain circumstances. See §1.302-2(c). The IRS and Treasury Department believe that the shifting of stock basis is inconsistent with the fundamental principle that each share is a separate unit of property, and can lead to inappropriate results. Accordingly, these proposed regulations do not permit the shifting of basis to other shares held (directly or by attribution) by the redeemed shareholder. Instead, the proposed regulations preserve the tax consequences of the unrecovered basis for the redeemed shareholder by treating the amount of the unrecovered basis as a deferred loss of the redeemed shareholder that can be accessed when the conditions of sections 302(b)(1), (2), or (3) are satisfied, or alternatively, when all the shares of the issuing corporation (or its successor) become worthless within the meaning of section 165(g).

C. Dividend equivalent reorganization exchanges

If, pursuant to a reorganization, a shareholder receives qualifying property and boot in exchange for its target corporation stock, the tax consequences of the receipt of the boot under these proposed regulations will depend upon whether the reorganization exchange is dividend equivalent or not. See section III. of this Preamble for a description of the proposed

rules that would apply if the reorganization is not dividend equivalent.

In general, the determination of whether an exchange has the effect of the distribution of a dividend for purposes of section 356(a)(2) is determined by examining the effect of the shareholder's "overall exchange." *Commissioner v. Clark*, 489 U.S. 726, 738 (1989). Thus, the key to this determination is the scope of the exchange. For example, if the shareholder exchanges shares of preferred stock solely for boot and shares of common stock solely for qualifying property pursuant to a plan of reorganization, is the determination of whether the exchange of the preferred stock for boot is dividend equivalent based solely on that particular exchange or on the overall exchange of the preferred and common stock for the qualifying property and the boot? The same question would arise with respect to each particular exchange if the shareholder exchanged the preferred and common stock for a combination of qualifying property and boot. The *Clark* decision examined a reorganization exchange involving a single class of stock, and does not provide guidance in the context of multiple classes of stock.

In the case of a section 302 redemption, the exchanging shareholder determines dividend equivalency based on all the facts and circumstances. See *Zenz v. Quinlivan*, 213 F.2d 914 (C.A.6 1954). To promote consistency between sale or exchange transactions, these proposed regulations provide that the overall reorganization exchange shall be taken into account in determining whether a particular exchange is dividend equivalent. Thus, a shareholder that exchanges a class of stock solely for boot and another class of stock solely for nonqualifying property shall consider the overall exchange (the exchange of the two classes of stock for boot and qualifying property) in determining whether each particular exchange is dividend equivalent.

If it is determined that a reorganization exchange is dividend equivalent, because different classes of stock have distinct legal entitlements that are respected for federal income tax purposes, the proposed regulations provide that an exchange of a class of stock solely for boot is an exchange to which section 302(d) (and not section 356(a)(2)) applies.

To ensure similar tax treatment of dividend equivalent reorganization exchanges and dividend equivalent redemptions, if the reorganization exchange is dividend equivalent the proposed regulations limit the ability of the exchanging shareholder to specify the terms of the exchange. Specifically, if the shareholder receives more than one class of stock or surrenders one class of stock and securities, the shareholder may specify the terms of the exchange between the classes of stock surrendered (or between one or more classes of stock and securities surrendered), provided the designation is economically reasonable, but not between particular shares of the same class of stock.

As with the redemption of shares of a redeemed class in a dividend equivalent redemption, a shareholder's receipt solely of boot with respect to a class of stock in a reorganization exchange is treated as received *pro rata*, on a share-by-share basis, with respect to each share in the class under the principles of *Johnson*, the shareholder cannot specify that the boot is received with respect to particular shares within the class. Consequently, such an exchange could result in gain recognition with respect to some shares while other shares in the class could have recovered basis.

In formulating the proposed regulations, the IRS and Treasury Department considered different alternatives. For example, in a dividend equivalent reorganization exchange pursuant to section 356(a)(2), the IRS and Treasury Department considered whether gain realized with respect to a class should be determined in the aggregate (for example, with respect to all shares within a class). Under this approach, no gain would be realized with respect to a class that has a block of built-in gain stock and block of built-in loss stock where the built-in loss is at least equal to the built-in gain. The IRS and Treasury Department rejected such an approach because it would contradict the fundamental principle that a share is a discrete unit of property, and also would compromise the principle that a reorganization exchange is not an event that justifies stock basis averaging. The IRS and Treasury Department also considered eliminating a shareholder's ability to specify the terms of a dividend equivalent reorganization exchange based on

the premise that under *Johnson*, all consideration received in such an exchange should be considered received *pro rata* among all shares, regardless of whether more than one class is surrendered. The IRS and Treasury Department rejected this approach in favor of the approach of the proposed regulations that is analogous to the proposed treatment of dividend equivalent redemptions, under which each share of the redeemed class is treated as receiving a *pro rata* share of the proceeds, and shares outside of the redeemed class are not treated as receiving any part of the distribution.

D. Special rules related to apportionment of interest and other expenses

Under section 864(e), taxpayers apportion interest expense between statutory and residual groupings on the basis of the relative values of their assets in each grouping. For this purpose, taxpayers may choose to value their assets using either fair market value or tax book value (adjusted basis). The proposed regulations provide that for purposes of apportioning expenses on the basis of the tax book value of assets, the adjusted basis in any remaining shares of the redeemed class owned by the redeemed shareholder, any shares that are not in the redeemed class, or any shares owned by certain affiliated corporations shall be increased by the amount of the unrecovered basis of redeemed shares. Thus, under the proposed regulations, the interest expense allocation and apportionment consequences of a dividend equivalent redemption are the same as an actual section 301 distribution.

E. Section 1059

Section 1059(a) provides that if a corporation receives an extraordinary dividend with respect to any share of stock and such corporation has not held such stock for more than two years before the dividend announcement date, then the corporation's basis in such stock shall be reduced (but not below zero) by the non-taxed portion of such dividends.

Except as provided in regulations, in the case of any redemption of stock which would not have been treated (in whole or in part) as a dividend if any options had not been taken into account under section

318(a)(4), or section 304(a) had not applied, any amount treated as a dividend is treated as an extraordinary dividend, without regard to the taxpayer's holding period in the stock. Section 1059(e)(1)(A)(iii). In the case of these types of redemptions, section 1059(e)(1)(A) (flush language) provides that only the basis of the stock redeemed shall be taken into account under section 1059(a). These proposed regulations do not affect the basis reduction provided for in section 1059(e)(1)(A) if section 1059(e)(1)(A)(iii) otherwise applies. Accordingly, to the extent of an extraordinary dividend described in section 1059(e)(1)(A)(iii), a redeeming shareholder would first reduce basis as prescribed by section 1059(e)(1)(A). These proposed regulations would then apply to the extent the distribution is not a dividend within the meaning of section 301(c)(1).

F. Redemptions of stock held by partnerships, trusts, and S corporations

The treatment of unrecovered basis as a deferred loss raises special issues where the redeemed shareholder is an S corporation, a partnership, or a trust (each a flow-through entity). These proposed regulations reserve with respect to the issues relating to redeemed shareholders that are flow-through entities pending further study and comment. The primary issue under study is whether an "outside" basis adjustment that reflects the deferred loss should occur at the time of the dividend equivalent redemption, or alternatively, when there is an inclusion date with respect to the deduction.

In general, a deferred loss is reflected in the outside basis of an interest in a flow-through entity when the deduction can be accessed by the entity. Accordingly, as a general matter, disconformity can exist between inside attributes and outside basis where an inside attribute is a deferred loss. Conversely, a net operating loss of a flow-through entity reduces the outside basis of an interest in the entity in the year that the net operating loss arises.

Although disconformity generally can exist where a flow-through entity has a deferred loss, the IRS and Treasury Department are concerned that deferred losses arising from unrecovered basis presents an

opportunity to separate the deferred loss from the dividend income resulting from the redemption. The IRS and Treasury Department question whether such a separation would be appropriate, and believe that treating the deferred loss as a net operating loss in the year of the redemption for basis adjustment purposes may be the better approach. However, the IRS and Treasury Department acknowledge that it may be inappropriate to require the owners of a flow-through entity to reduce outside basis before the deferred loss can be accessed, simply because the owners of the flow-through entity cannot access the deferred loss. The IRS and Treasury Department request comments on this issue.

Flow-through entities also present the question of when it is appropriate to treat an owner of the flow-through entity as the redeemed shareholder, and when it is appropriate to treat the flow-through entity itself as the redeemed shareholder. For example, where the owner completely divests of its interest in the flow-through entity, it may be appropriate to treat the owner as the redeemed shareholder for determining whether the sale of the flow-through entity interest is an inclusion date with respect to that owner. This treatment may be more appropriate if the deferred loss is treated as a net operating loss that already has reduced the outside basis of the entity's owner. Conversely, if the deferred loss is not treated as a net operating loss, it may be more appropriate to treat the flow-through entity as the redeemed shareholder in all cases. The IRS and Treasury Department request comments on this issue.

G. Consolidated groups and basis recovery in dividend equivalent redemptions

The IRS and Treasury Department continue to study the issues raised when a redeemed shareholder with a deferred loss files a consolidated return. The IRS and Treasury Department believe that certain of the concerns raised by REG-150313-01 are addressed in these proposed regulations by the deemed recapitalization mechanic described in section II.B.i. of this Preamble.

III. Redemptions Treated as a Sale or Exchange Pursuant to Section 302(a)

A. In general

Under current law for redemptions characterized under section 302(a), a shareholder that owns shares of stock with different bases can decide whether to surrender for redemption high basis shares, low basis shares or any combination thereof. See §1.1012-1(c). Consistent with treating a share as a discrete unit of property, the proposed regulations do not limit this electivity. Additionally, as further discussed below, these proposed regulations affirm the ability of a shareholder to specify the terms of a reorganization exchange where the receipt of boot results in sale or exchange treatment.

B. Reorganization exchanges that result in sale or exchange treatment

If it is determined that the reorganization exchange is not dividend equivalent (as described in section II.C. of this Preamble), section 302(a) will apply to the extent shares are exchanged solely for boot. Just as a shareholder can elect to surrender high basis shares, low basis shares or any combination thereof in a non-dividend equivalent redemption, a shareholder engaging in a reorganization exchange that is not dividend equivalent can specify the receipt solely of boot for a share, provided that the terms of the exchange are economically reasonable. In such case, the shareholder will recognize gain or loss with respect to that share pursuant to section 302(a), and section 356(a)(1) will not apply.

IV. Extension of Tracing Principles to Determine Basis in Certain stock Transfers that are Not Reorganizations, and Other Proposals in Response to Specific Comments

A. Application of tracing principles to certain section 351 exchanges and capital

The current section 358 regulations apply tracing principles to determine the basis of stock received in a section 351 exchange only where the section 351 exchange also qualifies as a reorganization and no liabilities was assumed in the exchange. The principal reason for this limitation is the interaction of the basis tracing

rules with the aggregate approach to gain determination under section 357(c). The IRS and Treasury Department continue to study this issue, but have concluded that the resolution of this issue is not necessary to broaden the application of the tracing rules to transfers of stock in section 351 exchanges in which no liabilities are assumed. Thus, for example, in an exchange to which section 351 applies where the transferor transfers two blocks of stock with disparate basis and other property, the separate bases will be preserved under section 358, provided that liabilities are not assumed in the exchange.

In addition, these proposed regulations incorporate the deemed issuance and recapitalization approach of the current section 358 regulations to section 351 exchanges to preserve basis if insufficient shares, or no shares at all, are actually issued in the exchange. These proposed regulations also extend the deemed issuance and recapitalization approach to shareholder capital contributions to which section 118 applies.

B. Miscellaneous

The IRS and Treasury Department have received a number of comments on the current section 358 regulations. These proposed regulations make a number of clarifying, but nonsubstantive, modifications to the current section 358 regulations. Specifically, the proposed regulations add headings throughout the existing final §§1.358-1 and 1.358-2 regulations without substantive change. In addition, the proposed regulations address the following comments received with respect to the current section 358 regulations.

Commentators questioned how shareholder elections factor into the terms of the exchange. These proposed regulations include two new examples illustrating the effect of such elections.

Commentators questioned the effect of the terms of an exchange on the determination of whether a transaction qualifies as a reorganization, and therefore is not subject to the general rule of section 1001. These proposed regulations include cross-references in the regulations under sections 368 and 1001 to clarify that, to the extent the terms of the exchange specify that a particular property is received in exchange for a particular property, such terms shall con-

trol for purposes of determining whether a transaction qualifies as a reorganization provided such terms are economically reasonable.

Finally, in addition to provisions relating to the determination of basis, these proposed regulations add a rule that addresses certain issues considered in Rev. Rul. 68-55, 1968-1 C.B. 140. Specifically, consistent with Rev. Rul. 68-55, these regulations provide that, for purposes of determining gain under section 351(b), the fair market value of each category of consideration received in a section 351 exchange is allocated between the transferred assets in based on relative fair market values.

V. Specifically Requested Comments

In addition to the comments requested throughout this Preamble, the IRS and Treasury request comments on the following areas.

The proposed regulations under section 302 do not apply to a redemption of stock described in section 306(c). Pursuant to section 306(a)(2), a redemption of stock described in section 306(c) is treated as a distribution of property to which section 301 applies. *Example 2* of §1.306-1 suggests that the unrecovered basis of redeemed section 306 stock is added to the basis of the stock with respect to which the section 306 stock was distributed. The IRS and Treasury Department request comments on whether such treatment is appropriate or whether an alternative regime should apply when such a section 306(c) redemption is treated as a section 301 distribution.

Comments are also requested regarding whether, after a section 355 *pro rata* split-up, the controlled corporations are the same as or different from the distributing corporation for purposes of determining whether the date of distribution would be an inclusion date for a deferred loss attributable to unrecovered basis.

Finally, the IRS and Treasury Department recognize that the proposed regulations may not address all related issues arising in all cash “D” reorganizations. Specifically, these proposed regulations may heighten the importance of whether the nominal share deemed issued in such a reorganization is received in respect of particular shares surrendered by the

exchanging shareholder. The IRS and Treasury Department request comments with respect to this issue.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. Further, it is hereby certified that these proposed regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that these regulations provide clarifying guidance of existing law and do not create additional obligations for, or impose an economic impact on small entities. Accordingly, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. All comments will be available for public inspection and copying. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these regulations are Theresa M. Kolish and Rebecca O. Burch of the Office of Associate Chief Counsel (Corporate). Other personnel from offices of the IRS and Treasury Department participated in their development.

Availability of IRS Documents

IRS revenue rulings, procedures, and notices cited in this preamble are made available by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

* * * * *

Proposed Amendments to the Regulations

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

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.301-2 is added to read as follows:

§1.301-2 Application to basis.

(a) *Application to basis.* That portion of a distribution which is not a dividend shall be applied *pro rata*, on a share-by-share basis, to reduce the adjusted basis of each share of stock held by the shareholder within the class of stock upon which the distribution is made. The following example illustrates this paragraph (a):

Example. (i) *Facts.* Corporation X, a calendar year taxpayer, has only common stock outstanding. A, an individual, owns all 100 shares; 25 were acquired on Date 1 for \$25 (Block 1) and 75 were acquired on Date 2 for \$175 (Block 2). On December 31, when Corporation X had earnings and profits of \$100, it made a \$3 distribution on each share of common stock.

(ii) *Analysis.* A is treated as receiving \$75 of the distribution on block 1 and \$225 on block 2. On Block 1, A will have a \$25 dividend under section 301(c)(1), a \$25 return of capital under section 301(c)(2) and a \$25 gain under section 301(c)(3). On Block 2, A will have a \$75 dividend under section 301(c)(1), a \$150 a return of capital under section 301(c)(2) and will have a remaining basis of \$25 in the shares of block 2.

(b) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 3. In §1.302-2, paragraph (c) is removed and reserved.

§1.302-2 [Amended]

Par. 4. Section 1.302-5 is added to read as follows:

§1.302-5 Redemptions under section 302(d).

(a) *In general*—(1) *Share-by-share basis reduction.* In any case in which an amount received in redemption of stock (as defined in section 317(b)) is treated as a

distribution to which section 301 applies, that portion of a distribution that is not a dividend shall be applied to reduce the adjusted basis of each share held by the redeemed shareholder (as defined in paragraph (b) of this section) in the redeemed class (as defined in paragraph (b) of this section). Such reduction shall be applied *pro rata*, on a share-by-share basis, to all shares of the redeemed class held by the redeemed shareholder. Gain, if any, on a share shall be determined under section 301(c)(3).

(2) *Deemed recapitalization.* Except as provided in paragraph (a)(3) of this section, immediately following the reduction of basis as provided in section 301(c)(2) and paragraph (a)(1) of this section, all shares of the redeemed class, including the redeemed shares, held by the redeemed shareholder will be treated as surrendered in a reorganization described in section 368(a)(1)(E) in exchange for the number of shares of the redeemed class directly held by the redeemed shareholder after the redemption. The basis of the shares deemed received in the reorganization described in section 368(a)(1)(E) will be determined under the rules of section 358 and §1.358-2.

(3) *Redemption of all shares of redeemed class*—(i) *Remaining basis treated as loss.* If all the shares of the redeemed class held by the redeemed shareholder are redeemed, an amount equal to the basis of the redeemed stock, after adjusting such basis to reflect the application of section 301(c)(2) as provided in paragraph (a)(1) of this section, will be treated as a loss on a disposition of the redeemed stock on the date of the redemption. Such loss is taken into account on the inclusion date as defined in paragraph (b) of this section.

(ii) *Attributes of loss.* Notwithstanding that a loss described in paragraph (a)(3)(i) of this section may be deferred and taken into account on a date later than the date of the redemption, the attributes (for example, character and source) of such loss are determined on the date of the redemption that gave rise to such loss.

(b) *Definitions*—(1) *Redeemed shareholder.* Except as provided in paragraph (c) of this section, the term *redeemed shareholder* means the person whose stock is redeemed in a transaction. If the redeemed shareholder is a corporation, and the assets of the redeemed shareholder

are acquired in a transaction described in section 381(a) (other than transactions described in paragraph (b)(4)(ii) of this section), the acquiring corporation (within the meaning of section 381) thereafter is treated as the redeemed shareholder.

(2) *Redeemed class.* With respect to a shareholder whose stock has been redeemed, the term *redeemed class* means all of the shares of that class held by the redeemed shareholder. For this purpose, a class is defined with respect to economic rights to distributions rather than the labels attached to shares or rights with respect to corporate governance.

(3) *Redeeming corporation.* The term *redeeming corporation* means the corporation that issued the stock that is redeemed.

(4) *Inclusion date*—(i) *Definition.* The term *inclusion date* means the earlier of—
(A) The first date on which the redeemed shareholder would satisfy the criteria of section 302(b)(1), (2), or (3), if the facts and circumstances that exist at the end of such day had existed immediately after the redemption; or

(B) The first date on which all classes of stock of the redeeming corporation become worthless within the meaning of section 165(g). Solely for purposes of this paragraph, if the assets of the redeeming corporation (or its successor) are acquired by another corporation in a transaction described in section 381(a), the inclusion date for the redeemed shareholder is determined by treating all of the facts and circumstances that exist at the end of the day that includes the section 381 transaction (including the acquisition of the assets of the redeeming corporation or its successor) as existing immediately after the redemption. A successor for this purpose means a corporation that acquires the assets of the redeeming corporation in a transaction to which section 381(a) applies.

(ii) *Special rules for corporate shareholders.* If the redeemed shareholder is a corporation, the inclusion date includes the date such corporation has disposed of all of its assets in a transaction in which all gain and loss with respect its assets is recognized in whole, and the corporation ceases to exist for tax purposes. If the redeemed shareholder is a foreign corporation, the inclusion date includes the date such corporation transfers its assets to a domestic corporation in either a liquidation described in

section 332 or a reorganization described in section 368(a)(1) to which section 381 applies. If the redeemed shareholder is a foreign corporation that is not a controlled foreign corporation within the meaning of section 957(a) on the date of the redemption, the inclusion date includes the date such corporation transfers its assets to a controlled foreign corporation in a liquidation described in section 332 or a reorganization described in section 368(a)(1) to which section 381 applies.

(c) *Rules for special shareholders—(1) Redeemed shareholder is a partnership.* [Reserved]

(2) *Redeemed shareholder is an S corporation.* [Reserved]

(3) *Redeemed shareholder is an estate or trust.* [Reserved]

(d) *Operating rules for treatment of loss attributable to basis of redeemed stock—*

(1) *Treatment as a deferred loss.* Any loss attributable to the basis of redeemed stock under paragraph (a) of this section that has not been permitted to be taken into account under such section shall be treated as a deferred loss. The character of the deferred loss as ordinary or capital is determined at the time of the redemption.

(2) *Effect of loss attributable to basis of redeemed stock on earnings and profits.* If the redeemed shareholder is a corporation, any deferred loss attributable to the basis of redeemed stock is not reflected in such corporation's earnings and profits before it is taken into account pursuant to the rules of paragraph (a)(3) of this section. See, for example, §§1.312-6(a) and 1.312-7.

(e) *Examples.* For the purposes of the examples in this section, Corporations X, Y and Z are domestic corporations that file U.S. tax returns on a calendar-year basis. The examples are as follows:

Example 1. (i) *Facts.* A and B, husband and wife, each own 100 shares (50 percent) of the common stock of Corporation X which they hold as a capital asset. On Date 1, A acquired 50 shares for \$100 (block 1) and 50 shares on Date 2 for \$200 (block 2). On December 31, Corporation X, which has no current or accumulated earnings and profits, redeems all of A's block 2 shares for \$300. Under section 302(d), the redemption proceeds are treated under section 301 as a recovery of basis.

(ii) *Analysis.* Under this section, immediately before the redemption, the distribution of property is applied on a *pro rata*, share-by-share basis with respect to each of the shares in the redeemed class held directly by A, the redeemed shareholder. Accordingly, A will have a \$50 capital gain on block 1 (\$150-100) under section 301(c)(3) and \$50 of basis remaining

on block 2 (\$150-200). To reflect the actual number of shares held by A after the redemption, A's shares in the redeemed class, including the shares actually surrendered, will be treated as exchanged in a recapitalization under section 368(a)(1)(E). The basis in A's recapitalized shares will be determined under §1.358-2. Accordingly, A will have 25 shares with a zero basis (attributable to block 1) and 25 shares with a basis of \$50 (attributable to block 2).

Example 2. (i) *Facts.* The facts are the same as in *Example 1*, except that, Corporation X, on the following December 31, when it has no current or accumulated earnings and profits, redeems all of A's remaining 50 shares for \$40. A does not file an agreement described in section 302(c)(2)(A)(iii) waiving family attribution under section 318.

(ii) *Analysis.* Since A is treated under section 318(a)(1) as owning B's shares, the redemption is described in section 302(d) and is treated as a distribution to which section 301 applies. As in *Example 1*, immediately before the redemption, the distribution is applied on a *pro rata*, share-by-share basis with respect to each of the shares in the redeemed class held by A. Accordingly, A recognizes a \$20 gain and a \$30 loss. The \$30 deferred loss under §1.302-5(a)(3) may be taken into account by A on the inclusion date (see §1.302-5(a)(3)(ii)).

Example 3. (i) *Facts.* Corporation X has both common and preferred stock outstanding. A, an individual, has 100 shares of common stock with a basis of \$100 and 100 shares of preferred stock with a basis of \$200. The 100 shares of common stock represent voting control of Corporation X. Corporation X, when it has no current or accumulated earnings and profits, redeems all of A's preferred stock for \$150. Section 302(d) applies to the redemption, and therefore the distribution is treated as a distribution of property to which section 301 applies.

(ii) *Analysis.* If Corporation X had declared a distribution under section 301 with respect to the redeemed preferred stock, the distribution would have been limited to the shares of common stock. Therefore, the only basis recovered under section 301(c)(2) is the basis of A's preferred stock. A has \$50 in excess basis after the redemption of all its preferred stock which will not shift to the common stock held by A. Under §1.302-5(a)(3), the excess basis will be treated as a deferred loss until the inclusion date.

Example 4. (i) *Facts.* Corporation Z has 100 shares of stock outstanding, 50 shares of which are owned by each of A and his son, B. A's basis in each of his shares of Corporation Z stock is \$1. In Year 1, Corporation Z redeems all of A's shares of Corporation Z stock for \$200. A does not file an agreement described in section 302(c)(2)(A)(iii) waiving family attribution under section 318. At the end of Year 1, Corporation Z has current and accumulated earnings and profits in excess of \$200. Section 302(d) applies to the redemption, and therefore the distribution is treated as a distribution to which section 301 applies. A recognizes dividend income of \$200. In Year 6, Corporation Y, a publicly traded corporation acquires all of Corporation Z's assets in exchange solely for voting stock in a reorganization described in section 368(a)(1)(C). In the reorganization, B surrenders his shares of Corporation Z stock which, at the time of the reorganization have an aggregate fair market value of \$200, and receives in exchange 5,000 shares of common stock of Corporation Y representing less than

one percent of the fair market value of all the stock of Y.

(ii) *Analysis.* Under this section, an amount equal to A's basis in the redeemed stock after the Year 1 redemption, \$50, is treated as a deferred loss on a disposition of the redeemed stock on the date of the redemption. Under paragraph (b)(3) of this section, solely for purposes of determining whether a particular date on or after the date of the reorganization is the inclusion date, Corporation Y, the acquiring corporation, is treated as the redeeming corporation. If the facts and circumstances that exist at the end of the day of the reorganization had existed on the date of the redemption, the redemption would have been treated as a distribution in part or full payment in exchange for the redeemed stock pursuant to section 302(a). Therefore, the date of the reorganization is the inclusion date and A is permitted to take into account the deferred loss of \$50 attributable to his basis in the redeemed stock in Year 6.

(f) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 5. Section 1.304-1 is revised to read as follows:

§1.304-1 In general.

(a) *In general.* Section 304 is applicable where a shareholder sells stock of one corporation to a related corporation as defined in section 304. Sales to which section 304 is applicable shall be treated as redemptions subject to sections 302 and 303.

(b) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 6. Section 1.304-2 is amended by revising paragraphs (a) and (c), and adding paragraph (d) to read as follows:

§1.304-2 Acquisition by related corporation (other than a subsidiary).

(a) *In general* (1) If a corporation (the acquiring corporation), in return for property, acquires the stock of another corporation (the issuing corporation) from one or more persons, and such person or persons from whom the stock was acquired were in control of both such corporations, then such property shall be treated as received in redemption of the common stock of the acquiring corporation. As to each person transferring stock, the amount received shall be treated as a distribution to which section 301 applies, if section 302(a) or

303 does not apply. For the amount constituting a dividend in such cases, see §1.304-6.

(2) *Section 302(b)*. In applying section 302(b), reference shall be made to the ownership of stock in the issuing corporation and not to the ownership of the acquiring corporation (except for the purposes of applying section 318(a)). Section 318(a) shall be applied without regard to the 50 percent limitation contained in section 318(a)(2)(C) and (3)(C).

(3) *Section 302(d)*. If, pursuant to section 302(d), section 301 applies to the property received in redemption of the common stock of the acquiring corporation pursuant to paragraph (a)(1) of this section, the transferor and the acquiring corporation shall be treated, for all Federal income tax purposes, in the same manner as if the transferor had transferred the stock of the issuing corporation to the acquiring corporation in exchange for the common stock of the acquiring corporation in a transaction to which section 351 applies, and then the acquiring corporation had redeemed the common stock it was treated as issuing in an exchange for property. Accordingly, the acquiring corporation's basis in the stock of the issuing corporation is determined under section 362, and, under section 358, the transferor's basis in the common stock of the acquiring corporation deemed issued to the transferor in the deemed section 351 transaction is equal to the transferor's basis in the stock of the issuing corporation it surrendered.

(4) *Basis of redeemed shares*. To the extent that section 301(c)(2) applies to the redemption of the common stock of the acquiring corporation issued in the deemed section 351 exchange, the amount distributed in such redemption shall be applied to reduce the adjusted basis of each share of common stock directly held or deemed held by the transferor on a *pro rata*, share-by-share basis. See §1.302-5(a).

(5) *Sale or exchange treatment*. If section 301 does not apply to the property treated as received in redemption of the common stock of the acquiring corporation pursuant to paragraph (a)(1) of this section, the property received by the transferor shall be treated as received in a distribution in full payment in exchange for such common stock of the acquiring corporation under section 302(a). The ba-

sis and the holding period of the common stock of the acquiring corporation that is treated as redeemed will be the same as the basis and holding period of the stock of the issuing corporation actually surrendered. The acquiring corporation shall take a cost basis in the stock of the issuing corporation that it acquires under section 1012.

* * * * *

(c) *Examples*. For purposes of the examples in this section, each of corporation is a domestic corporation that files a U.S. tax return on a calendar-year basis and in each instance the fair market value of the issuing corporation stock is in excess of its adjusted basis. The principles of this section are illustrated by the following examples:

Example 1. (i) *Facts*. Corporation X and Corporation Y each has 100 shares of common stock outstanding. A, an individual, owns one-half of the stock of each corporation, B owns one-half of the stock of Corporation X, and C owns one-half of the stock of Corporation Y. A, B, and C are unrelated. A sells 30 shares of the stock of Corporation X, which have an adjusted basis of \$10, to Corporation Y for \$50.

(ii) *Analysis*. Section 304(a)(1) applies to A's sale of 30 shares of Corporation X stock to Corporation Y because A controls both Corporation X and Corporation Y within the meaning of section 304(c), and Corporation Y acquires the 30 shares of Corporation X stock from A in exchange for property (\$50 of cash). Pursuant to section 304(a)(1), the cash received by A is treated as a redemption of the stock of Corporation Y. Because before the sale A owns 50 percent of the stock of Corporation X and after the sale A owns only 35 percent of such stock (20 shares directly and 15 constructively because one-half of the 30 shares owned by Corporation Y are attributed to A), the redemption is substantially disproportionate as to A pursuant to the provisions of section 302(b)(2). A, therefore, recognizes a gain of \$40 (\$50 minus \$10). If the stock surrendered is a capital asset, such gain is long-term or short-term capital gain depending on the period of time that A held such stock. A's basis in the stock of Corporation Y is not changed as a result of the sale. Under section 1012, the basis that Corporation Y takes in the acquired stock of Corporation X is its cost of \$50.

Example 2. (i) *Facts*. Corporation X and Corporation Y each has 200 shares of common stock outstanding, all of which are owned by H, an individual. H has a basis \$100 in his Corporation X stock and \$30 in his Corporation Y stock. Corporation X has \$40 and Corporation Y has \$20 of current and accumulated earnings and profits. H sells his 200 shares of Corporation X stock to Corporation Y for \$150 at a time when Corporation Y stock also has a fair market value of \$150.

(ii) *Analysis*. Section 304(a)(1) applies to H's sale of his 200 shares of Corporation X stock to Corporation Y because H controls both Corporation X and Corporation Y within the meaning of section 304(c), and Corporation Y acquires the 200 shares of Corporation X stock from H in exchange for property. Pur-

suant to section 304(a)(1), the cash received by H is treated as a redemption of the stock of Corporation Y. Because before the sale H directly owns 100 percent of Corporation X and after the sale H is treated as owning 100 percent of Corporation X, section 302(a) does not apply to the deemed redemption distribution. Under section 302(d), the proceeds of the deemed redemption are treated as a distribution to which section 301 applies. Therefore, H is treated as transferring the Corporation X stock to Corporation Y in exchange for Corporation Y common stock in a transaction to which section 351(a) applies. Corporation Y's basis in the Corporation X stock acquired is \$100 under section 362(a), the same basis that H had in the Corporation X stock surrendered. H takes a basis of \$100 in the Corporation Y common stock H is treated as receiving in the deemed section 351 exchange. Corporation Y is then treated as redeeming such Corporation Y common stock from H for \$150 in a transaction to which section 301 applies. H is treated as receiving a dividend of \$60 (\$20 from the current and accumulated earnings and profits of Corporation Y and then \$40 from the current and accumulated earnings and profits of Corporation X) (see section 304(b)). Under §1.302-5, the remaining \$90 of the distribution will be applied to and reduce the basis of each share of Corporation Y stock held by H. Accordingly, H will have no gain on the shares deemed received in the section 351 exchange which have a \$100 basis, but will have a \$15 gain on the Corporation Y shares with a \$30 basis. After the redemption transaction, all of H's shares in Corporation Y, including the deemed shares that are redeemed, are treated as exchanged in a recapitalization described in section 368(a)(1)(E). The basis of the redeemed shares and the shares actually outstanding in Corporation Y are allocated pursuant to §1.358-2(a). Accordingly, of H's 200 shares in Corporation Y common stock, 100 will have a basis of \$55, and 100 will have a zero basis.

Example 3. (i) *Facts*. Corporation W acquired all of the outstanding stock of Corporation X stock for \$75 (100 shares of common) and then acquired all of the outstanding stock of Corporation Y (50 shares of common stock for \$75 and 50 shares of common stock for \$100). Only corporation Y has current or accumulated earnings and profits (\$100). Corporation W sells all the shares in Corporation X to Corporation Y for \$300. At the time of the transaction, the Corporation X and Corporation Y stock have the same fair market value.

(ii) *Analysis*. Section 304(a)(1) applies to Corporation W's sale of Corporation X stock to Corporation Y because Corporation W is in control of both Corporation X and Corporation Y within the meaning of section 304(c), and Corporation Y acquires the Corporation X stock in exchange for property. Because before the sale Corporation W owns 100 percent of Corporation X, and after the sale is treated as owning 100 percent of Corporation X, section 302(a) does not apply to the deemed redemption distribution. Under section 302(d), the proceeds of the deemed redemption are treated as a distribution to which section 301 applies. Section 1059(e)(1)(A)(iii) also applies. Corporation W is treated as transferring the Corporation X stock to Corporation Y in exchange for Corporation Y common stock in a transaction to which section 351(a) applies. Corporation Y's basis in the Corporation X stock is \$75 under section 362(a), the same basis that Corporation W had in the stock it surren-

dered. Corporation W takes a \$75 basis in the Corporation Y common stock it is deemed to receive in the deemed section 351 transaction. Corporation Y is then treated as redeeming such Corporation Y common stock from Corporation W for \$300. In a redemption to which section 301 applies, Corporation W is treated as receiving a dividend of \$100 (from the current and accumulated earnings and profits of Corporation Y) (see section 304(b)). Under section 1059, the \$100 dividend is treated as an extraordinary dividend which, under the flush language of section 1059(e)(1)(A)(iii), reduces only the basis of the stock deemed redeemed, which has a basis of \$75. Accordingly, Corporation W recognizes a \$25 gain. Under §1.302-5, the remaining \$200 of the distribution is applied to reduce the basis of the Corporation Y stock held by Corporation W on a *pro rata*, share-by-share basis, including the basis in the shares deemed redeemed. Accordingly, \$100 is allocated to the Corporation Y stock that Corporation W deemed received in the section 351 transaction that now has a zero basis after the application of section 1059 and the remaining \$100 is allocated to Corporation W's other two blocks of Corporation Y stock. Corporation W has a total gain of \$125 on the Corporation Y stock deemed received and redeemed; and \$25 and \$50, respectively, of remaining basis in the other 2 blocks of Corporation Y shares. After the redemption transaction, all of Corporation W's shares in Corporation Y, including the deemed shares that are redeemed, are treated as exchanged in a recapitalization described in section 368(a)(1)(E). As a result, Corporation W will have 100 shares in Corporation Y, 50 shares will have a zero basis, 25 shares will have a \$25 basis, and 25 shares will have a \$50 basis.

(d) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 7. Section 1.304-3 is amended by revising paragraph (a) and adding paragraph (c) to read as follows:

§1.304-3 Acquisition by a subsidiary.

(a) *In general.* If a subsidiary, in return for property, acquires stock of its parent corporation from a shareholder of the parent corporation, the acquisition of such stock will be treated as if the parent corporation had redeemed its own stock in exchange for the property. For the purposes of this section, a corporation is a parent corporation if it meets the 50 percent ownership requirements of section 304(c). The determination of whether the amount received shall be treated as received in payment in exchange for the stock will be made by applying section 302(b) with reference to the stock of the issuing parent corporation, or by applying section 303.

* * * * *

(c) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 8. Section 1.304-5 is amended by adding a sentence at the end of paragraph (a) and revising paragraph (c) to read as follows:

§1.304-5 Control.

(a) * * * Specifically, section 318(a) will be applied by substituting "5 percent" for "50 percent" in section 318(a)(2)(C) and by substituting "5 percent" for "50 percent" in section 318(a)(3)(C), except that if section 318(a)(3)(C) would not have applied but for this substitution, by considering a corporation as owning the stock (other than stock in such corporation) owned by or for any shareholder of such corporation in that proportion which the value of the stock which such shareholder owned in such corporation bears to the value of all stock in such corporation.

* * * * *

(c) *Effective/applicability date.* This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

Par. 9. Section 1.351-2 is amended by:

1. Redesignating paragraphs (b), (c), (d) and (e) as paragraphs (c), (d), (e) and (f), respectively and adding new paragraphs (b) and (g) to read as follows:

§1.351-2 Receipt of property.

* * * * *

(b) To determine the amount of gain recognized under section 351(b), the fair market value of each category of consideration received by each transferor is allocated to the properties transferred in proportion to each property's relative fair market value. The application of this paragraph (b) is illustrated by the following example:

Example. C transfers \$2,000 in exchange for 200 shares of stock. D transfers Asset I, Asset II, and Asset III in exchange for \$100 cash and 100 shares of stock. The exchange is subject to section 351. At the time of the exchange, Asset I has a fair market value of \$220 and a basis of \$400, Asset II has a fair market value of \$330 and a basis of \$200, and Asset III has a fair market value of \$550 and a basis of \$250. No gain or loss is recognized to C. Gain, but not loss, is recognized by D. To determine the gain recognized

by D under section 351(b), the fair market value of each category of consideration received is allocated to the properties transferred in proportion to the relative fair market values of the properties transferred. Asset I represents 20 percent of the total fair market value of assets transferred (220/1100), Asset II represents 30 percent (330/1100), and Asset III represents 50 percent (550/1100). Under paragraph (b) of this section, the amount of gain recognized by D is determined by allocating a *pro rata* portion of each class of consideration received to each property transferred as follows: (A) \$20 cash and 20 shares of stock to Asset I (20 percent of 100 shares of stock and 20 percent of \$100)(B) \$30 cash and 30 shares of stock to Asset II (30 percent of 100 shares of stock and 30 percent of \$100); and (C) \$50 cash and 50 shares of stock to Asset III (50 percent of 100 shares of stock and 50 percent of \$100). D realizes a loss of \$180 on Asset I, none of which is recognized, a gain of \$130 on Asset II, \$30 of which is recognized, and a gain of \$300 on Asset III, \$50 of which is recognized.

* * * * *

(g) This section applies to exchanges that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges that occur on or before the date that these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 10. Section 1.354-1 is amended by:

1. Revising the section heading.
2. Redesignating paragraphs (d), (e) and (f) as paragraphs (e), (f) and (g), respectively.
3. Adding new paragraphs (d) and (h).
4. Adding *Example 5* to the end of newly designated paragraph (e).

The additions and revisions read as follows:

§1.354-1 Exchanges of stock, securities and other property in certain reorganizations.

* * * * *

(d) *Exchanges solely or partly for money or other property—(1) Determination of consideration for a share of stock or a security.* In determining the consideration received for a share of stock or a security, except as otherwise provided in this paragraph (d)(1), a *pro rata*

portion of any other property and money received shall be treated as received in exchange for each share of stock and security surrendered, based on the fair market value of such surrendered share of stock or security. However, to the extent the terms of the exchange specify the other property or money that is received in exchange for a particular share of stock or security surrendered or a particular class of stock or securities surrendered, such terms shall control provided that the terms are economically reasonable, unless the shareholder's exchange has the effect of a distribution of a dividend. If the exchange has the effect of a distribution of a dividend and the terms of an exchange specify the other property or money that is received with respect to a particular share of stock and such specification would otherwise be economically reasonable, such other property or money shall be treated as received *pro rata* in exchange for each share of stock within that class (as defined in section 1.302-5(b)(2)) held by the exchanging shareholder. Notwithstanding the preceding sentence, economically reasonable designations between classes of stock or securities (as opposed to within a class) shall generally control. All exchanges made by an exchanging shareholder, whether governed by section 354, 356, or 302, are taken into account to determine whether the shareholder's exchange has the effect of a distribution of a dividend.

(2) *Treatment of exchanges of stock solely for money or other property.* Neither section 354 nor so much of section 356 as relates to section 354 applies to a shareholder's surrender of a share of stock in exchange solely for money or other property that is not permitted to be received without the recognition of gain, even though such exchange is pursuant to a plan of reorganization described in section 368(a), and even though section 354, section 356 or both sections 354 and 356 apply to the exchange of other shares by that shareholder or other shareholders. See section 302 and the regulations under that section for the treatment of such an exchange.

(e) The rules of section 354 may be illustrated by the following examples:

* * * * *

Example 5. D owns shares of Class A common stock, Series 1 preferred stock, and Series 2 preferred

stock in Corporation T. The Series 1 preferred stock and the Series 2 preferred stock are different classes of stock. Pursuant to a reorganization described in section 368(a) to which corporations T and V are parties, D surrenders all of D's Class A common stock in Corporation T in exchange for common stock in Corporation V, all of D's Series 1 preferred stock in Corporation T in exchange for both cash and common stock in Corporation V, and all of D's Series 2 preferred stock in Corporation T in exchange solely for cash. Section 354 applies to the exchange of the Class A common stock in Corporation T for Corporation V common stock. Section 356 applies to the exchange of Series 1 preferred stock for Corporation V common stock and cash. Neither section 354 (nor so much of section 356 as relates to section 354) applies to the exchange of Series 2 preferred stock in Corporation T solely for cash (see section 302 and regulations thereunder).

* * * * *

(h) This section applies to exchanges that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 11. Section 1.355-1 is amended by adding new paragraph (e) to read as follows:

§1.355-1 Distribution of stock and securities of a controlled corporation.

* * * * *

(e) *Exchanges solely or partly for money and other property—(1) Determination of consideration for a share of stock or a security.* In determining the consideration received for a share of stock or a security, except as otherwise provided in this paragraph (e)(1), a *pro rata* portion of any other property and money received shall be treated as received in exchange for each share of stock and security surrendered, based on the fair market value of such surrendered share of stock or security. However, to the extent the terms of the exchange specify the other property or money that is received in exchange for a particular share of stock or security surrendered or a particular class of stock or securities surrendered, such

terms shall control provided that the terms are economically reasonable, unless the shareholder's exchange has the effect of a distribution of a dividend. If the exchange has the effect of a distribution of a dividend and the terms of an exchange specify the other property or money that is received with respect to a particular share of stock and such specification would otherwise be economically reasonable, such other property or money shall be treated as received *pro rata* in exchange for each share of stock within that class (as defined in §1.302-5(b)(2)) held by the exchanging shareholder. Notwithstanding the preceding sentence, economically reasonable designations among classes of stock (as opposed to within a class) shall generally control. All exchanges made by an exchanging shareholder, whether governed by section 355, 356, or 302, are taken into account to determine whether the shareholder's exchange has the effect of a distribution of a dividend.

(2) *Treatment of exchanges of stock solely for money or other property.* Neither section 355 nor so much of section 356 as relates to section 355 applies to a shareholder's surrender of a share of stock in exchange solely for money or other property that is not permitted to be received without the recognition of gain, even though such exchange is pursuant to a plan of reorganization described in section 368(a), or even though section 355, section 356 or both sections 355 and 356 apply to the exchange of other shares by that shareholder or other shareholders. See section 302 and the regulations under that section for the treatment of such an exchange. Any such exchange is treated as occurring immediately before any distribution of or exchange for the stock of the controlled corporation to which section 355 (or so much of section 356 as relates to section 355) applies.

(3) *Effective/applicability date.* This paragraph (e) applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**.

Par. 12. Section 1.356-1 is amended by revising paragraph (b), *Examples 3 and 4* to paragraph (d), and (g) to read as follows:

§1.356-1 Receipt of additional consideration in connection with an exchange.

* * * * *

(b) The rules of §1.354-1(d)(1) or §1.355-1(e)(1), as the case may be, apply for purposes of computing the gain, if any, recognized pursuant to section 356(a) and paragraph (a)(1) of this section.

* * * * *

(d) * * * *

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Example 3. (i) *Facts.* J, an individual, acquired 10 shares of stock of Corporation X on Date 1 for \$3 each (Block 1) and 10 shares of stock of Corporation X on Date 2 for \$9 each (Block 2). On Date 3, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(A). Pursuant to the terms of the plan of reorganization, J surrenders all of J's shares of Corporation X stock for 10 shares of Corporation Y stock and \$100 of cash. On the date of the exchange, the fair market value of each share of stock of Corporation X is \$10 and the fair market value of each share of Corporation Y stock is \$10. The terms of the exchange do not specify that shares of Corporation Y stock or cash are received in exchange for particular shares of stock of Corporation X. In addition, the distribution of the \$100 of cash does not have the effect of a distribution of a dividend.

(ii) *Analysis.* Under paragraph (b) of this section, because the terms of the exchange do not specify that the cash is received in exchange for particular shares of stock of Corporation X, a *pro rata* portion of the cash received is treated as received in exchange for each share of stock of Corporation X based on the fair market value of the surrendered shares. Therefore, J is treated as receiving shares of Corporation Y stock with a fair market value of \$100 and \$100 of cash in exchange for each block of J's stock of Corporation X. J realizes a gain of \$70 on the exchange of the Block 1 shares of Corporation X stock, \$50 of which is recognized under section 356 and paragraph (a) of this section, and J realizes a gain of \$10 on the exchange of the Block 2 shares of Corporation X stock, all of which is recognized under section 356 and paragraph (a) of this section. Because J's gain recognized is not treated as a dividend under section 356(a)(2), such gain shall be treated as gain from the exchange of property.

Example 4. (i) *Facts.* The facts are the same as in *Example 3*, except that the terms of the plan of reorganization specify that J receives 10 shares of stock of Corporation Y in exchange for J's Block 1 shares of stock of Corporation X and \$100 of cash in exchange for J's Block 2 shares of stock of corporation X.

(ii) *Analysis.* Under paragraph (b) of this section, because the terms of the exchange specify that J receives 10 shares of stock of Corporation Y in exchange for J's Block 1 shares of stock of Corporation X and \$100 of cash in exchange for J's Block 2 shares of stock of Corporation X and such terms are economically reasonable, such terms control. J realizes a gain of \$70 on the exchange of the Block 1 shares of stock,

none of which is recognized under section 354. J realizes a gain of \$10 on the exchange of the Block 2 shares of stock of Corporation X, all of which is recognized under section 302(a).

* * * * *

(g) This section applies to exchanges and distributions that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges and distributions that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 13. Section 1.358-1 is revised to read as follows:

§1.358-1 Basis to distributees.

(a) *Certain exchanges or distributions in which only nonrecognition property is received—(1) Exchanges to which section 354 or 355 applies.* In the case of an exchange to which section 354 or 355 applies in which only nonrecognition property is received, the sum of the basis of all of the stock and securities received in the transaction shall be the same as the basis of all of the stock and securities in such corporation surrendered in the transaction, allocated in the manner described in §1.358-2.

(2) *Distributions to which section 355 applies.* In the case of a distribution to which section 355 applies in which only nonrecognition property is received, the sum of the basis of all of the stock and securities with respect to which the distribution is made plus the basis of all of the stock and securities received in the distribution with respect to such stock and securities shall be the same as the basis of the stock and securities with respect to which the distribution is made immediately before the transaction, allocated in the manner described in §1.358-2.

(3) *Exchanges to which section 351 or 361 applies.* In the case of an exchange to which section 351 or 361 applies in which only nonrecognition property is received, the basis of all of the stock and securities received in the exchange shall be the

same as the basis of all of the property exchanged for such stock and securities.

(b) *Certain exchanges or distributions in which both nonrecognition property and "other property" or money are received—(1) Exchanges or distributions to which section 351, 356, or 361 applies.* If in an exchange or distribution to which section 351, 356, or 361 applies both nonrecognition property and "other property" or money are received, the basis of the nonrecognition property held after the transaction shall be determined as described in paragraph (a) of this section, decreased by the sum of the money and the fair market value of the "other property" (as of the date of the transaction) received and increased by the sum of the amount treated as a dividend (if any) and the amount of the gain recognized on the exchange (other than gain treated as a dividend).

(2) *Cases in which loss is recognized.* In any case in which a taxpayer transfers property with respect to which loss is recognized, such loss shall be reflected in determining the basis of the property received in the exchange.

(3) *Basis of "other property" received.* The basis of the "other property" is its fair market value as of the date of the transaction.

(c) *Other rules.* See §1.460-4(k)(3)(iv)(A) for rules relating to stock basis adjustments required where a contract accounted for using a long-term contract method of accounting is transferred in a transaction described in section 351 or a reorganization described in section 368(a)(1)(D) with respect to which the requirements of section 355 (or so much of section 356 as relates to section 355) are met.

(d) The application of this section may be illustrated by the following example:

Example. A purchased a share of stock in Corporation X on Date 1 for \$150. Since that date, A has received distributions under section 301(c)(2) totaling \$60, so that A's adjusted basis for the stock is \$90. In a transaction qualifying under section 356, A exchanged this share for one share in Corporation Y, with a value of \$100, cash of \$10, and other property with a fair market value of \$30. The exchange had the effect of the distribution of a dividend. A's ratable share of the earnings and profits of Corporation X was \$5. A realized a gain of \$50 on the exchange (\$140 - \$90), but the amount of gain recognized is limited to \$40, the sum of the cash received and the fair market value of the other property. Of the gain recognized, \$5 is taxable as a dividend, and \$35 is taxable as a

gain from the exchange of property. The basis to A of the one share of stock of Corporation Y is \$90, that is the adjusted basis of the one share of stock of Corporation X (\$90), decreased by the sum of the cash received (\$10) and the fair market value of the other property received (\$30) and increased by the sum of the amount treated as a dividend (\$5) and the amount treated as a gain from the exchange of property (\$35). The basis of the other property received is \$30.

(e) *Effective/applicability date.* This section applies to exchanges and distributions of stock and securities that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges and distributions that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 14. Section 1.358-2 is revised to read as follows:

§1.358-2 Allocation of basis among nonrecognition property in certain exchanges or distributions.

(a) *Introduction—(1) Scope.* This section prescribes rules for allocating basis in the case of an exchange or distribution to which section 354, 355 or 356 applies. For rules that apply to transfers of stock and other property where the transfer of stock is described in section 351 but does not qualify as a reorganization, see §1.358-2(g). For transfers of stock described in section 361, see §1.358-2(h).

(2) *Definitions.* As used in this section the term *stock* means stock which is not “other property” under sections 351, 356, or 361, as applicable. The term *securities* means securities (including, where appropriate, fractional parts of securities) which are not “other property” under sections 356 or 361, as applicable. Stock, or securities, as the case may be, which differ either because they are in different corporations or because the rights attributable to them differ (although they are in the same corporation) are considered different classes of stock or securities, as the case may be, for purposes of this section.

(b) *Exchanges to which section 354, 355, or 356 applies.* If a shareholder or security holder surrenders one or more shares of stock or one or more securities in an exchange under the terms of section 354, 355 or 356, the following rules apply:

(1) *In general.* Except as otherwise provided in this section, the basis of each share of stock or security received in the exchange shall be the same as the basis of the share or shares of stock or security or securities (or allocable portions thereof) exchanged therefor (as adjusted under §1.358-1).

(2) *More shares of stock or securities received than surrendered.* If more than one share of stock or security is received in exchange for one share of stock or one security, the basis of the share of stock or security surrendered shall be allocated to the shares of stock or securities received in proportion to the fair market value of the shares of stock or securities received.

(3) *Fewer shares of stock or securities received than surrendered—(i) In general.* If one share of stock or security is received in exchange for more than one share of stock or security or if a fraction of a share of stock or security is received, then the basis of the shares of stock or securities surrendered must be allocated to the shares of stock or securities (or allocable portions thereof) received in a manner that reflects, to the greatest extent possible, that a share of stock or security received is received in respect of shares of stock or securities that were acquired on the same date and at the same price. To the extent it is not possible to allocate basis in this manner, the basis of the shares of stock or securities surrendered must be allocated to the shares of stock or securities (or allocable portions thereof) received in a manner that minimizes the disparity in the holding periods of the surrendered shares of stock or securities whose basis is allocated to any particular share of stock or security received.

(ii) *Surrendered shares of stock or securities acquired on different dates or at different prices.* If a share of stock or a security is received in exchange for more than one share of stock or security and such shares of stock or securities were acquired on different dates or at different prices, the share of stock or security received shall be divided into segments based on the relative fair market values of the shares of stock or securities surrendered in exchange for

such share or security. Each segment shall have a basis determined under the rules of this section and a corresponding holding period.

(4) *“Other property,” money, or more than one class of stock or securities received.* If a shareholder or security holder receives shares of stock or securities of more than one class, or receives “other property” or money in addition to shares of stock or securities, the rules of §§1.354-1(d)(1) and 1.355-1(e)(1) apply for purposes of applying the rules of this section.

(5) *Pro rata exchanges to which section 355 or section 356(b) applies.* If a shareholder or security holder surrenders stock in distributing (as defined in §1.355-1(b)) for only stock in controlled and the receipt of the controlled stock would be treated, within the meaning of section 302(d), as a distribution of property to which section 301 applies if the controlled stock received were money or other property, then the basis of the shares received shall be determined under the rules of paragraph (c) of this section and not the rules of this paragraph (b). The rules of paragraph (c) and not the rules of this paragraph (b) also apply to distributions subject to section 356(b).

(c) *Distributions to which section 355 applies.* If a shareholder or security holder receives one or more shares of stock or one or more securities in a distribution under section 355 (or so much of section 356 as relates to section 355), the following rules apply:

(1) *In general.* Except as otherwise provided in this section, the basis of each share of stock or security of the distributing corporation (as defined in §1.355-1(b)), as adjusted under §1.358-1, shall be allocated between the share of stock or security of the distributing corporation with respect to which the distribution is made and the share or shares of stock or security or securities (or allocable portions thereof) received in proportion to their fair market values.

(2) *Fewer shares of stock or securities received than with respect to which distributed—(i) In general.* If one share of stock or security is received with respect to more than one share of stock or security or if a fraction of a share of stock or security is received, then the basis of each share of stock or security of the distribut-

ing corporation must be allocated to the shares of stock or securities (or allocable portions thereof) received in a manner that reflects that, to the greatest extent possible, a share of stock or security received is received with respect to shares of stock or securities acquired on the same date and at the same price. To the extent it is not possible to allocate basis in this manner, the basis of each share of stock or security of the distributing corporation must be allocated to the shares of stock or securities (or allocable portions thereof) received in a manner that minimizes the disparity in the holding periods of the shares of stock or securities with respect to which such shares of stock or securities are received.

(ii) *Distribution upon shares of stock or securities acquired on different dates or at different prices.* If a share of stock or a security is received with respect to more than one share of stock or security and such shares or securities were acquired on different dates or at different prices, the share of stock or security received shall be divided into segments based on the relative fair market values of the shares of stock or securities with respect to which the share of stock or security is received. Each segment shall have a basis determined under the rules of this section and a corresponding holding period.

(3) *“Other property,” money, or more than one class of stock or securities received.* If a shareholder or security holder receives shares of stock or securities of more than one class, or receives “other property” or money in addition to stock or securities, the rules of §1.355-1(e)(1) apply for purposes of applying the rules of this section as though the distribution were an exchange.

(d) *Reorganizations in which stock is deemed received.* For purposes of this section, if a shareholder or security holder surrenders a share of stock or a security in a transaction under the terms of section 354 (or so much of section 356 as relates to section 354) in which such shareholder or security holder receives no property or receives property (including property permitted by section 354 to be received without the recognition of gain or “other property” or money) with a fair market value less than that of the stock or securities surrendered in the transaction, such shareholder or security holder shall be treated as

provided in paragraphs (1) and (2) of this paragraph (d).

(1) *Step one: deemed issuance.* First, the shareholder or security holder shall be treated as receiving the stock, securities, other property, and money actually received by the shareholder or security holder in the transaction and an amount of stock of the issuing corporation (as defined in §1.368-1(b)) that has a value equal to the excess of the value of the stock or securities the shareholder or security holder surrendered in the transaction over the value of the stock, securities, other property, and money the shareholder or security holder actually received in the transaction. If the shareholder owns only one class of stock of the issuing corporation the receipt of which would be consistent with the economic rights associated with each class of stock of the issuing corporation, the stock deemed received by the shareholder pursuant to the previous sentence shall be stock of such class. If the shareholder owns multiple classes of stock of the issuing corporation the receipt of which would be consistent with the economic rights associated with each class of stock of the issuing corporation, the stock deemed received by the shareholder shall be stock of each such class owned by the shareholder immediately prior to the transaction, in proportion to the value of the stock of each such class owned by the shareholder immediately prior to the transaction. The basis of each share of stock or security deemed received and actually received shall be determined under the rules of this section.

(2) *Step two: deemed section 368(a)(1)(E) exchange.* Second, the shareholder or security holder shall then be treated as surrendering all of its shares of stock and securities in the issuing corporation, including those shares of stock or securities held immediately prior to the transaction, those shares of stock or securities actually received in the transaction, and those shares of stock deemed received pursuant to paragraph (d)(1) of this section, in a reorganization under section 368(a)(1)(E) in exchange for the shares of stock and securities of the issuing corporation that the shareholder or security holder actually holds immediately after the transaction. The basis of each share of stock and security deemed received in the reorganization under section 368(a)(1)(E)

shall be determined under the rules of this section.

(e) *Designating which stock or securities were received for, or with respect to, the stock or securities surrendered or distributed upon—(1) In general.* If a shareholder or security holder that purchased or acquired shares of stock or securities in a corporation on different dates or at different prices exchanges such shares of stock or securities under the terms of section 354, 355, or 356, or receives a distribution of shares of stock or securities under the terms of section 355 (or so much of section 356 as relates to section 355), and the shareholder or security holder is not able to identify which particular share of stock or security (or allocable portion of a share of stock or security) is received (or deemed received) in exchange for, or with respect to, a particular share of stock or security, the shareholder or security holder may designate subject to the limitations of this section, which share of stock or security is received in exchange for, or with respect to, a particular share of stock or security, provided that such designation is consistent with the terms of the exchange or distribution (or an exchange deemed to have occurred pursuant to paragraph (d) of this section), and the other rules of this section. The designation will be binding for purposes of determining the Federal tax consequences of any sale or transfer of, or distribution with respect to, the shares or securities received.

(2) *Timing for designation—(i) In exchanges under section 354 or 356.* In the case of an exchange under the terms of section 354 or 356 (including a deemed exchange as a result of the application of paragraph (d) of this section), the designation must be made on or before the first date on which the basis of a share of stock or a security received (or deemed received in the reorganization under section 368(a)(1)(E) in the case of a transaction to which paragraph (d) of this section applies) is relevant. The basis of the shares or securities received in an exchange under the terms of section 354 or section 356, for example, is relevant when such shares or securities are sold or otherwise transferred.

(ii) *In exchanges or distributions under section 355.* In the case of an exchange or distribution under the terms of section 355 (or so much of section 356 as relates to

section 355), the designation must be made on or before the first date on which the basis of a share of stock or a security of the distributing corporation or the controlled corporation (as defined in §1.355-1(b)) is relevant.

(3) *Failure to designate.* If the shareholder fails to make a designation in a case in which the shareholder is not able to identify which share of stock is received in exchange for, or with respect to, a particular share of stock, then the shareholder will not be able to identify which shares are sold or transferred for purposes of determining the basis of property sold or transferred under section 1012 and §1.1012-1(c) and, instead, will be treated as selling or transferring the share received in respect of the earliest share purchased or acquired.

(f) *Applicability of section to certain overlap situations—(1) Exchanges described in both section 1036 and section 354 or 356.* The rules of paragraphs (a) through (e) of this section shall apply to determine the basis of a share of stock or security received by a shareholder or security holder in an exchange described in both section 1036 and section 354 or 356.

(2) *Exchanges described in both section 351 and section 354 or 356.* The rules of paragraphs (a) through (e) of this section shall apply to determine the basis of a share of stock or security received by a shareholder or security holder in an exchange described in both section 351 and section 354 or 356, unless liabilities of the shareholder or security holder are assumed in connection with the exchange.

(g) *Section 351 exchanges—(1) In general.* Except as provided in paragraph (g)(2) of this section, if in an exchange to which section 351 applies property is transferred to a corporation and the transferor receives more than one share of stock, then the aggregate basis of the property transferred (as adjusted under §1.358-1) shall be allocated among all of the shares of stock received in proportion to the fair market values of each share of stock.

(2) *Stock and property transferred in an exchange without a liability assumption.* If in an exchange to which section 351 applies stock or stock and property is transferred to a corporation and no liability is assumed by the transferee in the exchange, then the basis of the stock trans-

ferred (as adjusted under §1.358-1) shall be allocated pursuant to paragraphs (b)(1) through (b)(3) of this section. Such rules also apply to other property, money or more than one class of stock or securities received.

(3) *Transactions in which stock is deemed received.* For purposes of this paragraph (g), if a shareholder transfers property to a corporation in a transaction to which section 351 applies, and such shareholder receives no property or property (including property permitted by section 351 to be received without the recognition of gain or “other property” or money) in such corporation with a fair market value less than that of the property transferred in the transaction, such shareholder shall be treated as provided in paragraphs (3)(i) and (ii) of this paragraph (g).

(i) *Step one: deemed issuance.* First, the shareholder shall be treated as receiving the stock, other property, and money actually received by the shareholder in the transaction and an amount of stock of the transferee corporation that has a value equal to the excess of the value of the property the shareholder transferred in the transaction over the value of the stock, other property, and money the shareholder actually received in the transaction. If the shareholder owns only one class of stock of the transferee corporation the receipt of which would be consistent with the economic rights associated with each class of stock of the transferee corporation, the stock deemed received by the shareholder pursuant to the previous sentence shall be stock of such class. If the shareholder owns multiple classes of stock of the transferee corporation the receipt of which would be consistent with the economic rights associated with each class of stock of the transferee corporation, the stock deemed received by the shareholder shall be stock of each such class owned by the shareholder immediately prior to the transaction, in proportion to the value of the stock of each such class owned by the shareholder immediately prior to the transaction.

(ii) *Step two: deemed section 368(a)(1)(E) exchange.* Second, the shareholder shall then be treated as surrendering all of its shares of stock in the transferee corporation, including those shares of stock held immediately prior to the transaction, those shares of stock actually re-

ceived in the transaction, and those shares of stock deemed received pursuant to paragraph (3)(i) of this paragraph (g), in a reorganization under section 368(a)(1)(E) in exchange for the shares of stock of the transferee corporation that the shareholder actually holds immediately after the transaction. The basis of each share of stock deemed received in the reorganization under section 368(a)(1)(E) shall be determined under the rules of this section.

(h) *Section 361 exchanges.* If in an exchange to which section 361 applies property is transferred to a corporation and the transferor receives stock or securities of more than one class or receives both stock and securities, then the basis of the property transferred (as adjusted under §1.358-1) shall be allocated among all of the stock and securities received in proportion to the fair market values of the stock of each class and the securities of each class.

(i) *Examples.* The application of this section is illustrated by the following examples:

Example 1. More shares of stock received than surrendered. (i) *Facts.* J, an individual, acquired 20 shares of Corporation X stock on Date 1 for \$3 each and 10 shares of Corporation X stock on Date 2 for \$6 each. On Date 3, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(A). Pursuant to the terms of the plan of reorganization, J receives 2 shares of Corporation Y stock in exchange for each share of Corporation X stock. Therefore, J receives 60 shares of Corporation Y stock. Pursuant to section 354, J recognizes no gain or loss on the exchange. J is not able to identify which shares of Corporation Y stock are received in exchange for each share of Corporation X stock.

(ii) *Analysis.* Under paragraph (b)(2) of this section, J has 40 shares of Corporation Y stock each of which has a basis of \$1.50 and is treated as having been acquired on Date 1 and 20 shares of Corporation Y stock each of which has a basis of \$3 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of the shares of corporation Y stock have a basis of \$1.50 and which have a basis of \$3.

Example 2. More shares of stock received than surrendered. (i) *Facts.* The facts are the same as in *Example 1*, except that instead of receiving 2 shares of Corporation Y stock in exchange for each share of Corporation X stock, J receives 1 1/2 shares of Corporation Y stock in exchange for each share of Corporation X stock. Therefore, J receives 45 shares of corporation Y stock. Again, J is not able to identify which shares (or portions of shares) of Corporation Y stock are received in exchange for each share of Corporation X stock.

(ii) *Analysis.* Under paragraph (b)(2) of this section, J has 30 shares of Corporation Y stock each of

which has a basis of \$2 and is treated as having been acquired on Date 1 and 15 shares of Corporation Y stock each of which has a basis of \$4 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of the shares of Corporation Y stock received have a basis of \$2 and which have a basis of \$4.

Example 3. More than one class of stock received.

(i) *Facts.* J, an individual, acquired 10 shares of Class A stock of Corporation X on Date 1 for \$3 each, 10 shares of Class A stock of Corporation X on Date 2 for \$9 each, and 10 shares of Class B stock of Corporation X on Date 3 for \$3 each. On Date 4, J surrenders all of J's shares of Class A stock in exchange for 20 shares of new Class C stock and 20 shares of new Class D stock in a reorganization under section 368(a)(1)(E). Pursuant to section 354, J recognizes no gain or loss on the exchange. On the date of the exchange, the fair market value of each share of Class A stock is \$6, the fair market value of each share of Class C stock is \$2, and the fair market value of each share of Class D stock is \$4. The terms of the exchange do not specify that shares of Class C stock or shares of Class D stock of Corporation X are received in exchange for particular shares of Class A stock of Corporation X.

(ii) *Analysis.* Under paragraph (b)(4) of this section, because the terms of the exchange do not specify that shares of Class C stock or shares of Class D stock of Corporation X are received in exchange for particular shares of Class A stock of Corporation X, a *pro rata* portion of the shares of Class C stock and shares of Class D stock received will be treated as received in exchange for each share of Class A stock based on the fair market value of the surrendered shares of Class A stock. Therefore, J is treated as receiving one share of Class C stock and one share of Class D stock in exchange for each share of Class A stock. Under paragraph (b)(2) of this section, J has 10 shares of Class C stock, each of which has a basis of \$1 and is treated as having been acquired on Date 1 and 10 shares of Class C stock, each of which has a basis of \$3 and is treated as having been acquired on Date 2. In addition, J has 10 shares of Class D stock, each of which has a basis of \$2 and is treated as having been acquired on Date 1 and 10 shares of Class D stock, each of which has a basis of \$6 and is treated as having been acquired on Date 2. J's basis in each share of Class B stock remains \$3. Under paragraph (e) of this section, on or before the date on which the basis of a share of Class C stock or Class D stock received becomes relevant, J may designate which of the shares of Class C stock have a basis of \$1 and which have a basis of \$3, and which of the shares of Class D stock have a basis of \$2 and which have a basis of \$6.

Example 4. Money received in addition to stock.

(i) *Facts.* J, an individual, acquired 10 shares of stock of Corporation X on Date 1 for \$2 each (Block 1), 10 shares of stock of Corporation X on Date 2 for \$4 each (Block 2), and 20 shares of stock of Corporation X on Date 3 for \$6 each (Block 3). On Date 4, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(A). Pursuant to the terms of the plan of reorganization, J surrenders all of J's shares of Corporation X stock for 40 shares of Corporation Y stock and \$200 of cash. The distribution of \$200 of cash does not have the effect

of a distribution of a dividend. On the date of the exchange, the fair market value of each share of stock of Corporation X is \$10, and the fair market value of each share of Corporation Y stock is \$5. The terms of the exchange do not specify that shares of Corporation Y stock or cash are received in exchange for particular shares of stock of Corporation X.

(ii) *Analysis.* Under paragraph (b)(4) of this section and under §1.356-1(b), because the terms of the exchange do not specify that shares of Corporation Y stock or cash are received in exchange for particular shares of stock of Corporation X, a *pro rata* portion of the shares of Corporation Y stock and cash received will be treated as received in exchange for each share of stock of Corporation X surrendered based on the fair market value of such stock. Therefore, J is treated as receiving one share of Corporation Y stock and \$5 of cash in exchange for each share of stock of Corporation X. J realizes a gain of \$80 on the exchange of Block 1, \$50 of which is recognized under §1.356-1(a). J realizes a gain of \$60 of the exchange of Block 2, \$50 of which is recognized under §1.356-1(a). J realizes a gain of \$80 on the exchange of the Block 3 shares of stock of Corporation X, all of which is recognized under §1.356-1(a). Under paragraph (b)(1) of this section, J has 10 shares of Corporation Y stock, each of which has a basis of \$2 and is treated as having been acquired on Date 1, 10 shares of Corporation Y stock, each of which has a basis of \$4 and is treated as having been acquired on Date 2, and 20 shares of Corporation Y stock, each of which has a basis of \$5 and is treated as having been acquired on Date 3. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of the shares of Corporation Y stock received have a basis of \$2, which have a basis of \$4, and which have a basis of \$5.

Example 5. Money received in addition to stock.

(i) *Facts.* The facts are the same as in *Example 4*, except that the terms of the plan of reorganization specify that J receives 40 shares of stock of Corporation Y in exchange for J's Block 1 and Block 2 shares of stock of Corporation X and \$200 of cash in exchange for J's Block 3 shares of stock of Corporation X.

(ii) *Analysis.* Under paragraph (b)(4) of this section and under §1.356-1(b), because the terms of the exchange specify that J receives 40 shares of stock of Corporation Y in exchange for J's Block 1 and Block 2 shares of stock of Corporation X and \$200 of cash in exchange for J's Block 3 shares of stock of Corporation X and such terms are economically reasonable and the distribution is not dividend equivalent, such terms control. J realizes a gain of \$80 on the exchange of Block 1, none of which is recognized under section 354. J realizes a gain of \$60 on the exchange of Block 2, none of which is recognized under section 354. J realizes a gain of \$80 on the exchange of the Block 3 shares of stock of Corporation X, all of which is recognized under section 302(a). Under paragraph (b)(2) of this section, J has 20 shares of Corporation Y stock, each of which has a basis of \$1 and is treated as having been acquired on Date 1, and 20 shares of Corporation Y stock, each of which has a basis of \$2 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of

the shares of Corporation Y stock received have a basis of \$1 and which have a basis of \$2.

Example 6. Stock and securities received as non-recognition property.

(i) *Facts.* J, an individual, acquired 10 shares of stock of Corporation X on Date 1 for \$2 each, and a security issued by Corporation X to J on Date 2 with a principal amount of \$100 and a basis of \$100. On Date 3, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(A). Pursuant to the terms of the plan of reorganization, J surrenders all of J's shares of Corporation X stock in exchange for 10 shares of Corporation Y stock and surrenders J's Corporation X security in exchange for a Corporation Y security. The distribution of neither the Y stock nor the Y security has the effect of a distribution of a dividend. On the date of the exchange, the fair market value of each share of stock of Corporation X is \$10, the fair market value of J's Corporation X security is \$100, the fair market value of each share of Corporation Y stock is \$10, and the fair market value and principal amount of the Corporation Y security received by J is \$100.

(ii) *Analysis.* Under paragraph (b)(4) of this section and under §1.354-1(d), because the terms of the exchange specify that J receives 10 shares of stock of Corporation Y in exchange for J's shares of Class A stock of Corporation X and a Corporation Y security in exchange for its Corporation X security and such terms are economically reasonable, such terms control. Pursuant to section 354, J recognizes no gain on either exchange. Under paragraph (b)(1) of this section, J has 10 shares of Corporation Y stock, each of which has a basis of \$2 and is treated as having been acquired on Date 1, and a security that has a basis of \$100 and is treated as having been acquired on Date 2.

Example 7. Fewer shares of stock received than surrendered.

(i) *Facts.* J, an individual, acquired 10 shares of Corporation X stock on Date 1 for \$2 each and 10 shares of Corporation X stock on Date 2 for \$5 each. On Date 3, Corporation Y acquires the stock of Corporation X in a reorganization under section 368(a)(1)(B). Pursuant to the terms of the plan of reorganization, J receives one share of Corporation Y stock in exchange for every 2 shares of Corporation X stock. Pursuant to section 354, J recognizes no gain or loss on the exchange. J is not able to identify which portion of each share of Corporation Y stock is received in exchange for each share of Corporation X stock.

(ii) *Analysis.* Under paragraph (b)(3) of this section, J has 5 shares of Corporation Y stock each of which has a basis of \$4 and is treated as having been acquired on Date 1 and 5 shares of Corporation Y stock each of which has a basis of \$10 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of the shares of Corporation Y stock received have a basis of \$4 and which have a basis of \$10.

Example 8. Exchange described in sections 351 and 354.

(i) *Facts.* J, an individual, acquired 10 shares of Corporation X stock on Date 1 for \$3 each and 10 shares of Corporation X stock on Date 2 for \$6 each. On Date 3, Corporation Z, a newly formed, wholly owned subsidiary of Corporation Y, merges with and into Corporation X with Corporation X sur-

living. As part of the plan of merger, J receives one share of Corporation Y stock in exchange for each share of Corporation X stock. In connection with the transaction, Corporation Y assumes a liability of J. In addition, after the transaction, J owns stock of Corporation Y satisfying the requirements of section 368(c). J's transfer of the Corporation X stock to Corporation Y is an exchange described in sections 351 and 354.

(ii) *Analysis.* Under paragraph (f)(2) of this section, because, in connection with the transfer of the Corporation X stock to Corporation Y, Corporation Y assumed a liability of J, the rules of paragraph (g) of this section apply to determine J's basis in the Corporation Y stock received in the transaction.

Example 9. Reorganization in which stock is deemed received. (i) *Facts.* Each of Corporation X and Corporation Y has a single class of stock outstanding, all of which is owned by J, an individual. J acquired 100 shares of Corporation X stock on Date 1 for \$1 each and 100 shares of Corporation Y stock on Date 2 for \$2 each. On Date 3, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(D). Pursuant to the terms of the plan of reorganization, J surrenders J's 100 shares of Corporation X stock but does not receive any additional Corporation Y stock. Immediately before the effective time of the reorganization, the fair market value of each share of Corporation X stock and each share of Corporation Y stock is \$1. Pursuant to section 354, J recognizes no gain or loss.

(ii) *Analysis.* Under paragraph (d) of this section, J is deemed to have received shares of Corporation Y stock with an aggregate fair market value of \$100 in exchange for J's Corporation X shares. Given the number of outstanding shares of stock of Corporation Y and their value immediately before the effective time of the reorganization, J is deemed to have received 100 shares of stock of Corporation Y in the reorganization. Under paragraph (b)(1) of this section, each of those shares has a basis of \$1 and is treated as having been acquired on Date 1. Then, the stock of Corporation Y is deemed to be recapitalized in a reorganization under section 368(a)(1)(E) in which J receives 100 shares of Corporation Y stock in exchange for those shares of Corporation Y stock that J held immediately prior to the reorganization and those shares J is deemed to have received in the reorganization. Under paragraph (b)(3) of this section, immediately after the reorganization, J holds 50 shares of Corporation Y stock each of which has a basis of \$2 and is treated as having been acquired on Date 1 and 50 shares of Corporation Y stock each of which has a basis of \$4 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of any share of J's Corporation Y stock becomes relevant, J may designate which of the shares of Corporation Y have a basis of \$2 and which have a basis of \$4.

Example 10. Reorganization in which stock is deemed received. (i) *Facts.* Corporation X has a single class of stock outstanding, all of which is owned by J, an individual. J acquired 100 shares of Corporation X stock on Date 1 for \$1 each. Corporation Y has two classes of stock outstanding, common stock and nonvoting preferred stock. On Date 2, J acquired 100 shares of Corporation Y common stock for \$2 each and 100 shares of Corporation Y preferred stock for \$4 each. On Date 3, Corporation Y acquires the assets of Corporation X in a reorganization under sec-

tion 368(a)(1)(D). Pursuant to the terms of the plan of reorganization, J surrenders J's 100 shares of Corporation X stock but does not receive any additional Corporation Y stock. Immediately before the effective time of the reorganization, the fair market value of each share of Corporation X stock is \$10, the fair market value of each share of Corporation Y common stock is \$10, and the fair market value of each share of Corporation Y preferred stock is \$20. Pursuant to section 354, J recognizes no gain or loss.

(ii) *Analysis.* Under paragraph (d) of this section, J is deemed to have received shares of Corporation Y stock with an aggregate fair market value of \$1,000 in exchange for J's Corporation X shares. Consistent with the economics of the transaction and the rights associated with each class of stock of Corporation Y owned by J, J is deemed to receive additional shares of Corporation Y common stock. Because the value of the common stock indicates that the liquidation preference associated with the Corporation Y preferred stock could be satisfied even if the reorganization did not occur, it is not appropriate to deem the issuance of additional Corporation Y preferred stock. Given the number of outstanding shares of common stock of Corporation Y and their value immediately before the effective time of the reorganization, J is deemed to have received 100 shares of common stock of Corporation Y in the reorganization. Under paragraph (b)(1) of this section, each of those shares has a basis of \$1 and is treated as having been acquired on Date 1. Then, the common stock of Corporation Y is deemed to be recapitalized in a reorganization under section 368(a)(1)(E) in which J receives 100 shares of Corporation Y common stock in exchange for those shares of Corporation Y common stock that J held immediately prior to the reorganization and those shares of Corporation Y common stock that J is deemed to have received in the reorganization. Under paragraph (b)(3) of this section, immediately after the reorganization, J holds 50 shares of Corporation Y common stock, each of which has a basis of \$2 and is treated as having been acquired on Date 1, and 50 shares of Corporation Y common stock, each of which has a basis of \$4 and is treated as having been acquired on Date 2. Under paragraph (e) of this section, on or before the date on which the basis of any share of J's Corporation Y common stock becomes relevant, J may designate which of those shares have a basis of \$2 and which have a basis of \$4.

Example 11. Distribution to which section 355 applies. (i) *Facts.* J, an individual, acquired 5 shares of Corporation X stock on Date 1 for \$4 each and 5 shares of Corporation X stock on Date 2 for \$8 each. Corporation X owns all of the outstanding stock of Corporation Y. The fair market value of the stock of Corporation X is \$1800. The fair market value of the stock of Corporation Y is \$900. In a distribution to which section 355 applies, Corporation X distributes all of the stock of Corporation Y *pro rata* to its shareholders. In the distribution, J receives 2 shares of Corporation Y stock with respect to each share of Corporation X stock. Pursuant to section 355, J recognizes no gain or loss on the receipt of the shares of Corporation Y stock. J is not able to identify which share of Corporation Y stock is received in respect of each share of Corporation X stock.

(ii) *Analysis.* Under paragraph (c)(1) of this section, because J receives 2 shares of Corporation Y stock with respect to each share of Corporation

X stock, the basis of each share of Corporation X stock is allocated between such share of Corporation X stock and two shares of Corporation Y stock in proportion to the fair market value of those shares. Therefore, each of the 5 shares of Corporation X stock acquired on Date 1 will have a basis of \$2 and each of the 10 shares of Corporation Y stock received with respect to those shares will have a basis of \$1. In addition, each of the 5 shares of Corporation X stock acquired on Date 2 will have a basis of \$4 and each of the 10 shares of Corporation Y stock received with respect to those shares will have a basis of \$2. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation Y stock received becomes relevant, J may designate which of the shares of Corporation Y stock have a basis of \$1 and which have a basis of \$2.

Example 12. Designation of stock surrendered and received. (i) *Facts.* J, an individual, acquired 20 shares of Corporation X stock on Date 1 for \$2 each and 20 shares of Corporation X stock on Date 2 for \$4 each. Corporation X has 80 shares of stock outstanding. Corporation X owns 40 shares of stock of Corporation Y, which represents all of the outstanding stock of Corporation Y. The fair market value of the stock of Corporation X is \$80. The fair market value of the stock of Corporation Y is \$40. Corporation X distributes all of the stock of Corporation Y in a transaction to which section 355 applies. In the transaction, J surrenders 20 shares of stock of Corporation X in exchange for 20 shares of stock of Corporation Y. J retains 20 shares of Corporation X stock. Pursuant to section 355, J recognizes no gain or loss on the receipt of the shares of Corporation Y stock. J is not able to identify which shares of Corporation X stock are surrendered. In addition, J is not able to identify which shares of Corporation Y stock are received in exchange for each surrendered share of Corporation X. In addition, the receipt of Y stock is not dividend equivalent.

(ii) *Analysis.* Under paragraph (b)(1) of this section, J has 20 shares of Corporation Y stock each of which is treated as received in exchange for one share of Corporation X stock. The basis of the 20 shares of Corporation X stock that are retained by J will remain unchanged. Under paragraph (e) of this section, on or before the date on which the basis of a share of Corporation X or Corporation Y stock becomes relevant, J may designate which shares of Corporation X stock J surrendered in the exchange and which share of the Corporation Y stock received is received for each share of Corporation X stock surrendered. Therefore, it is possible that a share of Corporation Y stock would have a basis of \$2 and be treated as having been acquired on Date 1, or would have a basis of \$4 and be treated as having been acquired on Date 2.

Example 13. Surrendered shares of stock or securities acquired on different dates or at different prices. (i) *Facts.* J, an individual, acquired 10 shares of Corporation X stock on Date 1 for \$3 each, 10 shares of Corporation X stock on Date 2 for \$18 each, 10 shares of Corporation X stock on Date 3 for \$6 each, and 10 shares of Corporation X stock on Date 4 for \$9 each. On Date 5, Corporation Y acquires the assets of Corporation X in a reorganization under section 368(a)(1)(A). Pursuant to the terms of the plan of reorganization, J receives a $\frac{3}{4}$ share of Corporation Y stock in exchange for each share of Corporation X stock. Therefore, J receives 30 shares of Corpora-

tion Y stock. Pursuant to section 354, J recognizes no gain or loss on the exchange. J is not able to identify which shares of Corporation Y stock are received in exchange for each share (or portions of shares) of Corporation X stock.

(ii) *Analysis.* Under paragraph (b)(3) of this section, J has 7 shares of Corporation Y stock each of which has a basis of \$4 and is treated as having been acquired on Date 1, 7 shares of Corporation Y stock each of which has a basis of \$24 and is treated as having been acquired on Date 2, 7 shares of Corporation Y stock each of which has a basis of \$8 and is treated as having been acquired on Date 3, and 7 shares of Corporation Y stock each of which has a basis of \$12 and is treated as having been acquired on Date 4. In addition, J has two shares of Corporation Y stock, each of which is divided into two equal segments under paragraph (b)(3) of this section. The first of those two shares has one segment with a basis of \$2 that is treated as having been acquired on Date 1 and a second segment with a basis of \$12 that is treated as having been acquired on Date 2. The second of those two shares has one segment with a basis of \$4 that is treated as having been acquired on Date 3 and a second segment with a basis of \$6 that is treated as having been acquired on Date 4. Under paragraph (e) of this section, on or before the date on which a share of Corporation Y stock received becomes relevant, J may designate which of the shares of Corporation Y stock have a basis of \$4, which have a basis of \$24, which have a basis of \$8, which have a basis of \$12, and which share has a split basis of \$2 and \$12, and which share has a split basis of \$4 and \$6.

Example 14. Shareholder election and terms of the exchange. (i) *Facts.* J, an individual, acquired 10 shares of stock of widely-held Corporation X on Date 1 for \$2 each, 10 shares of stock of Corporation X on Date 2 for \$4 each, and 10 shares of stock of Corporation X on Date 3 for \$6. On Date 5, Corporation X and Corporation Y sign a binding contract pursuant to which, in a reorganization under section 368(a)(1)(A), Corporation X will be merged with and into Corporation Y on Date 6. The fair market value of each share of Corporation X stock is \$10 and the fair market value of each share of Corporation Y stock is \$5. In exchange for each share of stock of Corporation X, the shareholders of Corporation X may elect to receive 2 shares of stock of Corporation Y or \$10 cash. If, however, the elected consideration is oversubscribed, by default a *pro-rata* mix of consideration will be received for the corresponding shares of stock of Corporation X (the default *pro-rata* term). J elects to receive 2 shares of stock of Corporation Y in exchange for each of the 10 shares of stock of Corporation X acquired on Date 1, and \$10 cash for each of the remaining 20 shares of stock of Corporation X. Neither of the elections is oversubscribed by the shareholders of Corporation X. The distribution of cash does not have the effect of a distribution of a dividend.

(ii) *Analysis.* Under paragraph (b)(4) of this section and under §1.356-1(b), because the receipt does not have the effect of dividend, and the terms of the exchange specify that J receives 2 shares of stock of Corporation Y in exchange for each of the 10 shares of stock of Corporation X acquired on Date 1, and \$10 cash for each of the remaining 20 shares of stock of Corporation X, and such terms are economically reasonable, such terms control. J realizes a gain of

\$80 on the exchange of the 10 shares of stock of Corporation X acquired on Date 1, none of which is recognized under §1.356-1(a). J realizes a gain of \$60 on the exchange of the 10 shares of stock of Corporation X acquired on Date 2 and realizes \$40 on the exchange of the 10 shares of stock of Corporation X acquired on Date 3, all of which is recognized under §1.356-1(a). Under paragraph (b)(2) of this section, J has 20 shares of stock of Corporation Y, each of which has a basis of \$1 and is treated as having been acquired on Date 1.

Example 15. Shareholder election and terms of the exchange. (i) *Facts.* The facts are the same as in *Example 14*, except that the cash election is oversubscribed and, pursuant to the default *pro-rata* term, for each of the shares of stock of Corporation X that J acquired on Date 2 and Date 3, J receives 1 share of stock of Corporation Y and \$5 cash.

(ii) *Analysis.* Under paragraph (b)(4) of this section and under §1.356-1(b), because the terms of the exchange specify that J receives 2 shares of stock of Corporation Y in exchange for each of the 10 shares of stock of Corporation X acquired on Date 1, and 1 share of stock of Corporation Y and \$5 cash for each of the remaining 20 shares of stock of Corporation X, and such terms are economically reasonable, such terms control. J realizes a gain of \$80 on the exchange of the 10 shares of stock of Corporation X acquired on Date 1, none of which is recognized under §1.356-1(a). J realizes a gain of \$60 on the exchange of the 10 shares of stock of Corporation X acquired on Date 2, \$50 of which is recognized under §1.356-1(a), and \$40 on the exchange of the 10 shares of stock of Corporation X acquired on Date 3, all of which is recognized under §1.356-1(a). Of the 40 shares of stock of Corporation Y received by J, 20 of the shares each has a basis of \$1 and is treated as having been acquired on Date 1 under paragraph (b)(2) of this section, and 10 of the shares each has a basis of \$4 and is treated as having been acquired on Date 2 and 10 of the shares each has a basis of \$6 and is treated as having been acquired on Date 3 under paragraph (b)(1) of this section.

Example 16. Exchange described in section 351 in which only stock is received. (i) *Facts.* J transfers Asset I, Asset II, and 50 shares of Corporation X stock in exchange for 110 shares of Corporation Y in an exchange to which section 351 applies. At the time of the exchange, Asset I has a fair market value of \$220 and a basis of \$400, Asset II has a fair market value of \$330 and a basis of \$200, and the 50 shares of Corporation X stock each have a fair market value of \$22 (\$550 total) and a basis of \$10 (\$250 total). The fair market value of each share of Corporation Y stock is \$10.

(ii) *Analysis.* Pursuant to section 351(a), J recognizes no gain or loss on the exchange. Under paragraph (g)(2) of this section, J has 55 shares of Corporation Y stock each of which has a basis of \$10.91 (\$600 total, the aggregate basis of Asset I and Asset II). Under paragraph (g)(2) of this section, J has 55 shares of Corporation Y stock each of which has a basis of \$4.55 (\$250 total).

Example 17. Exchange described in section 351 in which "other property" is received. (i) *Facts.* The facts are the same as *Example 1*, except J receives 100 shares of Corporation Y stock and \$100 in the exchange.

(ii) *Analysis.* Pursuant to section 351(b), J recognizes gain, but no loss, on the exchange, but not in excess of the amount of money received. Under §1.351-2, J realizes a loss of \$180 on Asset I, none of which is recognized, a gain of \$130 on Asset II, \$30 of which is recognized, and a gain of \$300 on shares of Corporation X stock, \$50 of which is recognized. Under paragraph (g)(2) of this section, J has 50 shares of Corporation Y stock each of which has a basis of \$11.60 (\$580 total), and 50 shares of Corporation Y stock each of which has a basis of \$5.00 (\$250 total).

(j) *Effective/applicability date.* This section applies to exchanges and distributions of stock and securities that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges and distributions of stock and securities that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations were published as final regulations in the **Federal Register**.

Par. 15. Section 1.358-6 is amended by revising paragraphs (c)(1)(i)(B), (c)(3)(ii), and (f)(3) to read as follows:

§1.358-6 Stock basis in certain triangular reorganizations.

- * * * * *
- (c) * * *
- (1) * * *
- (i) * * *

(B) P transferred the T assets (and liabilities which S assumed or to which the T assets acquired by S were subject) to S in a transaction in which P received no property and P's basis in S stock was determined under section 358. See §1.358-2(g)(3) (allocation of basis in a section 351 transaction in which stock is deemed received).

- * * * * *
- (3) * * *

(ii) P transferred the T stock to S in a transaction in which P received no property and P's basis in its S stock was determined under section 358. See §1.358-2(g)(3) (allocation of basis in a section 351 transaction in which stock is deemed received).

- * * * * *
- (f) * * *

(3) This section applies to exchanges that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For exchanges that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, 2008, for the year before the date these regulations are published as final regulations in the **Federal Register**.

Par. 16. Section 1.368-1 is amended by adding a sentence to the end of paragraph (a) and by revising paragraph (e)(9) to read as follows:

§1.368-1 Purpose and scope of exception of reorganization exchanges.

(a) * * * For purposes of determining whether a transaction qualifies as a reorganization under section 368(a), to the extent the terms of the exchange specify that a particular property is received in exchange for a particular property, such terms shall control provided such terms are economically reasonable.

* * * * *

(e) * * *

(9) This section applies to exchanges that occur after the date these regulations are published as final regulations in the **Federal Register**, except for exchanges which occur pursuant to a written agreement that is binding on or before the date these regulations are published as final in the **Federal Register**. For effective dates for transactions that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see paragraph (e) of this section, as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

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Par. 17. Section 1.861-12 is added to read as follows:

§1.861-12 Characterization rules and adjustments for certain assets.

(a) through (c)(2)(v) [Reserved]. For further guidance, see §1.861-12T(a) through (c)(2)(v).

(c)(2)(vi) Adjustments in respect of redeemed stock for taxpayers using the tax book value method. Solely for purposes of apportioning expenses on the basis of the tax book value of assets, the adjusted basis of any other class of stock in a 10 percent owned corporation owned directly by a taxpayer that is a redeemed shareholder (as defined in §1.302-5(b)(1)) with respect to such corporation shall be increased by the amount of any loss that has not been taken into account under §1.302-5(a)(3) as of the close of the redeemed shareholder's taxable year (unrecovered loss). If the redeemed shareholder does not own directly any shares in the 10 percent owned corporation as of the end of the taxable year, but is treated for purposes of section 302(b) as owning shares actually owned by another member of the redeemed shareholder's affiliated group, as defined in section §1.861-11(d)(1) and §1.861-11T(d)(6) with respect to the redeemed shareholder, then, solely for purposes of this paragraph (c)(2)(vi), the adjusted basis of the shares in the 10 percent owned corporation, if any, that are owned by such other corporation or corporations shall be increased by the amount of the redeemed shareholder's unrecovered loss (and allocated among such corporations, if applicable, in proportion to their relative adjusted bases (as adjusted pursuant to this paragraph and §1.861-12T(c)(2)) in the stock of the redeeming corporation). These adjustments are to be made annually and are noncumulative.

(vii) *Examples.* Certain of the rules of this paragraph (c)(2) may be illustrated by the following examples:

Examples 1 and 2. [Reserved]. For further guidance, see §1.861-12T(c)(2)(vii), *Examples 1 and 2.*

Example 3. X, an unaffiliated domestic corporation that was organized on January 1, 2000, owns all of the stock of Y, a foreign corporation with a functional currency other than the U.S. dollar since January 1, 2000. The Y stock held by X includes Class A and Class B common stock. X's adjusted basis in the Class A and Class B common stock is \$25,000 and \$50,000, respectively. Y has earnings and profits for the 2008 taxable year of \$40,000. During the 2008 taxable year, Y redeems all of the Class A common stock held by X for \$40,000. Because X still

owns all of the outstanding stock of Y, the redemption is treated as a distribution with respect to the stock of Y under section 301. Under §1.302-5(a)(3), X's \$25,000 adjusted basis in the redeemed shares of Class A common stock is treated as a loss recognized on the date of the redemption, none of which is taken into account in 2008. Under paragraph (c)(2)(vi) of this section, solely for purposes of apportioning expenses on the basis of the tax book value of assets, X's adjusted basis in its remaining Class B common stock of Y is considered to be \$75,000 (\$50,000 adjusted basis in the Class B common stock plus \$25,000 unrecovered basis in the redeemed Class A common stock).

(c)(2)(viii) *Effective/applicability date.* Paragraph (c)(2)(vi) and *Example 3* apply to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**.

(c)(3) through (j) [Reserved]. For further guidance, see §1.861-12T(c)(3) through (j).

Par. 18. Section 1.1002-1 is redesignated as 1.1001-6 and amended by:

1. Revising paragraph (c) and adding a new paragraph (e) to read as follows:

§1.1001-6 Sales or exchanges.

* * * * *

(c) *Certain exceptions to general rule.* Exceptions to the general rule are made, for example, by sections 351(a), 354, 361(a), 721, 1031, 1035 and 1036. These sections describe certain specific exchanges of property in which at the time of the exchange particular differences exist between the property parted with and the property acquired, but such differences are more formal than substantial. As to these, the Internal Revenue Code provides that such differences shall not be deemed controlling, and that gain or loss shall not be recognized at the time of the exchange. The underlying assumption of these exceptions is that the new property is substantially a continuation of the old investment still unliquidated; and, in the case of reorganizations, that the new enterprise, the new corporate structure and the new property are substantially continuations of the old still unliquidated. Solely for purposes of determining whether the exceptions to the general rule under sections 354 and 361 apply to an exchange, to the extent the terms of the exchange specify that a particular property is received in exchange for a particular property, such terms shall control provided such terms are economically reasonable.

* * * * *

(e) *Effective/applicability date.* This section applies to exchanges that occur after the date these regulations are published as final regulations in the **Federal Register**. For exchanges that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 19. Section 1.1016-2 is amended by adding paragraphs (e) and (f) to read as follows:

§1.1016-2 Items properly chargeable to capital account.

* * * * *

(e) Solely for purposes of determining basis in stock, in the case of a shareholder capital contribution to which section 118 applies, the principles of §1.358-2(g)(3) (allocation of basis in a section 351 transaction in which stock is deemed received) shall apply.

(f) This section applies to transactions that occur after the date these regulations are published as final regulations in the **Federal Register**. For exchanges that occur on or before the date these regulations are published as final regulations in the **Federal Register**, see this section as contained in 26 CFR part 1 revised April 1, for the year before these regulations are published as final regulations in the **Federal Register**.

Par. 20. Section 1.1374-10, the first sentence of paragraph (a) is revised to read as follows:

§1.1374-10 Effective date and additional rules.

(a) *In general.* For transactions to which §1.302-5 applies [Reserved]. Sections 1.1374-1 through 1.1374-9, other than §1.1374-3(b) and (c) *Examples 2 through 4*, apply for taxable years ending on or after December 27, 1994, but only in cases where the S corporation's return for the taxable year is filed pursuant to an S election or a section 1374(d)(8) transaction occurring on or after December 27, 1994. * * *

* * * * *

Linda M. Kroening,
(Acting) Deputy Commissioner
for Services and Enforcement.

(Filed by the Office of the Federal Register on January 16, 2009, 8:45 a.m., and published in the issue of the Federal Register for January 21, 2009, 74 F.R. 3509)

Withdrawal of Notice of Proposed Rulemaking Regarding Section 707 Regarding Disguised Sales, Generally

Announcement 2009-4

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Withdrawal of notice of proposed rulemaking.

SUMMARY: This document withdraws proposed regulations relating to the treatment of transactions between a partnership and its partners as disguised sales of partnership interests between the partners under section 707(a)(2)(B) of the Internal Revenue Code. The withdrawal affects partnerships and their partners.

FOR FURTHER INFORMATION CONTACT: Deane M. Burke or Allison R. Carmody, (202) 622-3070 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

Section 707(a)(2)(B) provides that, under regulations prescribed by the Secretary, if transfers of property between a partner or partners and a partnership, when viewed together, are properly characterized as a sale or exchange of property, such transfers shall be treated as either transactions between the partnership and one who is not a partner or between two or more partners acting other than in their capacity as partners. The legislative history of section 707(a)(2)(B) indicates the provision was adopted as a result of Congressional concern that taxpayers were deferring or avoiding tax on sales of partnership property, including sales of partnership interests, by characterizing sales as contributions of property, including money,

followed or preceded by related partnership distributions. See H.R. Rep. No. 861, 98th Cong. 2nd Sess. 861 (1984), 1984-3 (Vol. 2) CB 115. Specifically, Congress was concerned about court decisions that allowed tax-free treatment in cases that were economically indistinguishable from sales of property to a partnership or another partner, and believed that these transactions should be treated for tax purposes in a manner consistent with their underlying economic substance. See H.R. Rep. No. 432, 98th Cong. 2nd Sess. 1218 (1984) (H.R. Rep.), and S. Prt. No. 169 (Vol. I), 98th Cong. 2nd Sess. 225 (1984) (S. Prt.) (discussing *Communications Satellite Corp. v. United States*, 625 F.2d 997 (Ct. Cl. 1980), and *Jupiter Corp. v. United States*, 2 Cl. Ct. 58 (1983), both of which involved disguised sales of a partnership interest).

On October 9, 2001, the IRS and the Treasury Department issued Notice 2001-64, 2001-2 C.B. 316, (see § 601.601(d)(2)(ii)(b)), announcing that the IRS and the Treasury Department were considering issuing proposed regulations under section 707(a)(2)(B), relating to disguised sales of partnership interests. The IRS and the Treasury Department requested comments on the scope and substance of guidance concerning disguised sales of partnership interests, including any applicable safe harbors or exceptions. Written comments in response to Notice 2001-64 were received and considered in drafting proposed regulations.

In response to requests, on November 26, 2004, the Treasury Department and the IRS published in the **Federal Register** (REG-149513-03, 2004-2 C.B. 1009 [69 FR 68838]) a notice of proposed rulemaking under section 707(a)(2)(B), (REG-149519-03) relating to disguised sales of partnership interests. The proposed regulations sought to amend the existing regulations for disguised sales of property (existing property regulations) by adding rules for disguised sales of partnership interests and by revising the rules relating to disguised sales of property. The proposed regulations for disguised sales of partnership interests include a framework similar to that in the existing property regulations, with a general rule that would apply based on all of the facts and circumstances.

The Treasury Department and the IRS received written comments on the proposed regulations from interested parties. The Treasury Department and the IRS, having now thoroughly considered those comments, have decided to withdraw the proposed regulations. The Treasury Department and the IRS will continue to study this area and may issue guidance in the future. Until new guidance is issued, any determination of whether transfers between a partner or partners and

a partnership is a transfer of a partnership interest will be based on the statutory language, guidance provided in legislative history, and case law.

* * * * *

Withdrawal of Notice of Proposed Rulemaking

Accordingly, under the authority of 26 U.S.C. 7805, the notice of proposed rulemaking (REG-149519-03) that was

published in the **Federal Register** on November 26, 2004 (69 FR 68838) is withdrawn.

Linda E. Stiff,
*Deputy Commissioner for
Services and Enforcement.*

(Filed by the Office of the Federal Register on January 15, 2009, 8:45 a.m., and published in the issue of the Federal Register for January 16, 2009, 74 F.R. 3508)

Announcement of Disciplinary Sanctions From the Office of Professional Responsibility

Announcement 2009-8

The Office of Professional Responsibility (OPR) announces recent disciplinary sanctions involving attorneys, certified public accountants, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and appraisers. These individuals are subject to the regulations governing practice before the Internal Revenue Service (IRS), which are set out in Title 31, Code of Federal Regulations, Part 10, and which are published in pamphlet form as Treasury Department Circular No. 230. The regulations prescribe the duties and restrictions relating to such practice and prescribe the disciplinary sanctions for violating the regulations.

The disciplinary sanctions to be imposed for violation of the regulations are:

Disbarred from practice before the IRS—An individual who is disbarred is not eligible to represent taxpayers before the IRS.

Suspended from practice before the IRS—An individual who is suspended is not eligible to represent taxpayers before the IRS during the term of the suspension.

Censured in practice before the IRS—Censure is a public reprimand. Unlike disbarment or suspension, censure does not affect an individual's eligibility to represent taxpayers before the IRS, but OPR may subject the individual's future representations to conditions designed to promote high standards of conduct.

Monetary penalty—A monetary penalty may be imposed on an individual who engages in conduct subject to sanction or on an employer, firm, or entity

if the individual was acting on its behalf and if it knew, or reasonably should have known, of the individual's conduct.

Disqualification of appraiser—An appraiser who is disqualified is barred from presenting evidence or testimony in any administrative proceeding before the Department of the Treasury or the IRS.

Under the regulations, attorneys, certified public accountants, enrolled agents, enrolled actuaries, and enrolled retirement plan agents may not assist, or accept assistance from, individuals who are suspended or disbarred with respect to matters constituting practice (*i.e.*, representation) before the IRS, and they may not aid or abet suspended or disbarred individuals to practice before the IRS.

Disciplinary sanctions are described in these terms:

Disbarred by decision after hearing, Suspended by decision after hearing, Censured by decision after hearing, Monetary penalty imposed after hearing, and Disqualified after hearing—An administrative law judge (ALJ) conducted an evidentiary hearing upon OPR's complaint alleging violation of the regulations and issued a decision imposing one of these sanctions. After 30 days from the issuance of the decision, in the absence of an appeal, the ALJ's decision became the final agency decision.

Disbarred by default decision, Suspended by default decision, Censured by default decision, Monetary penalty imposed by default decision, and Disqualified by default decision—An ALJ, after

finding that no answer to OPR's complaint had been filed, granted OPR's motion for a default judgment and issued a decision imposing one of these sanctions.

Disbarment by decision on appeal, Suspended by decision on appeal, Censured by decision on appeal, Monetary penalty imposed by decision on appeal, and Disqualified by decision on appeal—The decision of the ALJ was appealed to the agency appeal authority, acting as the delegate of the Secretary of the Treasury, and the appeal authority issued a decision imposing one of these sanctions.

Disbarred by consent, Suspended by consent, Censured by consent, Monetary penalty imposed by consent, and Disqualified by consent—In lieu of a disciplinary proceeding being instituted or continued, an individual offered a consent to one of these sanctions and OPR accepted the offer. Typically, an offer of consent will provide for: suspension for an indefinite term; conditions that the individual must observe during the suspension; and the individual's opportunity, after a stated number of months, to file with OPR a petition for reinstatement affirming compliance with the terms of the consent and affirming current eligibility to practice (*i.e.*, an active professional license or active enrollment status). An enrolled agent or an enrolled retirement plan agent may also offer to resign in order to avoid a disciplinary proceeding.

Suspended by decision in expedited proceeding, Suspended by default de-

cision in expedited proceeding, Suspended by consent in expedited proceeding—OPR instituted an expedited proceeding for suspension (based on certain limited grounds, including loss of a professional license and criminal convictions).

OPR has authority to disclose the grounds for disciplinary sanctions in these situations: (1) an ALJ or the Secretary's delegate on appeal has issued a decision

on or after September 26, 2007, which was the effective date of amendments to the regulations that permit making such decisions publicly available; (2) the individual has settled a disciplinary case by signing OPR's "consent to sanction" form, which requires consenting individuals to admit to one or more violations of the regulations and to consent to the disclosure of the individual's own return information related to the admitted violations (for example,

failure to file Federal income tax returns); or (3) OPR has issued a decision in an expedited proceeding for suspension.

Announcements of disciplinary sanctions appear in the Internal Revenue Bulletin at the earliest practicable date. The sanctions announced below are alphabetized first by the names of states and second by the last names of individuals. Unless otherwise indicated, section numbers (*e.g.*, § 10.51) refer to the regulations.

| City & State | Name | Professional Designation | Disciplinary Sanction | Effective Date(s) |
|-------------------|----------------------|--------------------------|---|---------------------------------|
| Arizona | | | | |
| Glendale | Casper, Eric M. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 8, 2009 |
| Scottsdale | Morrison, John G. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 5, 2009 |
| California | | | | |
| Hacienda Heights | Phillips, Richard A. | Attorney | Suspended by decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 5, 2009 |
| Los Angeles | Rezak, Donald | Attorney | Suspended by decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 8, 2009 |
| Palm Springs | Selzer, Paul T. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (conviction under 26 U.S.C. § 7212, corrupt endeavor to obstruct due administration of the Internal Revenue Code) | Indefinite from January 8, 2009 |
| San Diego | Stockton, Rick A. | CPA | Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license) | Indefinite from January 5, 2009 |
| Mill Valley | Wiener, Lewis R. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 8, 2009 |

| City & State | Name | Professional Designation | Disciplinary Sanction | Effective Date(s) |
|-------------------------|--------------------|---------------------------------|---|-----------------------------------|
| Florida | | | | |
| Jupiter | Cullen, John F. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license in Massachusetts) | Indefinite from January 12, 2009 |
| Ft. Lauderdale | Legel, Lawrence | CPA | Suspended by decision in expedited proceeding under § 10.82 (conviction under 26 U.S.C. § 7203, aiding and abetting in failure to pay income tax) | Indefinite from January 13, 2009 |
| Pensacola | Roche, Ernest L. | CPA | Suspended by consent for violation of § 10.51 (failure to file several tax returns) | Indefinite from December 18, 2008 |
| Georgia | | | | |
| Roswell | Bishop, Winford K. | Attorney | Suspended by decision in expedited proceeding under § 10.82 (attorney disbarment in New York) | Indefinite from December 15, 2008 |
| Atlanta | Roberts, John A. | Attorney | Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 13, 2009 |
| Illinois | | | | |
| Urbana | Ucherek, David M. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 5, 2009 |
| Maine | | | | |
| Falmouth | Duncan, John D. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 12, 2009 |
| Maryland | | | | |
| St. Michaels | Farris, Peter D. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 12, 2009 |

| City & State | Name | Professional Designation | Disciplinary Sanction | Effective Date(s) |
|-------------------------|---|---------------------------------|--|----------------------------------|
| Massachusetts | | | | |
| | Cullen, John F., See Florida | | | |
| Randolph | Udo, John | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 12, 2009 |
| Minnesota | | | | |
| | Varriano, Richard D., See North Dakota | | | |
| New Jersey | | | | |
| Manalapan | Meiterman, Bernard | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (conviction under 18 U.S.C. § 1952, use of US mail in aid of racketeering enterprises) | Indefinite from January 12, 2009 |
| New York | | | | |
| | Bishop, Winford A., See Georgia | | | |
| Yonkers | Spiegler, Barry I. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 12, 2009 |
| Saratoga Springs | Tessitore, William F. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 12, 2009 |
| North Carolina | | | | |
| Greensboro | Beavers, Harold W. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 12, 2009 |
| Asheville | Erickson, Paul L. | Attorney | Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 23, 2009 |
| Boone | Marsh, Randall S. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license) | Indefinite from January 12, 2009 |

| City & State | Name | Professional Designation | Disciplinary Sanction | Effective Date(s) |
|-------------------------|----------------------|---------------------------------|---|----------------------------------|
| North Dakota | | | | |
| Fargo | Varriano, Richard D. | Attorney | Suspended by decision in expedited proceeding under § 10.82 (attorney suspension in Minnesota) | Indefinite from January 12, 2009 |
| Tennessee | | | | |
| Hixson | Miller, Herbert | CPA | Suspended by consent for violation of § 10.51 (late filed three of his Forms 1040 and seven of his Forms 941) | Indefinite from January 1, 2009 |
| Texas | | | | |
| Tyler | Sims, Steven R. | Attorney | Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment) | Indefinite from January 23, 2009 |

Definition of Terms

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

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

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

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

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

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

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

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

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

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

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

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

Abbreviations

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

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

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

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

Numerical Finding List¹

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¹ A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2008–27 through 2008–52 is in Internal Revenue Bulletin 2008–52, dated December 29, 2008.

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Key to Abbreviations:

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

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