Internal Revenue
bulletin

Bulletin No. 2011-48
November 28, 2011

# HIGHLIGHTS OF THIS ISSUE

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

## INCOME TAX

### Rev. Rul. 2011–26, page 803.

**Geographical areas included in North American area.** This ruling contains an updated list of all geographical areas included in the North American area for purposes of section 274 of the Code. Rev. Rul. 2007–28 superseded.

### Rev. Rul. 2011–27, page 805.

**Section 1274A – inflation adjusted numbers for 2012.** This ruling provides the dollar amounts, increased by the 2012 inflation adjustment, for section 1274A of the Code. Rev. Rul. 2010–30 supplemented and superseded.

### REG–146537–06, page 813.

Proposed regulations under section 892 of the Code relate to the taxation of certain investment income earned by foreign governments in the United States.

### REG–114749–09, page 819.

Proposed regulations under section 964 of the Code clarify and add examples illustrating the application of final regulations relating to the procedures for U.S. shareholders of foreign corporations to make tax accounting elections on behalf of the foreign corporations for purposes of computing the foreign corporation's earnings and profits for U.S. tax purposes. The regulations also update the rules relating to required book-to-tax adjustments in respect of depreciation and amortization and contain a rule related to mandated changes in methods of accounting in connection with an audit or audits of a foreign corporation's controlling domestic shareholders.

### Announcement 2011–73, page 822.

This announcement notifies taxpayers that the Service has withdrawn Weld Rite, Inc.'s right to certify its hydronic outdoor wood-burning furnaces. Therefore, this announcement also notifies taxpayers that they may no longer rely on Weld Rite, Inc.'s certification statement to claim a section 25C credit for the furnaces.

### Announcement 2011–75, page 823.

This document contains a withdrawal of proposed regulations (REG–158677–05, 2007–1 C.B. 975) clarifying that if a bank is an S corporation within the meaning of section 1361(a)(1) of the Code, its status as an S corporation does not affect the applicability of the special rules for banks under the Internal Revenue Code.

## EMPLOYEE PLANS

### Notice 2011–93, page 810.

**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 November 2011; the 24-month average segment rates; the funding transitional segment rates applicable for November 2011; and the minimum present value transitional rates for October 2011. In addition, the Service requests comments on whether these monthly interest rate notices should continue to provide the Composite Corporate Bond Rate and the Corporate Bond Weighted Average in 2012.

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Department of the Treasury
Internal Revenue Service

## EMPLOYMENT TAX

**T.D. 9553, page 806.**
Final regulations under section 7701 of the Code clarify that a single-owner eligible entity that is generally disregarded as an entity separate from its owner for any purpose, but regarded as a separate entity for certain excise tax purposes, is treated as a corporation for those excise tax purposes. The regulations also make conforming changes to the tax liability rule for disregarded entities and the treatment of entity rule for disregarded entities with respect to employment taxes. The regulations affect disregarded entities in general and, in particular, disregarded entities that pay or pay over certain federal excise taxes or that are required to be registered by the IRS.

## EXCISE TAX

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**Notice 2011–92, page 809.**
This notice provides guidance on the branded prescription drug fee for the 2012 fee year related to (1) the submission of Form 8947, *"Report of Branded Prescription Drug Information"*, (2) the time and manner for notifying covered entities of the preliminary fee calculation, (3) the time and manner for submitting error reports for the dispute resolution process, and (4) the time for notifying covered entities of their final fee calculation. Rev. Proc. 2011–24 obsoleted.

## TAX CONVENTIONS

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**Geographical areas included in North American area.** This ruling contains an updated list of all geographical areas included in the North American area for purposes of section 274 of the Code. Rev. Rul. 2007–28 superseded.

## ADMINISTRATIVE

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# The IRS Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.

# Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly 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.



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

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

## Section 274.—Disallowance of Certain Entertainment, Etc., Expenses

*26 CFR 1.274–1: Disallowance of certain entertainment, etc., expenses.*

**Geographical areas included in North American area.** This ruling contains an updated list of all geographical areas included in the North American area for purposes of section 274 of the Code. Rev. Rul. 2007–28 superseded.

## Rev. Rul. 2011–26

ISSUE

Section 274(h) of the Internal Revenue Code (the "Code") limits deductions for expenses incurred in connection with a convention, seminar, or similar meeting (collectively, a "convention") held outside the "North American area." This revenue ruling contains an updated list of all geographical areas currently included in the North American area for purposes of section 274(h).

LAW AND ANALYSIS

Section 274(h) disallows deductions under section 162 for expenses allocable to attendance of an individual at a convention held outside the North American area unless the taxpayer demonstrates that the location of the convention satisfies specified standards of reasonableness.

A geographical area may be included in the North American area for purposes of section 274(h) under one of the four provisions described below.

*Section 274(h)(3)(A)*

Section 274(h)(3)(A) defines the term "North American area" as the United States, its possessions, the Trust Territory of the Pacific Islands, Canada, and Mexico. Under section 7701(a)(9), the United States consists of the fifty states and the District of Columbia. The Internal Revenue Service treats the following as the possessions of the United States for this purpose: American Samoa, Baker Island, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, Guam, Howland Island, Jarvis Island, Johnston Island, Kingman Reef, the Midway Islands, Palmyra Atoll, the United States Virgin Islands, Wake Island, and other United States islands, cays, and reefs not part of the fifty states or the District of Columbia. The jurisdictions that formerly constituted the Trust Territory of the Pacific Islands — the Republic of the Marshall Islands, the Federated States of Micronesia, and the Republic of Palau — are now covered by the compacts with the United States described below.

*The Compact of Free Association Act of 1985*

The Compact of Free Association Act of 1985, Pub. L. No. 99–239, 99 Stat. 1770 (1986), went into effect on October 21, 1986, with respect to the Republic of the Marshall Islands, and on November 3, 1986, with respect to the Federated States of Micronesia. Section 405 of Title IV of the Compact provides that, for purposes of section 274(h)(3)(A) of the Code, the Republic of the Marshall Islands and the Federated States of Micronesia are included in the North American area.

*The Compact of Free Association Between the United States and the Republic of Palau*

The Compact of Free Association between the United States and the Republic of Palau, Pub. L. No. 99–658, 100 Stat. 3672 (1986), went into effect on October 1, 1994. Section 225(d) of Title II of the Compact with Palau provides that, for purposes of section 274(h)(3)(A) of the Code, Palau is included in the North American area.

*Section 274(h)(6)*

Section 274(h)(6)(A) provides that the term "North American area" includes any "beneficiary country" if, as of the time a convention begins: (i) there is in effect an agreement described in section 274(h)(6)(C) providing for the exchange of information between the United States and the beneficiary country; and (ii) there is not in effect a finding by the Secretary of the Treasury that the tax laws of the beneficiary country discriminate against conventions held in the United States.

Section 274(h)(6)(B) defines the term "beneficiary country" as a beneficiary country as defined in section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act, Pub. L. No. 98–67, 97 Stat. 384 (1983), and Bermuda. Under section 274(h)(6)(C)(i), to constitute an agreement that provides for the exchange of information between the United States and a beneficiary country, an agreement generally must provide for the exchange of such information (not limited to information concerning nationals or residents of the United States or the beneficiary country) as may be necessary or appropriate to carry out and enforce the tax laws of the United States and the beneficiary country (whether criminal or civil proceedings), including information which may otherwise be subject to nondisclosure provisions of the local law of the beneficiary country such as provisions respecting bank secrecy and bearer shares.

Where an exchange of information agreement between a beneficiary country and the United States does not qualify as an agreement described in section 274(h)(6)(C)(i) or is not in effect within the meaning of section 274(h)(6)(A)(i), the beneficiary country is not included as part of the North American area under section 274(h)(6) for purposes of determining whether deductions are allowed for expenses incurred in connection with a convention.

Rev. Rul. 2007–28, 2007–1 C.B. 1039, identified each of the following jurisdictions as a beneficiary country for which there was in effect an agreement with the United States as described in section 274(h)(6)(C)(i) and for which there was not in effect a finding by the Secretary of the Treasury that the tax laws of the beneficiary country discriminate against conventions held in the United States: Antigua and Barbuda, Aruba, Bahamas,

Barbados, Bermuda, Costa Rica, Dominica, Dominican Republic, Grenada, Guyana, Honduras, Jamaica, Netherlands Antilles, and Trinidad and Tobago.

Since publication of Rev. Rul. 2007–28, the "Agreement Between the Government of the United States of America and the Republic of Panama for Tax Cooperation and the Exchange of Information with Respect to Taxes" entered into force on April 18, 2011. *See* Treas. News Release at *http://www.treasury.gov/press-center/press-releases/Pages/tg1144.aspx* (April 18, 2011). This new agreement qualifies as an agreement described in section 274(h)(6)(C)(i). Panama is a beneficiary country, and no finding is in effect by the Secretary of the Treasury that the tax laws of Panama discriminate against conventions held in the United States. Therefore, Panama is included within the North American area under section 274(h)(6) as of April 18, 2011.

Three other beneficiary countries — the Cayman Islands, the British Virgin Islands, and Saint Lucia — have entered into tax information exchange agreements with the United States that are not of the type described in section 274(h)(6)(C)(i) because of certain limitations in the scope or implementation of those agreements. Accordingly, these three beneficiary countries are not included as part of the North American area under section 274(h)(6). In the case of Saint Lucia, certain transition relief has been provided, as reflected in the Holding below.

HOLDING

For purposes of determining whether deductions are allowed for expenses incurred in connection with a convention, the following areas are included in the North American area as of the effective date of section 274(h) except as otherwise indicated:

1. The fifty states of the United States and the District of Columbia;
2. The possessions of the United States, which for this purpose are American Samoa, Baker Island, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, Guam, Howland Island, Jarvis Island, Johnston Island, Kingman Reef, the Midway Islands, Palmyra Atoll, the United States Virgin Islands, Wake Island, and other United States islands, cays, and reefs not part of the fifty states or the District of Columbia;
3. Canada;
4. Mexico;
5. The Republic of the Marshall Islands;
6. The Federated States of Micronesia;
7. The Republic of Palau;

| | | *For expenses incurred in attending a convention that began after:* |
|---|---|---|
| 8. | Antigua and Barbuda | February 9, 2003 |
| 9. | Aruba | September 12, 2004 |
| 10. | Bahamas | December 31, 2005 |
| 11. | Barbados | November 2, 1984 |
| 12. | Bermuda | December 1, 1988 |
| 13. | Costa Rica | February 11, 1991 |
| 14. | Dominica | May 8, 1988 |
| 15. | Dominican Republic | October 11, 1989 |
| 16. | Grenada | July 12, 1987 |
| 17. | Guyana | August 26, 1992 |
| 18. | Honduras | October 9, 1991 |
| 19. | Jamaica | December 17, 1986 |
| 20. | Netherlands Antilles | March 21, 2007 |
| 21. | Panama | April 18, 2011 |
| 22. | Trinidad and Tobago | February 8, 1990 |

The Internal Revenue Service will continue to treat Saint Lucia as not included in the North American area under section 274(h)(6) with respect to conventions that begin after April 4, 2007, except with respect to expenses for which the taxpayer demonstrates a nonrefundable contractual obligation existing as of April 4, 2007.

This revenue ruling will be updated as future developments result in the inclusion of other areas in, or the exclusion of areas from, the North American area.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 2007–28 is superseded.

DRAFTING INFORMATION

The principal author of this revenue ruling is Terra-Lynn Zentara of the Office of Associate Chief Counsel (International), Branch 7. For further information regarding this revenue ruling, contact the principal author at (202) 435–5262 (not a toll-free call).

## Section 483.—Interest on Certain Deferred Payments

This ruling provides the dollar amounts, increased by the 2012 inflation adjustment, for section 1274A of the Code. Rev. Rul. 2010-30 supplemented and superseded. See Rev. Rul. 2011-27, page 805.

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

This ruling provides the dollar amounts, increased by the 2012 inflation adjustment, for section 1274A of the Code. Rev. Rul. 2010-30 supplemented and superseded. See Rev. Rul. 2011-27, page 805.

## Section 1274A.—Special Rules for Certain Transactions Where Stated Principal Amount Does Not Exceed $2,800,000

*26 CFR 1.1274A–1: Special rules for certain transactions where stated principal amount does not exceed $2,800,000.*
*(Also §§ 483, 1274.)*

**Section 1274A – inflation adjusted numbers for 2012.** This ruling provides the dollar amounts, increased by the 2012 inflation adjustment, for section 1274A of the Code. Rev. Rul. 2010–30 supplemented and superseded.

## Rev. Rul. 2011–27

This revenue ruling provides the dollar amounts, increased by the 2012 inflation adjustment, for § 1274A of the Internal Revenue Code.

BACKGROUND

In general, §§ 483 and 1274 determine the principal amount of a debt instrument given in consideration for the sale or exchange of nonpublicly traded property. In addition, any interest on a debt instrument subject to § 1274 is taken into account under the original issue discount provisions of the Code. Section 1274A, however, modifies the rules under §§ 483 and 1274 for certain types of debt instruments.

In the case of a "qualified debt instrument," the discount rate used for purposes of §§ 483 and 1274 may not exceed nine percent, compounded semiannually. Section 1274A(b) defines a qualified debt instrument as any debt instrument given in consideration for the sale or exchange of property (other than new § 38 property within the meaning of § 48(b), as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990) if the stated principal amount of the instrument does not exceed the amount specified in § 1274A(b). For debt instruments arising out of sales or exchanges before January 1, 1990, this amount is $2,800,000.

In the case of a "cash method debt instrument," as defined in § 1274A(c), the borrower and lender may elect to use the cash receipts and disbursements method of accounting. In particular, for any cash method debt instrument, § 1274 does not apply, and interest on the instrument is accounted for by both the borrower and the lender under the cash method of accounting. A cash method debt instrument is a qualified debt instrument that meets the following additional requirements: (A) In the case of instruments arising out of sales or exchanges before January 1, 1990, the stated principal amount does not exceed $2,000,000; (B) the lender does not use an accrual method of accounting and is not a dealer with respect to the property sold or exchanged; (C) § 1274 would have applied to the debt instrument but for an election under § 1274A(c); and (D) an election under § 1274A(c) is jointly made with respect to the debt instrument by the borrower and the lender. Section 1.1274A–1(c)(1) of the Income Tax Regulations provides rules concerning the time for, and manner of, making this election.

Section 1274A(d)(2) provides that, for any debt instrument arising out of a sale or exchange during any calendar year after 1989, the dollar amounts stated in § 1274A(b) and § 1274A(c)(2)(A) are increased by the inflation adjustment for the calendar year. Any increase due to the inflation adjustment is rounded to the nearest multiple of $100 (or, if the increase is a multiple of $50 and not of $100, the increase is increased to the nearest multiple of $100). The inflation adjustment for any calendar year is the percentage (if any) by which the CPI for the preceding calendar year exceeds the CPI for calendar year 1988. Section 1274A(d)(2)(B) defines the CPI for any calendar year as the average of the Consumer Price Index as of the close of the 12-month period ending on September 30 of that calendar year.

INFLATION-ADJUSTED AMOUNTS UNDER § 1274A

For debt instruments arising out of sales or exchanges after December 31, 1989, the inflation-adjusted amounts under § 1274A are shown in Table 1.

Rev. Rul. 2011–27 Table 1

Inflation-Adjusted Amounts Under Section 1274A

| Calendar Year of Sale or Exchange | 1274A(b) Amount (qualified debt instrument) | 1274A(c)(2)(A) Amount (cash method debt instrument) |
|---|---|---|
| 1990 | $2,933,200 | $2,095,100 |
| 1991 | $3,079,600 | $2,199,700 |
| 1992 | $3,234,900 | $2,310,600 |
| 1993 | $3,332,400 | $2,380,300 |
| 1994 | $3,433,500 | $2,452,500 |
| 1995 | $3,523,600 | $2,516,900 |
| 1996 | $3,622,500 | $2,587,500 |
| 1997 | $3,723,800 | $2,659,900 |
| 1998 | $3,823,100 | $2,730,800 |
| 1999 | $3,885,500 | $2,775,400 |
| 2000 | $3,960,100 | $2,828,700 |
| 2001 | $4,085,900 | $2,918,500 |
| 2002 | $4,217,500 | $3,012,500 |
| 2003 | $4,280,800 | $3,057,700 |
| 2004 | $4,381,300 | $3,129,500 |
| 2005 | $4,483,000 | $3,202,100 |
| 2006 | $4,630,300 | $3,307,400 |
| 2007 | $4,800,800 | $3,429,100 |
| 2008 | $4,913,400 | $3,509,600 |
| 2009 | $5,131,700 | $3,665,500 |
| 2010 | $5,115,100 | $3,653,600 |
| 2011 | $5,201,300 | $3,715,200 |
| 2012 | $5,339,300 | $3,813,800 |

*Note*: These inflation adjustments were computed using the All-Urban, Consumer Price Index, 1982–1984 base, published by the Bureau of Labor Statistics.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 2010–30, 2010–50 I.R.B. 820, is supplemented and superseded.

DRAFTING INFORMATION

The author of this revenue ruling is Andrea M. Hoffenson of the Office of the Associate Chief Counsel (Financial Institutions and Products). For further information regarding this revenue ruling, please contact Ms. Hoffenson at (202) 622–3920 (not a toll-free call).

## Section 7701.—Definitions

*26 CFR 301.7701–2: Business entities; definitions.*

## T.D. 9553

## DEPARTMENT OF THE TREASURY
## Internal Revenue Service
## 26 CFR Part 301

## Disregarded Entities; Excise Taxes and Employment Taxes

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations relating to disregarded entities and excise taxes. These regulations also make conforming changes to the tax liability rule for disregarded entities and the treatment of entity rule for disregarded entities with respect to employment taxes. These regulations affect disregarded entities in general and, in particular, disregarded entities that pay or pay over certain federal excise taxes or that are required to be registered by the IRS.

DATES: *Effective Date:* These regulations are effective on October 26, 2011.

*Applicability Date:* For dates of applicability, see §§301.7701–2(e)(2), 301.7701–2(e)(5), and 301.7701–2(e)(6).

FOR FURTHER INFORMATION CONTACT: Michael H. Beker, (202) 622–3070 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

**Background**

This document contains amendments to the Procedure and Administration Regulations (26 CFR part 301) under section 7701 of the Internal Revenue Code (Code).

Temporary regulations (T.D. 9462, 2009–42 I.R.B. 504 [74 FR 46903]) and a cross-reference notice of proposed

rulemaking (REG–116614–08, 2009–42 I.R.B. 536 [74 FR 46957]) were published in the **Federal Register** on September 14, 2009 (the 2009 proposed regulations). On October 14, 2009, corrections to the temporary regulations (74 FR 52677) and to the cross-reference notice of proposed rulemaking (74 FR 52708) were published in the **Federal Register.**

The 2009 proposed regulations clarify that a single-owner eligible entity that is disregarded as an entity separate from its owner for any purpose under §301.7701–2, but regarded as an entity for certain excise tax purposes under §301.7701–2(c)(2)(v), is treated as a corporation with respect to those excise taxes. In addition, the 2009 proposed regulations make conforming changes to the tax liability rule for disregarded entities in §301.7701–2(c)(2)(iii) and the treatment of entity rule for disregarded entities with respect to employment taxes in §301.7701–2(c)(2)(iv)(B).

No public hearing was requested or held. One written comment was received. After consideration of the comment, the proposed regulations are adopted by this Treasury decision and the temporary regulations are removed.

**Summary of the Comment and Explanation of Provisions**

A. *Air transportation excise tax*

The commenter asked whether an amount paid to a single-member limited liability company (SMLLC) by its owner for air transportation provided to its owner will be deemed to be paid to a separate corporation and therefore subject to federal transportation excise taxes under section 4261.

On August 16, 2007, final regulations under §301.7701–2(c)(2)(v)(A) were published in the **Federal Register** (T.D. 9356, 2007–2 C.B. 675 [72 FR 45891]) (the 2007 final regulations). The 2007 final regulations provide that a single-owner eligible entity that is disregarded as an entity separate from its owner for Federal tax purposes is treated as a separate entity for certain excise tax purposes, including Federal tax liabilities imposed by Chapter 33 of the Code. Under this rule, amounts paid after December 31, 2007, to an SMLLC by its owner for air transportation are subject to the tax imposed by section 4261. The commenter suggested that the rule in the 2007 final regulations created a tax liability where one did not exist before.

Prior to the adoption of the §301.7701–2 regulations in 1997, amounts paid from one state law entity to another for air transportation were potentially subject to the section 4261 tax, regardless of the relationship between the entities. See for example, Rev. Ruls. 76–394, 1976–2 C.B. 355, and 70–325, 1970–1 C.B. 231, which involve transportation between related corporations and between corporations and their shareholders. Because there are separate and distinct entities in each case, these rulings hold that payments made from one entity to another for taxable air transportation are "amounts paid" for purposes of the section 4261 tax. While section 4282 provides a limited exception in the case of air transportation excise taxes for certain affiliated groups that do not offer air transportation services to non-affiliated members, no exception had been provided prior to 1997 for other situations.

The adoption of the §301.7701–2 regulations in 1997 departed from this long-standing precedent by making those previously taxable transactions no longer subject to excise tax when the owner of an eligible entity elected to be a disregarded entity. The 2007 regulations merely restored the long-standing and reasonable pre–1997 rule. Accordingly, the final regulations retain the rule that excise taxes imposed on amounts paid for covered services (such as air transportation) apply to amounts paid between state law entities for such services (unless a statutory exception applies).

B. *Indoor tanning services excise tax*

After the 2009 proposed regulations were published, section 10907 of the Patient Protection and Affordable Care Act, Public Law 111–148 (124 Stat. 119 (2010)) added new Chapter 49 to the Code, which contains an excise tax on amounts paid for indoor tanning services under new section 5000B. The IRS and Treasury Department are aware of issues relating to the treatment of qualified subchapter S subsidiaries and single-owner eligible entities that are disregarded as entities separate from their owners with respect to tax liabilities imposed by Chapter 49 of the Code. The issues are similar to those addressed in §301.7701–2(c)(2)(v). Accordingly, the IRS and the Treasury Department plan to issue regulations addressing the treatment of those entities with respect to tax liabilities imposed by Chapter 49 of the Code.

C. *Firearms excise tax and harbor maintenance tax*

The rules in the final regulations do not apply to the firearms excise tax administered by the Alcohol and Tobacco Tax and Trade Bureau (TTB) and the harbor maintenance tax administered by U.S. Customs and Border Protection (Customs). Rules in 26 CFR part 301 generally do not apply for purposes of these taxes and taxpayers should not assume that a single owner entity will be disregarded under applicable TTB or Customs rules.

*Availability of IRS documents*

The IRS revenue rulings cited in this preamble are published in the Internal Revenue Cumulative Bulletin and are available from the Superintendent of Documents, P.O. Box 371954, Pittsburgh PA, 15250–7954.

**Special Analyses**

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

**Drafting Information**

The principal author of these regulations is Michael H. Beker, Office of the Associate Chief Counsel (Passthroughs

and Special Industries). However, other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

**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 301.7701–2 is amended by:

1. Revising paragraphs (c)(2)(iii), (c)(2)(iv)(B), (c)(2)(v)(B), (c)(2)(v)(C) *Example* (iv), (e)(2), and (e)(6).

2. Adding two sentences at the end of paragraph (e)(5).

The additions and revisions read as follows:

*§301.7701–2 Business entities; definitions*.

* * * * *

(c) * * *

(2) * * *

(iii) *Tax liabilities of certain disregarded entities*—(A) *In general*. An entity that is disregarded as separate from its owner for any purpose under this section is treated as an entity separate from its owner for purposes of—

(*1*) Federal tax liabilities of the entity with respect to any taxable period for which the entity was not disregarded;

(*2*) Federal tax liabilities of any other entity for which the entity is liable; and

(*3*) Refunds or credits of Federal tax.

(B) *Examples*. The following examples illustrate the application of paragraph (c)(2)(iii)(A) of this section:

*Example 1*. In 2006, X, a domestic corporation that reports its taxes on a calendar year basis, merges into Z, a domestic LLC wholly owned by Y that is disregarded as an entity separate from Y, in a state law merger. X was not a member of a consolidated group at any time during its taxable year ending in December 2005. Under the applicable state law, Z is the successor to X and is liable for all of X's debts. In 2009, the Internal Revenue Service (IRS) seeks to extend the period of limitations on assessment for X's 2005 taxable year. Because Z is the successor to X and is liable for X's 2005 taxes that remain unpaid, Z is the proper party to sign the consent to extend the period of limitations.

*Example 2*. The facts are the same as in *Example 1*, except that in 2007, the IRS determines that X miscalculated and underreported its income tax liability for 2005. Because Z is the successor to X and is liable for X's 2005 taxes that remain unpaid, the deficiency may be assessed against Z and, in the event that Z fails to pay the liability after notice and demand, a general tax lien will arise against all of Z's property and rights to property.

(iv) * * *

(B) *Treatment of entity*. An entity that is disregarded as an entity separate from its owner for any purpose under this section is treated as a corporation with respect to taxes imposed under Subtitle C—Employment Taxes and Collection of Income Tax (Chapters 21, 22, 23, 23A, 24, and 25 of the Internal Revenue Code).

* * * * *

(v) * * *

(B) *Treatment of entity*. An entity that is disregarded as an entity separate from its owner for any purpose under this section is treated as a corporation with respect to items described in paragraph (c)(2)(v)(A) of this section.

(C) * * *

*Example*. * * *

(iv) Assume the same facts as in paragraph (c)(2)(v)(C) *Example* (i) and (ii) of this section. If LLCB does not pay the tax on its sale of coal under chapter 32 of the Internal Revenue Code, any notice of lien the Internal Revenue Service files will be filed as if LLCB were a corporation.

* * * * *

(e) * * *

(2) Paragraph (c)(2)(iii) of this section applies on and after September 14, 2009. For rules that apply before September 14, 2009, see 26 CFR part 301, revised as of April 1, 2009.

* * * * *

(5) * * * However, paragraph (c)(2)(iv)(B) of this section applies with respect to wages paid on or after September 14, 2009. For rules that apply before September 14, 2009, see 26 CFR part 301 revised as of April 1, 2009.

(6)(i) Except as provided in this paragraph (e)(6), paragraph (c)(2)(v) of this section applies to liabilities imposed and actions first required or permitted in periods beginning on or after January 1, 2008.

(ii) Paragraphs (c)(2)(v)(B) and (c)(2)(v)(C) *Example* (iv) of this section apply on and after September 14, 2009.

* * * * *

**§301.7701–2T [Removed]**

Par. 5. Section 301.7701–2T is removed.

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

Approved October 18, 2011.

Emily S. McMahon,
*Acting Assistant Secretary of the Treasury (Tax Policy).*

(Filed by the Office of the Federal Register on October 25, 2011, 8:45 a.m., and published in the issue of the Federal Register for October 26, 2011, 76 F.R. 66181)

# Part III. Administrative, Procedural, and Miscellaneous

## Branded Prescription Drug Fee; Guidance for the 2012 Fee Year

## Notice 2011–92

*Purpose*

This notice provides guidance on the branded prescription drug fee for the 2012 fee year related to (1) the submission of Form 8947, "*Report of Branded Prescription Drug Information,*" (2) the time and manner for notifying covered entities of their preliminary fee calculation, (3) the time and manner for submitting error reports for the dispute resolution process, and (4) the time for notifying covered entities of their final fee calculation.

*Background*

An annual fee on covered entities engaged in the business of manufacturing or importing branded prescription drugs is imposed by section 9008 of the Patient Protection and Affordable Care Act, Public Law 111–148 (124 Stat. 119 (2010)), as amended by section 1404 of the Health Care and Education Reconciliation Act of 2010, Public Law 111–152 (124 Stat. 1029 (2010)).

The Branded Prescription Drug Fee Regulations in 26 C.F.R. Part 51, which were published on August 18, 2011 (76 FR 51245), provide the method by which each covered entity's annual fee is calculated. These regulations also define terms for the administration of the fee. As relevant for this notice, § 51.2T(g) defines fee year as the calendar year in which the fee for a particular sales year must be paid and § 51.2T(m) defines *sales year* as the second calendar year preceding the fee year.

Section 51.3T provides that annually, each covered entity may submit a completed Form 8947, *"Report of Branded Prescription Drug Information,"* in accordance with the instructions for the form. Generally, the form solicits information from covered entities on National Drug Codes, orphan drugs, designated entities, rebates, and other information specified by the form or its instructions. The form is to be filed by the date prescribed in guidance published in the Internal Revenue Bulletin.

Section 51.6T provides that for each sales year the IRS will make a preliminary fee calculation for each covered entity and will notify each covered entity of this calculation by the date prescribed in guidance published in the Internal Revenue Bulletin. This notification will also include additional prescribed information. As used in this notice, "notice of preliminary fee calculation" includes the additional prescribed information.

Section 51.7T provides that upon receipt of its preliminary fee calculation, each covered entity will have an opportunity to dispute this calculation by submitting to the IRS an error report with prescribed information. Sections 51.7T(b) and (c) set out the information that a covered entity must submit to support each asserted error. Section 51.7T(d) provides that each covered entity must submit its error report(s) in the form and manner that is prescribed in guidance published in the Internal Revenue Bulletin. This guidance will also prescribe the date by which each covered entity must submit its report(s).

Section 51.8T provides that the IRS will send each covered entity its final fee calculation no later than August 31st of each fee year and also provides that covered entities must pay their fee by September 30th of the fee year.

*Submission of Form 8947*

For the 2012 fee year, a covered entity that chooses to submit Form 8947 must file the form by December 15, 2011.

*Time and manner for notifying covered entities of their preliminary fee calculation*

For the 2012 fee year, the IRS will mail each covered entity a paper notice of its preliminary fee calculation by April 2, 2012. This mailing will include a National Drug Code (NDC) attachment (NDC attachment) that lists the covered entity's NDCs and the sales data reported to the IRS by each government program pursuant to § 51.4T.

A covered entity may request that the IRS send a CD-ROM with the NDC attachment in Microsoft Excel format. The covered entity must make this request by March 1, 2012. This request must be made either by telephone to Lou Milano at (908) 301–2118 or Mi Lim at (312) 566–3775 (not toll-free calls) or by email to *mits.bpd.fee@irs.gov*. If a covered entity makes this request timely, the IRS will mail the covered entity its notice of preliminary fee calculation on paper and the NDC attachment on paper and CD-ROM by April 2, 2012.

*Time and manner for submitting error reports for the dispute resolution process*

For the 2012 fee year, a covered entity that chooses to submit an error report regarding its preliminary fee calculation must mail the error report by May 16, 2012.

When the IRS mails each covered entity a notice of its preliminary fee calculation by April 2, 2012, the IRS will also send each covered entity a template on a CD-ROM that the covered entity must use to prepare its error report. All completed templates and the supporting documentation must be submitted on a CD-ROM and sent by mail to:

Department of the Treasury
Internal Revenue Service
1973 N. Rulon White Boulevard,
Mail Stop 4916
Ogden, UT 84404

*Notification of Final Fee Calculation*

In accordance with § 51.8T(a), the IRS will notify each covered entity of its final fee calculation for 2012 by August 31, 2012. In accordance with §51.8T(c), each covered entity must pay this fee by September 30, 2012.

*Effect on Other Documents*

Rev. Proc 2011–24 is obsoleted.

*Drafting Information*

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

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

## Notice 2011-93

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), and the 24-month average segment rates under § 430(h)(2). In addition, this notice provides guidance as to the interest rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning before 2008, the 30-year Treasury weighted average rate under § 431(c)(6)(E)(ii)(I), and the minimum present value segment rates under § 417(e)(3)(D) as in effect for plan years beginning after 2007.

CORPORATE BOND WEIGHTED AVERAGE INTEREST RATE

Sections 412(b)(5)(B)(ii) and 412(l)(7)(C)(i), as amended by the Pension Funding Equity Act of 2004 and by the Pension Protection Act of 2006 (PPA), provide that the interest rates used to 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 October 2011 is 4.79 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% | to | 100% |
| November | 2011 | 5.82 | 5.23 | | 5.82 |

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. Section 430(h)(2)G) set forth a transitional rule applicable to plan years beginning in 2008 and 2009 under which the segment rates were blended with the corporate bond weighted average described above, including an election under § 430(h)(2)(G)(iv) for an employer to use the segment rates without the transitional rule.

Notice 2007-81, 2007-2 C.B. 899, provides guidelines for determining the monthly corporate bond yield curve, and the 24-month average corporate bond segment rates used to compute the target normal cost and the funding target. Pursuant to Notice 2007-81, the monthly corporate bond yield curve derived from October 2011 data is in Table I at the end of this notice. The spot first, second, and third segment rates for the month of October 2011 are, respectively, 2.09, 4.56, and 5.50. The three 24-month average corporate bond segment rates applicable for November 2011 are as follows:

| First Segment | Second Segment | Third Segment |
|---|---|---|
| 2.01 | 5.16 | 6.28 |

The transitional rule of § 430(h)(2)(G) does not apply to plan years beginning after December 31, 2009. Therefore, for a plan year beginning after 2009 with a lookback month to November 2011, the funding segment rates are the three 24-month average corporate bond segment rates applicable for November 2011, listed above without blending for any transitional period.

30-YEAR TREASURY SECURITIES INTEREST RATES

Section 417(e)(3)(A)(ii)(II) (prior to amendment by PPA) defines the appli-

cable 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 October 2011 is 3.13 percent. The Service has determined this rate as the average of the daily determinations of yield on the 30-year Treasury bond maturing in August 2041.

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% | to | 105% |
| November | 2011 | 4.16 | 3.74 | | 4.37 |

MINIMUM PRESENT VALUE SEGMENT RATES

Generally for plan years beginning after December 31, 2007, the applicable interest rates under § 417(e)(3)(D) are segment rates computed without regard to a 24-month average. For plan years beginning in 2008 through 2011, the applicable interest rates are the monthly spot segment rates blended with the applicable rate under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning in 2007. Notice 2007-81 provides guidelines for determining the minimum present value segment rates. Pursuant to that notice, the minimum present value transitional segment rates determined for October 2011, taking into account the October 2011 30-year Treasury rate of 3.13 stated above, are as follows:

| For Plan Years Beginning in | First Segment | Second Segment | Third Segment |
|---|---|---|---|
| 2010 | 2.51 | 3.99 | 4.55 |
| 2011 | 2.30 | 4.27 | 5.03 |
| 2012 | 2.09 | 4.56 | 5.50 |

REQUEST FOR COMMENTS

The IRS requests comments on whether these monthly interest rate notices should continue to provide the Composite Corporate Bond Rate and the Corporate Bond Weighted Average in 2012. Comments should be submitted by December 15, 2011, to CC:PA:LPD:PR (Notice 2011-93), Room 5203, Internal Revenue Service, POB 7604 Ben Franklin Station, Washington, D.C. 20044. Comments may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Notice 2011-93), Courier's Desk, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington D.C. Alternatively, comments may be submitted via the Internet at *Notice.comments@irscounsel.treas.gov*. Please include "Notice 2011-93" in the subject line of any electronic communication. All materials submitted will be available for public inspection and copying.

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 October 2011
Derived from October 2011 Data

| *Maturity* | *Yield* | *Maturity* | *Yield* | *Maturity* | *Yield* | *Maturity* | *Yield* | *Maturity* | *Yield* |
|---|---|---|---|---|---|---|---|---|---|
| 0.5 | 0.54 | 20.5 | 5.19 | 40.5 | 5.53 | 60.5 | 5.65 | 80.5 | 5.71 |
| 1.0 | 1.01 | 21.0 | 5.21 | 41.0 | 5.54 | 61.0 | 5.65 | 81.0 | 5.71 |
| 1.5 | 1.45 | 21.5 | 5.23 | 41.5 | 5.54 | 61.5 | 5.66 | 81.5 | 5.71 |
| 2.0 | 1.82 | 22.0 | 5.24 | 42.0 | 5.55 | 62.0 | 5.66 | 82.0 | 5.71 |
| 2.5 | 2.13 | 22.5 | 5.25 | 42.5 | 5.55 | 62.5 | 5.66 | 82.5 | 5.72 |
| 3.0 | 2.39 | 23.0 | 5.27 | 43.0 | 5.56 | 63.0 | 5.66 | 83.0 | 5.72 |
| 3.5 | 2.61 | 23.5 | 5.28 | 43.5 | 5.56 | 63.5 | 5.66 | 83.5 | 5.72 |
| 4.0 | 2.80 | 24.0 | 5.29 | 44.0 | 5.56 | 64.0 | 5.67 | 84.0 | 5.72 |
| 4.5 | 2.98 | 24.5 | 5.30 | 44.5 | 5.57 | 64.5 | 5.67 | 84.5 | 5.72 |
| 5.0 | 3.15 | 25.0 | 5.32 | 45.0 | 5.57 | 65.0 | 5.67 | 85.0 | 5.72 |
| 5.5 | 3.30 | 25.5 | 5.33 | 45.5 | 5.57 | 65.5 | 5.67 | 85.5 | 5.72 |
| 6.0 | 3.45 | 26.0 | 5.34 | 46.0 | 5.58 | 66.0 | 5.67 | 86.0 | 5.72 |
| 6.5 | 3.59 | 26.5 | 5.35 | 46.5 | 5.58 | 66.5 | 5.67 | 86.5 | 5.72 |
| 7.0 | 3.72 | 27.0 | 5.36 | 47.0 | 5.58 | 67.0 | 5.68 | 87.0 | 5.73 |
| 7.5 | 3.85 | 27.5 | 5.37 | 47.5 | 5.59 | 67.5 | 5.68 | 87.5 | 5.73 |
| 8.0 | 3.96 | 28.0 | 5.38 | 48.0 | 5.59 | 68.0 | 5.68 | 88.0 | 5.73 |
| 8.5 | 4.07 | 28.5 | 5.38 | 48.5 | 5.59 | 68.5 | 5.68 | 88.5 | 5.73 |
| 9.0 | 4.18 | 29.0 | 5.39 | 49.0 | 5.60 | 69.0 | 5.68 | 89.0 | 5.73 |
| 9.5 | 4.27 | 29.5 | 5.40 | 49.5 | 5.60 | 69.5 | 5.68 | 89.5 | 5.73 |
| 10.0 | 4.36 | 30.0 | 5.41 | 50.0 | 5.60 | 70.0 | 5.68 | 90.0 | 5.73 |
| 10.5 | 4.44 | 30.5 | 5.42 | 50.5 | 5.61 | 70.5 | 5.69 | 90.5 | 5.73 |
| 11.0 | 4.51 | 31.0 | 5.43 | 51.0 | 5.61 | 71.0 | 5.69 | 91.0 | 5.73 |
| 11.5 | 4.58 | 31.5 | 5.43 | 51.5 | 5.61 | 71.5 | 5.69 | 91.5 | 5.73 |
| 12.0 | 4.65 | 32.0 | 5.44 | 52.0 | 5.61 | 72.0 | 5.69 | 92.0 | 5.73 |
| 12.5 | 4.71 | 32.5 | 5.45 | 52.5 | 5.62 | 72.5 | 5.69 | 92.5 | 5.73 |
| 13.0 | 4.76 | 33.0 | 5.45 | 53.0 | 5.62 | 73.0 | 5.69 | 93.0 | 5.74 |
| 13.5 | 4.81 | 33.5 | 5.46 | 53.5 | 5.62 | 73.5 | 5.69 | 93.5 | 5.74 |
| 14.0 | 4.85 | 34.0 | 5.47 | 54.0 | 5.62 | 74.0 | 5.70 | 94.0 | 5.74 |
| 14.5 | 4.89 | 34.5 | 5.47 | 54.5 | 5.63 | 74.5 | 5.70 | 94.5 | 5.74 |
| 15.0 | 4.93 | 35.0 | 5.48 | 55.0 | 5.63 | 75.0 | 5.70 | 95.0 | 5.74 |
| 15.5 | 4.96 | 35.5 | 5.48 | 55.5 | 5.63 | 75.5 | 5.70 | 95.5 | 5.74 |
| 16.0 | 5.00 | 36.0 | 5.49 | 56.0 | 5.63 | 76.0 | 5.70 | 96.0 | 5.74 |
| 16.5 | 5.02 | 36.5 | 5.50 | 56.5 | 5.64 | 76.5 | 5.70 | 96.5 | 5.74 |
| 17.0 | 5.05 | 37.0 | 5.50 | 57.0 | 5.64 | 77.0 | 5.70 | 97.0 | 5.74 |
| 17.5 | 5.08 | 37.5 | 5.51 | 57.5 | 5.64 | 77.5 | 5.70 | 97.5 | 5.74 |
| 18.0 | 5.10 | 38.0 | 5.51 | 58.0 | 5.64 | 78.0 | 5.71 | 98.0 | 5.74 |
| 18.5 | 5.12 | 38.5 | 5.52 | 58.5 | 5.64 | 78.5 | 5.71 | 98.5 | 5.74 |
| 19.0 | 5.14 | 39.0 | 5.52 | 59.0 | 5.65 | 79.0 | 5.71 | 99.0 | 5.75 |
| 19.5 | 5.16 | 39.5 | 5.53 | 59.5 | 5.65 | 79.5 | 5.71 | 99.5 | 5.75 |
| 20.0 | 5.18 | 40.0 | 5.53 | 60.0 | 5.65 | 80.0 | 5.71 | 100.0 | 5.75 |

# Part IV. Items of General Interest

## Notice of Proposed Rulemaking

## Income of Foreign Governments and International Organizations

## REG–146537–06

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed Income Tax Regulations that provide guidance relating to the taxation of the income of foreign governments from investments in the United States under section 892 of the Internal Revenue Code of 1986 (Code). The regulations will affect foreign governments that derive income from sources within the United States.

DATES: Written or electronic comments and requests for a public hearing must be received by February 1, 2012.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–146537–06), Room 5205, Internal Revenue Service, PO 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–146537–06), 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–146537–06).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, David A. Juster, (202) 622–3850 (not a toll-free number); concerning submission of comments, contact Richard A. Hurst at *Richard.A.Hurst@irscounsel.treas.gov*.

SUPPLEMENTARY INFORMATION:

**Paperwork Reduction Act**

The collections of information contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review and approval under OMB approval number 1545–1053 in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collections of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collections of information should be received by January 3, 2012. Comments are specifically requested concerning:

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

The accuracy of the estimated burden associated with the proposed collections of information;

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

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

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

The collections of information in this proposed regulation are in §§1.892–5(a)(2)(ii)(B) and 1.892–5(a)(2)(iv). This information is required to determine if taxpayers qualify for exemption from tax under section 892. The collections of information are voluntary to obtain a benefit. The likely respondents are foreign governments.

Estimated total annual reporting burden: 975 hours.

Estimated average annual burden hours per respondent: 5 hours.

Estimated number of respondents: 195.

Estimated annual frequency of responses: 1.

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

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

**Background**

This document contains proposed amendments to 26 CFR part 1 and to 26 CFR part 602. On June 27, 1988, temporary regulations under section 892 (T.D. 8211, 53 FR 24060) (1988 temporary regulations) with a cross-reference notice of proposed rulemaking (53 FR 24100) were published in the **Federal Register** to provide guidance concerning the taxation of income of foreign governments and international organizations from investments in the United States. The proposed regulations contained herein supplement the cross-reference notice of proposed rulemaking to provide additional guidance for determining when a foreign government's investment income is exempt from U.S. taxation.

**Explanation of Provisions**

The Treasury Department and the IRS have recently received numerous written comments on the 1988 temporary regulations. The proposed regulations are issued in response to those comments.

*Treatment of Controlled Entities*

Section 892 exempts from U.S. income taxation certain qualified investment income derived by a foreign government. Section 1.892–2T defines the term foreign government to mean only the integral parts or controlled entities of a foreign sovereign. The exemption from U.S. income tax under section 892 does not apply to income (1) derived from the conduct of any commercial activity, (2) received by a controlled commercial entity or received

(directly or indirectly) from a controlled commercial entity, or (3) derived from the disposition of any interest in a controlled commercial entity. Section 892(a)(2)(B) defines a controlled commercial entity as an entity owned by the foreign government that meets certain ownership or control thresholds and that is engaged in commercial activities anywhere in the world. Accordingly, an integral part of a foreign sovereign that derives income from both qualified investments and from the conduct of commercial activity is eligible to claim the section 892 exemption with respect to the income from qualified investments, but not with respect to the income derived from the conduct of commercial activity. In contrast, if a controlled entity (as defined in §1.892–2T(a)(3)) engages in commercial activities anywhere in the world, it is treated as a controlled commercial entity, and none of its income (including income from otherwise qualified investments) qualifies for exemption from tax under section 892. In addition, none of the income derived from the controlled entity (*e.g.,* dividends), including the portion attributable to qualified investments of the controlled entity, will be eligible for the section 892 exemption. Several comments raised concerns that this so-called "all or nothing" rule represents an unnecessary administrative and operational burden for foreign governments and a trap for unwary foreign governments that inadvertently conduct a small level of commercial activity. These comments have requested that the Treasury Department and the IRS revise §1.892–5T(a) to provide for a *de minimis* exception under which an entity would not be treated as a controlled commercial entity as a result of certain inadvertent commercial activity.

In response to these comments, the proposed regulations at §1.892–5(a)(2) provide that an entity will not be considered to engage in commercial activities if it conducts only inadvertent commercial activity. Commercial activity will be treated as inadvertent commercial activity only if: (1) the failure to avoid conducting the commercial activity is reasonable; (2) the commercial activity is promptly cured; and (3) certain record maintenance requirements are met. However, none of the income derived from such inadvertent commercial activity will qualify for exemption from tax under section 892.

In determining whether an entity's failure to avoid conducting a particular commercial activity is reasonable, due regard will be given to the number of commercial activities conducted during the taxable year, as well as the amount of income earned from, and assets used in, the conduct of the commercial activity in relationship to the entity's total income and assets. However, a failure to avoid conducting commercial activity will not be considered reasonable unless adequate written policies and operational procedures are in place to monitor the entity's worldwide activities. The proposed regulations include a safe harbor at §1.892–5(a)(2)(ii)(C) under which, provided that there are adequate written policies and operational procedures in place to monitor the entity's worldwide activities, the controlled entity's failure to avoid the conduct of commercial activity during a taxable year will be considered reasonable if: (1) the value of the assets used in, or held for use in, the activity does not exceed five percent of the total value of the assets reflected on the entity's balance sheet for the taxable year as prepared for financial accounting purposes; and (2) the income earned by the entity from the commercial activity does not exceed five percent of the entity's gross income as reflected on its income statement for the taxable year as prepared for financial accounting purposes.

Comments also requested further guidance on the duration of a determination that an entity is a controlled commercial entity. In response to these comments, the proposed regulations at §1.892–5(a)(3) provide that the determination of whether an entity is a controlled commercial entity within the meaning of section 892(a)(2)(B) will be made on an annual basis. Accordingly, an entity will not be considered a controlled commercial entity for a taxable year solely because the entity engaged in commercial activities in a prior taxable year.

*Definition of Commercial Activity*

Section 1.892–4T of the 1988 temporary regulations provides rules for determining whether income is derived from the conduct of a commercial activity, and specifically identifies certain activities that are not commercial, including certain investments, trading activities, cultural events, non-profit activities, and governmental functions. Several comments have expressed uncertainty about the applicable U.S. standard for determining when an activity will be considered a commercial activity, a non-profit activity, or governmental function for purposes of section 892 and §1.892–4T.

Section 1.892–4(d) of the proposed regulations restates the general rule adopted in the 1988 temporary regulations that, subject to certain enumerated exceptions, all activities ordinarily conducted for the current or future production of income or gain are commercial activities. Section 1.892–4(d) of the proposed regulations further provides that only the nature of an activity, not the purpose or motivation for conducting the activity, is determinative of whether the activity is a commercial activity. This standard also applies for purposes of determining whether an activity is characterized as a non-profit activity or governmental function under §1.892–4T(c)(3) and (c)(4). In addition, §1.892–4(d) of the proposed regulations clarifies the rule in the 1988 temporary regulations by providing that an activity may be considered a commercial activity even if the activity does not constitute a trade or business for purposes of section 162 or does not constitute (or would not constitute if undertaken in the United States) the conduct of a trade or business in the United States for purposes of section 864(b).

Section 1.892–4T(c) lists certain activities that will not be considered commercial activities. One such activity is investments in financial instruments, as defined in §1.892–3T(a)(4), which, if held in the execution of governmental financial or monetary policy, are not commercial activities for purposes of section 892. Several comments have requested that the condition that financial instruments be "held in the execution of governmental financial or monetary policy" be eliminated to more closely conform the treatment of investments in financial instruments, including derivatives, with investments in physical stocks and securities, which under the 1988 temporary regulations generally are not commercial activities regardless of whether they are held in the execution of governmental financial or monetary policy. Section 1.892–4(e)(1)(i) of the

proposed regulations modifies the rules in §1.892–4T(c)(1)(i) by providing that investments in financial instruments will not be treated as commercial activities for purposes of section 892, irrespective of whether such financial instruments are held in the execution of governmental financial or monetary policy. In addition, §1.892–4(e)(1)(ii) of the proposed regulations expands the existing exception in §1.892–4T(c)(1)(ii) from commercial activity for trading of stocks, securities, and commodities to include financial instruments, without regard to whether such financial instruments are held in the execution of governmental financial or monetary policy. These revisions address only the definition of commercial activity for purposes of determining whether a government will be considered to derive income from the conduct of a commercial activity, or whether an entity will be considered to be engaged in commercial activities. They do not address whether income from activities that are not commercial activities will be exempt from tax under section 892. Pursuant to §1.892–3T(a), only income derived from investments in financial instruments held in the execution of governmental financial or monetary policy will qualify for exemption from tax under section 892.

Comments have requested clarification as to whether an entity that disposes of a United States real property interest (USRPI) as defined in section 897(c) will be deemed to be engaged in commercial activities solely by reason of this disposition. Section 897(a)(1) requires that a nonresident alien or foreign corporation take into account gain or loss from the disposition of a USRPI as if the taxpayer were engaged in a trade or business within the United States during the taxable year and as if such gain or loss were effectively connected with that trade or business. The Treasury Department and the IRS believe that an entity that only holds passive investments and is not otherwise engaged in commercial activities should not be deemed to be engaged in commercial activities solely by reason of the operation of section 897(a)(1). Accordingly, §1.892–4(e)(1)(iv) of the proposed regulations provides that a disposition, including a deemed disposition under section 897(h)(1), of a USRPI, by itself, does not constitute the conduct of a commercial activity. However, as provided in §1.892–3T(a), the income derived from the disposition of the USRPI described in section 897(c)(1)(A)(i) shall in no event qualify for the exemption from tax under section 892.

After the 1988 temporary regulations were published, section 892(a)(2)(A) was amended by the Technical and Miscellaneous Revenue Act of 1988 (TAMRA), Public Law No. 100–647, 102 Stat. 3342 to provide that income derived from the disposition of any interest in a controlled commercial entity does not qualify for the exemption under section 892. The proposed regulations revise §1.892–5(a) to reflect the amendment of section 892 by TAMRA.

*Treatment of Partnerships*

Section 1.892–5T(d)(3) provides a general rule that commercial activities of a partnership are attributable to its general and limited partners ("partnership attribution rule") and provides a limited exception to this rule for partners of publicly traded partnerships (PTPs). Several comments have requested that the Treasury Department and the IRS modify the partnership attribution rule to provide that the activities of a partnership will not be attributed to a foreign government partner if that government: (i) holds a minority interest, as a limited partner, in the partnership; and (ii) has no greater rights to participate in the management and conduct of the partnership's business than would a minority shareholder in a corporation conducting the same activities as the partnership. The comments assert that the partnership attribution rule causes many controlled entities of foreign sovereigns to forego making investments in foreign partnerships or other foreign entities that do not invest in the United States out of concern that such investments might cause those controlled entities to be treated as controlled commercial entities.

In response to these comments, §1.892–5(d)(5)(iii) of the proposed regulations modifies the existing exception to the partnership attribution rule for PTP interests by providing a more general exception for limited partnership interests. Under this revised exception, an entity that is not otherwise engaged in commercial activities will not be treated as engaged in commercial activities solely because it holds an interest as a limited partner in a limited partnership, including a publicly traded partnership that qualifies as a limited partnership.

For this purpose, an interest as a limited partner in a limited partnership is defined as an interest in an entity classified as a partnership for federal tax purposes if the holder of the interest does not have rights to participate in the management and conduct of the partnership's business at any time during the partnership's taxable year under the law of the jurisdiction in which the partnership is organized or under the governing agreement. This definition of an interest as a limited partner in a limited partnership applies solely for purposes of this exception, and no inference is intended that the same definition would apply for any other provision of the Code making or requiring a distinction between a general partner and a limited partner.

Although the commercial activity of a limited partnership will not cause a controlled entity of a foreign sovereign limited partner meeting the requirements of the exception for limited partnerships to be engaged in commercial activities, the controlled entity partner's distributive share of partnership income attributable to such commercial activity will be considered to be derived from the conduct of commercial activity, and therefore will not be exempt from taxation under section 892. Additionally, in the case of a partnership that is a controlled commercial entity, no part of the foreign government partner's distributive share of partnership income will qualify for exemption from tax under section 892.

Comments also assert that disparity in tax treatment exists under the temporary regulations regarding foreign government trading activity described in §1.892–4T(c)(1)(ii) because trading for a foreign government's own account does not constitute a commercial activity but no similar rule applies in the case of trading done by a partnership of which a foreign government is a partner. The comments note that this disparity is not generally present in determining whether an activity is a trade or business within the United States under section 864(b). See §1.864–2(c)(2)(i) and (d)(2)(i). In response to these comments, §1.892–5(d)(5)(ii) of the proposed regu-

lations provides that an entity that is not otherwise engaged in commercial activities will not be considered to be engaged in commercial activities solely because it is a member of a partnership that effects transactions in stocks, bonds, other securities, commodities, or financial instruments for the partnership's own account. However, this exception does not apply in the case of a partnership that is a dealer in stocks, bonds, other securities, commodities, or financial instruments. For this purpose, whether a partnership is a dealer is determined under the principles of §1.864–2(c)(2)(iv)(a).

**Proposed Effective/Applicability Date**

These regulations are proposed to apply on the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**. For rules applicable to periods prior to the publication date, see the corresponding provisions in §§1.892–4T and 1.892–5T in the 1988 temporary regulations and in §1.892–5(a) as issued under T.D. 9012, 2002–2 C.B. 389 (August 1, 2002).

**Reliance on Proposed Regulations**

Taxpayers may rely on the proposed regulations until final regulations are issued.

**Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and because the proposed regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

**Comments and Requests for Public Hearing**

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

**Drafting Information**

The principal author of these regulations is David A. Juster of the Office of Associate Chief Counsel (International), within the Office of Chief Counsel, IRS. Other personnel from the Treasury Department and the IRS participated in developing the regulations.

* * * * *

**Proposed Amendments to the Regulations**

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

**PART 1—INCOME TAX REGULATIONS**

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

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

Section 1.892–4 also issued under 26 U.S.C. 892(c). * * *

Par. 2. Section 1.892–4 is added to read as follows:

*§1.892–4 Commercial activities.*

(a) through (c) [Reserved]. For further guidance, see §1.892–4T(a) through (c).

(d) *In general.* Except as provided in paragraph (e) of this section, all activities (whether conducted within or outside the United States) which are ordinarily conducted for the current or future production of income or gain are commercial activities. Only the nature of the activity, not the purpose or motivation for conducting the activity, is determinative of whether the activity is commercial in character. An activity may be considered a commercial activity even if such activity does not constitute a trade or business for purposes of section 162 or does not constitute (or would not constitute if undertaken in the United States) the conduct of a trade or business in the United States for purposes of section 864(b).

(e) *Activities that are not commercial*—(1) *Investments*—(i) *In general.* Subject to the provisions of paragraphs (e)(1)(ii) and (e)(1)(iii) of this section, the following are not commercial activities: investments in stocks, bonds, and other securities (as defined in §1.892–3T(a)(3)); loans; investments in financial instruments (as defined in §1.892–3T(a)(4)); the holding of net leases on real property; the holding of real property which is not producing income (other than on its sale or from an investment in net leases on real property); and the holding of bank deposits in banks. Transferring securities under a loan agreement which meets the requirements of section 1058 is an investment for purposes of this paragraph (e)(1)(i). An activity will not cease to be an investment solely because of the volume of transactions of that activity or because of other unrelated activities.

(ii) *Trading.* Effecting transactions in stocks, bonds, other securities (as defined in §1.892–3T(a)(3)), commodities, or financial instruments (as defined in §1.892–3T(a)(4)) for a foreign government's own account does not constitute a commercial activity regardless of whether such activity constitutes a trade or business for purposes of section 162 or constitutes (or would constitute if undertaken within the United States) the conduct of a trade or business in the United States for purposes of section 864(b). Such transactions are not commercial activities regardless of whether they are effected by the foreign government through its employees or through a broker, commission agent, custodian, or other independent agent and regardless of whether or not any such employee or agent has discretionary authority to make decisions in effecting the transactions. Such transactions undertaken as a dealer (as determined under the principles of §1.864–2(c)(2)(iv)(a)), however, constitute commercial activity. For purposes of this paragraph (e)(1)(ii),

the term *commodities* means commodities of a kind customarily dealt in on an organized commodity exchange but only if the transaction is of a kind customarily consummated at such place.

(iii) *Banking, financing, etc*. Investments (including loans) made by a banking, financing, or similar business constitute commercial activities, even if the income derived from such investments is not considered to be income effectively connected with the active conduct of a banking, financing, or similar business in the U.S. by reason of the application of §1.864–4(c)(5).

(iv) *Disposition of a U.S. real property interest***.** A disposition (including a deemed disposition under section 897(h)(1)) of a U.S. real property interest (as defined in section 897(c)), by itself, does not constitute the conduct of a commercial activity. As described in §1.892–3T(a), however, gain derived from a disposition of a U.S. real property interest defined in section 897(c)(1)(A)(i) will not qualify for exemption from tax under section 892.

(2) through (5) [Reserved]. For further guidance, see §1.892–4T(c)(2) through (c)(5).

(f) *Effective/applicability date*. This section applies on the date the regulations are published as final regulations in the **Federal Register**. See §1.892–4T for the rules that apply before the date the regulations are published as final regulations in the **Federal Register**.

Par. 3. Section 1.892–5 is revised to read as follows:

*§1.892–5 Controlled commercial entity*.

(a) *In general*—(1) *General rule and definition of the term "controlled commercial entity"*. Under section 892(a)(2)(A)(ii) and (a)(2)(A)(iii), the exemption generally applicable to a foreign government (as defined in §1.892–2T) for income described in §1.892–3T does not apply to income received by a controlled commercial entity or received (directly or indirectly) from a controlled commercial entity, or to income derived from the disposition of any interest in a controlled commercial entity. For purposes of section 892 and the regulations thereunder, the term *entity* means and includes a corporation, a partnership, a trust (including a pension trust described in §1.892–2T(c)), and an estate, and the term *controlled commercial entity* means any entity (including a controlled entity as defined in §1.892–2T(a)(3)) engaged in commercial activities (as defined in §§1.892–4 and 1.892–4T) (whether conducted within or outside the United States) if the government—

(i) Holds (directly or indirectly) any interest in such entity which (by value or voting power) is 50 percent or more of the total of such interests in such entity, or

(ii) Holds (directly or indirectly) any other interest in such entity which provides the foreign government with effective practical control of such entity.

(2) *Inadvertent commercial activity*—(i) *General rule*. For purposes of determining whether an entity is a controlled commercial entity for purposes of section 892(a)(2)(B) and paragraph (a)(1) of this section, an entity that conducts only inadvertent commercial activity will not be considered to be engaged in commercial activities. However, any income derived from such inadvertent commercial activity will not qualify for exemption from tax under section 892. Commercial activity of an entity will be treated as inadvertent commercial activity only if:

(A) Failure to avoid conducting the commercial activity is reasonable as described in paragraph (a)(2)(ii) of this section;

(B) The commercial activity is promptly cured as described in paragraph (a)(2)(iii) of this section; and

(C) The record maintenance requirements described in paragraph (a)(2)(iv) of this section are met.

(ii) *Reasonable failure to avoid commercial activity*—(A) *In general*. Subject to paragraphs (a)(2)(ii)(B) and (a)(2)(ii)(C) of this section, whether an entity's failure to prevent its worldwide activities from resulting in commercial activity is reasonable will be determined in light of all the facts and circumstances. Due regard will be given to the number of commercial activities conducted during the taxable year and in prior taxable years, as well as the amount of income earned from, and assets used in, the conduct of the commercial activities in relationship to the entity's total income and assets, respectively. For purposes of this paragraph (a)(2)(ii)(A) and paragraph (a)(2)(ii)(C) of this section, where a commercial activity conducted by a partnership is attributed under paragraph (d)(5)(i) of this section to an entity owning an interest in the partnership—

(*1*) Assets used in the conduct of the commercial activity by the partnership are treated as assets used in the conduct of commercial activity by the entity in proportion to the entity's interest in the partnership; and

(*2*) The entity's distributive share of the partnership's income from the conduct of the commercial activity shall be treated as income earned by the entity from the conduct of commercial activities.

(B) *Continuing due diligence requirement*. A failure to avoid commercial activity will not be considered reasonable unless there is continuing due diligence to prevent the entity from engaging in commercial activities within or outside the United States as evidenced by having adequate written policies and operational procedures in place to monitor the entity's worldwide activities. A failure to avoid commercial activity will not be considered reasonable if the management-level employees of the entity have not undertaken reasonable efforts to establish, follow, and enforce such written policies and operational procedures.

(C) *Safe Harbor*. Provided that adequate written policies and operational procedures are in place to monitor the entity's worldwide activities as required in paragraph (a)(2)(ii)(B) of this section, the entity's failure to avoid commercial activity during the taxable year will be considered reasonable if:

(*1*) The value of the assets used in, or held for use in, all commercial activity does not exceed five percent of the total value of the assets reflected on the entity's balance sheet for the taxable year as prepared for financial accounting purposes, and

(*2*) The income earned by the entity from commercial activity does not exceed five percent of the entity's gross income as reflected on its income statement for the taxable year as prepared for financial accounting purposes.

(iii) *Cure requirement*. A timely cure shall be considered to have been made if the entity discontinues the conduct of the commercial activity within 120 days of discovering the commercial activity. For

example, if an entity that holds an interest as a general partner in a partnership discovers that the partnership is conducting commercial activity, the entity will satisfy the cure requirement if, within 120 days of discovering the commercial activity, the entity discontinues the conduct of the activity by divesting itself of its interest in the partnership (including by transferring its interest in the partnership to a related entity), or the partnership discontinues its conduct of commercial activity.

(iv) *Record maintenance*. Adequate records of each discovered commercial activity and the remedial action taken to cure that activity must be maintained. The records shall be retained so long as the contents thereof may become material in the administration of section 892.

(3) *Annual determination of controlled commercial entity status*. If an entity described in paragraph (a)(1)(i) or paragraph (a)(1)(ii) of this section engages in commercial activities at any time during a taxable year, the entity will be considered a controlled commercial entity for the entire taxable year. An entity not otherwise engaged in commercial activities during a taxable year will not be considered a controlled commercial entity for a taxable year even if the entity engaged in commercial activities in a prior taxable year.

(b) through (d)(4) [Reserved]. For further guidance, see §1.892–5T(b) through (d)(4).

(5) *Partnerships*—(i) *General rule*. Except as provided in paragraph (d)(5)(ii) or (d)(5)(iii) of this section, the commercial activities of an entity classified as a partnership for federal tax purposes will be attributable to its partners for purposes of section 892. For example, if an entity described in paragraph (a)(1)(i) or paragraph (a)(1)(ii) of this section holds an interest as a general partner in a partnership that is engaged in commercial activities, the partnership's commercial activities will be attributed to that entity for purposes of determining if the entity is a controlled commercial entity within the meaning of section 892(a)(2)(B) and paragraph (a) of this section.

(ii) *Trading activity exception*. An entity not otherwise engaged in commercial activities will not be considered to be engaged in commercial activities solely because the entity is a member of a partnership (whether domestic or foreign) that effects transactions in stocks, bonds, other securities (as defined in §1.892–3T(a)(3)), commodities (as defined in §1.892–4(e)(1)(ii)), or financial instruments (as defined in §1.892–3T(a)(4)) for the partnership's own account or solely because an employee of such partnership, or a broker, commission agent, custodian, or other agent, pursuant to discretionary authority granted by such partnership, effects such transactions for the account of the partnership. This exception shall not apply to any member in the case of a partnership that is a dealer in stocks, bonds, other securities, commodities, or financial instruments, as determined under the principles of §1.864–2(c)(2)(iv)(a).

(iii) *Limited partner exception*—(A) *General rule*. An entity that is not otherwise engaged in commercial activities (including, for example, performing services for a partnership as described in section 707(a) or section 707(c)) will not be deemed to be engaged in commercial activities solely because it holds an interest as a limited partner in a limited partnership. Nevertheless, pursuant to sections 875, 882, and 892(a)(2)(A)(i), a foreign government member's distributive share of partnership income will not be exempt from taxation under section 892 to the extent that the partnership derived such income from the conduct of a commercial activity. For example, where a controlled entity described in §1.892–2T(a)(3) that is not otherwise engaged in commercial activities holds an interest as a limited partner in a limited partnership that is a dealer in stocks, bonds, other securities, commodities, or financial instruments in the United States, although the controlled entity partner will not be deemed to be engaged in commercial activities solely because of its interest in the limited partnership, its distributive share of partnership income derived from the partnership's activity as a dealer will not be exempt from tax under section 892 because it was derived from the conduct of a commercial activity.

(B) *Interest as a limited partner in a limited partnership*. Solely for purposes of paragraph (d)(5)(iii) of this section, an interest in an entity classified as a partnership for federal tax purposes shall be treated as an interest as a limited partner in a limited partnership if the holder of such interest does not have rights to participate in the management and conduct of the partnership's business at any time during the partnership's taxable year under the law of the jurisdiction in which the partnership is organized or under the governing agreement. Rights to participate in the management and conduct of a partnership's business do not include consent rights in the case of extraordinary events such as admission or expulsion of a general or limited partner, amendment of the partnership agreement, dissolution of the partnership, disposition of all or substantially all of the partnership's property outside of the ordinary course of the partnership's activities, merger, or conversion.

(iv) *Illustration*. The following example illustrates the application of this paragraph (d)(5):

*Example 1*. K, a controlled entity of a foreign sovereign, has investments in various stocks and bonds of United States corporations and in a 20% interest in Opco, a limited liability company that is classified as a partnership for federal tax purposes. Under the governing agreement of Opco, K has the authority to participate in the management and conduct of Opco's business. Opco has investments in various stocks and bonds of United States corporations and also owns and manages an office building in New York. Because K has authority to participate in the management and conduct of Opco's business, its interest in Opco is not a limited partner interest. Therefore, K will be deemed to be engaged in commercial activities because of attribution of Opco's commercial activity, even if K does not actually make management decisions with regard to Opco's commercial activity, the operation of the office building. Accordingly, K is a controlled commercial entity, and all of its income, including its distributive share of partnership income from its interest in Opco and its income from the stocks and bonds it owns directly, will not be exempt from tax under section 892.

*Example 2*. The facts are the same as in *Example 1*, except that Opco has hired a real estate management firm to lease offices and manage the office building. Notwithstanding the fact that an independent contractor is performing the activities, Opco will still be deemed to be engaged in commercial activities. Accordingly, K is a controlled commercial entity, and all of its income, including its distributive share of partnership income from its interest in Opco and its income from the stocks and bonds it owns directly, will not be exempt from tax under section 892.

*Example 3*. The facts are the same as in *Example 1*, except that K is a member that has no right to participate in the management and conduct of Opco's business. Assume further that K is not otherwise engaged in commercial activities. Under paragraph (d)(5)(iii) of this section, Opco's commercial activities will not be attributed to K. Accordingly, K will not be a controlled commercial entity, and its income derived from the stocks and bonds it owns directly and the portion of its distributive share of partnership income from its interest in Opco that is derived

from stocks and bonds will be exempt from tax under section 892. The portion of K's distributive share of partnership income from its interest in Opco that is derived from the operation of the office building will not be exempt from tax under section 892 and §1.892–3T(a)(1).

(e) *Effective/applicability date*. This section applies on the date these regulations are published as final regulations in the **Federal Register**. See §1.892–5(a) as issued under T.D. 9012 (August 1, 2002) for rules that apply on or after January 14, 2002, and before the date these regulations are published as final regulations in the **Federal Register**. See §1.892–5T(a) for rules that apply before January 14, 2002, and §1.892–5T(b) through (d) for rules that apply before the date these regulations are published as final regulations in the **Federal Register**.

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

Par. 4. The authority for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 5. In §602.101, paragraph (b) is amended by adding an entry to the table in numerical order to read as follows:

*§602.101 OMB Control numbers*.

* * * * *

(b) * * *

| CFR part or section where identified and described | Current OMB control No. |
|---|---|
| * * * * * | |
| 1.892–5 | 1545–1053 |
| * * * * * | |

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

(Filed by the Office of the Federal Register on November 2, 2011, 8:45 a.m., and published in the issue of the Federal Register for November 3, 2011, 76 F.R. 68110)

## Withdrawal of Notice of Proposed Rulemaking and Notice of Proposed Rulemaking

## Tax Accounting Elections on Behalf of Foreign Corporations

## REG–114749–09

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Withdrawal of notice of proposed rulemaking and notice of proposed rulemaking.

SUMMARY: These proposed regulations would clarify the rules for controlling domestic shareholders to adopt or change a method of accounting or taxable year on behalf of a foreign corporation. The regulations affect United States persons that own stock in certain foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by February 2, 2012.

ADDRESSES: Send submissions to CC:PA:LPD:PR (REG–114749–09), Room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–114749–09), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW; Washington DC, 20224 or sent electronically via the Federal Rulemaking Portal at *www.regulations.gov* (IRS REG–114749–09).

FOR FURTHER INFORMATION CONTACT: Concerning submission of comments, Oluwafunmilayo (Funmi) Taylor (202) 622–7180; concerning the regulations, Joseph W. Vetting (202) 622–3402 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

**Background**

On April 17, 1991, a notice of proposed rulemaking (INTL–939–86) under sections 953, 954, 964, 1248, and 6046 of the Internal Revenue Code (Code) was published in the **Federal Register** (56 FR 15540) (the 1991 proposed regulations). No comments were received with respect to the proposed amendments under section 964, which would provide a special definition of controlling domestic shareholders for certain controlled foreign corporations with insurance income. Comments were received on other provisions of the 1991 proposed regulations, but no public hearing was requested and none was held.

On July 1, 1992, a notice of proposed rulemaking (INTL–0018–92) under sections 952 and 964 of the Code was published in the **Federal Register** (57 FR 29246). A correction to the notice of proposed rulemaking was published on October 8, 1992, in the **Federal Register** (57 FR 46355). The proposed regulations would modify the regulations relating to required book-to-tax adjustments in respect of depreciation and inventory accounting. Comments were received. A public hearing was not requested and none was held.

Final regulations published on June 10, 2009 (T.D. 9452, 2009–27 I.R.B. 1) provided guidance for shareholders of certain foreign corporations to elect or change a method of accounting or a taxable year on behalf of the foreign corporation under section 964 of the Code.

**Explanation of Provisions**

These proposed regulations provide clarification of the required book-to-tax adjustments, including those in respect of depreciation and amortization, and additional examples illustrating the application of §1.964–1(a) and (c). The proposed regulations also would delete §1.964–1(b)(3), *Example 2*. The example refers to section 963, which was repealed for taxable years beginning after December 31, 1975. Additionally, the proposed regulations pro-

vide rules regarding IRS-initiated method changes.

The Treasury Department and the IRS again request comments on whether the special control group definition contained in the 1991 proposed regulations should be adopted.

**Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small businesses.

**Comments and Request for a Public Hearing**

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

**Drafting Information**

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

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**Withdrawal of Proposed Regulations**

Accordingly, under the authority of 26 U.S.C. 7805, the notice of proposed rulemaking published in the **Federal Register** on July 1, 1992 (57 FR 29246) is withdrawn.

**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 for part 1 continues to read in part as follows:

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

Par. 2. Section 1.964–1 is amended as follows:

1. Adding a new paragraph (a)(4).

2. In paragraph (b)(3), revising the introductory text, redesignating *Example(1)* as *Example*, and removing *Example (2)*.

3. Revising the first sentence of paragraph (c)(1).

4. Revising paragraph (c)(1)(iii) and removing paragraphs (c)(1)(iii)(*a*), (c)(1)(iii)(*b*), and (c)(1)(iii)(*c*).

5. Revising paragraph (c)(1)(v).

6. Inserting a sentence after the fourth sentence of paragraph (c)(2), revising the fifth sentence of paragraph (c)(2), and adding a sentence at the end of paragraph (c)(2).

7. Revising paragraph (c)(8).

8. Adding a new paragraph (c)(9).

9. Revising paragraph (d).

The additions and revisions read as follows:

*§1.964–1 Determination of the earnings and profits of a foreign corporation.*

* * * * *

(a)(4) *Example*. The rules of this paragraph (a) are illustrated by the following example.

*Example*. (i) *Facts*. P, a domestic corporation, owns all of the outstanding stock of FX, a controlled foreign corporation. In preparing its books for purposes of accounting to its shareholders, FX uses an accounting method (Local Books Method) to determine the amount of its depreciation expense that does not conform to accounting principles generally accepted in the United States (U.S. GAAP) or to U.S. income tax accounting standards as described in paragraph (c). The amount of the adjustment necessary to conform the depreciation expense determined under the Local Books Method with the amount that would be determined under U.S. GAAP for purposes of paragraph (a)(1)(ii) of this section if FX were a domestic corporation is not material. However, the adjustment necessary to conform the amount of the depreciation expense under the Local Books Method to U.S. income tax accounting standards for purposes of paragraph (a)(1)(iii) of this section is material.

(ii) *Result*. Although FX is not required to make the adjustment necessary to conform the amount of its tax expense reserve deduction determined under the Local Books Method to the amount that would be determined under U.S. GAAP, FX is required to make the adjustment necessary to conform the amount of the depreciation expense determined under the Local Books Method to the amount of depreciation expense for the current year that would be allowed under U.S. income tax accounting standards as described in paragraph (c).

(b) * * *

(3) *Example*. The rules of this paragraph (b) are illustrated by the following example.

* * * * *

(c) * * *(1) *In general*. Except as otherwise provided in the Code and regulations (for example, section 952(c)(3) (earnings and profits determined without regard to section 312(n)(4)-(6) for purposes of section 952(c)), the tax accounting standards to be applied in making the adjustments required by paragraph (a)(1)(iii) of this section shall be those applied to domestic corporations, including but not limited to the following:

* * * * *

(iii) *Depreciation and amortization*. Depreciation and amortization shall be computed in accordance with the provisions of section 312(k) and the regulations under that section. In the case of a foreign corporation described in section 312(k)(4) (one with less than 20 percent U.S.-source gross income), depreciation and amortization of items that are not described in section 312(k)(2) or (k)(3) shall be determined under the rules for determining taxable income. For example, amortization for amortizable section 197 intangibles (as defined in section 197(c)) is calculated in accordance with section 197, and depreciation for real property is calculated in accordance with section 168(g)(2)(C)(iii). For any taxable year beginning before July 1, 1972, depreciation shall be computed in accordance with section 167 and the regulations under that section.

* * * * *

(v) *Taxable years*. The period for computation of taxable income and earnings

and profits known as the taxable year shall reflect the provisions of sections 441 and 898 and the regulations under those sections.

* * * * *

(2) *Adoption or change of method or taxable year.* * * * Once adopted, a method of accounting or taxable year may be changed by or on behalf of the foreign corporation only in accordance with the applicable provisions of the Code and regulations. Adjustments to the appropriate separate category (as defined in §1.904–5(a)(1)) of earnings and profits and income of the foreign corporation (including a category of subpart F income described in section 952(a) or, in the case of foreign base company income, described in §1.954–1(c)(1)(iii)) shall be required under section 481 to prevent any duplication or omission of amounts attributable to previous years that would otherwise result from any change in a method of accounting. * * * See paragraph (c)(9) of this section for rules if the change in method of accounting is required in connection with an audit of the foreign corporation's controlling domestic shareholders (as defined in paragraph (c)(5) of this section).

* * * * *

(8) *Examples.* The following examples illustrate the application of paragraph (c) of this section:

*Example 1.* P, a domestic corporation, owns all of the outstanding stock of FX, a controlled foreign corporation organized in 2012. In maintaining its books for the purpose of accounting to its shareholders, FX deducts additions to a reserve for bad debts. Assume that if FX were a domestic corporation, it would be required to use the specific charge-off method under section 166 with respect to allowable bad debt losses. In accordance with paragraph (c)(1)(i) of this section, FX's reserve deductions must be adjusted (if the adjustments are material) in order to compute its earnings and profits in accordance with U.S. income tax accounting standards as described in paragraph (c). Accordingly, P must compute FX's earnings and profits using the specific charge-off method of accounting for bad debts in accordance with section 166.

*Example 2.* FX, a controlled foreign corporation, maintains its books for the purpose of accounting to its shareholders by capitalizing research and experimental expenses. A, B, and C, the United States shareholders (as defined in section 951(b)) of FX, own 45 percent, 30 percent, and 25 percent, respectively, of its only class of outstanding stock. For the first taxable year of FX, pursuant to paragraph (c)(3) of this section, B and C adopt on its behalf the section 174 method of currently deducting research and experimental expenses. Regardless of whether A objects to this action or receives the notice required by paragraph (c)(3)(iii) of this section, adjustments must be made to reflect the use of the section 174 method in computing the earnings and profits of FX with respect to A as well as with respect to B and C.

*Example 3.* (i) P, a calendar year domestic corporation that uses the fair market value method of apportioning interest expense, owns all of the outstanding stock of FX, a controlled foreign corporation organized in 2002 that uses the calendar year as its taxable year for foreign tax purposes. On June 1, 2012, FX makes a distribution to P. Prior to that distribution, none of the significant events specified in paragraph (c)(6) of this section had occurred. In addition, neither P nor FX had ever made or adopted, or been required to make or adopt, an election or method of accounting or taxable year for United States tax purposes with respect to FX. FX does not act to make any election or adopt any method of accounting or a taxable year for United States tax purposes.

(ii) P must compute FX's earnings and profits for FX's 2002 through 2012 taxable years in order to determine if any portion of the 2012 distribution is taxable as a dividend and to determine P's deemed paid foreign tax credit on such portion under section 902. Under paragraph (c)(2) of this section, P may make an election or adopt a method or methods of accounting and a taxable year on behalf of FX by satisfying the requirements of paragraph (c)(3) of this section by the due date (with extensions) of P's Federal income tax return for 2012, its taxable year with which ends FX's 2012 taxable year. Under paragraph (c)(4) of this section, any such election or adoption will govern the computation of FX's earnings and profits for its taxable years beginning in 2002 and subsequent taxable years for purposes of determining the Federal income tax liability of P and any subsequent shareholders of FX in 2012 and subsequent taxable years, unless the Commissioner consents to a change.

(iii) If P fails to satisfy the requirements under paragraph (c)(3) of this section and such failure is not shown to the satisfaction of the Commissioner to be due to reasonable cause, the earnings and profits of FX will be computed on the basis of a calendar taxable year as if no elections were made and any permissible methods of accounting not requiring an election and reflected in FX's books were adopted. Any subsequent attempt by FX or P to change an accounting method or taxable year of FX shall be effective only if the Commissioner consents to the change.

*Example 4.* (i) The facts are the same as in *Example 3*, except that P owns 80 percent, rather than all, of the outstanding stock of FX. M, a calendar year domestic corporation, owns the remaining 20 percent of the stock of FX beginning in 2002. M uses the tax book value method to allocate its interest expense under section 864(e)(4).

(ii) M, but not P, must compute FX's earnings and profits beginning in 2002 in order to determine the adjustment under §1.861–12(c) and §1.861–12T(c) to M's basis in the stock of FX for M's 2002 through 2011 taxable years. Because P, the controlling domestic shareholder of FX, has not made or adopted, or been required to make or adopt, an election or a method of accounting or taxable year with respect to FX, the earnings and profits of FX for 2002 through 2011 will be computed on the basis of a calendar taxable year as if no elections were made and any permissible methods of accounting not requiring an election and reflected in FX's books were adopted. However, a properly filed, timely election or adoption of a method of accounting or taxable year by, or on behalf of, FX with respect to FX's taxable year ending in 2012, when FX's earnings and profits are first significant for United States tax purposes for P, FX's controlling domestic shareholder, shall not be treated as a change in accounting method or a change in taxable year for any pre–2012 taxable year of FX. M will not be required to recompute its basis adjustments for 2002 through 2011 by reason of P's adoption of a method or methods of accounting or taxable year with respect to FX for 2012. See paragraph (c)(4)(iii) of this section. However, any method of accounting or taxable year adopted on behalf of FX by P pursuant to this paragraph (c) with respect to FX is binding on P, FX, and M for purposes of computing FX's earnings and profits in 2002 and subsequent taxable years for purposes of determining the Federal income tax liability of P, M, and any subsequent shareholders of FX in 2012 and subsequent taxable years, unless the Commissioner consents to a change.

*Example 5.* (i) In 1987, P, a calendar year domestic corporation that uses the tax book value method to allocate its interest expense under section 864(e)(4), acquired 50 percent of the outstanding stock of 10/50 Corp, a noncontrolled section 902 corporation organized in 1980. For taxable years beginning on or before April 25, 2006, the provisions of this paragraph (c) did not provide a mechanism for shareholders of noncontrolled section 902 corporations to make elections or adopt methods of accounting or a taxable year on behalf of noncontrolled section 902 corporations. However, P had to compute 10/50 Corp's earnings and profits in order to determine the adjustment under §1.861–12(c) and §1.861–12T(c) to P's basis in the stock of 10/50 Corp beginning with P's 1987 taxable year.

(ii) For taxable years beginning on or before April 25, 2006, P was required to compute 10/50 Corp's earnings and profits as if any permissible method of accounting not requiring an election and reflected in 10/50 Corp's books had been adopted. See paragraph (c)(4)(ii) of this section. In taxable years beginning after April 25, 2006, in accordance with paragraph (c)(3) of this section P may request the consent of the Commissioner to change any method of accounting or the taxable year on behalf of 10/50 Corp.

(9) *Change of method on audit.* If, in connection with an audit (or audits) of one or more shareholders of the foreign corporation who collectively would constitute the foreign corporation's controlling domestic shareholder(s) if they undertook to act on the corporation's behalf, the Commissioner determines that a method of accounting of the foreign corporation does not clearly reflect income, the computation of earnings and profits shall be made in a manner which, in the opinion of the Commissioner, does clearly reflect income. See section 446 and the related regulations. The Commissioner shall provide written notice of the change in method of accounting to each such shareholder and to all other persons

known by the Commissioner to be domestic shareholders who own (within the meaning of section 958(a)) stock of the foreign corporation. However, the failure of the Commissioner to provide such notice to any such other person shall not invalidate the change of method, which shall bind both the foreign corporation and all of its domestic shareholders as to the computation of the foreign corporation's earnings and profits for the taxable year of the foreign corporation for which the method of accounting is changed and in subsequent taxable years unless the Commissioner consents to a change.

(d) *Effective/applicability date*. This section applies in computing earnings and profits of foreign corporations in taxable years of foreign corporations beginning on or after the date of publication of these regulations as final regulations in the **Federal Register**, and taxable years of shareholders with or within which such taxable years of the foreign corporations end. See 26 CFR §1.964–1 (revised as of April 1, 2011) for rules applicable to taxable years beginning before such date.

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

(Filed by the Office of the Federal Register on November 3, 2011, 8:45 a.m., and published in the issue of the Federal Register for November 4, 2011, 76 F.R. 68370)

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# Withdrawal of a Manufacturer's Right to Provide Certifications Under the Qualifying Nonbusiness Energy Property Credit of Section 25C

## Announcement 2011–73

This announcement withdraws the right of a manufacturer, Weld Rite, Inc., to certify that its hydronic outdoor wood-burning furnaces qualify for the nonbusiness energy property credit under § 25C of the Internal Revenue Code.

SECTION 1. BACKGROUND

Section 25C provides a tax credit to individuals for nonbusiness energy property. Section 25C(a) allows a credit for the taxable year in an amount equal to: (1) 10 percent of the amount paid or incurred for qualified energy efficiency improvements installed during such taxable year; and (2) the amount of the residential energy property expenditures paid or incurred during such taxable year.

Under § 25C(d)(1), the residential energy property expenditures are expenditures made by the taxpayer for qualified energy property which the taxpayer installs on or in connection with a dwelling unit located in the United States that the taxpayer owns and uses as the taxpayer's principal residence (within the meaning of § 121), and that the taxpayer originally placed in service.

Section 25C(d)(2)(A)(i) provides that qualified energy property includes energy-efficient building property.

Under § 25C(d)(3)(E), energy-efficient building property includes, among others, a stove which uses the burning of biomass fuel to heat a dwelling unit located in the United States and used as a residence by the taxpayer, or to heat water for use in such a dwelling unit, and which has a thermal efficiency rating of at least 75 percent. For property placed in service after December 31, 2008, and prior to January 1, 2011, the law also required that the thermal efficiency rating of at least 75 percent be measured using a lower heating value.

On June 22, 2009, the Internal Revenue Service ("Service") issued Notice 2009–53, 2009–25 I.R.B. 1095, to provide procedures that manufacturers may follow to certify property as qualified energy property, as well as guidance regarding the conditions under which taxpayers seeking a credit may rely on a manufacturer's certification.

Section 6.01 of the notice allows a manufacturer to provide the certification by including a written copy of the statement with the packaging of the property, in printable form on the manufacturer's website, or in any other manner that will permit the taxpayer to retain the certification statement for tax recordkeeping purposes.

Section 6.02 of the notice provides that a taxpayer may rely on a manufacturer's certification that energy property is qualified energy property except as provided in sections 6.03 and 6.08 of the notice.

Section 6.03 of the notice does not apply to qualified energy property. Pursuant to section 6.08 of the notice, the Service may, upon examination (and after any appropriate consultation with the Department of Energy or Environmental Protection Agency), determine that property that has been certified under section 6 of the notice is not qualified energy property. In that event, or if the manufacturer of the property fails to satisfy the requirements relating to documentation in section 6.07 of the notice, the manufacturer's right to provide a certification on which future purchasers of the property can rely will be withdrawn, and taxpayers purchasing the property after the date on which the Service publishes an announcement of the withdrawal may not rely on the manufacturer's certification.

SECTION 2. WITHDRAWAL OF THE MANUFACTURER'S RIGHT

Weld Rite, Inc. ("Weld") manufactures certain hydronic outdoor wood-burning furnaces, sold under the name of "Shaver Wood Burning Furnace" ("Furnace"). Pursuant to Notice 2009–53, Weld provided certification to its consumers that the Furnace uses the burning of biomass fuel to heat a dwelling unit or to heat hot water for use in such a dwelling unit and has efficiency ratings of at least 75% as measured using a lower heating value. The manufacturer certified that the Furnace constitutes qualified energy property under § 25C.

The Service, upon examination, determined that the Furnace is not qualified energy property. Specifically, the Service found that the Furnace failed to meet the efficiency ratings of at least 75% as measured using a lower heating value. Accordingly, as of August 17, 2011, the Service withdraws the manufacturer's right to provide a certification on which future purchasers of the Furnace can rely. This withdrawal applies to the following Furnace models: Shaver Pro Series 165, 250, 290 and 340. Taxpayers purchasing the Furnace after the date of the publication of this announcement of the withdrawal may not rely on Weld's certification.

The Service may impose penalties under § 7206 or § 6701 on Weld if Weld continues to provide the erroneous certification to purchasers of the Furnace after August 17, 2011.

SECTION 3. DRAFTING INFORMATION

The principal author of this announcement is Martha McRee of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this announcement, contact Ms. McRee at (202) 622–3110 (not a toll-free call).

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## Effect of Election on Corporation

## Announcement 2011–75

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Withdrawal of notice of proposed rulemaking.

SUMMARY: This document withdraws the proposed regulation seeking to clarify that if a bank is an S corporation within the meaning of section 1361(a)(1), its status as an S corporation does not affect the applicability of the special rules for banks under the Internal Revenue Code.

FOR FURTHER INFORMATION CONTACT: Laura Fields at (202) 622–3050 (not a toll-free number).

SUPPLEMENTAL INFORMATION:

**Background**

On August 24, 2006, the Treasury Department and the IRS published in the **Federal Register** (71 FR 50007) a notice of proposed rulemaking under section 1363 (REG–158677–05, 2007–1 C.B. 975), relating to the applicability of the special banking rules to banks that are S corporations within the meaning of section 1361(a)(1) of the Internal Revenue Code.

The Treasury Department and the IRS received written comments on the proposed regulation from various interested parties. The Treasury Department and the IRS have decided to withdraw the proposed regulation.

* * * * *

**Withdrawal of Notice of Proposed Rulemaking**

Accordingly, under the authority of 26 U.S. C. 7805, the notice of proposed rulemaking (REG–158677–05) that was published in the **Federal Register** on August 24, 2006 (71 FR 50007) is withdrawn.

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

(Filed by the Office of the Federal Register on October 25, 2011, 8:45 a.m., and published in the issue of the Federal Register for October 26, 2011, 76 F.R. 66239)

# Definition of Terms

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

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

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

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

*Modified* is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

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

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

*Superseded* describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

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

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

# Abbreviations

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

*A*—Individual.
*Acq.*—Acquiescence.
*B*—Individual.
*BE*—Beneficiary.
*BK*—Bank.
*B.T.A.*—Board of Tax Appeals.
*C*—Individual.
*C.B.*—Cumulative Bulletin.
*CFR*—Code of Federal Regulations.
*CI*—City.
*COOP*—Cooperative.
*Ct.D.*—Court Decision.
*CY*—County.
*D*—Decedent.
*DC*—Dummy Corporation.
*DE*—Donee.
*Del. Order*—Delegation Order.
*DISC*—Domestic International Sales Corporation.
*DR*—Donor.
*E*—Estate.
*EE*—Employee.
*E.O.*—Executive Order.
*ER*—Employer.
*ERISA*—Employee Retirement Income Security Act.
*EX*—Executor.
*F*—Fiduciary.
*FC*—Foreign Country.
*FICA*—Federal Insurance Contributions Act.
*FISC*—Foreign International Sales Company.
*FPH*—Foreign Personal Holding Company.
*F.R.*—Federal Register.
*FUTA*—Federal Unemployment Tax Act.
*FX*—Foreign corporation.
*G.C.M.*—Chief Counsel's Memorandum.
*GE*—Grantee.
*GP*—General Partner.
*GR*—Grantor.
*IC*—Insurance Company.
*I.R.B.*—Internal Revenue Bulletin.
*LE*—Lessee.
*LP*—Limited Partner.
*LR*—Lessor.
*M*—Minor.
*Nonacq.*—Nonacquiescence.
*O*—Organization.
*P*—Parent Corporation.
*PHC*—Personal Holding Company.
*PO*—Possession of the U.S.
*PR*—Partner.
*PRS*—Partnership.
*PTE*—Prohibited Transaction Exemption.
*Pub. L.*—Public Law.
*REIT*—Real Estate Investment Trust.
*Rev. Proc.*—Revenue Procedure.
*Rev. Rul.*—Revenue Ruling.
*S*—Subsidiary.
*S.P.R.*—Statement of Procedural Rules.
*Stat.*—Statutes at Large.
*T*—Target Corporation.
*T.C.*—Tax Court.
*T.D.* —Treasury Decision.
*TFE*—Transferee.
*TFR*—Transferor.
*T.I.R.*—Technical Information Release.
*TP*—Taxpayer.
*TR*—Trust.
*TT*—Trustee.
*U.S.C.*—United States Code.
*X*—Corporation.
*Y*—Corporation.
*Z* —Corporation.

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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 |

# EMPLOYEE PLANS



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