INTERNAL REVENUE
BULLETIN

IRS

HIGHLIGHTS OF THIS ISSUE

Bulletin No. 2019–22
May 28, 2019

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

ADMINISTRATIVE

ANN. 2019-05, page 1262.

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

T.D. 9858, page 1251.

These regulations remove the initial enrollment user fee for enrolled retirement plan agents because the IRS no longer offers initial enrollment as an enrolled retirement plan agent. These regulations also increase the amount of the renewal user fee for enrolled retirement plan agents from $30 to $67. In addition, these regulations increase the amount of both the initial enrollment and renewal user fees for enrolled agents from $30 to $67.

EMPLOYMENT TAX & INCOME TAX

NOT. 2019-34, page 1257.

This Notice provides the maximum fair market value of a vehicle eligible to use the fleet-average and cents-per-mile special valuation rules of Treas. Reg. section 1.61-21(d) and (e), respectively, for 2019. These special valuation rules may be used to value an employee's personal use of an employer-provided vehicle for income and employment tax purposes.

EXEMPT ORGANIZATIONS

REV. PROC. 2019-22, page 1260.

This revenue procedure modifies Revenue Procedure 75-50, 1975-2 C.B. 587, to reflect technological advances since its publication and provides a third method for a private school to satisfy the requirement contained in section 4.03 of the revenue procedure by using its Internet website to publicize the school's racially nondiscriminatory policy as to students.

INCOME TAX

REG-113604-18, page 1265.

Nonresident aliens and foreign corporations are taxable in the United States on taxable income that is effectively connected with the conduct of a trade or business in the United States. These proposed regulations under section 864(c)(8) would provide rules for determining the amount of gain or loss recognized by a nonresident alien individual or foreign corporation from the sale or exchange of a partnership interest that is treated as effectively connected with the conduct of a trade or business within the United States.

T.D. 9857, page 1239.

The final regulations contain rules relating to combinations and separations of qualified business units (QBUs) subject to section 987 and the recognition and deferral of foreign currency gain or loss with respect to a QBU subject to section 987 in connection with certain QBU terminations and certain other transactions involving partnerships. In addition, this document withdraws temporary regulations regarding the allocation of assets and liabilities of certain partnerships for purposes of section 987.

Finding Lists begin on page ii.

NOT. 2019-33, page 1255.
This notice requests comments about normalization issues that have arisen or are anticipated in ratemaking proceedings due to the decrease in the corporate tax rate under § 11 of the Internal Revenue Code (Code) that was included in the Tax Cuts and Jobs Act, Pub. L. 115-97, enacted on December 22, 2017. Based on comments received from stakeholders, we expect to issue future guidance under § 168(f)(2) and (i)(9) of the Code addressing excess deferred income taxes and public utility companies.

REV. PROC. 2019-25, page 1261.
This revenue procedure provides the 2020 inflation adjusted amounts for health savings accounts as determined under section 223 of the Internal Revenue Code.

The IRS Mission

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

Introduction

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

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

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

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

The Bulletin is divided into four parts as follows:

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

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

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

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

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

Part I.

26 CFR 1.987-2, 26 CFR 1.987-2T, 26 CFR 1.987-4, 26 CFR 1.987-4T, 26 CFR 1.987-7, 26 CFR 1.987-7T, 26 CFR 1.987-12, 26 CFR 1.987-12T

T.D. 9857

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Recognition and Deferral of Section 987 Gain or Loss

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations relating to combinations and separations of qualified business units (QBUs) subject to section 987 and the recognition and deferral of foreign currency gain or loss with respect to a QBU subject to section 987 in connection with certain QBU terminations and certain other transactions involving partnerships. In addition, this document withdraws temporary regulations regarding the allocation of assets and liabilities of certain partnerships for purposes of section 987. The final regulations affect taxpayers that own certain QBUs.

DATES: *Effective date*: These regulations are effective on May 13, 2019.

Applicability dates: For dates of applicability, see §§1.987-2(e), 1.987-4(h), and 1.987-12(j).

FOR FURTHER INFORMATION CONTACT: Steven D. Jensen at (202) 317-6938 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains final regulations under §§1.987-2 and 1.987-4 relating to combinations and separations of QBUs subject to section 987. This document also contains final regulations under §1.987-12 relating to the recognition and deferral of foreign currency gain or loss under section 987 with respect to a QBU subject to section 987 in connection with certain QBU terminations and certain other transactions involving partnerships (together with the final regulations under §§1.987-2 and 1.987-4, the final regulations). In addition, this document withdraws temporary regulations under §1.987-7T regarding the allocation of assets and liabilities of certain partnerships for purposes of section 987.

I. *Background on Section 987 Regulations*

On December 8, 2016, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) published Treasury Decision 9794 (the 2016 final regulations) in the **Federal Register** (81 FR 88806), which contains rules relating to the determination of the taxable income or loss of a taxpayer with respect to a section 987 QBU; the timing, amount, character, and source of any section 987 gain or loss; and other provisions.

On the same date, the Treasury Department and the IRS also published Treasury Decision 9795 (the temporary regulations) in the **Federal Register** (81 FR 88854) and a notice of proposed rulemaking (REG-128276-12) in the **Federal Register** (81 FR 88882) by cross-reference to the temporary regulations. The temporary regulations include the following rules that are not specifically affected by this Treasury decision: an annual deemed termination election for a section 987 QBU; an elective method, available to taxpayers that make the annual deemed termination election, for translating all items of income or loss with respect to a section 987 QBU at the yearly average exchange rate; rules regarding the treatment of section 988 transactions of a section 987 QBU; rules regarding QBUs with the U.S. dollar as their functional currency; rules regarding the translation of income used to pay creditable foreign income taxes; and rules under section 988 requiring the deferral of certain section 988 loss that arises with respect to related-party loans.

In addition, the temporary regulations contain the following provisions that are specifically affected by this Treasury decision: §§1.987-2T and 1.987-4T, relating to combinations and separations of QBUs; §1.987-7T, which provides a liquidation value percentage methodology for allocating assets and liabilities of certain partnerships (section 987 aggregate partnerships, as defined in §1.987-1(b)(5) of the 2016 final regulations); and §1.987-12T, which requires deferral of foreign currency gain or loss under section 987 with respect to certain transactions defined as deferral events or outbound loss events--transactions that generally include QBU terminations and certain partnerships transactions.

On January 17, 2017, the Treasury Department and the IRS published Notice 2017-07, 2017-3 I.R.B. 423, announcing that certain rules under §1.987-12T would be modified to prevent potential abuse by taxpayers making retroactive check-the-box elections. Section 1.987-12T(j)(1) states that §1.987-12T generally applies to any deferral event or outbound loss event that occurs on or after January 6, 2017 (that is, thirty days after the date that §1.987-12T was filed with the **Federal Register**). Under §1.987-12T(j)(2), however, §1.987-12T also applies to any deferral event or outbound loss event that occurs on or after December 7, 2016, if such deferral event or outbound loss event is undertaken with a principal purpose of recognizing section 987 loss. Notice 2017-07 indicated

[1] Notice 2017-07 inadvertently referred to a principal purpose of recognizing section 987 gain or loss. These final regulations, by contrast, finalize the rule in the temporary regulations by applying § 1.987-12(j)(2) solely to deferral events and outbound loss events undertaken with a principal purpose of recognizing section 987 loss.

that §1.987-12T(j)(2) would be modified so that §1.987-12T also will apply to any deferral event or outbound loss event that is undertaken with a principal purpose of recognizing section 987 loss[1] and that occurs as a result of an entity classification election made under §301.7701-3 that is filed on or after December 22, 2016, and that is effective before December 7, 2016. Additionally, Notice 2017-07 provided that §1.987-12T(j)(1) would be modified so that §1.987-12T also will apply to any deferral event or outbound loss event that occurs as a result of an entity classification election made under §301.7701-3 that is filed on or after January 6, 2017, and that is effective before January 6, 2017.

On October 16, 2017, the Treasury Department and the IRS issued Notice 2017-57, 2017-42 I.R.B. 325, announcing that future guidance would defer the applicability dates of §§1.987-2T, 1.987-4T, and 1.987-7T (along with certain other provisions of the 2016 final regulations and temporary regulations) by one year. The temporary regulations provide that these sections apply to taxable years beginning on or after the day that is one year after the first day of the first taxable year following December 7, 2016. *See* §§1.987-2T(e); 1.987-4T(h); 1.987-7T(d).

On June 25, 2018, the Treasury Department and the IRS published Notice 2018-57, 2018-26 IRB 774, announcing that future guidance would defer the applicability dates of §§1.987-2T, 1.987-4T, and 1.987-7T (along with certain other provisions of the 2016 final regulations and temporary regulations) by one additional year.

II. *Executive Order 13789*

Executive Order 13789, issued on April 21, 2017, instructs the Secretary of the Treasury (the Secretary) to review all significant tax regulations issued on or after January 1, 2016, and to take concrete action to alleviate the burdens of regulations that (i) impose an undue financial burden on U.S. taxpayers; (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the IRS. Executive Order 13789 further instructs the Secretary to submit to the President within 60 days an interim report that identifies regulations that meet these criteria. Notice 2017-38, 2017-30 I.R.B. 147, which was published on July 24, 2017, included the 2016 final regulations in a list of eight regulations identified by the Secretary in the interim report as meeting at least one of the first two criteria specified in Executive Order 13789.

Executive Order 13789 further instructs the Secretary to submit to the President by September 18, 2017, a final report that recommends specific actions to mitigate the burden imposed by regulations identified in the interim report. On October 16, 2017, the Secretary published in the **Federal Register** this final report (82 FR 48013), which indicated, among other things, that the Treasury Department and the IRS intend to propose certain modifications to the 2016 final regulations to reduce burden and compliance challenges associated with those regulations and are actively considering other rules in connection with that proposal.

III. *Deferral of Section 987 Gain or Loss on Certain Terminations and Other Transactions Involving Partnerships*

Under the 2016 final regulations, the owner of a section 987 QBU that terminates includes in income all of the net unrecognized section 987 gain or loss with respect to the section 987 QBU in the year it terminates. Under these rules, a termination can result, for example, solely from a transfer of a section 987 QBU from a taxpayer to a related party, notwithstanding that the QBU's assets continue to be used in the same trade or business by the related party.

Because a termination can result in the deemed remittance of all the assets of a section 987 QBU in circumstances in which the assets continue to be used by a related person in the conduct of the same trade or business that formerly was conducted by the section 987 QBU, terminations can facilitate the selective recognition of section 987 losses. In issuing the temporary regulations, the Treasury Department and the IRS determined that terminations of section 987 QBUs generally should not be permitted to facilitate the selective recognition of losses when the assets and liabilities of the section 987 QBU are transferred to a related person and remain subject to section 987 in the hands of the transferee. Similar policy considerations arise when the transfer of a partnership interest to a related person results in deemed transfers that cause the recognition of section 987 loss with respect to a section 987 QBU owned through the partnership, notwithstanding that the trade or business of the section 987 QBU continues without interruption and remains subject to section 987, and in the context of certain outbound transfers even when the assets do not remain subject to section 987 in the hands of the transferee (because, for example, the transferee has the same functional currency as the QBU). In order to address these policy concerns, the temporary regulations defer section 987 losses resulting from certain termination events, partnership transactions, and certain other transactions involving outbound transfers.

In addition, the temporary regulations generally apply to defer the recognition of section 987 gains as well as losses when the transferee is subject to section 987 with respect to the assets of the section 987 QBU. The temporary regulations do not, however, defer gain to the extent the assets of a section 987 QBU are transferred by a U.S. person to a related foreign person, consistent with the policies underlying section 367.

IV. *Combinations and Separations of QBUs*

The temporary regulations also include rules to prevent similarly inappropriate results when certain section 987 QBUs are combined or separated. Absent a special rule, the combination of multiple section 987 QBUs that have the same owner, or the separation of a section 987 QBU into two or more section 987 QBUs that have the same owner, would give rise to a transfer between an owner and one or more section 987 QBUs under the 2016 final regulations.

Consistent with the policy of deferring section 987 gain or loss under §1.987-12T when assets of a section 987 QBU are reflected on the books and records of another section 987 QBU in the same controlled group as a result of certain transactions that result in deemed transfers, the temporary regulations provide that section 987 gain or loss generally is not recognized when two or more section 987

QBUs (combining QBUs) with the same owner combine into a single section 987 QBU (combined QBU) or when a section 987 QBU (separating QBU) separates into multiple section 987 QBUs (each, a separated QBU).

The temporary regulations also include certain mechanical rules applicable in this context, including (i) rules related to determining the net unrecognized section 987 gain or loss of combined QBUs and separated QBUs, and (ii) provisions regarding combining section 987 QBUs that have different functional currencies than their respective combined QBUs.

V. *Determination of a Partner's Share of Assets and Liabilities of a Section 987 Aggregate Partnership*

The 2016 final regulations set forth rules applicable to section 987 aggregate partnerships, which are defined as partnerships for which all of the capital and profits interests are owned, directly or indirectly, by persons that are related within the meaning of section 267(b) or section 707(b). Under the aggregate approach set forth in the 2016 final regulations, assets and liabilities reflected on the books and records of an eligible QBU of a section 987 aggregate partnership are allocated to each partner, which is considered an indirect owner of the eligible QBU. If the eligible QBU has a different functional currency than its indirect owner, then the assets and liabilities of the eligible QBU that are allocated to the partner are treated as a section 987 QBU of the indirect owner.

The temporary regulations provide specific rules for determining a partner's share of the assets and liabilities reflected on the books and records of an eligible QBU owned indirectly through a section 987 aggregate partnership. Specifically, §1.987-7T(b) provides that, in any taxable year, a partner's share of each asset and liability of a section 987 aggregate partnership is proportional to the partner's liquidation value percentage with respect to the aggregate partnership. A partner's liquidation value percentage is defined as the ratio of the liquidation value of the partner's interest in the partnership to the aggregate liquidation value of all the partners' interests in the partnership. The liquidation value of the partner's interest in the partnership is the amount of cash the partner would receive with respect to its interest if, immediately following the applicable determination date, the partnership sold all of its assets for cash equal to the fair market value of such assets (taking into account section 7701(g)), satisfied all of its liabilities (other than those described in §1.752-7), paid an unrelated third party to assume all of its §1.752-7 liabilities in a fully taxable transaction, and then liquidated.

Summary of Comments and Explanation of Revisions

The Treasury Department and the IRS received one comment regarding the temporary regulations. In addition, the Treasury Department and the IRS received several comments in response to Notice 2017-38 pertaining to the temporary regulations. After consideration of all the comments, the regulations under §§1.987-2T, 1.987-4T, and 1.987-12T, as revised by this Treasury decision, are adopted as final regulations. In addition, the regulations under §1.987-7T are withdrawn. The Treasury Department and the IRS are continuing to study the other provisions of the temporary regulations that are not specifically addressed by this Treasury decision. In addition, several comments were received that relate to rules in the 2016 final regulations. Comments on the 2016 final regulations, and provisions of the temporary regulations that are not specifically addressed by this Treasury decision, are beyond the scope of this rulemaking and are not addressed in this preamble. The Treasury Department and the IRS will consider these comments in connection with any future guidance projects addressing the issues discussed in the comments.

I. *Comments Recommending Withdrawal of the Temporary Regulations*

A number of comments recommended that all of the temporary regulations, including §§1.987-2T, 1.987-4T, and 1.987-12T, be withdrawn. Comments generally indicated that the 2016 final regulations and the temporary regulations are unduly complex and present significant financial and compliance burdens for taxpayers subject to the 2016 final regulations.

As described in the Background section of this Preamble, in its final report to the President in response to Executive Order 13789, the Treasury Department indicated that the 2016 final regulations have proved difficult to apply for many taxpayers. The final report indicated that the Treasury Department and the IRS intend to propose modifications to the 2016 final regulations that will reduce the compliance burdens associated with the regulations. While the Treasury Department and the IRS intend to reduce those burdens as described in the final report, the Treasury Department and the IRS continue to consider it inappropriate to permit the selective recognition of section 987 losses and the deferral of section 987 gains. This is particularly true when such selective loss recognition may be accomplished through related-party transactions that do not significantly impact the conduct of the trade or business of a section 987 QBU or its owner but nonetheless generate significant tax benefits, as is true of deferral events and outbound loss events.

Accordingly, the Treasury Department and the IRS have determined that finalizing §§1.987-2T, 1.987-4T, and 1.987-12T, while simultaneously deferring the applicability date of the 2016 final regulations and developing guidance to mitigate the complexity and administrative challenges associated with, the 2016 final regulations, appropriately balances taxpayers' burdens with the need to prevent abuse under the 2016 final regulations or under another method of complying with section 987 utilized by a taxpayer during a period for which the 2016 final regulations are not applicable. Accordingly, this Treasury decision finalizes the rules in §§1.987-2T, 1.987-4T, and 1.987-12T with certain clarifications.

II. *Comments Recommending a Delay of the Applicability Date of the Temporary Regulations*

Comments recommended that the applicability date for the 2016 final regulations and the temporary regulations, including §§1.987-2T, 1.987-4T, and 1.987-12T, be delayed for a specified period, such as one or two years. Similarly, comments recommended that the final and temporary regulations, including §§1.987-

2T, 1.987-4T, and 1.987-12T, be withdrawn in their entirety and reproposed (in one case, with an effective date at least two years after such regulations are finalized) to allow taxpayers time to effectively plan to implement the final and temporary regulations. Generally, the comments indicated that taxpayers required additional time to update and implement existing systems to comply with the 2016 final regulations and the temporary regulations. One comment specifically recommended that the applicability date for §1.987-12T be delayed until the applicability date of the 2016 final regulations. The comment indicated that, in certain instances, the applicability date of §1.987-12T prevented the recognition of losses in connection with certain transactions that were in the planning and implementation stages when the temporary regulations were issued. No comments identified specific compliance challenges associated with §1.987-12T.

The Treasury Department and the IRS decline to delay the applicability date of §1.987-12T. As discussed in Part I of this Summary of Comments and Explanation of Revisions, §1.987-12T prevents taxpayers from selectively recognizing section 987 losses through certain technical terminations of a section 987 QBU and similar transactions that would be relatively easy to effect through related-party transactions without meaningfully impacting a taxpayer's business operations. If the applicability date were delayed, taxpayers would be incentivized to engage in such selective recognition of section 987 losses, which would be contrary to the purposes of section 987 and §1.987-12T. Delaying the application of related provisions under §§1.987-2T and 1.987-4T concerning combinations and separations of a section 987 QBU could similarly incentivize transactions designed to accelerate section 987 losses for taxpayers that have elected to apply the 2016 final regulations early. In this regard, the Treasury Department and the IRS observe that the transactions to which §§1.987-2T, 1.987-4T, and 1.987-12T are applicable occur exclusively among related persons, such that taxpayers may avoid the application of those sections by avoiding undertaking such transactions.

Accordingly, the final regulations retain the applicability dates of the temporary regulations, as modified by Notice 2017-07, Notice 2017-57, and Notice 2018-57. Specifically, the final regulations provide that §§1.987-2(c)(9), 1.987-4(c)(2), and 1.987-4(f) apply to taxable years beginning on or after the day that is three years after the first day of the first taxable year following December 7, 2016. If, however, a taxpayer makes an election under §1.987-11(b), then §§1.987-2(c)(9), 1.987-4(c)(2), and 1.987-4(f) apply to taxable years to which §§1.987-1 through 1.987-10 apply as a result of such election.

Similarly, §1.987-12 incorporates the applicability date provisions of §1.987-12T, as modified by Notice 2017-07. Thus, the final regulations under §1.987-12 generally apply to any deferral event or outbound loss event that occurs on or after January 6, 2017. Section 1.987-12 also applies to any deferral event or outbound loss event that occurs as a result of an entity classification election made under §301.7701-3 that is filed on or after January 6, 2017, and that is effective before January 6, 2017. However, §1.987-12 applies to any deferral event or outbound loss event occurring on or after December 7, 2016, if such deferral event or outbound loss event was undertaken with a principal purpose of recognizing section 987 loss. Similarly, §1.987-12 applies to any deferral event or outbound loss event that occurs as a result of an entity classification election made under §301.7701-3 that was filed on or after December 22, 2016, that was effective before December 7, 2016, and that was undertaken with a principal purpose of recognizing section 987 loss.

III. *Comments Regarding the Determination of a Partner's Share of Assets and Liabilities of a Section 987 Aggregate Partnership*

Comments recommended alternative approaches for determining a partner's share of the assets and liabilities of a section 987 aggregate partnership. Comments recommended that §1.987-7 be withdrawn and replaced with the approach of the 2006 proposed regulations under section 987, which provided that a partner's share of assets and liabilities reflected on the books and records of an eligible QBU held indirectly through the partnership must be determined in a manner consistent with how the partners have agreed to share the economic benefits and burdens corresponding to those partnership assets and liabilities, taking into account the rules and principles of subchapter K. The comment indicated that that the liquidation value percentage approach was inconsistent with certain principles of subchapter K, resulting in distortions in the calculation of section 987 gain or loss in certain cases.

The Treasury Department and the IRS have determined that, in the absence of a more comprehensive set of rules for determining a partner's share of assets and liabilities reflected on the books and records of an eligible QBU held indirectly through the partnership that also articulates the interaction of those rules with applicable rules in subchapter K, a more flexible approach is warranted. Moreover, the Treasury Department and the IRS have determined that, in certain instances, the liquidation value percentage methodology set forth in §1.987-7T may be interpreted as applying in a way that inappropriately distorts the computation of section 987 gain or loss. Specifically, under such an interpretation, certain changes in a partner's liquidation value percentage may introduce distortions in the calculation of net unrecognized section 987 gain or loss under §1.987-4, giving rise to net unrecognized section 987 gain or loss that is not attributable to fluctuations in exchange rates. For example, an appreciation or depreciation in property value can result in a change in liquidation value percentage that causes a change in owner functional currency net value for purposes of Step 1 of the §1.987-4(d) calculation of unrecognized section 987 gain or loss for a taxable year without an offsetting adjustment under Step 6 or otherwise that would prevent the change in liquidation value percentage from distorting the calculation of unrecognized section 987 gain or loss. As a result, such unrecognized appreciation or depreciation generally can result in unrecognized section 987 gain or loss for a taxable year being allocated to each partner that indirectly owns a section 987 QBU even when there is no change in exchange rates.

Accordingly, the Treasury Department and the IRS are withdrawing §1.987-7T (and making a conforming change to an example in §1.987-12). Until new regulations are proposed and finalized, taxpayers may use any reasonable method for determining a partner's share of assets and liabilities reflected on the books and records of an eligible QBU held indirectly through the partnership. For this purpose, taxpayers may rely on subchapter K principles (consistent with the 2006 proposed regulations under section 987) or an approach similar to the liquidation value percentage method set forth in §1.987-7T. However, the Treasury Department and the IRS do not believe that it would be reasonable to apply the liquidation value percentage method without corresponding adjustments to the determination of net unrecognized section 987 gain or loss. Thus, for example, a taxpayer using the liquidation value percentage method may be required to adjust its determination of net unrecognized section 987 gain or loss of a section 987 QBU that is owned indirectly through a partnership to prevent the determination of unrecognized section 987 gain or loss that is not attributable to fluctuations in exchange rates. These adjustments may include, for example, treating any change in a partner's owner functional currency net value that is attributable to a change in the partner's liquidation value percentage as resulting in a transfer to or from an indirectly owned section 987 QBU.

Special Analyses

I. Regulatory Planning and Review—Economic Analysis

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

This regulation is not subject to review under section 6(b) of Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Department of the Treasury and the Office of Management and Budget regarding review of tax regulations. Therefore, a regulatory impact assessment is not required.

II. Paperwork Reduction Act

This regulation does not establish a new collection of information nor modify an existing collection that requires the approval of the Office of Management and Budget under the Paperwork Reduction Act (44 U.S.C. chapter 35).

III. Regulatory Flexibility Act

It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities within the meaning of section 601(6) of the Regulatory Flexibility Act (5 U.S.C. chapter 6). Accordingly, a regulatory flexibility analysis is not required. This certification is based on the fact that these regulations will primarily affect U.S. corporations that have foreign operations, which tend to be larger businesses. Accordingly, a regulatory flexibility analysis under the Regulatory Flexibility Act is not required.

Pursuant to section 7805(f), the notice of proposed rulemaking preceding this regulation was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses. No comments were received.

IV. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of $100 million in 1995 dollars, updated annually for inflation. In 2018, that threshold is approximately $150 million. This rule does not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

V. Executive Order 13132: Federalism

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This proposed rule does not have federalism implications, does not impose substantial direct compliance costs on state and local governments, and does not preempt state law within the meaning of the Executive Order.

Drafting Information

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

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry for §1.987-12 in numerical order to read in part as follows:

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

* * * * *

Section 1.987-12 is issued under 26 U.S.C. 987 and 989.

* * * * *

Par. 2. Section 1.987-0 is amended by:

1. Revising the entries for §1.987-2(c)(9), §1.987-4(c)(2), (f), §1.987-12(a), (a)(1), (a)(2), (a)(3), (b), (b)(1), (b)(2), (b)(3), (b)(4), (c), (c)(1), (c)(2), (c)(3), (c)(4), (d), (d)(1), (d)(2), (d)(3), (d)(4), (d)(5), (e), (e)(1), (e)(2), (f), (f)(1), (f)(2), (g), and (h).

2. Adding entries for §1.987-2(e), (e)(1), (e)(2), §1.987-4(f)(1), (f)(2), (f)(3), (h), (h)(1), (h)(2), §1.987-12(i), (i)(1), (i)(2), (i)(3), (j), (j)(1), and (j)(2).

The revisions and additions read as follows:

§1.987-0 Table of contents.

* * * * *

§1.987-2 Attribution of items to eligible QBUs; definition of a transfer and related rules.

* * * * *

(c)(9) Certain disregarded transactions not treated as transfers.

* * * * *

(e) Effective/applicability date.

(1) In general.

(2) Certain disregarded transactions not treated as transfers.

* * * * *

§1.987-4 Determination of net unrecognized section 987 gain or loss of a section 987 QBU.

* * * * *

(c)(2) Coordination with §1.987-12.

* * * * *

(f) Combinations and separations.

(1) Combinations.

(2) Separations.

(3) Examples.

* * * * *

(h) Effective/applicability date.

(1) In general.

(2) Combinations and separations.

* * * * *

§1.987-12 Deferral of section 987 gain or loss.

(a) In general.

(1) Overview.

(2) Scope.

(3) Exceptions.

(b) Gain or loss recognition in connection with a deferral event.

(1) In general.

(2) Deferral event.

(3) Gain or loss recognized under §1.987-5 in the taxable year of a deferral event.

(4) Successor QBU.

(c) Recognition of deferred section 987 gain or loss in the taxable year of a deferral event and in subsequent taxable years.

(1) In general.

(2) Recognition upon a subsequent remittance

(3) Recognition of deferred section 987 loss in certain outbound successor QBU-terminations.

(4) Special rules regarding successor QBUs.

(d) Loss recognition upon an outbound loss event.

(1) In general.

(2) Outbound loss event.

(3) Loss recognized upon an outbound loss event.

(4) Adjustment of basis of stock received in certain nonrecognition transactions.

(5) Recognition of outbound section 987 loss that is not converted into stock basis.

(e) Source and character.

(1) Deferred section 987 gain or loss and certain outbound section 987 loss.

(2) Outbound section 987 loss reflected in stock basis.

(f) Definitions.

(1) Controlled group.

(2) Qualified successor.

(g) Anti-abuse.

(h) Examples.

(i) Coordination with fresh start transition method.

(1) In general.

(2) Adjustment to deferred section 987 gain or loss.

(3) Adjustments in the case of an outbound loss event.

(j) Effective/applicability date.

(1) In general.

(2) Exceptions.

Par. 3. Section 1.987-2 is amended by

1. Revising paragraphs (c)(9).

2. Adding paragraph (e).

The revision and addition read as follows:

§1.987-2 Attribution of items to eligible QBUs; definition of a transfer and related rules.

* * * * *

(c) * * *

(9) *Certain disregarded transactions not treated as transfers*--(i) *Combinations of section 987 QBUs*. The combination of two or more separate section 987 QBUs (combining QBUs) that are directly owned by the same owner, or that are indirectly owned by the same partner through a single section 987 aggregate partnership, into one section 987 QBU (combined QBU) does not give rise to a transfer of any combining QBU's assets or liabilities to the owner under §1.987-2(c). In addition, transactions between the combining QBUs occurring in the taxable year of the combination do not result in a transfer of the combining QBUs' assets or liabilities to the owner under §1.987-2(c). For this purpose, a combination occurs when the assets and liabilities that are properly reflected on the books and records of two or more combining QBUs begin to be properly reflected on the books and records of a combined QBU and the separate existence of the combining QBUs ceases. A combination may result from any transaction or series of transactions in which the combining QBUs become a combined QBU. For rules regarding the determination of net unrecognized section 987 gain or loss of a combined QBU, see §1.987-4(f)(1).

(ii) *Change in functional currency from a combination*. If, following a combination of section 987 QBUs described in paragraph (c)(9)(i) of this section, the combined section 987 QBU has a different functional currency than one or more of the combining section 987 QBUs, any such combining section 987 QBU is treated as changing its functional currency and the owner of the combined section 987 QBU must comply with the regulations under section 985 regarding the change in functional currency. See §§1.985-1(c)(6) and 1.985-5.

(iii) *Separation of section 987 QBUs*. The separation of a section 987 QBU (separating QBU) into two or more section 987 QBUs (separated QBUs) that, after the separation, are directly owned by the same owner, or that are indirectly owned by the same partner through a single section 987 aggregate partnership, does not result in a transfer of the separating QBU's assets or liabilities to the owner under §1.987-2(c). Additionally, transactions that occurred between the separating QBUs in the taxable year of the separation prior to the completion of the separation do not result in transfers for purposes of section 987. For this purpose, a separation occurs when the assets and liabilities that are properly reflected on the books and records of a separating QBU begin to be properly reflected on the books and records of two or more separated QBUs. A separation may result from any transaction or series of transactions in which a separating QBU becomes two or more separated QBUs. A separation may also result when a section 987 QBU that is subject to a grouping election under §1.987-1(b)(2)(ii)(A) changes its functional currency. For rules regarding the determination of net unrecognized section 987 gain or loss of a separated QBU, see §1.987-4(f)(2).

* * * * *

(e) *Effective/applicability date*--(1) *In general*. Except as set forth in paragraph (h)(2) of this section, this section is applicable as specified in §1.987-11.

(2) *Certain disregarded transactions not treated as transfers*. Paragraph (c)(9) of this section applies to taxable years beginning on or after the day that is three years after the first day of the first taxable year following December 7, 2016. Notwithstanding the preceding sentence, if a taxpayer makes an election under §1.987-11(b), then paragraph (c)(9) of this section applies to taxable years to which §§1.987-1 through 1.987-10 apply as a result of such election.

§ 1.987-2T [Removed]

Par. 4. Section 1.987-2T is removed.

Par. 5. Section 1.987-4 is amended by

1. Revising paragraphs (c)(2) and (f).

2. Adding paragraph (h).

The revisions and addition read as follows:

§1.987-4 Determination of net unrecognized section 987 gain or loss of a section 987 QBU.

* * * * *

(c) * * *

(2) *Coordination with §1.987-12*. For purposes of paragraph (c)(1) of this section, amounts taken into account under §1.987-5 are determined without regard to §1.987-12.

* * * * *

(f) *Combinations and separations*--(1) *Combinations*. The net unrecognized section 987 gain or loss of a combined QBU (as defined in §1.987-2(c)(9)(i)) for a taxable year is determined under paragraph (b) of this section by taking into account the net accumulated unrecognized section 987 gain or loss of each combining QBU (as defined in §1.987-2(c)(9)(i)) for all prior taxable years to which the regulations under section 987 apply, as determined under paragraph (c) of this section, and by treating the combining QBUs as having combined immediately prior to the beginning of the taxable year of combination. See paragraph (f)(3) of this section, *Example 1*, for an illustration of this rule.

(2) *Separations*. The net unrecognized section 987 gain or loss of a separated QBU (as defined in §1.987-2(c)(9)(iii)) for a taxable year is determined under paragraph (b) of this section by taking into account the separated QBU's share of the net accumulated unrecognized section 987 gain or loss of the separating QBU (as defined in §1.987-2(c)(9)(iii)) for all prior taxable years to which the regulations under section 987 apply, as determined under paragraph (c) of this section, and by treating the separating QBU as having separated immediately prior to the beginning of the taxable year of separation. A separated QBU's share of the separating QBU's net accumulated unrecognized section 987 gain or loss for all such prior taxable years is determined by apportioning the separating QBU's net accumulated unrecognized section 987 gain or loss for all such prior taxable years to each separated QBU in proportion to the aggregate adjusted basis of the gross assets properly reflected on the books and records of each separated QBU immediately after the separation. For purposes of determining the owner functional currency net value of the separated QBUs on the last day of the taxable year preceding the taxable year of separation under §1.987-5(d)(1)(B) and (e), the balance sheets of the separated QBUs on that day will be deemed to reflect the assets and liabilities reflected on the balance sheet of the separating QBU on that day, apportioned between the separated QBUs in a reasonable manner that takes into account the assets and liabilities reflected on the balance sheets of the separated QBUs immediately after the separation. See paragraph (f)(3) of this section, *Example 2*, for an illustration of this rule.

(3) *Examples*. The following examples illustrate the rules of paragraphs (f)(1) and (2) of this section.

(i) Example 1. Combination of two section 987 QBUs that have the same owner. (A) *Facts*. DC1, a domestic corporation, owns Entity A, a DE. Entity A conducts a business in France that constitutes a section 987 QBU (French QBU) that has the euro as its functional currency. French QBU has a net accumulated unrecognized section 987 loss from all prior taxable years to which the regulations under section 987 apply of $100. DC1 also owns Entity B, a DE. Entity B conducts a business in Germany that constitutes a section 987 QBU (German QBU) that has the euro as its functional currency. German QBU has a net accumulated unrecognized section 987 gain from all prior taxable years to which the regulations under section 987 apply of $110. During the taxable year, Entity A and Entity B merge under local law. As a result, the books and records of French QBU and German QBU are combined into a new single set of books and records. The combined entity has the euro as its functional currency.

(B) *Analysis*. Pursuant to §1.987-2(c)(9)(i), French QBU and German QBU are combining QBUs, and their combination does not give rise to a transfer that is taken into account in determining the amount of a remittance (as defined in §1.987-5(c)). For purposes of computing net unrecognized section 987 gain or loss under this section for the year of the combination, the combination is deemed to have occurred on the last day of the owner's prior taxable year, such that the owner functional currency net value of the combined section 987 QBU at the end of that taxable year described under paragraph (d)(1)(B) of this section takes into account items reflected on the balance sheets of both French QBU and German QBU at that time. Additionally, any transactions between French QBU and German QBU occurring during the year of the merger will not result in transfers to or from a section 987 QBU. Pursuant to paragraph (f)(1) of this section, the combined QBU will have a net accumulated unrecognized section 987 gain from all prior taxable years of $10 (the $100 loss from French QBU plus the $110 gain from German QBU).

(ii) Example 2. Separation of two section 987 QBUs that have the same owner. (A) *Facts*. DC1, a domestic corporation, owns Entity A, a DE. Entity A conducts a business in the Netherlands that constitutes a section 987 QBU (Dutch QBU) that has the euro as its functional currency. The business of Dutch QBU consists of manufacturing and selling bicycles and scooters and is recorded on a single set of books and records. On the last day of Year 1, the adjusted basis of the gross assets of Dutch QBU is €1,000. In Year 2, the net accumulated unrecognized section 987 loss of Dutch QBU from all prior taxable years is $200. During Year 2, Entity A separates the bicycle and scooter business such that each business begins to have its own books and records and to meet the definition of a section 987 QBU under §1.987-1(b)(2) (hereafter, "bicycle QBU" and "scooter QBU"). There are no transfers between DC1 and Dutch QBU before the separation. After the separation, the aggregate adjusted basis of bicycle QBU's assets is €600 and the aggregate adjusted basis of scooter QBU's assets is €400. Each section 987 QBU continues to have the euro as its functional currency.

(B) *Analysis*. Pursuant to §1.987-2(c)(9)(iii), bicycle QBU and scooter QBU are separated QBUs, and the separation of Dutch QBU, a separating QBU, does not give rise to a transfer taken into account in determining the amount of a remittance (as defined in §1.987-5(c)). For purposes of computing net unrecognized section 987 gain or loss under this section for Year 2, the separation will be deemed to have occurred on the last day of the owner's prior taxable year, Year 1. Pursuant to paragraph (f)(2) of this section, bicycle QBU will have a net accumulated unrecognized section 987 loss of $120 (€600/€1,000 x $200), and scooter QBU will have a net accumulated unrecognized section 987 loss of $80 (€400/€1,000 x $200).

* * * * *

(h) *Effective/applicability date*--(1) *In general*. Except as set forth in paragraph (h)(2) of this section, this section is applicable as specified in §1.987-11.

(2) *Combinations and separations*. Paragraphs (c)(2) and (f) of this section apply to taxable years beginning on or after the day that is three years after the first day of the first taxable year following December 7, 2016. Notwithstanding the

preceding sentence, if a taxpayer makes an election under §1.987-11(b), then paragraphs (c)(2) and (f) of this section applies to taxable years to which §§1.987-1 through 1.987-10 apply as a result of such election.

§ 1.987-4T [Removed]

Par. 6. Section 1.987-4T is removed.

§ 1.987-7 [Amended]

Par. 7. Section 1.987-7 is amended by removing and reserving paragraph (b).

§ 1.987-7T [Removed]

Par. 8. Section 1.987-7T is removed.

Par. 9. Section 1.987-12 is revised to read as follows:

§1.987-12 Deferral of section 987 gain or loss.

(a) *In general*--(1) *Overview*. This section provides rules that defer the recognition of section 987 gain or loss that, but for this section, would be recognized in connection with certain QBU terminations and certain other transactions involving partnerships. This paragraph (a) provides an overview of this section and describes the section's scope of application, including with respect to QBUs subject to section 987 but to which §§1.987-1 through 1.987-11 generally do not apply. Paragraph (b) of this section describes the extent to which section 987 gain or loss is recognized under §1.987-5 or similar principles in the taxable year of a deferral event (as defined in paragraph (b)(2) of this section) with respect to a QBU. Paragraph (c) of this section describes the extent to which section 987 gain or loss that, as a result of paragraph (b), is not recognized under §1.987-5 or similar principles is recognized upon the occurrence of subsequent events. Paragraph (d) of this section describes the extent to which section 987 loss is recognized under §1.987-5 or similar principles in the taxable year of an outbound loss event (as defined in paragraph (d)(2) of this section) with respect to a QBU. Paragraph (e) of this section provides rules for determining the source and character of gains and losses that, as a result of this section, are not recognized under §1.987-5 or similar principles in the taxable year of a deferral event or outbound loss event. Paragraph (f) of this section defines controlled group and qualified successor for purposes of this section. Paragraph (g) of this section provides an anti-abuse rule. Paragraph (h) of this section provides examples illustrating the rules described in this section. Paragraph (i) of this section provides rules coordinating the application of this section with the fresh start transition method. Paragraph (j) of this section provides dates of applicability.

(2) *Scope*. This section applies to any foreign currency gain or loss realized under section 987(3), including foreign currency gain or loss of an entity described in §1.987-1(b)(1)(ii) (certain entities not otherwise subject to the regulations under section 987). References in this section to section 987 gain or loss refer to any foreign currency gain or loss realized under section 987(3), references to a section 987 QBU refer to any eligible QBU (as defined in §1.987-1(b)(3)(i), but without regard to §1.987-1(b)(3)(ii)) that is subject to section 987, and references to a section 987 aggregate partnership refer to any partnership for which the acquisition or disposition of a partnership interest could give rise to foreign currency gain or loss realized under section 987(3). Additionally, references to recognition of section 987 gain or loss under §1.987-5 encompass any determination and recognition of gain or loss under section 987(3) that would occur but for this section. Accordingly, the principles of this section apply to a QBU subject to section 987 regardless of whether the QBU otherwise is subject to §§1.987-1 through 1.987-11. An owner of a QBU that is not subject to §1.987-5 must adapt the rules set forth in this section as necessary to recognize section 987 gains or losses that are subject to this section consistent with the principles of this section.

(3) *Exceptions*--(i) *Annual deemed termination elections*. This section does not apply to section 987 gain or loss of a section 987 QBU with respect to which the annual deemed termination election described in §1.987-8(d) is in effect.

(ii) *De minimis exception*. This section does not apply to a section 987 QBU for a taxable year if the net unrecognized section 987 gain or loss of the section 987 QBU that, as a result of this section, would not be recognized under §1.987-5 in the taxable year does not exceed $5 million.

(b) *Gain and loss recognition in connection with a deferral event*--(1) *In general*. Notwithstanding §1.987-5, the owner of a section 987 QBU with respect to which a deferral event occurs (a deferral QBU) includes in taxable income section 987 gain or loss in connection with the deferral event only to the extent provided in paragraphs (b)(3) and (c) of this section. However, if the deferral event also constitutes an outbound loss event described in paragraph (d) of this section, the amount of loss recognized by the owner may be further limited under that paragraph.

(2) *Deferral event*--(i) *In general*. A deferral event with respect to a section 987 QBU means any transaction or series of transactions that satisfy the conditions described in paragraphs (b)(2)(ii) and (iii) of this section.

(ii) *Transactions*. The transaction or series of transactions include either:

(A) A termination of the section 987 QBU other than any of the following terminations: a termination described in §1.987-8(b)(3), a termination described in §1.987-8(c), or a termination described solely in §1.987-8(b)(1); or

(B) A disposition of part of an interest in a section 987 aggregate partnership or DE through which the section 987 QBU is owned, a disposition of part of a directly held section 987 QBU, or any contribution by another person to a section 987 aggregate partnership, DE, or section 987 QBU of assets that, immediately after the contribution, are not considered to be included on the books and records of an eligible QBU, provided that the contribution gives rise to a deemed transfer from the section 987 QBU to the owner. See paragraph (h) of this section, *Examples 1*, *2*, and *4*, for illustrations of this rule.

(iii) *Assets on books of successor QBU*. Immediately after the transaction or series of transactions, assets of the section 987 QBU are reflected on the books and records of a successor QBU (as defined in paragraph (b)(4) of this section).

(3) *Gain or loss recognized under §1.987-5 in the taxable year of a deferral event*. In the taxable year of a deferral event with respect to a deferral QBU, the owner of the deferral QBU recognizes section 987 gain or loss as determined under §1.987-5, except that, solely for purposes of applying §1.987-5, all assets and liabilities of the deferral QBU that, immediate-

ly after the deferral event, are reflected on the books and records of a successor QBU are treated as not having been transferred and therefore as remaining on the books and records of the deferral QBU notwithstanding the deferral event.

(4) *Successor QBU*. For purposes of this section, a section 987 QBU (potential successor QBU) is a successor QBU with respect to a section 987 QBU referred to in paragraph (b)(2)(ii) of this section if, immediately after the transaction or series of transactions described in that paragraph, the potential successor QBU satisfies all of the conditions described in paragraphs (b)(4)(i) through (iii) of this section.

(i) The books and records of the potential successor QBU reflect assets that, immediately before the transaction or series of transactions described in paragraph (b)(2)(ii) of this section, were reflected on the books and records of the section 987 QBU referred to in that paragraph.

(ii) The owner of the potential successor QBU and the owner of the section 987 QBU referred to in paragraph (b)(2)(ii) of this section immediately before the transaction or series of transactions described in that paragraph are members of the same controlled group.

(iii) In the case of a section 987 QBU referred to in paragraph (b)(2)(ii)(A) of this section, if the owner of the section 987 QBU immediately before the transaction or series of transactions described in that paragraph was a U.S. person, the potential successor QBU is owned by a U.S. person.

(c) *Recognition of deferred section 987 gain or loss in the taxable year of a deferral event and in subsequent taxable years*--(1) *In general*--(i) *Deferred section 987 gain or loss*. A deferral QBU owner (as defined in paragraph (c)(1)(ii) of this section) recognizes section 987 gain or loss attributable to the deferral QBU that, as a result of paragraph (b) of this section, is not recognized in the taxable year of the deferral event under §1.987-5 (deferred section 987 gain or loss) in the taxable year of the deferral event and in subsequent taxable years as provided in paragraphs (c)(2) through (4) of this section.

(ii) *Deferral QBU owner*. For purposes of this paragraph (c), a deferral QBU owner means, with respect to a deferral QBU, the owner of the deferral QBU immediately before the deferral event, or the owner's qualified successor.

(2) *Recognition upon a subsequent remittance*--(i) *In general*. Except as provided in paragraph (c)(3) of this section, a deferral QBU owner recognizes deferred section 987 gain or loss in the taxable year of the deferral event and in subsequent taxable years upon a remittance from a successor QBU to the owner of the successor QBU (successor QBU owner) in the amount described in paragraph (c)(2)(ii) of this section.

(ii) *Amount*. The amount of deferred section 987 gain or loss that is recognized pursuant to this paragraph (c)(2) in a taxable year of the deferral QBU owner is the outstanding deferred section 987 gain or loss (that is, the amount of deferred section 987 gain or loss not previously recognized) multiplied by the remittance proportion of the successor QBU owner with respect to the successor QBU for the taxable year ending with or within the taxable year of the deferral QBU owner, as determined under §1.987-5(b) (and, to the extent relevant, paragraphs (b) and (c)(2)(iii) of this section) without regard to any election under §1.987-8(d). For purposes of computing this remittance proportion, multiple successor QBUs of the same deferral QBU are treated as a single successor QBU. See paragraph (h) of this section, *Example 5*, for an illustration of this rule.

(iii) *Deemed remittance when a successor QBU ceases to be owned by a member of the deferral QBU owner's controlled group*. For purposes of this paragraph (c)(2), in a taxable year of the deferral QBU owner in which a successor QBU ceases to be owned by a member of a controlled group that includes the deferral QBU owner, the successor QBU owner is treated as having a remittance proportion of 1. Accordingly, if there is only one successor QBU with respect to a deferral QBU and that successor QBU ceases to be owned by a member of the controlled group that includes the deferral QBU owner, all outstanding deferred section 987 gain or loss with respect to that deferral QBU will be recognized. This paragraph (c)(2)(iii) does not affect the application of §§1.987-1 through 1.987-11 to the successor QBU owner with respect to its ownership of the successor QBU.

(3) *Recognition of deferred section 987 loss in certain outbound successor QBU terminations*. Notwithstanding paragraph (c)(2) of this section, if assets of the successor QBU (transferred assets) are transferred (or deemed transferred) in a transaction that would constitute an outbound loss event if the successor QBU had a net accumulated section 987 loss at the time of the exchange, then the deferral QBU owner recognizes outstanding deferred section 987 loss, if any, to the extent it would recognize loss under paragraph (d)(1) of this section if (i) the deferral QBU owner owned the successor QBU, (ii) the deferral QBU owner had net unrecognized section 987 loss with respect to the successor QBU equal to its outstanding deferred section 987 loss with respect to the deferral QBU, and (iii) the transferred assets were transferred (or deemed transferred) in an outbound loss event. Any outstanding deferred section 987 loss with respect to the deferral QBU that is not recognized as a result of the preceding sentence is recognized by the deferral QBU owner in the first taxable year in which the deferral QBU owner (including any qualified successor) ceases to be a member of a controlled group that includes the acquirer of the transferred assets or any qualified successor of such acquirer.

(4) *Special rules regarding successor QBUs*--(i) *Successor QBU with respect to a deferral QBU that is a successor QBU*. If a section 987 QBU is a successor QBU with respect to a deferral QBU that is a successor QBU with respect to another deferral QBU, the first-mentioned section 987 QBU is considered a successor QBU with respect to the second-mentioned deferral QBU. For example, if QBU A is a successor QBU with respect to QBU B, and QBU B is a successor QBU with respect to QBU C, then QBU A is a successor QBU with respect to QBU C.

(ii) *Separation of a successor QBU*. If a successor QBU with respect to a deferral QBU separates into two or more separated QBUs (as defined in §1.987-2(c)(9)(iii)), each separated QBU is considered a successor QBU with respect to the deferral QBU.

(iii) *Combination of a successor QBU*. If a successor QBU with respect to a deferral QBU combines with another section 987 QBU of the same owner, resulting in a combined QBU (as defined in §1.987-2(c)(9)(i)), the combined QBU is considered a successor QBU with respect to the deferral QBU.

(d) *Loss recognition upon an outbound loss event*--(1) *In general*. Notwithstanding §1.987-5, the owner of a section 987 QBU with respect to which an outbound loss event occurs (an outbound loss QBU) includes in taxable income in the taxable year of an outbound loss event section 987 loss with respect to that section 987 QBU only to the extent provided in paragraph (d)(3) of this section.

(2) *Outbound loss event*. An outbound loss event means, with respect to a section 987 QBU:

(i) Any termination of the section 987 QBU in connection with a transfer by a U.S. person of assets of the section 987 QBU to a foreign person that is a member of the same controlled group as the U.S. transferor immediately before the transaction or, if the transferee did not exist immediately before the transaction, immediately after the transaction (related foreign person), provided that the termination would result in the recognition of section 987 loss with respect to the section 987 QBU under §1.987-5 and paragraph (b) of this section but for this paragraph (d); or

(ii) Any transfer by a U.S. person of part of an interest in a section 987 aggregate partnership or DE through which the U.S. person owns the section 987 QBU to a related foreign person that has the same functional currency as the section 987 QBU, or any contribution by such a related foreign person to such a partnership or DE of assets that, immediately after the contribution, are not considered to be included on the books and records of an eligible QBU, provided that the transfer would result in the recognition of section 987 loss with respect to the section 987 QBU under §1.987-5 and paragraph (b) of this section but for this paragraph (d). See paragraph (h) of this section, *Example 3*, for an illustration of this rule.

(3) *Loss recognized upon an outbound loss event*. In the taxable year of an outbound loss event with respect to an outbound loss QBU, the owner of the outbound loss QBU recognizes section 987 loss as determined under §1.987-5 and paragraphs (b) and (c) of this section, except that, solely for purposes of applying §1.987-5, the following assets and liabilities of the outbound loss QBU are treated as not having been transferred and therefore as remaining on the books and records of the outbound loss QBU notwithstanding the outbound loss event:

(i) In the case of an outbound loss event described in paragraph (d)(2)(i) of this section, assets and liabilities that, immediately after the outbound loss event, are reflected on the books and records of the related foreign person described in that paragraph or of an eligible QBU owned by such related foreign person; and

(ii) In the case of an outbound loss event described in paragraph (d)(2)(ii) of this section, assets and liabilities that, immediately after the outbound loss event, are reflected on the books and records of the eligible QBU from which the assets and liabilities of the outbound loss QBU are allocated and not on the books and records of a section 987 QBU.

(4) *Adjustment of basis of stock received in certain nonrecognition transactions*. If an outbound loss event results from the transfer of assets of the outbound loss QBU in a transaction described in section 351 or section 361, the basis of the stock that is received in the transaction is increased by an amount equal to the section 987 loss that, as a result of this paragraph (d), is not recognized with respect to the outbound loss QBU in the taxable year of the outbound loss event (outbound section 987 loss).

(5) *Recognition of outbound section 987 loss that is not converted into stock basis*. Outbound section 987 loss attributable to an outbound loss event that is not described in paragraph (d)(4) of this section is recognized by the owner of the outbound loss QBU in the first taxable year in which the owner or any qualified successor of the owner ceases to be a member of a controlled group that includes the related foreign person referred to in paragraph (d)(2)(i) or (ii) of this section, or any qualified successor of such person.

(e) *Source and character*--(1) *Deferred section 987 gain or loss and certain outbound section 987 loss*. The source and character of deferred section 987 gain or loss recognized pursuant to paragraph (c) of this section, and of outbound section 987 loss recognized pursuant to paragraph (d)(5) of this section, is determined under §1.987-6 as if such deferred section 987 gain or loss were recognized pursuant to §1.987-5 without regard to this section on the date of the related deferral event or outbound loss event.

(2) *Outbound section 987 loss reflected in stock basis*. If loss is recognized on the sale or exchange of stock described in paragraph (d)(4) of this section within two years of the outbound loss event described in that paragraph, then, to the extent of the outbound section 987 loss, the source and character of the loss recognized on the sale or exchange is determined under §1.987-6 as if such loss were section 987 loss recognized pursuant to §1.987-5 without regard to this section on the date of the outbound loss event.

(f) *Definitions*--(1) *Controlled group*. For purposes of this section, a controlled group means all persons with the relationships to each other specified in sections 267(b) or 707(b).

(2) *Qualified successor*. For purposes of this section, a qualified successor with respect to a corporation (transferor corporation) means another corporation (acquiring corporation) that acquires the assets of the transferor corporation in a transaction described in section 381(a), but only if (A) the acquiring corporation is a domestic corporation and the transferor corporation was a domestic corporation, or (B) the acquiring corporation is a controlled foreign corporation (as defined in section 957(a)) (CFC) and the transferor corporation was a CFC. A qualified successor of a corporation includes the qualified successor of a qualified successor of the corporation.

(g) *Anti-abuse*. No section 987 loss is recognized under §1.987-5 or this section in connection with a transaction or series of transactions that are undertaken with a principal purpose of avoiding the purposes of this section.

(h) *Examples*. The following examples illustrate the application of this section. For purposes of the examples, DC1 is a domestic corporation that owns all of the stock of DC2, which is also a domestic corporation, and CFC1 and CFC2 are CFCs. In addition, DC1, DC2, CFC1, and CFC2 are members of a controlled group as defined in paragraph (f)(1) of this section, and the de minimis rule of paragraph (a)(3)(ii) of this section is not applicable. Finally, except as otherwise provided, Business A is a section 987 QBU with the euro as its functional currency, there are no transfers between Business A and its owner, and Business A's assets are not depreciable or amortizable.

(1) Example 1. Contribution of a section 987 QBU to a member of the controlled group. (i) *Facts*. DC1 owns all of the interests in Business A. The balance sheet of Business A reflects assets with an aggregate adjusted basis of €1,000x and no liabilities. DC1 contributes €900x of Business A's assets to DC2 in an exchange to which section 351 applies. Immediately after the contribution, the remaining €100x of Business A's assets are no longer reflected on the books and records of a section 987 QBU. DC2, which has the U.S. dollar as its functional currency, uses the former Business A assets in a business (Business B) that constitutes a section 987 QBU. At the time of the contribution, Business A has net accumulated unrecognized section 987 gain of $100x.

(ii) *Analysis*. (A) Under §1.987-2(c)(2)(ii), DC1's contribution of €900x of Business A's assets to DC2 is treated as a transfer of all of the assets of Business A to DC1, immediately followed by DC1's contribution of €900x of Business A's assets to DC2. The contribution of Business A's assets is a deferral event within the meaning of paragraph (b)(2) of this section because:

(*1*) The transfer from Business A to DC1 is a transfer of substantially all of Business A's assets to DC1, resulting in a termination of Business A under §1.987-8(b)(2); and

(*2*) Immediately after the transaction, assets of Business A are reflected on the books and records of Business B, a section 987 QBU owned by a member of DC1's controlled group and a successor QBU within the meaning of paragraph (b)(4) of this section. Accordingly, Business A is a deferral QBU within the meaning of paragraph (b)(1) of this section, and DC1 is a deferral QBU owner of Business A within the meaning of paragraph (c)(1)(ii) of this section.

(B) Under paragraph (b)(3) of this section, DC1's taxable income in the taxable year of the deferral event includes DC1's section 987 gain or loss determined with respect to Business A under §1.987-5, except that, for purposes of applying §1.987-5, all assets and liabilities of Business A that are reflected on the books and records of Business B immediately after Business A's termination are treated as not having been transferred and therefore as though they remained on Business A's books and records (notwithstanding the deemed transfer of those assets under §1.987-8(e)). Accordingly, in the taxable year of the deferral event, DC1 is treated as making a remittance of €100x, corresponding to the assets of Business A that are no longer reflected on the books and records of a section 987 QBU, and is treated as having a remittance proportion with respect to Business A of 0.1, determined by dividing the €100x remittance by the sum of the remittance and the €900x aggregate adjusted basis of the gross assets deemed to remain on Business A's books at the end of the year. Thus, DC1 recognizes $10x of section 987 gain in the taxable year of the deferral event. DC1's deferred section 987 gain equals $90x, which is the amount of section 987 gain that, but for the application of paragraph (b) of this section, DC1 would have recognized under §1.987-5 ($100x), less the amount of section 987 gain recognized by DC1 under §1.987-5 and this section ($10x).

(2) Example 2. Election to be classified as a corporation. (i) *Facts*. DC1 owns all of the interests in Entity A, a DE. Entity A conducts Business A, which has net accumulated unrecognized section 987 gain of $500x. Entity A elects to be classified as a corporation under §301.7701-3(a). As a result of the election and pursuant to §301.7701-3(g)(1)(iv), DC1 is treated as contributing all of the assets and liabilities of Business A to newly-formed CFC1, which has the euro as its functional currency. Immediately after the contribution, the assets and liabilities of Business A are reflected on CFC1's balance sheet.

(ii) *Analysis*. Under §1.987-2(c)(2)(ii), DC1's contribution of all of the assets and liabilities of Business A to CFC1 is treated as a transfer of all of the assets and liabilities of Business A to DC1, followed immediately by DC1's contribution of those assets and liabilities to CFC1. Because the deemed transfer from Business A to DC1 is a transfer of substantially all of Business A's assets to DC1, the Business A QBU terminates under §1.987-8(b)(2). The contribution of Business A's assets is not a deferral event within the meaning of paragraph (b)(2) of this section because, immediately after the transaction, no assets of Business A are reflected on the books and records of a successor QBU within the meaning of paragraph (b)(4) of this section due to the fact that the assets of Business A are not reflected on the books and records of a section 987 QBU immediately after the termination as well as the fact that the requirement of paragraph (b)(4)(iii) of this section is not met. Accordingly, DC1 recognizes section 987 gain with respect to Business A under §1.987-5 without regard to this section. Because the requirement of paragraph (b)(4)(iii) of this section is not met, the result would be the same even if the assets of Business A were transferred in a section 351 exchange to an existing foreign corporation that had a different functional currency than Business A.

(3) Example 3. Outbound loss event. (i) *Facts*. The facts are the same as in *Example 2 in paragraph (h)(2) of this section*, except that Business A has net accumulated unrecognized section 987 loss of $500x rather than net accumulated unrecognized section 987 gain of $500x.

(ii) *Analysis*. (A) The analysis of the transactions under §§1.987-2(c)(2)(ii), 1.987-8(b)(2), and paragraph (b) of this section is the same as in *Example 2 in paragraph (h)(2) of this section*. However, the termination of Business A as a result of the transfer of the assets of Business A by a U.S. person (DC1) to a foreign person (CFC1) that is a member of DC1's controlled group is an outbound loss event described in paragraph (d)(2) of this section.

(B) Under paragraphs (d)(1) and (3) of this section, in the taxable year of the outbound loss event, DC1 includes in taxable income section 987 loss recognized with respect to Business A as determined under §1.987-5, except that, for purposes of applying §1.987-5, all assets and liabilities of Business A that are reflected on the books and records of CFC1, a related foreign person described in paragraph (d)(2) of this section, are treated as not having been transferred. Accordingly, DC1's remittance proportion with respect to Business A is 0, and DC1 recognizes no section 987 loss with respect to Business A. DC1's outbound section 987 loss is $500x, which is the amount of section 987 loss that DC1 would have recognized under §1.987-5 ($500x) without regard to paragraph (d) of this section, less the amount of section 987 loss recognized by DC1 under paragraph (d)(3) of this section ($0). Under paragraph (d)(4) of this section, DC1 must increase its basis in its CFC1 shares by the amount of the outbound section 987 loss ($500x).

(4) Example 4. Conversion of a DE to a partnership. (i) *Facts*. (A) DC1 owns all of the interests in Entity A, a DE that conducts Business A. On the last day of Year 1, DC1 sells 50 percent of its interest in Entity A to DC2 (the Entity A sale).

(B) For Federal income tax purposes, Entity A is converted to a partnership when DC2 purchases the 50 percent interest in Entity A. DC2's purchase is treated as the purchase of 50 percent of the assets of Entity A (that is, the assets of Business A), which, prior to the purchase, were treated as held directly by DC1 for Federal income tax purposes. Immediately after DC2's deemed purchase of 50 percent of Business A assets, DC1 and DC2 are treated as contributing their respective interests in Business A assets to a partnership. *See* Rev. Rul. 99-5, 1999-1 CB 434 (situation 1). In connection with the deemed contribution, DC1 and DC2 agree to share equally in all items of the partnership's profits and loss, and, for purposes of §1.987-7, to determine their share of assets and liabilities of the resulting partnership in accordance with their respective shares of partnership profits.

(ii) *Analysis*. (A) The transactions deemed to occur under Rev. Rul. 99-5 are not taken into account for purposes of this section. The Entity A sale and resulting existence of a partnership, however, have consequences under section 987 and this section, as described in this Example 4 in paragraphs (h)(4)(ii)(B) through (D) of this section.

(B) Immediately after the Entity A sale, Entity A is a section 987 aggregate partnership within the meaning of §1.987-1(b)(5) because DC1 and DC2 own all the interests in partnership capital and profits, DC1 and DC2 are related within the meaning of section 267(b), and the partnership has an eligible QBU (Business A) that would be a section 987 QBU with respect to a partner if owned by the partner directly. As a result of the Entity A sale, 50 percent of the assets and liabilities of Business A ceased to be reflected on the books and records of DC1's Business A section 987 QBU. As a result, such assets and liabilities are treated as if they were transferred from DC1's Business A section 987

QBU to DC1. Additionally, following DC2's acquisition of 50 percent of the interest in Entity A, DC2 is allocated 50 percent of the assets and liabilities of Business A under §§1.987-2(b). Because DC2 and Business A have different functional currencies, DC2's portion of the Business A assets and liabilities constitutes a section 987 QBU. Accordingly, 50 percent of the assets and liabilities of Business A are treated as transferred by DC2 to DC2's Business A section 987 QBU.

(C) The Entity A sale is a deferral event described in paragraph (b)(2) of this section because:

(1) The sale constitutes the disposition of part of an interest in a DE; and

(2) Immediately after the transaction, assets of DC1's Business A section 987 QBU are reflected on the books and records of DC1's Business A section 987 QBU and DC2's Business A section 987 QBU, each of which is a successor QBU with respect to DC1's Business A section 987 QBU within the meaning of paragraph (b)(4) of this section. Accordingly, DC1's Business A section 987 QBU is a deferral QBU within the meaning of paragraph (b)(1) of this section, and DC1 is a deferral QBU owner within the meaning of paragraph (c)(1)(ii) of this section. Under paragraph (b)(1) of this section, DC1 includes in taxable income section 987 gain or loss with respect to Business A in connection with the deferral event to the extent provided in paragraphs (b)(3) and (c) of this section.

(D) Under paragraph (b) of this section, in the taxable year of the Entity A sale, DC1 includes in taxable income section 987 gain or loss with respect to Business A as determined under §1.987-5, except that, for purposes of applying §1.987-5, all assets and liabilities of Business A that, immediately after the Entity A sale, are reflected on the books and records of successor QBUs are treated as though they were not transferred and therefore as remaining on the books and records of DC1's Business A section 987 QBU notwithstanding the Entity A sale. Accordingly, DC1's remittance amount under §1.987-5 is $0, and DC1 recognizes no section 987 gain or loss with respect to Business A.

(5) Example 5. Partial recognition of deferred gain or loss. (i) *Facts*. DC1 owns all of the interests in Entity A, a DE that conducts Business A in Country X. During Year 1, DC1 contributes all of its interests in Entity A to DC2 in an exchange to which section 351 applies. At the time of the contribution, Business A has net accumulated unrecognized section 987 gain of $100x. After the contribution, Entity A continues to conduct business in Country X (Business B). In Year 3, as a result of a net transfer of property from Business B to DC2, DC2's remittance proportion with respect to Business B, as determined under §1.987-5, is 0.25.

(ii) *Analysis*. (A) For the reasons described in *Example 1 in paragraph (h)(1) of this section*, the contribution of Entity A by DC1 to DC2 results in a termination of Business A and a deferral event with respect to Business A, a deferral QBU; DC1 is a deferral QBU owner within the meaning of paragraph (c)(1)(ii) of this section; Business B is a successor QBU with respect to Business A; DC2 is a successor QBU owner; and the $100x of net accumulated unrecognized section 987 gain with respect to Business A becomes deferred section 987 gain as a result of the deferral event.

(B) Under paragraph (c)(1) of this section, DC1 recognizes deferred section 987 gain with respect to Business A in accordance with paragraphs (c)(2) through (4) of this section. Under paragraph (c)(2)(i) of this section, DC1 recognizes deferred section 987 gain in Year 3 as a result of the remittance from Business B to DC2. Under paragraph (c)(2)(ii) of this section, the amount of deferred section 987 gain that DC1 recognizes is $25x, which is DC1's outstanding deferred section 987 gain or loss ($100x) with respect to Business A multiplied by the remittance proportion (0.25) of DC2 with respect to Business B for the taxable year as determined under §1.987-5(b).

(i) *Coordination with fresh start transition method*--(1) *In general*. If a taxpayer is a deferral QBU owner, or is or was the owner of an outbound loss QBU, and the taxpayer is required under §1.987-10(a) to apply the fresh start transition method described in §1.987-10(b) to the deferral QBU or outbound loss QBU, or would have been so required if the taxpayer had owned the deferral QBU or outbound loss QBU on the transition date (as defined in §1.987-11(c)), the adjustments described in paragraphs (i)(2) and (3) of this section, as applicable, must be made on the transition date.

(2) *Adjustment to deferred section 987 gain or loss*. The amount of any outstanding deferred section 987 gain or loss of a deferral QBU owner with respect to a deferral QBU described in paragraph (i)(1) of this section must be adjusted to equal the amount of outstanding deferred section 987 gain or loss that the deferral QBU owner would have had with respect to the deferral QBU on the transition date if, immediately before the deferral event, the deferral QBU had transitioned to the method prescribed by §§1.987-1 through 1.987-10 pursuant to the fresh start transition method.

(3) *Adjustments in the case of an outbound loss event*. The basis of any stock described in paragraph (d)(4) of this section that was received in connection with the transfer (or deemed transfer) of assets of an outbound loss QBU described in paragraph (i)(1) of this section and that is held on the transition date must be adjusted to equal the basis that such stock would have had on the transition date if, immediately prior to the outbound loss event, the outbound loss QBU had transitioned to the method prescribed by §§1.987-1 through 1.987-10 pursuant to the fresh start transition method. If no such stock was received, the amount of any outbound section 987 loss with respect to the outbound loss QBU that may be recognized on or after the transition date pursuant to paragraph (d)(5) of this section must be adjusted to equal the amount of such loss that would be outstanding and that may be recognized pursuant to that paragraph if, immediately before the outbound loss event, the outbound loss QBU had transitioned to the method prescribed by §§1.987-1 through 1.987-10 pursuant to the fresh start transition method.

(j) *Applicability date*--(1) *In general*. Except as described in paragraph (j)(2) of this section, this section applies to any deferral event or outbound loss event that occurs on or after January 6, 2017. This section also applies to any deferral event or outbound loss event that occurs as a result of an entity classification election made under §301.7701-3 that is filed on or after January 6, 2017, and that is effective before January 6, 2017.

(2) *Exceptions*--(i) *Principal purpose*. This section applies to any deferral event or outbound loss event occurring on or after December 7, 2016, if such deferral event or outbound loss event was undertaken with a principal purpose of recognizing section 987 loss.

(ii) *Entity classification*. This section also applies to any deferral event or outbound loss event that occurs as a result of an entity classification election made under §301.7701-3 that was filed on or after December 22, 2016, that was effective before December 7, 2016, and that was undertaken with a principal purpose of recognizing section 987 loss.

§ 1.987-12T [Removed]

Par. 10. Section 1.987-12T is removed.

Kirsten Wielobob,
Deputy Commissioner for Services and Enforcement.

Approved: April 8, 2019.

David J. Kautter,
Assistant Secretary of the Treasury (Tax Policy).

T.D. 9858

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 300

User Fees Relating to Enrolled Agents and Enrolled Retirement Plan Agents

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains final regulations that amend regulations relating to imposing user fees for enrolled agents and enrolled retirement plan agents. The final regulations remove the initial enrollment user fee for enrolled retirement plan agents because the IRS no longer offers initial enrollment as an enrolled retirement plan agent. The final regulations also increase the amount of the renewal user fee for enrolled retirement plan agents from $30 to $67. In addition, the final regulations increase the amount of both the enrollment and renewal user fee for enrolled agents from $30 to $67. The final regulations affect individuals who are, or apply to become, enrolled agents and individuals who are enrolled retirement plan agents. The Independent Offices Appropriations Act of 1952 authorizes charging user fees.

DATES: *Effective date*: This regulation is effective June 12, 2019.

Applicability Date: For the dates of applicability, see §§300.5(d), 300.6(d), and 300.10(d).

FOR FURTHER INFORMATION CONTACT: Mark Shurtliff at (202) 317-6845 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

This document contains amendments to 26 CFR part 300 regarding user fees.

A. User Fee Authority and Enrolled Agent and Enrolled Retirement Plan Agent User Fees

The Independent Offices Appropriations Act of 1952 (IOAA) (31 U.S.C. 9701) authorizes each agency to promulgate regulations establishing a charge for services the agency provides (user fees). The charges must be fair and must be based on the costs to the government, the value of the service to the recipient, the public policy or interest served, and other relevant facts. Under the IOAA, user fee regulations are subject to policies prescribed by the President. Those policies are currently set forth in the Office of Management and Budget (OMB) Circular A-25, 58 FR 38142 (July 15, 1993).

Under OMB Circular A-25, Federal agencies that provide services that confer special benefits on identifiable recipients beyond those accruing to the general public are to establish user fees that recover the full cost of providing the special benefit. An agency that seeks to impose a user fee for government-provided services must calculate the full cost of providing those services, review user fees biennially, and update them as necessary. Section 330(a)(1) of title 31 of the United States Code authorizes the Secretary of the Treasury to regulate the practice of representatives before the Department of the Treasury (Treasury Department). Pursuant to section 330 of title 31, the Secretary has published regulations governing practice before the IRS in 31 CFR part 10 and reprinted the regulations as Treasury Department Circular No. 230 (Circular 230). Section 10.3 of Circular 230 defines who may practice before the IRS and includes individuals who have been granted enrollment to practice as enrolled agents and enrolled retirement plan agents. Section 10.4 of Circular 230 authorizes the IRS to grant enrollment as an enrolled agent or enrolled retirement plan agent to individuals who demonstrate special competence in tax matters by passing a written examination administered by, or under the oversight of, the IRS and who have not engaged in any conduct that would justify suspension or disbarment under Circular 230. Section 10.4 also authorizes the IRS to grant enrollment as an enrolled agent or an enrolled retirement plan agent to a qualifying former IRS employee by virtue of past IRS service and technical experience if the former employee has not engaged in any conduct that would justify suspension or disbarment under the provisions of Circular 230 and meets certain other requirements. The ability to practice before the IRS is a special benefit that is conferred on enrolled agents and enrolled retirement plan agents that does not accrue to the general public.

Once eligible for enrollment as an enrolled agent, whether by examination or former employment with the IRS, an individual must file an application for enrollment with the IRS and pay a $30 nonrefundable user fee. To maintain active enrollment and eligibility to practice before the IRS, an individual who has been enrolled as an enrolled agent or enrolled retirement plan agent must file an application to renew enrollment every three years and pay a $30 nonrefundable user fee. 31 CFR 10.6(d).

As required by the IOAA and OMB Circular A-25, the IRS Return Preparer Office (RPO) completed its 2017 biennial review of the enrollment and renewal user fees associated with enrolled agents and enrolled retirement plan agents. As discussed in section B of this preamble, during its review the RPO took into account the increase in labor, benefits, and overhead costs incurred in connection with providing services to individuals who enroll or renew enrollment as enrolled agents and enrolled retirement plan agents since the user fee was last changed in 2011. In addition, RPO determined that costs associated with Federal tax-compliance checks and suitability checks on enrolled individuals should be recovered as part of the user fee for administering the enrollment and renewal programs. The 2017 biennial review also took into account new costs associated with administering the program for enrolled agents and enrolled retirement plan agents, including the costs of operating a dedicated toll-free helpline in the RPO for enrollment and renewal matters.

B. *Calculation of the User Fee*

The IRS follows generally accepted accounting principles (GAAP) in calculating the full cost of administering the program for enrollment or renewal. GAAP is established by the Financial Accounting Standards Board (FASB). Recognition of costs is based on Statement of Federal Financial Accounting Standards (SFFAS) No. 4: Managerial Cost Accounting Concepts and Standards for the Federal Government, issued by the Federal Accounting Standard Advisory Board (FASAB). The FASAB Handbook of Federal Accounting Standards and Other Pronouncements, as Amended, is available at https://files.fasab.gov/pdffiles/2018_fasab_handbook.pdf.

1. *Cost Center Allocation*

The IRS determines the cost of its services and activities using a cost-accounting system that tracks costs to organizational units. The lowest organizational unit in the IRS's cost-accounting system is a cost center. Cost centers are usually separate offices that are distinguished by subject-matter area of responsibility or geographic region. Costs of operating a cost center are recorded in the IRS's cost-accounting system. Costs of user fees include direct costs, such as labor, and indirect costs. Indirect costs are not easily traceable and are allocated using a method or by applying an overhead rate.

2. *Determining the Per Unit Cost*

To establish the per-unit cost, the total cost of providing the service is divided by the volume of services provided.

3. *Cost Estimation of Direct Labor*

Not all cost centers are fully devoted to one service for which the IRS charges user fees. Some cost centers work on a number of different services across the IRS. In these cases, the IRS uses various cost-measurement techniques to estimate the cost incurred in those cost centers attributable to the program. These techniques include using various timekeeping systems to measure the time required to accomplish activities, or using information provided by subject-matter experts on the time devoted to a program. Once the IRS has estimated the average time required to accomplish an activity, it multiplies that time estimate by the relevant organizational unit's average labor and benefits cost per unit of time to determine the labor and benefits cost incurred to provide the service. To determine the full cost, IRS then adds overhead as discussed below.

4. *Overhead*

Overhead is an indirect cost of operating an organization that cannot be immediately associated with an activity that the organization performs. Overhead includes costs of resources that are jointly or commonly consumed by one or more organizational unit's activities but are not specifically identifiable to a single activity.

These costs can include:

- General management and administrative services of sustaining and supporting organizations.
- Facilities management and ground maintenance services (security, rent, utilities, and building maintenance).
- Procurement and contracting services.
- Financial management and accounting services.
- Information technology services.
- Services to acquire and operate property, plants and equipment.
- Publication, reproduction, and graphics and video services.
- Research, analytical, and statistical services.
- Human resources/personnel services.
- Library and legal services.

To calculate the overhead allocable to a service, the IRS multiplies a Corporate Overhead rate by the labor and benefits costs determined as discussed previously. The IRS calculates the Corporate Overhead rate annually based on cost elements underlying the Statement of Net Cost included in the IRS Annual Financial Statements, which are audited by the Government Accountability Office. The Corporate Overhead rate is the ratio of the sum of the IRS's indirect labor and benefits costs from the supporting and sustaining organizational units—those that do not interact directly with taxpayers—and all non-labor costs to the IRS's labor and benefits costs of its organizational units that interact directly with taxpayers.

The Corporate Overhead rate of 68.00 percent for costs reviewed during FY 2017 was calculated based on FY 2016 costs (which are assumed to be fixed and reoccurring) as follows:

Indirect Labor and Benefits Costs		$1,681,373,747
Non-Labor Costs	+	$2,879,907,032
Total Indirect Costs		$4,561,280,779
Direct Labor and Benefits Costs	÷	$6,708,063,559
Corporate Overhead Rate		68.00%

5. *Calculation of the Per Unit Cost of the User Fee*

The IRS used projections for fiscal years 2018 through 2020 to determine the direct costs associated with enrolled agent enrollment and renewal and enrolled retirement plan agent renewal. Direct costs are incurred by the RPO and include labor costs for enrollment and renewal submission processing; tax compliance and background checks; continuing education and testing-related activities; and communications, which include the new toll-free helpline.

The labor and benefits for the work performed related to administering the program for enrolled agent enrollment and renewal and enrolled retirement plan agent renewal is projected to be $2,708,603 in total over fiscal years 2018 through 2020. The labor and benefits costs include the cost to perform background checks and tax compliance checks, which are services that were not included in the previous $30 user fee. The number of enrollment and renewal applications is based on the FY2016 numbers adjusted by the anticipated increase in enrollment. Adding Corporate Overhead expenses to the total labor and benefits results in total costs of $4,550,453 as shown below:

Labor and Benefits	$2,708,603
Corporate Overhead (68%)	$1,841,850
Labor, Benefits, and Overhead	$4,550,453

Dividing this total cost by the projected population of initial enrollment and renewal applications for fiscal years 2018 through 2020 results in a cost per application of $67 as shown below:

Labor, Benefits and Overhead	$4,550,453
Number of Applications	÷ 68,343
Cost Per Application	$ 67

Taking into account the full amount of these costs, the RPO determined that the full cost of administering the program for enrolled agents and enrolled retirement plan agents has increased from $30 to $67 per application for enrollment or renewal. The user fee complies with the directive in OMB Circular A-25 to recover the full cost of providing a service that confers special benefits on identifiable recipients beyond those accruing to the general public.

C. *Notice of Proposed Rulemaking and Final Regulations*

On November 19, 2018, a notice of proposed rulemaking (REG-122898-17) proposing to amend the regulations relating to imposing user fees for enrolled agents and retirement plan agents was published in the **Federal Register** (83 FR 58202). The notice proposed removing the initial enrollment user fee for enrolled retirement plan agents because the IRS no longer offers initial enrollment as an enrolled retirement plan agent.

The notice also proposed increasing the amount of the renewal user fee for enrolled retirement plan agents from $30 to $67. In addition, the notice proposed increasing the amount of both the enrollment and renewal user fees for enrolled agents from $30 to $67. The notice contains a detailed explanation regarding the amendments to these regulations.

Two comments responding to the notice were received. A public hearing on the notice was scheduled for January 24, 2019. As stated in the notice, requests to speak and outlines of topics to be discussed at the hearing were required to be submitted by January 18, 2019. On January 22, 2019, the public hearing was cancelled due to a lapse in appropriations (IR-2019-05). Because no requests to speak at the hearing had been received, the hearing was not rescheduled. After consideration of the comments, this Treasury Decision adopts the regulations proposed by the notice without change.

Summary of Comments

Two comments were submitted on the notice of proposed rulemaking. The comments are available at *www.regulations.gov* or upon request.

One of the comments agreed with the proposed user fee regulations because the commenter's status as an enrolled agent allows him to earn income by representing taxpayers before the IRS. The comment stated that the commenter supported the increase, so long as the user fees comply with the relevant authorities. As discussed in the background section of this preamble, the IOAA authorizes each agency to promulgate regulations that impose user fees for services the agency provides to identifiable recipients. User fee regulations under the IOAA are subject to policies prescribed by the President, which are set forth in OMB Circular A-25. As described in the background section of this preamble, the Treasury Department and IRS complied with the requirements of the IOAA and OMB Circular A-25 in promulgating these regulations. The notice of proposed rulemaking and the background section of this preamble provide a detailed analysis of how the RPO determined the full cost of providing services to enrolled agents and enrolled retirement plan agents (83 FR 58202). Accordingly, the user fee complies with the relevant authorities.

The other comment generally disagreed with enrollment and renewal user fees associated with enrolled agents and enrolled retirement plan agents. The comment stated that the Federal government should bear the full cost of administering programs related to tax professionals. This comment was not accepted because it is contrary to the policies prescribed by the President as set forth in OMB Circular A-25. Accordingly, the proposed regulations are adopted without change.

Special Analyses

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

OIRA has determined that this regulation is significant and subject to review under section 6(b) of Executive Order 12866.

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that this regulation will not have a significant economic impact on a substantial number of small entities. The user fee primarily affects individuals who are enrolled agents, apply to become enrolled agents, or are enrolled retirement plan agents. Only individuals, not businesses, can be enrolled agents or enrolled retirement plan agents. Thus, any economic impact of the user fee on small entities generally will occur only when an enrolled agent or enrolled retirement plan agent owns a small business or when a small business employs enrolled agents or enrolled retirement plan agents and reimburses them for their renewal fees. The Treasury Department and IRS estimate that approximately 22,781 individuals will apply annually for enrollment as an enrolled agent, renewal as an enrolled agent, or renewal as an enrolled retirement plan agent. Due to the relatively small number of small businesses that employ enrolled agents or enrolled retirement plan agents, a substantial number of small entities are not likely to be affected. Further, the economic impact on any small entities affected would be limited to paying the $37 difference in cost between the $67 user fee and the previous $30 user fee for each enrolled agent or enrolled retirement plan agent that a small entity employs and reimburses, or otherwise pays for, the cost of the user fee. The total economic impact of this regulation is thus approximately $842,897 annually, which is the product of the approximately 22,781 individuals and the $37 increase in the fee which is not a significant economic impact. Accordingly, it is certified that the rule will not have a significant economic impact on a substantial number of small entities.

It is not anticipated that the increase in user fee that is paid every three years and averages to $12.33 per year will negatively affect enrollment, which has historically remained steady as user fee amounts have changed. Pursuant to section 7805(f), the notice of proposed rulemaking was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business (83 FR 58202). No comments on the notice were received from the Chief Counsel for Advocacy of the Small Business Administration.

Drafting Information

The principal author of these regulations is Mark Shurtliff of the Office of the Associate Chief Counsel (Procedure and Administration). Other personnel from the Treasury Department and the IRS participated in their development.

List of Subjects in 26 CFR Part 300

Reporting and recordkeeping requirements, User fees.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 300 is amended as follows:

PART 300—USER FEES

Paragraph. 1. The authority citation for part 300 continues to read as follows:

Authority: 31 U.S.C. 9701.

§300.0 [Amended]

Par. 2. Section 300.0 is amended by removing paragraph (b)(10) and redesignating paragraphs (b)(11) through (13) as paragraphs (b)(10) through (12).

Par. 3. Section 300.5 is amended by revising paragraphs (b) and (d) to read as follows:

§300.5 Enrollment of enrolled agent fee.

* * * * *

(b) *Fee*. The fee for initially enrolling as an enrolled agent with the IRS is $67.

* * * * *

(d) *Applicability date.* This section applies beginning June 12, 2019.

Par. 4. Section 300.6 is amended by revising paragraphs (b) and (d) to read as follows:

§300.6 Renewal of enrollment of enrolled agent fee.

* * * * *

(b) *Fee*. The fee for renewal of enrollment as an enrolled agent with the IRS is $67.

* * * * *

(d) *Applicability date.* This section applies beginning June 12, 2019.

§300.10 [Removed]

Par. 5. Section 300.10 is removed.

§300.11 [Redesignated as §300.10 and Amended]

Par. 6. Redesignate §300.11 as §300.10 and amend newly redesignated §300.10 by revising paragraphs (b) and (d) to read as follows:

§300.10 Renewal of enrollment of enrolled retirement plan agent fee.

* * * * *

(b) *Fee*. The fee for renewal of enrollment as an enrolled retirement plan agent with the IRS is $67.

* * * * *

(d) *Applicability date.* This section applies beginning June 12, 2019.

§§ 300.12 and 300.13 [Redesignated as §§ 300.11 and 300.12]

Par. 7. Redesignate §§300.12 and 300.13 as §§300.11 and 300.12.

Kirsten Wielobob,
Deputy Commissioner for Services
and Enforcement.

Approved: April 19, 2019.

David J. Kautter
Assistant Secretary of the Treasury
(Tax Policy).

Part III.

Request for Comments on Necessary Clarifications to Normalization Requirements for Excess Tax Reserves Resulting from the Corporate Tax Rate Decrease

Notice 2019-33

SECTION 1. PURPOSE

This notice announces that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) intend to issue guidance under § 168 of the Internal Revenue Code to clarify the normalization requirements for excess tax reserves resulting from the corporate tax rate decrease in the Tax Cuts and Jobs Act (TCJA), Pub. L. 115-97 (131 Stat. 2054). This notice requests comments about ratemaking issues that have arisen or are anticipated due to the corporate tax rate decrease and the requirements of section 13001(d) of the TCJA.

SECTION 2. BACKGROUND

In general, normalization is a system of accounting used by regulated public utilities to reconcile the tax treatment of accelerated depreciation of public utility assets with their regulatory treatment. Under normalization, a utility receives the tax benefit of accelerated depreciation in the early years of an asset's regulatory useful life and passes that benefit through to ratepayers ratably over the regulatory useful life of the asset in the form of reduced rates.

Section 168 of the Code generally allows taxpayers to compute their depreciation deduction for federal income tax purposes under the accelerated cost recovery system. Section 168(f)(2) provides that § 168 does not apply to any public utility property, as defined in § 168(i)(10), if the taxpayer does not use a normalization method of accounting. Section 168(i)(9) describes what constitutes a "normalization method of accounting."

In order to use a normalization method of accounting, § 168(i)(9)(A)(i) requires a taxpayer, in computing its tax expense for establishing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account (regulated tax expense), to use a method of depreciation for property that is the same as, and a depreciation period for such property that is no shorter than, the method and period used to compute its depreciation expense for establishing its cost of service for ratemaking purposes. Under § 168(i)(9)(A)(ii), if the amount allowable as a deduction under § 168 differs from the amount that would be allowable as a deduction under § 167 using the method, period, first and last year convention, and salvage value used to compute regulated tax expense under § 168(i)(9)(A)(i), then the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from such difference.

Former § 167(l) generally contained the requirements discussed above regarding permitting public utilities to use accelerated methods for calculating depreciation only if they used a "normalization method of accounting." The requirements for establishing and adjusting the reserve required by § 168(i)(9)(A)(ii) are contained in § 1.167(l)-1 of the Income Tax Regulations.

Section 1.168(i)–3, finalized in 2008 (2008 regulations), provides rules on the treatment of excess deferred income tax reserve upon disposition of deregulated public utility property.

Section 1.168(i)-3(a)(1) generally provides rules for the application of section 203(e) of the Tax Reform Act of 1986 (1986 Act), Public Law 99–514 (100 Stat. 2146), to a taxpayer with respect to public utility property (within the meaning of § 168(i)(10)) that ceases, whether by disposition, deregulation, or otherwise, to be public utility property with respect to the taxpayer and that is not described in § 1.168(i)-3(a)(2) (deregulated public utility property).

Section 1.168(i)-3(b) provides that if a public utility property of a taxpayer becomes deregulated public utility property to which this section applies, the reduction in the taxpayer's excess tax reserve permitted under section 203(e) of the 1986 Act is equal to the amount by which the reserve could be reduced under that provision if all such property had remained public utility property of the taxpayer and the taxpayer had continued use of its normalization method of accounting with respect to such property.

SECTION 3: TAX CUTS AND JOBS ACT

The TCJA, enacted on December 22, 2017, generally reduced the corporate tax rate under § 11 of the Code from 35 percent to 21 percent for taxable years beginning after December 31, 2017. Section 13001(a).

Section 13001(d) of the TCJA includes accompanying but uncodified normalization requirements. Section 13001(d)(1) provides that a normalization method of accounting shall not be treated as being used with respect to any public utility property for purposes of §§ 167 or 168 if the taxpayer, in computing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account, reduces the excess tax reserve more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method (ARAM).

Section 13001(d)(2) provides an alternative method for certain taxpayers. If, as of the first day of the taxable year that includes the date of enactment of the TCJA, the taxpayer was required by a regulatory agency to compute depreciation for public utility property on the basis of an average life or composite rate method, and the taxpayer's books and underlying records did not contain the vintage account data necessary to apply ARAM, the taxpayer will be treated as using a normalization method of accounting if, with respect to such jurisdiction, the taxpayer uses the alternative method for public utility property that is subject to the regulatory authority of that jurisdiction.

Section 13001(d)(3) provides definitions for purposes of section 13001(d). Section 13001(d)(3)(A) defines an "excess tax reserve" to mean the excess of the reserve for deferred taxes (as described in § 168(i)(9)(A)(ii)) as of the day before the corporate rate reductions provided in the amendments made by section 13001(a) take effect, over the amount which would be the balance in such reserve if the amount of such reserve were determined by assuming that the corporate tax rate reductions provided in the TCJA were in effect for all prior periods.

Section 13001(d)(3)(B) defines ARAM as the method under which the excess in the reserve for deferred taxes is reduced over the remaining lives of the property as used in the taxpayer's regulated books of account which gave rise to the reserve for deferred taxes. Under such method, during the time period in which the timing differences for the property reverse, the amount of the adjustment to the reserve for the deferred taxes is calculated by multiplying the ratio of the aggregate deferred taxes for the property to the aggregate timing differences for the property as of the beginning of the period in question, by the amount of the timing differences which reverse during such period.

Section 13001(d)(3)(C) defines the "alternative method" as the method in which the taxpayer computes the excess tax reserve on all public utility property included in the plant account on the basis of the weighted average life or composite rate used to compute depreciation for regulatory purposes, and reduces the excess tax reserve ratably over the remaining regulatory life of the property.

Section 13001(d)(4) provides that, for any taxable year ending after the date of the enactment of the TCJA, if the taxpayer does not use a normalization method of accounting for the corporate rate reductions provided in the amendments made by section 13001, then the taxpayer's tax for the taxable year shall be increased by the amount by which it reduces its excess tax reserve more rapidly than permitted under a normalization method of accounting, and such taxpayer shall not be treated as using a normalization method of accounting for purposes of § 168(f)(2) and (i)(9)(C).

The Joint Explanatory Text of the Committee of Conference, H. Rept. 115-466 (Conference Report), adds more clarification about the normalization rules in section 13001(d) of the TCJA. The Conference Report states that the excess tax reserve is the reserve for deferred taxes as of the day before the corporate rate reduction takes effect over what the reserve for deferred taxes would be if the corporate rate reduction had been in effect for all prior periods. Conference Report, at 343. If an excess tax reserve is reduced more rapidly or to a greater extent than such reserve would be reduced under ARAM[1], the taxpayer will not be treated as using a normalization method with respect to the corporate rate reduction. If the taxpayer does not use a normalization method of accounting for the corporate rate reduction, the taxpayer's tax for the taxable year shall be increased by the amount by which it reduces its excess tax reserve more rapidly than permitted under a normalization method of accounting and the taxpayer will not be treated as using a normalization method of accounting for purposes of § 168(f)(2) and (i)(9)(C).

The Conference Report also explains in greater detail the application of ARAM. According to the Conference Report, ARAM reduces the excess tax reserve over the remaining regulatory lives of the property that gave rise to the reserve for deferred taxes during the years in which the deferred tax reserve related to such property is reversing. *Id*. Under this method, the excess tax reserve is reduced as the timing differences reverse over the remaining life of the asset. The reversal of timing differences generally occurs when the amount of the tax depreciation taken with respect to an asset is less than the amount of the regulatory depreciation taken with respect to the asset. To ensure that the deferred tax reserve, including the excess tax reserve, is reduced to zero at the end of the regulatory life of the asset that generated the reserve, the amount of the timing difference which reverses during a taxable year is multiplied by the ratio of (1) the aggregate deferred taxes as of the beginning of the period in question to (2) the aggregate timing differences for the property as of the beginning of the period in question.

SECTION 4: THE TAX REFORM ACT OF 1986 AND REV. PROC. 88-12

For taxable years beginning on or after July 1, 1987, section 601 of the 1986 Act reduced the maximum federal income tax applicable for corporations from 46 percent to 34 percent.

Similar to section 13001(d) of the TCJA, section 203(e) of the 1986 Act provided rules for reducing the excess tax reserve resulting both from that reduction and from the smaller reduction in rates for tax years starting before and ending after July 1, 1987. Section 203(e)(2)(B) of the 1986 Act defined ARAM as the method under which the excess tax reserve is reduced over the remaining lives of the property (as used in a public utility's regulated books of account) that gave rise to the reserve for deferred taxes. Some taxpayers, however, did not necessarily have adequate data to apply ARAM because they were required by regulatory agencies to depreciate property for regulatory purposes using a weighted average life or composite rate, and such a method focuses on the entire plan and does not account for property by vintage accounts. The 1986 Act, however, did not provide taxpayers an alternative method to ARAM.

Rev. Proc. 88-12, 1988-1 C.B. 637, provides an alternative method sometimes referred to as the Reverse South Georgia Method (RSGM). Under section 4.01 of Rev. Proc. 88-12, a taxpayer uses the RSGM if it computed the excess tax reserve on all public utility property included in the plant account on the basis of the weighted average life or composite rate used to compute depreciation for regulatory purposes, and reduced the excess tax reserve ratably over the remaining regulatory life of the property. Section 5.01 of Rev. Proc. 88-12 provides generally that for eligible taxpayers the RSGM satisfied the requirements of section 203(e) of the 1986 Act.

[1]Section 13001(d)(2) provides that certain taxpayers may use the alternative method to calculate the reduction of their excess tax reserve and such taxpayers will be treated as using a normalization method of accounting.

In summary, section 13001(d)(1) of the TCJA provides ARAM as the regular method in the same manner as that provided in section 203(e)(2)(B) of the 1986 Act. Section 13001(d)(2) of the TCJA provides an alternative method that, while not specifically referred to as the RSGM, is nevertheless the same as the RSGM as originally provided in Rev. Proc. 88-12.

SECTION 5. REQUEST FOR COMMENTS

The Treasury Department and the IRS request comments on issues that should be addressed in proposed guidance to clarify the normalization requirements for excess tax reserves resulting from the corporate tax rate decrease in the TCJA and the requirements of section 13001(d) of the TCJA as well as comments regarding what form of guidance would be most useful. Specifically, the Treasury Department and the IRS request comments that address the following:

(1) Situations where taxpayers may have vintage account data in their underlying books and records in some form but such data is not necessarily useful for ARAM without significant additional analysis and expense. More specifically, comments on whether some sort of "reasonable" test should be provided, under which the use of the alternative method by a taxpayer is permissible if the cost to the taxpayer of assembling the data contained in the underlying books and records in a way necessary to apply ARAM exceeds a reasonable amount, based on a percentage of rate base or some other factor.

(2) Other fact patterns where taxpayers may use the alternative method instead of ARAM including but not limited to comments on when the RSGM is a taxpayer's current normalization method of accounting for excess deferred taxes, regardless of the availability of vintage or class information for the accumulated deferred income taxes (ADIT) that had been accrued after the 1986 Act.

(3) Net operating loss (NOL) issues including but not limited to comments on the significance of a depreciation-related NOL carryforward in the context of excess deferred taxes, and comments on whether a depreciation-related NOL as of December 31, 2017, must be analyzed for normalization purposes based on the underlying loss year.

(4) By their terms, the 2008 regulations apply only to section 203(e) of the 1986 Act, but the Treasury Department and the IRS believe it may be appropriate to extend their application to section 13001(d) of the TCJA. Comments on the ongoing relevance of the 2008 regulations including but not limited to comments on the treatment of book-only retirements and tax dispositions in regard to significant transactions (such as sales of power plants) versus day-to-day (ordinary or not significant) transactions as well as comments on transactions not addressed in the 2008 regulations such as like-kind exchanges or other dispositions of public utility property.

(5) The implementation of interim rates to reflect the TCJA's decrease in the corporate tax rate including but not limited to comments about the meaning of the phrase "reduces the excess tax reserve more rapidly or to a greater extent than such reserve would be reduced under ARAM."

(6) Whether the proration formula required by § 1.167(l)-1(h)(6)(ii) must be applied to excess deferred tax activity related to reversals (refunds) of excess deferred taxes if the company uses a future test period or a part-historical, part-future test period.

(7) Methodology of reversing protected (by the normalization rules) versus unprotected ADIT after the 2017 rate changes.

SECTION 6. ADDRESS TO SEND COMMENTS

Any comments must be received by July 29. 2019. Taxpayers may submit comments electronically via the Federal eRulemaking Portal at *www.regulations.gov* (indicate IRS and Notice 2019-33). Alternatively, taxpayers may submit hard copy submissions to:

CC:PA:LPD:PR (Notice 2019-33), Room 5203, Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, D.C., 20044

Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to:

CC:PA:LPD:PR (Notice 2019-33), Courier's Desk, Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224
Attn: CC:PA:LPD:PR

All comments received will be available for public inspection on *www.regulations.gov*.

SECTION 7. DRAFTING INFORMATION

The principal author of this notice is Martha M. Garcia of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice contact Ms. Garcia at (202) 317-6853 (not a toll-free number).

Maximum Values For 2019 For Use With Vehicle Cents-Per-Mile and Fleet-Average Valuation Rules

Notice 2019-34

This Notice 2019-34 provides the maximum fair market value of a vehicle for use with the fleet-average and vehicle cents-per-mile special valuation rules under Treas. Reg. § 1.61-21(d) and (e), respectively, for 2019. These special valuation rules may be used to value an employee's personal use of an employer-provided vehicle for income and employment tax purposes.

I. PURPOSE

This Notice 2019-34 provides the maximum vehicle value for 2019 for purposes of the special valuation rules provided in Treas. Reg. § 1.61-21(d) and (e) that may be used to determine the value of personal use of an employer-provided vehicle. This Notice 2019-34 also provides information about the way the Internal Revenue

Service (IRS) and the Department of the Treasury (Treasury Department) intend to publish this maximum vehicle value in the future. Additionally, this Notice 2019-34 provides temporary relief from the consistency requirements in Treas. Reg. § 1.61-21(e)(5) for use with the vehicle cents-per-mile valuation rule. Finally, this Notice 2019-34 allows flexibility with respect to the Treas. Reg. § 1.61-21(d)(5)(v)(B) rules relating to the period of use for the fleet-average valuation rule, which is an optional component of the automobile lease valuation rule under Treas. Reg. § 1.61-21(d).

II. BACKGROUND

If an employer provides an employee with a vehicle that is available to the employee for personal use, the value of the personal use generally must be included in the employee's income. Internal Revenue Code § 61(a)(1); Treas. Reg. § 1.61-21.

A. The Vehicle Cents-Per-Mile Rule

For employer-provided vehicles made available to employees for personal use that meet the requirements of Treas. Reg. § 1.61-21(e)(1), generally the value of the personal use may be determined under the vehicle cents-per-mile valuation rule of Treas. Reg. § 1.61-21(e). However, Treas. Reg. § 1.61-21(e)(1)(iii) currently provides that the value of the personal use may not be determined under the vehicle cents-per-mile valuation rule for a calendar year if the fair market value of the vehicle (determined pursuant to Treas. Reg. § 1.61-21(d)(5)(i) through (iv)) on the first date the vehicle is made available to the employee exceeds a base value of $12,800 that is adjusted annually under section 280F(d)(7).

Treas. Reg. § 1.61-21(e)(5)(i) states that an employer must adopt the vehicle cents-per-mile valuation rule by the first day on which the vehicle is used by an employee of the employer for personal use (or, if the commuting valuation rule of Treas. Reg. § 1.61-21(f) is used when the vehicle is first used by an employee of the employer for personal use and the employer switches to the vehicle cents-per-mile valuation rule, the first day on which the commuting valuation rule is not used). Treas. Reg. § 1.61-21(e)(5)(ii) provides, in part, that once the vehicle cents-per-mile valuation rule has been adopted for a vehicle by an employer, the rule must be used by the employer for all subsequent years in which the vehicle qualifies for use of the rule, except that the employer may, for any year during which use of the vehicle qualifies for the commuting valuation rule of Treas. Reg. § 1.61-21(f), use the commuting valuation rule with respect to the vehicle.

B. The Fleet-Average Valuation Rule

For employer-provided automobiles available to employees for personal use for an entire year, generally the value of the personal use may be determined under the automobile lease valuation rule of Treas. Reg. § 1.61-21(d). Under this valuation rule, the value of the personal use is the Annual Lease Value. Provided the requirements of Treas. Reg. § 1.61-21(d)(5)(v) are met, an employer with a fleet of 20 or more automobiles may use a fleet-average value for purposes of calculating the Annual Lease Values of the automobiles in the employer's fleet. The fleet-average value is the average of the fair market values of all the automobiles in the fleet. However, Treas. Reg. § 1.61-21(d)(5)(v)(D) provides that the value of an employee's personal use of an automobile may not be determined under the fleet-average valuation rule for a calendar year if the fair market value of the automobile (determined pursuant to Treas. Reg. § 1.61-21(d)(5)(i) through (iv)) on the first date the automobile is made available to an employee exceeds the base value of $16,500, as adjusted annually for inflation pursuant to section 280F(d)(7).

Treas. Reg. § 1.61-21(d)(5)(v)(B) generally provides that the fleet-average valuation rule may be used by an employer as of January 1 of any calendar year following the calendar year in which the employer acquires a sufficient number of automobiles to total a fleet of 20 or more, each one satisfying the maximum value limitation of Treas. Reg. § 1.61-21(d)(5)(v)(D). The Annual Lease Value calculated for automobiles in the fleet, based on the fleet-average value, shall remain in effect for the period that begins with the first January 1 the fleet-average valuation rule is applied by the employer to the automobiles in the fleet and ends on December 31 of the subsequent calendar year. The Annual Lease Value for each subsequent two-year period is calculated by determining the fleet-average value of the automobiles in the fleet as of the first January 1 of that period. An employer may cease using the fleet-average valuation rule as of any January 1.

C. Notice 2019-08

Notice 2019-08 provides interim guidance on new procedures using section 280F(d)(7), as modified by sections 11002 and 13202 of the Tax Cuts and Jobs Act, Pub. L. No. 115-97 (the "Act"), for calculating the inflation adjustments to the maximum vehicle values for use with the special valuation rules under Treas. Reg. § 1.61-21(d) and (e). Additionally, Notice 2019-08 states that the IRS and the Treasury Department anticipate that further guidance on these issues will be issued in the form of proposed regulations and expect that the regulations will be consistent with the rules set forth in Notice 2019-08.

Notice 2019-08 states that, consistent with the substantial increase in the dollar limitations on depreciation deductions under section 280F(a), as modified by section 13202(a)(1) of the Act, the IRS and the Treasury Department intend to amend Treas. Reg. § 1.61-21(d) and (e) to incorporate a higher base value of $50,000 as the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules effective for the 2018 calendar year. Notice 2019-08 further states that the IRS and the Treasury Department intend that the regulations will be modified to provide that this $50,000 base value will be adjusted annually using section 280F(d)(7) for 2019 and subsequent years. Notice 2019-08 also provides that, for 2018, the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules is $50,000. Finally, Notice 2019-08 provides that, for 2018 and 2019, the IRS and the Treasury Department will not publish separate maximum values for trucks and vans for use with the vehicle cents-per-mile and fleet-average valuation rules.

D. The Maximum Standard Automobile Cost for an Allowance Under a FAVR Plan

Rev. Proc. 2010-51, 2010-51 I.R.B. 883, provides rules for using optional standard mileage rates in computing the deductible costs of operating an automobile for business, charitable, medical, or moving expense purposes. Section 2.12(1) of Rev. Proc. 2010-51 provides that the IRS publishes both the standard mileage rates for the use of an automobile for business, charitable, medical, and moving expense purposes, and the maximum standard automobile cost for purposes of an allowance under a fixed and variable rate (FAVR) plan, in a separate annual notice.

When Treas. Reg. § 1.61-21(d) and (e) are amended to incorporate a higher base value of $50,000 as the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules, the IRS and the Treasury Department expect that the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules for 2019 and subsequent years will be the same as the maximum standard automobile cost for purposes of an allowance under a FAVR plan. The maximum standard automobile cost for purposes of an allowance under a FAVR plan and the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules will each be calculated using the base value of $50,000, adjusted annually in accordance with section 280F(d)(7). Accordingly, the IRS and the Treasury Department anticipate that once Treas. Reg. § 1.61-21(d) and (e) are amended, the maximum value for use of the vehicle cents-per-mile and fleet-average valuation rules will be published in the annual notice providing the standard mileage rates for the use of an automobile for business, charitable, medical, and moving expense purposes and the maximum standard automobile cost for purposes of an allowance under a FAVR plan.

E. Notice 2019-02

Notice 2019-02, 2019-02 I.R.B. 281, provides the optional 2019 standard mileage rates for taxpayers to use in computing the deductible costs of operating an automobile for business, charitable, medical, or moving expense purposes. Section 5 of Notice 2019-02 states that, for purposes of computing the allowance under a FAVR plan, the standard automobile cost for 2019 may not exceed $50,400.

III. GUIDANCE

Based on the foregoing:

(1) The maximum value of an employer-provided vehicle (including cars, vans and trucks) first made available to employees for personal use in calendar year 2019 for which the vehicle cents-per-mile valuation rule provided under Treas. Reg. § 1.61-21(e) may be applicable is $50,400.

(2) The maximum value of an employer-provided automobile (including vans and trucks) first made available to employees for personal use in calendar year 2019 for which the fleet-average valuation rule provided under Treas. Reg. § 1.61-21(d)(5)(v) may be applicable is $50,400.

Furthermore, the Treasury Department and the IRS intend to revise Treas. Reg. § 1.61-21(e) to provide that if an employer did not qualify under Treas. Reg. § 1.61-21(e)(5) to adopt the vehicle cents-per-mile valuation rule on the first day on which a vehicle was used by an employee of the employer for personal use because, under the rules in effect before 2018, the vehicle had a fair market value in excess of the maximum permitted in accordance with Treas. Reg. § 1.61-21(e)(1)(iii), the employer may first adopt the vehicle cents-per-mile valuation rule for the 2018 or 2019 taxable year based on the maximum fair market value of a vehicle for purposes of the vehicle cents-per-mile valuation rule set forth in Notice 2019-08 or this Notice 2019-34, as applicable. Similarly, the IRS and Treasury Department intend that the proposed regulations will further provide that if the commuting valuation rule of Treas. Reg. § 1.61-21(f) was used when the vehicle was first used by an employee of the employer for personal use, and the employer did not qualify to switch to the vehicle cents-per-mile rule on the first day on which the commuting valuation rule was not used because, under the rules in effect before 2018, the vehicle had a fair market value in excess of the maximum permitted in accordance with Treas. Reg. § 1.61-21(e)(1)(iii), the employer may adopt the vehicle cents-per-mile valuation rule for the 2018 or 2019 taxable year based on the maximum fair market value of a vehicle for purposes of the vehicle cents-per-mile valuation rule set forth in Notice 2019-08 or this Notice 2019-34, as applicable. However, consistent with Treas. Reg. § 1.61-21(e)(5), an employer that adopts the vehicle cents-per-mile valuation rule must continue to use the rule for all subsequent years in which the vehicle qualifies for use of the rule, except that the employer may, for any year during which use of the vehicle qualifies for the commuting valuation rule of Treas. Reg. § 1.61-21(f), use the commuting valuation rule with respect to the vehicle.

In addition, with respect to an employer that did not qualify to use the fleet-average valuation rule prior to January 1, 2019, because the maximum value limitation of Treas. Reg. § 1.61-21(d)(5)(v)(D) prior to 2018 could not be met, the Treasury Department and the IRS intend to revise Treas. Reg. §1.61-21(d) to provide that an employer may adopt the fleet-average valuation rule for 2018 or 2019, provided the requirements of § 1.61-21(d)(5)(v) are met for that year using the maximum vehicle values set forth in Notice 2019-08 or this Notice 2019-34, respectively.

Employer-provided vehicles are noncash fringe benefits under section 3501(b). Announcement 85-113, 1985-31 I.R.B. 31, provides guidelines for withholding, paying, and reporting employment tax on taxable noncash fringe benefits. Announcement 85-113 provides generally that taxpayers may rely on the guidelines in the announcement until the issuance of regulations that supersede the temporary and proposed regulations under section 3501(b). No regulations have been issued under section 3501(b) that supersede the announcement. Thus, Announcement 85-113 generally is applicable to current payments of noncash fringe benefits, including vehicles.

Section 1 of Announcement 85-113 allows payors of certain noncash fringe benefits to treat the benefits as paid on any day(s) during the year so long as they treat benefits provided in a calendar year as paid not later than December 31 of the calendar year. Section 5 of the announcement allows employers to treat certain benefits paid during the last two months of the year (or any shorter period) as paid during the subsequent calendar year.

Employers that wish to use the vehicle cents-per-mile rule or the fleet-average valuation rule for 2019 based on the maximum values set forth in this notice may use the rules in Announcement 85-113 or the adjustment process under section 6413 or the refund claim process under section 6402 to correct any overpayment of federal employment taxes on these amounts (see the regulations under these sections, Rev. Rul. 2009-39, 2009-52 I.R.B. 951, section 13 of Publication 15 (Circular E), Employer's Tax Guide, and the Instructions for Form 941-X, Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund for information on these adjustment and refund claim processes).

Until revised final regulations are published under Treas. Reg. § 1.61-21(d) and (e), taxpayers may rely on the interim guidance provided in this Notice 2019-34.

REQUEST FOR COMMENTS

Interested parties are invited to submit comments on this notice by July 29, 2019. Comments should include a reference to Notice 2019-34. Comments may be submitted electronically via the Federal eRulemaking Portal at ***www.regulations.gov*** (type IRS-2019-34 in the search field on the ***regulations.*gov** homepage to find this notice and submit comments). Alternatively, submissions may be sent to CC:PA:LPD:PR (Notice 2019-34), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions also may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Notice 2019-34), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20044. All comments submitted by the public in response to this notice will be available for public inspection and copying in their entirety.

IV. DRAFTING INFORMATION

The principal author of this notice is Gabriel Minc of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). For further information regarding this notice contact Mr. Minc at (202) 317-4774 (not a toll-free number).

---

26 CFR 601.201: Rulings and determination letters. (Also: Part I, § 501; 1.501(c)(3)-1.)

Rev. Proc. 2019-22

SECTION 1. PURPOSE

This revenue procedure modifies Revenue Procedure 75-50, 1975-2 C.B. 587, to reflect technological advances since its publication and provides a third method for a private school to satisfy the requirement contained in section 4.03 of the revenue procedure by using its Internet website to publicize the school's racially nondiscriminatory policy as to students.

SECTION 2. BACKGROUND

.01 Revenue Procedure 75-50 sets forth guidelines and recordkeeping requirements for determining whether a private school, which is applying to be or currently recognized as exempt from federal income tax under section 501(a) and described in section 501(c)(3) of the Internal Revenue Code, has adopted a racially nondiscriminatory policy regarding students and operates in a bona fide manner in accordance with that policy. Section 4.03 of Revenue Procedure 75-50 requires a private school to make its racially nondiscriminatory policy known to all segments of the general community served by the school in one of two ways. Subsection 1(a) of section 4.03 permits a school to satisfy this publicity requirement by publishing, at least once annually, a notice of its racially nondiscriminatory policy in a newspaper of general circulation that serves all racial segments of the community. Subsection 1(b) of section 4.03 permits a school to use the broadcast media to publicize its racially nondiscriminatory policy, provided that the means by which the policy is communicated is reasonably expected to be effective.

.02 The purpose of the publicity requirement in section 4.03 of Revenue Procedure 75-50 is for a private school to make its racially nondiscriminatory policy as to students known to all segments of the general community served by the school. Because of technological advances since the publication of Revenue Procedure 75-50, including the advent and widespread use of the Internet, in many cases a school can accomplish the purpose of the publicity requirement by using its Internet website.

SECTION 3. MODIFICATIONS TO REVENUE PROCEDURE 75-50

.01 Subsection 1 of section 4.03 is modified to read as follows:

1 The school must use one of the following three methods to satisfy this requirement:

.02 Section 4.03 is modified by adding new subsection 1(c) to read as follows:

(c) The school may display a notice of its racially nondiscriminatory policy on its primary publicly accessible Internet homepage at all times during its taxable year (excluding temporary outages due to website maintenance or technical problems) in a manner reasonably expected to be noticed by visitors to the homepage. The following notice, which is identical to the notice that may be used to satisfy the publicity requirement using a newspaper of general circulation that serves all racial segments of the community, is acceptable:

NOTICE OF NONDISCRIMINATORY POLICY AS TO STUDENTS

The M school admits students of any race, color, national and ethnic origin to all the rights, privileges, programs, and activities generally accorded or made available to students at the school. It does not discriminate on the basis of race, color, national and ethnic origin in administration of its educational policies, admissions policies, scholarship and loan programs, and athletic and other school-administered programs.

A publicly accessible homepage is one that does not require a visitor to input information, such as an email address or a username and password, to access the homepage. Factors to be considered in determining whether a notice is reasonably expected to be noticed by visitors to the homepage include the size, color, and graphic treatment of the notice in relation to other parts of the homepage, whether the notice is unavoidable, whether other parts of the homepage distract attention from the notice, and whether the notice is visible without a visitor having to do anything other than simple scrolling on the homepage. A link on the homepage to another page where the notice appears, or a notice that appears in a carousel or only by selecting a dropdown or by hover (mouseover) is not acceptable. If a school does not have its own website, but it has webpages contained in a website, the school must display a notice of its racially nondiscriminatory policy on its primary landing page within the website in a manner that satisfies all other requirements of this subsection 1(c) to use this publication method.

SECTION 4. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 75-50 is modified.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective May 28, 2019.

SECTION 6. DRAFTING INFORMATION

The principal author of this revenue procedure is Matthew Giuliano of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). For further information regarding this revenue procedure contact Mr. Giuliano at (202) 317-4086 (not a toll-free number).

---

26 CFR 601.602: Tax forms and instructions.
(Also Part 1, §§ 1, 223.)

Rev. Proc. 2019-25

SECTION 1. PURPOSE

This revenue procedure provides the 2020 inflation adjusted amounts for Health Savings Accounts (HSAs) as determined under § 223 of the Internal Revenue Code.

SECTION 2. 2020 INFLATION ADJUSTED ITEMS

Annual contribution limitation. For calendar year 2020, the annual limitation on deductions under § 223(b)(2)(A) for an individual with self-only coverage under a high deductible health plan is $3,550. For calendar year 2020, the annual limitation on deductions under § 223(b)(2)(B) for an individual with family coverage under a high deductible health plan is $7,100.

High deductible health plan. For calendar year 2020, a "high deductible health plan" is defined under § 223(c)(2)(A) as a health plan with an annual deductible that is not less than $1,400 for self-only coverage or $2,800 for family coverage, and the annual out-of-pocket expenses (deductibles, co-payments, and other amounts, but not premiums) do not exceed $6,900 for self-only coverage or $13,800 for family coverage.

SECTION 3. EFFECTIVE DATE

This revenue procedure is effective for calendar year 2020.

SECTION 4. DRAFTING INFORMATION

The principal author of this revenue procedure is Bill Ruane of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding § 223 and HSAs, contact William Fisher at 202.317.5500 (not a toll-free number). For further information regarding the calculation of the inflation adjustments in this revenue procedure, contact Mr. Ruane at 202.317.4718 (not a toll-free number).

Part IV.

Announcement of Disciplinary Sanctions From the Office of Professional Responsibility

Announcement 2019-05

The Office of Professional Responsibility (OPR) announces recent disciplinary sanctions involving attorneys, certified public accountants, enrolled agents, enrolled actuaries, enrolled retirement plan agents, appraisers, and unenrolled/unlicensed return preparers (individuals who are not enrolled to practice and are not licensed as attorneys or certified public accountants). Licensed or enrolled practitioners are subject to the regulations governing practice before the Internal Revenue Service (IRS), which are set out in Title 31, Code of Federal Regulations, Subtitle A, Part 10, and which are released as Treasury Department Circular No. 230. The regulations prescribe the duties and restrictions relating to such practice and prescribe the disciplinary sanctions for violating the regulations. Unenrolled/unlicensed return preparers are subject to Revenue Procedure 81-38 and superseding guidance in Revenue Procedure 2014-42, which govern a preparer's eligibility to represent taxpayers before the IRS in examinations of tax returns the preparer both prepared for the taxpayer **and** signed as the preparer. Additionally, unenrolled/unlicensed return preparers who voluntarily participate in the Annual Filing Season Program under Revenue Procedure 2014-42 agree to be subject to the duties and restrictions in Circular 230, including the restrictions on incompetent or disreputable conduct.

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

Disbarred from practice before the IRS—An individual who is disbarred is not eligible to practice before the IRS as defined at 31 C.F.R. § 10.2(a)(4) for a minimum period of five (5) years.

Suspended from practice before the IRS—An individual who is suspended is not eligible to practice before the IRS as defined at 31 C.F.R. § 10.2(a)(4) during the term of the suspension.

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

Monetary penalty—A monetary penalty may be imposed on an individual who engages in conduct subject to sanction, or on an employer, firm, or entity if the individual was acting on its behalf and it knew, or reasonably should have known, of the individual's conduct.

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

Ineligible for limited practice—An unenrolled/unlicensed return preparer who fails to comply with the requirements in Revenue Procedure 81-38 or to comply with Circular 230 as required by Revenue Procedure

2014-42 may be determined ineligible to engage in limited practice as a representative of any taxpayer. Under the regulations, individuals subject to Circular 230 may not assist, or accept assistance from, individuals who are suspended or disbarred with respect to matters constituting practice (*i.e.*, representation) before the IRS, and they may not aid or abet suspended or disbarred individuals to practice before the IRS.

Disciplinary sanctions are described in these terms:

Disbarred by decision, Suspended by decision, Censured by decision, Monetary penalty imposed by decision, and Disqualified after hearing—An administrative law judge (ALJ) issued a decision imposing one of these sanctions after the ALJ either (1) granted the government's summary judgment motion or (2) conducted an evidentiary hearing upon OPR's complaint alleging violation of the regulations. After 30 days from the issuance of the decision, in the absence of an appeal, the ALJ's decision becomes the final agency decision.

Disbarred by default decision, Suspended by default decision, Censured by default decision, Monetary penalty imposed by default decision, and Disqualified by default decision—An ALJ, after finding that no answer to OPR's complaint was filed, granted OPR's motion for a default judgment and issued a decision imposing one of these sanctions.

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

Disbarred by consent, Suspended by consent, Censured by consent, Monetary penalty imposed by consent, and Disqualified by consent—In lieu of a disciplinary proceeding being instituted or continued, an individual offered a consent to one of these sanctions and OPR accepted the offer. Typically, an offer of consent will provide for: suspension for an indefinite term; conditions that the individual must observe during the suspension; and the individual's opportunity, after a stated number of months, to file with OPR a petition for reinstatement affirming compliance with the terms of the consent and affirming current fitness and eligibility to practice (i.e., an active professional license or active enrollment status, with no intervening violations of the regulations).

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

Determined ineligible for limited practice—-There has been a final determination that an unenrolled/unlicensed return preparer is not eligible for limited representation of any taxpayer because the preparer violated standards of conduct or failed to comply with any of the requirements to act as a representative.

A practitioner who has been disbarred or suspended under 31 C.F.R. § 10.60, or suspended under § 10.82, or a disqualified appraiser may petition for reinstatement before the IRS after the expiration of 5 years following such disbarment, suspension, or disqualification (or immediately following the expiration of the suspension or disqualification period if shorter than 5 years). Reinstatement will not be granted unless the IRS is satisfied that the petitioner is not likely to engage thereafter in conduct contrary to Circular 230, and that granting such reinstatement would not be contrary to the public interest.

Reinstatement decisions are published at the individual's request, and described in these terms:

Reinstated to practice before the IRS—The individual's petition for reinstatement has been granted. The individual is an attorney, certified public accountant, enrolled agent, enrolled actuary, or an enrolled retirement plan agent, and eligible to practice before the IRS, or in the case of an appraiser, the individual is no longer disqualified.

Reinstated to engage in limited practice before the IRS—The individual's petition for reinstatement has been granted. The individual is an unenrolled/unlicensed return preparer and eligible to engage in limited practice before the IRS.

OPR has authority to disclose the grounds for disciplinary sanctions in these situations: (1) an ALJ or the Secretary's delegate on appeal has issued a final decision; (2) the individual has settled a disciplinary case by signing OPR's "consent to sanction" agreement admitting to one or more violations of the regulations and consenting to the disclosure of the admitted violations (for example, failure to file Federal income tax returns, lack of due diligence, conflict of interest, etc.); (3) OPR has issued a decision in an expedited proceeding for indefinite suspension; or (4) OPR has made a final determination (including any decision on appeal) that an unenrolled/unlicensed return preparer is ineligible to represent any taxpayer before the IRS.

Announcements of disciplinary sanctions appear in the Internal Revenue Bulletin at the earliest practicable date. The sanctions announced below are alphabetized first by state and second by the last names of the sanctioned individuals.

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Arizona				
Cottonwood	Heath, Nannette L.	CPA	Suspended by decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 6, 2019
California				
Cherry Valley	Aylward, William K.	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 22, 2019
Los Angeles	Kim, Jae Young	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 8, 2019
	Aka, Wilfred I.	Attorney/ CPA	Suspended by decision on appeal by Treasury Appellate Authority 31 C.F.R. §10.82(b)	Indefinite from November 15, 2017 (and may petition for reinstatement after at least 36 months)
Orange	Dial, Thomas lee	CPA	Suspended by default decision in expedited proceeding under31 C.F.R. § 10.82(b)	Indefinite from February 6, 2019
Rowland Heights	Zhong, John Z.	CPA/Enrolled Agent	Disbarred by ALJ Decision	January 27, 2017
Seaside	McEwan, John G.	Enrolled Agent	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 8, 2019
	Jonavic, Theodore P., see Nevada			

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Florida				
Miami	Takesian, Greg C.	CPA	Suspended by decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 8, 2019
Rockledge	Warrington, Tara M.	Attorney	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 5, 2019
Indiana				
Lowell	Schaefer, James M.	CPA	Suspended by consent under 31 C.F.R. §§ 10.51(a)(2) and 10.51(a)(3)	Indefinite from October 1, 2018
Kansas				
Westwood	Arnold, III, Robert E.	Attorney	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from November 1, 2018
Overland Park	Muir, Timothy J.	Attorney	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from October 29, 2018
Kentucky				
Southgate	Vater, Gayle G.	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 6, 2019
Massachusetts				
	Takesian, Greg C., see Florida			

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Minnesota				
	Zhong, John Z. See California			
New York				
Olean	Stevens, Joseph F.	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 21, 2019
Nevada				
Las Vegas	Jonavic, Theodore P.	CPA	Suspended by decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from March 7, 2019
Pennsylvania				
Koppel	Prence, Neal P.	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 21, 2019
Texas				
Plano	Thakkar, Mahesh K.	CPA	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 8, 2019
Washington				
Kennewick	Neal, Christopher L.	Attorney	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from March 28, 2019
Wisconsin				
Milwaukee	Wiensch, Adam J.	Attorney	Suspended by default decision in expedited proceeding under 31 C.F.R. § 10.82(b)	Indefinite from February 8, 2019

Notice of Proposed Rulemaking

Gain or Loss of Foreign Persons from Sale or Exchange of Certain Partnership Interests

REG-113604-18

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations implementing section 864(c)(8) of the Internal Revenue Code. The proposed regulations affect certain foreign persons that recognize gain or loss from the sale or exchange of an interest in a partnership that is engaged in a trade or business within the United States. The proposed regulations also affect partnerships that, directly or indirectly, have foreign persons as partners.

DATES: Written or electronic comments and requests for a public hearing must be received by February 25, 2019.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-113604-18), Internal Revenue Service, Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-113604-18), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224, or sent electronically via the Federal eRulemaking Portal at *http://www.regulations.gov* (IRS REG-113604-18).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Ronald M. Gootzeit or Chadwick Rowland, (202) 317-6937; concerning submissions of comments or requests for a public hearing, Regina L. Johnson, (202) 317-6901 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

A foreign partner in a partnership that is engaged in the conduct of a trade or business within the United States is itself considered to be so engaged. *See* section 875. Under a 1991 revenue ruling, in determining the tax consequences of the sale or exchange of a foreign partner's interest in a partnership engaged in the conduct of a trade or business within the United States, the IRS held that the partnership's property located in the United States that is used or held for use in the partnership's trade or business within the United States is used to determine the extent to which income derived from the sale or exchange of the partnership interest is effectively connected with the conduct of the partner's trade or business within the United States. Rev. Rul. 91-32, 1991-1 C.B. 107. Under the ruling, if there is unrealized gain or loss in partnership assets that would be treated as effectively connected with the conduct of the partnership's trade or business within the United States if those assets were sold by the partnership, some or all of the foreign person's gain or loss from the sale or exchange of a partnership interest may be treated as effectively connected with the partner's conduct of a trade or business within the United States. However, a 2017 Tax Court case held instead that, generally, gain or loss on the sale or exchange by a foreign person of an interest in such a partnership is foreign source gain or loss based on the residence of the selling partner because gain on the sale of the partnership interest is not attributable to the partnership's assets and activities. As a result, such gain or loss generally would not be treated as effectively connected with the conduct of a trade or business. *Grecian Magnesite Mining v. Commissioner*, 149 T.C. No. 3 (2017), *appeal argued*, No. 17-1268 (D.C. Cir. Oct. 9, 2018).

Section 864(c)(8), which was added to the Internal Revenue Code (the "Code") by section 13501 of the Tax Cuts and Jobs Act, Public Law 115-97 (2017) (the "Act"), generally overturns the result of *Grecian Magnesite Mining v. Commissioner* by providing that gain or loss of a nonresident alien individual or foreign corporation (a "foreign transferor") from the sale, exchange, or other disposition ("transfer") of a partnership interest is treated as effectively connected with the conduct of a trade or business within the United States ("effectively connected gain" or "effectively connected loss") to the extent that the transferor would have had effectively connected gain or loss if the partnership had sold all of its assets at fair market value as of the date of the sale or exchange ("deemed sale").

Section 864(c)(8)(E) generally provides that the Secretary shall prescribe such regulations or other guidance as the Secretary determines appropriate for the application of section 864(c)(8). Section 864(c)(8) is effective for sales, exchanges, and dispositions on or after November 27, 2017.

New section 1446(f) was also added to the Code by section 13501 of the Act. Section 1446(f)(1) requires that the transferee of a partnership interest withhold 10 percent of the amount realized on the transferor's disposition of the partnership interest (if any portion of the gain would be treated as effectively connected gain) unless the transferor certifies that the transferor is not a foreign person. Section 1446(f) is effective for sales, exchanges, and dispositions after December 31, 2017.

On December 29, 2017, the Department of the Treasury (the "Treasury Department") and the IRS released Notice 2018-08, 2018-7 I.R.B. 352 (the "PTP Notice"). The PTP Notice temporarily suspends the requirement to withhold on amounts realized in connection with the sale, exchange, or disposition of certain interests in publicly traded partnerships ("PTPs") in response to stakeholder concerns that applying section 1446(f) to dispositions of interests in PTPs without guidance presented significant practical problems. On April 2, 2018, the Treasury Department and the IRS released Notice 2018-29, 2018-16 I.R.B. 495, which announced an intent to issue proposed regulations under section 1446(f) that apply in the case of a disposition of a partnership interest that is not publicly traded and provided temporary guidance.

Explanation of Provisions

I. *Gain or Loss on the Transfer of a Partnership Interest*

Section 864(c)(8)(A) provides that gain or loss of a foreign transferor from the transfer of an interest, owned directly or indirectly, in a partnership that is engaged in any trade or business within the United States is treated as effectively connected gain or loss to the extent such gain or loss does not exceed the amount determined under section 864(c)(8)(B). In general, section 864(c)(8)(B) limits the amount of effectively connected gain or loss to the portion of the foreign transferor's distributive share of gain or loss that would have been effectively connected gain or loss if the partnership had sold all of its assets at fair market value. The proposed regulations set forth rules for determining gain or loss described in section 864(c)(8)(A) and the limitation described in section 864(c)(8)(B), each of which is discussed in this section I of this Explanation of Provisions.

A. *Determination of Gain or Loss Described in Section 864(c)(8)(A)*

To determine the amount of gain or loss described in section 864(c)(8)(A), generally, the proposed regulations require that a foreign transferor first determine its gain or loss on the transfer of a partnership interest ("outside gain" and "outside loss"). For this purpose, the proposed regulations provide that outside gain or loss is determined under all relevant provisions of the Code and the regulations thereunder. As described in section I.A.1 of this Explanation of Provisions, a foreign transferor may recognize capital gain or loss ("outside capital gain" or "outside capital loss") and ordinary gain or loss ("outside ordinary gain" or "outside ordinary loss") on the transfer of its partnership interest and must separately apply section 864(c)(8) with respect to its capital gain or loss and its ordinary gain or loss.

1. Interaction with Sections 741 and 751

Section 864(c)(8) provides rules regarding the treatment of gain or loss on the transfer of a partnership interest as effectively connected gain or loss, but it does not address the computation of the amount of gain or loss to a partner upon the transfer. Rather, applicable tax law, including subchapter K, determines the amount and character of outside gain or loss on the transfer of a partnership interest. For example, the reduction in a transferor's share of partnership liabilities is treated as an amount realized on the transfer of the partnership interest under section 1001 and the regulations thereunder. See section 752(d) and §1.752-1(h).

Section 741 provides that on a sale or exchange of an interest in a partnership, gain or loss is recognized by the transferor, and shall be considered capital gain or loss except as otherwise provided in section 751. Section 751 provides that an amount received by a transferor of a partnership interest that is attributable to unrealized receivables or inventory items of the partnership ("section 751 property") is considered ordinary income or loss. As a result of sections 741 and 751 and the regulations thereunder, gain or loss on a sale or exchange of a partnership interest can comprise capital gain, capital loss, ordinary income, or ordinary loss (or a combination thereof). See §§1.741-1(a) and 1.751-1(a).

In general, the proposed regulations provide that a foreign transferor must determine the portion of its capital gain or loss, and the portion of its ordinary income or loss from section 751 property, that must each be characterized as effectively connected gain or loss under section 864(c)(8). See proposed §1.864(c)(8)-1(b). As provided in section 864(c)(8)(A) and further described in section I.B of this Explanation of Provisions, the proposed regulations provide that a foreign partner's effectively connected gain or loss will not exceed its outside gain or loss on the sale of the interest as determined under sections 741 and 751 and the regulations thereunder. Thus, the amount of gain or loss determined under section 741 (before application of section 751) is not a limitation on the amount of gain or loss characterized as effectively connected with the conduct of a trade or business within the United States under the proposed regulations.

2. Nonrecognition Transactions

The proposed regulations provide that the gain or loss on the transfer of a partnership interest that is subject to tax as effectively connected gain or loss is limited to gain or loss otherwise recognized under the Code. See proposed §1.864(c)(8)-1(b)(2)(ii). When a nonrecognition provision results in a foreign transferor recognizing only a portion of its gain or loss on the transfer of an interest in a partnership, section 864(c)(8) may apply with respect to the portion of the gain or loss recognized.

Although section 864(c)(8)(E) authorizes regulations or other guidance with respect to the application of section 864(c)(8) to nonrecognition transactions, the proposed regulations do not contain special rules applicable to nonrecognition transactions. The Treasury Department and the IRS recognize, however, that certain nonrecognition transactions may have the effect of reducing gain or loss that would be taken into account for U.S. federal income tax purposes. For example, if a partnership that conducts a trade or business within the United States owns property not subject to tax under section 871(b) or 882(a) in the hands of a foreign partner, the partnership may distribute that property to the foreign partner rather than a U.S. partner. The Treasury Department and the IRS continue to consider, and comments are requested regarding, whether other Code provisions adequately address transactions that rely on section 731 distributions to reduce the scope of assets subject to U.S. federal income taxation, and may propose rules addressing these types of transactions.

B. *Determination of Deemed Sale Gain or Loss*

1. In General

After outside gain and loss are determined under proposed §1.864(c)(8)-1(b), the proposed regulations set forth three amounts that a foreign transferor must determine to derive the limitation in section 864(c)(8)(B) against which the outside gain or loss is compared: (1) With respect to each asset held by the partnership, the amount of gain or loss that the partnership would recognize in connection with a deemed sale to an unrelated party in a fully taxable transaction for cash equal to the asset's fair market value immediately before the partner's transfer of its partnership interest; (2) the amount of that gain or loss that would be treated as effectively connected gain or loss ("deemed sale EC gain" and "deemed sale EC loss"); and (3) the foreign transferor's distributive share of the ordinary and capital components of any deemed sale EC gain and deemed sale EC loss. The proposed regulations refer to the separate sums of the foreign transferor's distributive shares of the ordinary and capital components of deemed sale EC gain and deemed sale EC loss items for all assets, determined at the level of the foreign transferor, as "aggregate deemed sale EC capital gain," "aggregate deemed sale EC capital loss," "aggregate deemed sale EC ordinary gain," and "aggregate deemed sale EC ordinary loss."

After each of these aggregate amounts is determined, the proposed regulations implement the limitation described in section 864(c)(8)(B), generally, by comparing the foreign transferor's outside gain or loss amounts with the relevant aggregate deemed sale EC gain or loss. This determination is made separately with respect to capital gain or capital loss and gain or loss treated as ordinary income or ordinary loss. Thus, for example, a foreign transferor would compare its outside capital gain to its aggregate deemed sale EC capital gain, treating the former as effectively connected gain only to the extent it does not exceed the latter. See proposed §1.864(c)(8)-1(b)(3).

2. Treatment of Deemed Sale Gain or Loss as Effectively Connected Gain or Loss

As described in Part I.B.1 of this Explanation of Provisions, the proposed regulations require a foreign transferor to determine the amount of gain or loss that would arise in a deemed asset sale that would be treated as effectively connected gain or loss. In general, gain or loss on the sale of personal property is effectively connected with the conduct of a trade or business within the United States if the gain is from sources within the United States and it satisfies the requirements of section 864(c) and the regulations thereunder. Accordingly, the proposed regulations provide that section 864 and the regulations thereunder apply for purposes of determining whether gain or loss that would arise in a deemed asset sale would be treated as effectively connected gain or loss. See proposed §1.864(c)(8)-1(c)(2)(i).

The determination as to whether gain or loss from a deemed asset sale by the partnership would be from sources within or without the United States, and whether that income would be treated as effectively connected gain or loss, is based on certain factual determinations, including whether the gain or loss results from a sale that is attributable to an office or other fixed place of business in the United States. The proposed regulations provide that, for purposes of determining whether gain or loss recognized in connection with a deemed asset sale by the partnership would be from sources within or without the United States, and thus whether that income would be treated as effectively connected gain or loss, the deemed asset sale is treated as attributable to an office or fixed place of business in the United States maintained by the partnership. As a result, deemed sale gain or loss generally would be treated as from sources within the United States. To prevent this rule from potentially converting gain or loss from assets with no connection to the partnership's trade or business within the United States into effectively connected gain or loss, the proposed regulations provide that gain or loss from the deemed sale of a partnership asset is not treated as effectively connected gain or loss if (1) no income or gain previously produced by the asset was taxable as effectively connected with the conduct of a trade or business within the United States by the partnership (or a predecessor of the partnership) during the ten-year period ending on the date of the transfer, and (2) the asset was not used, or held for use, in the conduct of a trade or business within the United States by the partnership (or a predecessor of the partnership) during the ten-year period ending on the date of transfer. See proposed §1.864(c)(8)-1(c)(2)(ii). Comments are requested as to whether additional guidance is needed regarding the source of gain or loss resulting from a deemed sale by the partnership, including rules coordinating this rule with section 865(e)(2)(B).

3. Determining Distributive Share of Deemed Sale EC Gain and Deemed Sale EC Loss

The flush language of section 864(c)(8)(B) provides that a transferor partner's distributive share of gain or loss on the deemed sale is determined in the same manner as the transferor partner's distributive share of the non-separately stated taxable income or loss of the partnership. The term "non-separately stated taxable income or loss of the partnership" is not defined in the Code or regulations. The proposed regulations provide that a partner's distributive share of gain or loss from the deemed sale is determined under all applicable Code sections (including section 704), taking into account allocations of tax items applying the principles of section 704(c), including any remedial allocations under §1.704-3(d), and any section 743 basis adjustment pursuant to §1.743-1(j)(3). The Treasury Department and IRS propose this approach because applying section 704 more closely ties the results of the deemed sale with regard to the selling foreign partner to the economic results of an actual sale, as compared (for example) to an approach that did not consider special allocations or considered only a partner's share of ordinary business income, which would distort the economic agreement among the partners. See proposed §1.864(c)(8)-1(c)(3)(i).

The Treasury Department and the IRS are considering whether section 704 and the regulations thereunder adequately prevent the avoidance of the purposes of section 864(c)(8) through allocations of effectively connected gain or loss to specific partners. For example, immediately before a foreign transferor sells its interest in a partnership, adjustments could be made to partnership allocations that would result in the foreign transferor recognizing less effectively connected gain from the deemed sale by the partnership. While statutory and regulatory provisions, as well as judicial doctrines, may limit the extent to which inappropriate results may be obtained in that transaction or similar transactions, the Treasury Department and the IRS are considering whether additional guidance is necessary to prevent abuse. Comments are requested as to whether there are specific situations in which the purposes of section 864(c)(8) may be avoided and specific suggestions for additional guidance to address those situations.

C. *Source*

Neither section 864(c)(8) nor the proposed regulations address the source of gain or loss from the transfer of a partnership interest. Section 864(c)(4) provides that, except as enumerated in section 864(c)(4)(B) and (C), no income, gain, or loss from sources without the United States is treated as effectively connected gain or loss. Section 864(c)(8)(A) and the proposed regulations, however, apply "[n]otwithstanding any other provision of [subtitle A of the Code]," such that gain or loss recognized on the transfer of an interest in a partnership that is engaged in a trade or business within the United States may be treated as effectively connected gain or loss even if it is from sources without the United States. Comments are requested as to whether, and what, additional guidance is necessary regarding the source of gain or loss subject to section 864(c)(8).

D. *Provision is Non-Exclusive*

The proposed regulations clarify that they do not apply to prevent any portion of gain or loss recognized on the transfer of a partnership interest from being treated as effectively connected gain or loss under other provisions of the Code (subject to a special rule coordinating the application of section 864(c)(8) and section 897). Thus, if a foreign transferor maintains an office or fixed place of business in the United States, and sells a partnership interest in a transaction that generates gain or loss attributable to that office, gain or loss recognized in connection with that transfer may be United States source income under section 865(e)(2), and may be treated as effectively connected income under section 864(c)(2). If the amount of gain or loss recognized that would be treated as effectively connected gain or loss under section 864(c)(2) exceeds the amount of gain that would be treated as effectively connected gain under section 864(c)(8), then the larger amount would be treated as effectively connected gain. See proposed §1.864(c)(8)-1(b)(1).

II. *Coordination with Section 897*

Section 897(g) generally provides that, under regulations prescribed by the Secretary, the amount realized by a nonresident alien individual or foreign corporation in exchange for all or part of its interest in a partnership is, to the extent attributable to United States real property interests (as defined in section 897(c)), considered as an amount received from the sale or exchange in the United States of such property. Accordingly, section 897(g) generally provides the same result for United States real property interests as Revenue Ruling 91-32 provides for property used, or held for use, in a trade or business in the United States. In general, section 864(c)(8)(C) provides that if a partnership described in section 864(c)(8)(A) holds any United States real property interest at the time of the transfer of the partnership interest, then the gain or loss treated as effectively connected gain or loss under section 864(c)(8)(A) is reduced by the amount treated as effectively connected gain or loss with respect to that United States real property interest under section 897. The effect of section 864(c)(8)(C) is to prevent gain or loss from a United States real property interest that is taxed under section 897 from being taken into account a second time under section 864(c)(8).

In the proposed regulations, the limitation on effectively connected gain or loss in section 864(c)(8)(B) is based on a deemed sale by the partnership of all of its assets, including all United States real property interests held by the partnership, which are treated as effectively connected assets under section 897. See proposed §1.864(c)(8)-1(c)(2)(i). To coordinate the taxation of United States real property interests under sections 897(g) and 864(c)(8), the proposed regulations provide that when a partnership holds United States real property interests and is also subject to section 864(c)(8) because it is engaged in the conduct of a trade or business within the United States without regard to section 897, the amount of the foreign transferor's effectively connected gain or loss will be determined under section 864(c)(8) and not under section 897(g). Therefore, the reduction called for by section 864(c)(8)(C) is not necessary. See proposed §1.864(c)(8)-1(d).

The regulations include a proposed rule in regulations under section 897, which serves as a cross-reference to this coordination rule. See section V of this Explanation of Provisions for a discussion of a proposed anti-stuffing rule that also applies in the context of section 897. Further, comments are requested as to the interaction of this rule with other rules in the regulations under section 897, including the special rule for publicly traded partnerships in §1.897-1(c)(2)(iv).

III. *Tiered Partnerships*

Section 864(c)(8) applies to a foreign nonresident alien individual or foreign corporation that owns an interest in a partnership directly or indirectly. Consistent with section 12 of Notice 2018-29, the proposed regulations provide that if a foreign transferor transfers an interest in an upper-tier partnership that owns, directly or indirectly, an interest in one or more lower-tier partnerships that are engaged in the conduct of a trade or business within the United States, then the deemed sale gain or loss must be computed with respect to each lower-tier partnership, the amount of effectively connected gain or loss that would be allocated to the upper-tier partnership must be determined, and the amount of gain or loss recognized by a foreign transferor that is treated as effectively connected gain or loss under proposed §1.864(c)(8)-1(c) must be determined by reference to the transferor's distributive share of effectively connected gain or loss arising from each lower-tier partnership. See proposed §1.864(c)(8)-1(e)(1).

The proposed regulations also clarify that when a foreign transferor is a partner in an upper-tier partnership and the upper-tier partnership transfers an interest in a lower-tier partnership that is engaged in the conduct of a trade or business within the United States, the upper-tier partnership must determine its effectively connected gain or loss by applying the principles of the proposed regulations, including the tiered partnership rules described in proposed §1.864(c)(8)-1(e)(1).

IV. *Treaties*

The business profits articles of many U.S. income tax treaties limit the taxation of income that is otherwise treated as effectively connected with the conduct of a trade or business within the United States under the Code to income and gain attributable to a permanent establishment in the United States. The applicable gains articles of many U.S. income tax treaties allow the country in which a permanent establishment is located to tax gains from the alienation of movable property forming part of the business property of a permanent establishment, including gains from the alienation of a permanent establishment, alone or with the whole enterprise of which it is a part. In general, the permanent establishment of a partnership in the United States is considered a permanent establishment of the partners of the partnership. See *Donroy, Ltd. v. United States*, 196 F.Supp. 54 (N.D. Cal. 1961), *aff'd* 301 F.2d 200 (9th Cir. 1962), and *Unger v. Comm'r*, T.C. Memo. 1990-15, 58 TCM 1157, *aff'd* 936 F.2d 1316 (D.C. Cir. 1991).

The proposed regulations provide that the disposition of a foreign partner's interest in a partnership, in whole or in part, is a disposition of all or part of a partner's permanent establishment. Thus, to the extent the partnership's assets form part of a foreign partner's permanent establishment in the United States, the permanent establishment paragraph of the gains article would generally preserve the United States' taxing jurisdiction over the gain on the transfer of a partnership interest that is subject to tax under section 864(c)(8). In addition, if an income tax treaty has a gains article that permits the United States to apply its domestic laws to tax gains or does not have a gains article, the treaty does not prevent the application of section 864(c)(8).

Gains articles of treaties also frequently have special provisions covering certain assets, regardless of whether the assets form part of a permanent establishment, such as gains from dispositions of United States real property interests and ships and aircraft used in international traffic. If a gains article of an income tax treaty prohibits taxation of the gain from the disposition of any asset, such as ships or aircraft used in international traffic, the gains and losses from those assets will not be considered assets that form part of the permanent establishment, nor will they be taken into account in determining deemed sale EC gain or deemed sale EC loss, for purposes of computing the section 864(c)(8)(B) limitation. If the gains article of an applicable income tax treaty allows the taxation of gain from the disposition of a United States real property interest, the transfer of an interest in a partnership that holds a United States real property interest remains subject to section 897(g) even if the transfer is not subject to section 864(c)(8) (because the partnership's assets are not treated as forming part of a permanent establishment in the United States). See proposed §1.864(c)(8)-1(d).

V. *Anti-Stuffing Rule*

The proposed regulations include an anti-stuffing rule applicable to both these regulations and section 897. This rule is included to prevent inappropriate reductions in amounts characterized as effectively connected with the conduct of a trade or business within the United States under section 864(c)(8) or section 897. A cross-reference to this rule is also included in the proposed regulation under section 897.

VI. *Section 1446(f) Guidance*

The proposed regulations do not provide guidance under section 1446(f). The Treasury Department and the IRS intend to issue guidance under section 1446(f) expeditiously.

Applicability Dates

The proposed regulations apply to transfers occurring on or after November 27, 2017, the effective date of section 864(c)(8). See section 7805(b)(2). If any provision is finalized after June 22, 2019, the Treasury Department and the IRS expect that such provision will apply only to transfers occurring on or after December 21, 2018. *See* section 7805(b)(1)(B).

Special Analyses

Executive Orders 13771, 13563, and 12866 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits, including potential economic, environmental, public health and safety effects, distributive impacts, and equity. Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility.

These proposed regulations have been designated by the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA) as subject to review under Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding review of tax regulations. OIRA has determined that the proposed rulemaking is significant and subject to review under EO 12866 and section 1(b) of the Memorandum of Agreement. Accordingly, the proposed regulations have been reviewed by the Office of Management and Budget.

The Treasury Department and the IRS have assessed the benefits and costs of the proposed regulations relative to a no-action baseline reflecting anticipated tax-related behavior and other economic behavior in the absence of these proposed regulations. Because the proposed regulations generally provide taxpayers with additional certainty on the amount and character of gain or loss treated as effectively connected income as a result of section 864(c)(8) and concurrently coordinate section 864(c)(8) with other provisions in the Code, the Treasury Department and the IRS anticipate only minimal economic or revenue effects from the proposed regulations. The Treasury Department and the IRS estimate that between 5,000 and 10,000 taxpayers are potentially affected by section 864(c)(8), with only a fraction of these taxpayers having gain or loss from disposition of a partnership in any one year. The Treasury Department and the IRS estimate that the affected taxpayers would see a minimal difference in treatment between these proposed regulations and Revenue Ruling 91-32. Comments are requested regarding these assessments. The Treasury Department and the IRS have assessed that the proposed regulations do not establish a new collection of information nor modify an existing collection that requires the approval of the Office of Management and Budget under the Paperwork Reduction Act (44 U.S.C. chapter 35). The Treasury Department and the IRS seek comments on this assessment.

Section 864(c)(8) and the proposed regulations generally apply to nonresident alien individuals and foreign corporations on the transfer of an interest in a partnership that is engaged in a trade or business within the United States, and not directly to the trade or business the partnership conducts in the United States. Under section 605 of the Regulatory Flexibility Act (5 U.S.C. chapter 6), the Treasury Department and the IRS certify that the proposed regulations will not have a significant economic impact on a substantial number of small entities. The reason is that the proposed regulations generally apply to nonresident alien individuals and foreign corporations on the transfer of an interest in a partnership and not directly to a domestic small business. Pursuant to section 7805(f), this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their 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 comments that are submitted timely to the IRS as prescribed in this preamble under the "**ADDRESSES**" heading. The Treasury Department and the IRS request comments on all aspects of the proposed regulations, and specifically on the issues identified in sections I.A.2, I.B, and I.C of the Explanations of Provisions. All comments will be available at *www.regulations.gov* or upon request. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, then notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of the proposed regulations are Ronald M. Gootzeit and Chadwick Rowland, Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in their development.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings, notices, and other guidance cited in this document are published in the Internal Revenue Bulletin (or Cumulative Bulletin) and are available from the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402, or by visiting the IRS website at *http://www.irs.gov*.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

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

PART 1— INCOME TAXES

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

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

Section 1.864(c)(8)-1 also issued under 26 U.S.C. 864(c)(8) and 897(g).

*****

Section 1.897-7 also issued under 26 U.S.C. 897(g).

*****

Par. 2. Section 1.864(c)(8)-1 is added to read as follows:

§1.864(c)(8)-1 Gain or loss by foreign persons on the disposition of certain partnership interests.

(a) *Overview*. This section provides rules and definitions under section 864(c)(8). Paragraph (b) of this section provides the general rule treating gain or loss recognized by a nonresident alien individual or foreign corporation from the sale or exchange of a partnership interest as effectively connected gain or effectively connected loss. Paragraph (c) of this section provides rules for determining the limitation on the amount of effectively connected gain or effectively connected loss under section 864(c)(8) and paragraph (b) of this section. Paragraph (d) of this section provides rules regarding coordination with section 897. Paragraph (e) of this section provides rules regarding certain tiered partnerships. Paragraph (f) of this section provides rules regarding U.S. income tax treaties. Paragraph (g) of this section provides definitions. Paragraph (h) of this section provides a rule regarding certain contributions of property to a partnership. Paragraph (i) of this section contains examples illustrating the rules set forth in this section. Paragraph (j) of this section provides the applicability date.

(b) *Gain or loss treated as effectively connected gain or loss*—(1) *In general*. Notwithstanding any other provision of subtitle A of the Internal Revenue Code, if a foreign transferor owns, directly or indirectly, an interest in a partnership that is engaged in the conduct of a trade or business within the United States, outside capital gain, outside capital loss, outside ordinary gain, or outside ordinary loss (each as defined in paragraph (b)(2) of this section) recognized by the foreign transferor on the transfer of all (or any portion) of the interest is treated as effectively connected gain or effectively connected loss, subject to the limit described in paragraph (b)(3) of this section. Except as provided in paragraph (d) of this section, this section does not apply to prevent any portion of the gain or loss that is otherwise treated as effectively connected gain or effectively connected loss under provisions of the Internal Revenue Code other than section 864(c)(8) from being so treated.

(2) *Determination of outside gain and loss*—(i) *In general*. The amount of gain or loss recognized by the foreign transferor in connection with the transfer of its partnership interest is determined under all relevant provisions of the Internal Revenue Code and the regulations thereunder.

See, e.g., §§1.741-1(a) and 1.751-1(a)(2). For purposes of this section, the amount of gain or loss that is treated as capital gain or capital loss under sections 741 and 751 is referred to as *outside capital gain* or *outside capital loss*, respectively. The amount of gain or loss that is treated as ordinary gain or ordinary loss under sections 741 and 751 is referred to as *outside ordinary gain* or *outside ordinary loss*, respectively.

(ii) *Nonrecognition provisions*. A foreign transferor's gain or loss recognized in connection with the transfer of its partnership interest does not include gain or loss to the extent that the gain or loss is not recognized by reason of one or more nonrecognition provisions of the Internal Revenue Code.

(3) *Limitations*. This paragraph (b)(3) limits the amount of gain or loss recognized by a foreign transferor that may be treated as effectively connected gain or effectively connected loss.

(i) *Capital gain limitation*. Outside capital gain recognized by a foreign transferor is treated as effectively connected gain to the extent it does not exceed aggregate deemed sale EC capital gain determined under paragraph (c)(3)(ii)(B) of this section.

(ii) *Capital loss limitation*. Outside capital loss recognized by a foreign transferor is treated as effectively connected loss to the extent it does not exceed aggregate deemed sale EC capital loss determined under paragraph (c)(3)(ii)(B) of this section.

(iii) *Ordinary gain limitation*. Outside ordinary gain recognized by a foreign transferor is treated as effectively connected gain to the extent it does not exceed aggregate deemed sale EC ordinary gain determined under paragraph (c)(3)(ii)(A) of this section.

(iv) *Ordinary loss limitation*. Outside ordinary loss recognized by a foreign transferor is treated as effectively connected loss to the extent it does not exceed aggregate deemed sale EC ordinary loss determined under paragraph (c)(3)(ii)(A) of this section.

(c) *Amount treated as effectively connected with the conduct of a trade or business within the United States*. This paragraph (c) describes the steps to be followed in computing the limitations described in paragraph (b)(3) of this section.

(1) *Step 1: Determine deemed sale gain and loss*. Determine the amount of gain or loss that the partnership would recognize with respect to each of its assets (other than interests in partnerships described in paragraph (e) of this section) upon a deemed sale of all of the partnership's assets on the date of the transfer of the partnership interest described in paragraph (b)(1) of this section (deemed sale). For this purpose, a deemed sale is a hypothetical sale by the partnership to an unrelated person of each of its assets (tangible and intangible) in a fully taxable transaction for cash in an amount equal to the fair market value of each asset (taking into account section 7701(g)) immediately before the partner's transfer of the interest in the partnership. For rules concerning the deemed sale of certain partnership interests, see paragraph (e) of this section.

(2) *Step 2: Determine deemed sale EC gain and loss*—(i) *In general*. With respect to each asset deemed sold in paragraph (c)(1) of this section, determine the amount of gain or loss from the deemed sale that would be treated as effectively connected gain or effectively connected loss (including by reason of section 897, taking into account any exceptions thereto, such as section 897(k) or section 897(l)). Gain described in this paragraph (c)(2) is referred to as *deemed sale EC gain*, and loss described in this paragraph (c)(2) is referred to as *deemed sale EC loss*. Section 864 and the regulations thereunder apply for purposes of determining whether gain or loss that would arise in a deemed asset sale would be treated as effectively connected gain or loss. For purposes of this paragraph (c)(2)(i), gain or loss from the deemed sale of an asset is treated as attributable to an office or other fixed place of business maintained by the partnership in the United States, and is not treated as sold for use, disposition, or consumption outside the United States in a sale in which an office or other fixed place of business maintained by the partnership in a foreign country materially participated in the sale.

(ii) *Exception*. Gain or loss from the deemed sale of an asset described in paragraph (c)(2)(i) of this section (other than a United States real property interest) is not treated as deemed sale EC gain or deemed sale EC loss if—

(A) No income or gain produced by the asset was taxable as income that was effectively connected with the conduct of a trade or business within the United States by the partnership (or a predecessor of the partnership) during the ten-year period ending on the date of the transfer; and

(B) The asset has not been used, or held for use, in the conduct of a trade or business within the United States by the partnership (or a predecessor of the partnership) during the ten-year period ending on the date of the transfer.

(3) *Step 3: Determine the foreign transferor's distributive share of deemed sale EC gain or deemed sale EC loss*—(i) *In general.* Determine the foreign transferor's distributive share of deemed sale EC gain and deemed sale EC loss. A foreign transferor's distributive share of deemed sale EC gain or deemed sale EC loss with respect to each asset is the amount of the deemed sale EC gain and deemed sale EC loss determined under paragraph (c)(2) of this section that would have been allocated to the foreign transferor by the partnership under all applicable Code sections (including section 704) upon the deemed sale described in paragraph (c)(1) of this section, taking into account allocations of tax items applying the principles of section 704(c), including any remedial allocations under §1.704-3(d), and any section 743 basis adjustment pursuant to §1.743-1(j)(3)).

(ii) *Aggregate deemed sale EC items*—(A) *Ordinary gain or loss*. A foreign transferor's *aggregate deemed sale EC ordinary gain* (if the aggregate results in a gain) or *aggregate deemed sale EC ordinary loss* (if the aggregate results in a loss) is the sum of—

(*1*) The portion of the foreign transferor's distributive share of deemed sale EC gain and deemed sale EC loss that is attributable to the deemed sale of the partnership's assets that are section 751(a) property; and

(*2*) Deemed sale EC gain and deemed sale EC loss from the sale of assets that are section 751(a) property that would be allocated to the foreign transferor with respect to interests in partnerships that are engaged in the conduct of a trade or business within the United States under paragraph (e)(1)(ii) of this section upon the deemed asset sales described in paragraph (e)(1)(i) of this section.

(B) *Capital gain or loss*. A foreign transferor's *aggregate deemed sale EC capital gain* (if the aggregate of the foreign transferor's distributive share of the deemed sale EC capital gain and loss results in a gain) or *aggregate deemed sale EC capital loss* (if the aggregate of the foreign transferor's distributive share of the deemed sale EC capital gain and loss results in a loss) is the sum of—

(*1*) The portion of the foreign transferor's distributive share of deemed sale EC gain and deemed sale EC loss that is attributable to the deemed sale of assets that are not section 751(a) property; and

(*2*) Deemed sale EC gain and deemed sale EC loss from the sale of assets that are not section 751(a) property and that would be allocated to the foreign transferor with respect to all interests in partnerships that are engaged in the conduct of a trade or business within the United States under paragraph (e)(1)(ii) of this section upon the deemed asset sales described in paragraph (e)(1)(i) of this section.

(iii) *Partial transfers*. If a foreign transferor transfers less than all of its interest in a partnership, then for purposes of paragraph (c)(3)(i) of this section, the foreign transferor's distributive share of deemed sale EC gain and deemed sale EC loss is determined by reference to the amount of deemed sale EC gain or deemed sale EC loss determined under paragraph (c)(3)(i) of this section that is attributable to the portion of the foreign transferor's partnership interest that was transferred.

(d) *Coordination with section 897*. If a foreign transferor transfers an interest in a partnership in a transfer that is subject to section 864(c)(8), and the partnership owns one or more United States real property interests (as defined in section 897(c)), then the foreign transferor determines its effectively connected gain and effectively connected loss under this section, and not pursuant to section 897(g). Accordingly, with respect to a transfer described in the preceding sentence, section 864(c)(8)(C) does not reduce the amount of gain or loss treated as effectively connected gain or loss under this section. For rules regarding a transfer not subject to section 864(c)(8) of an interest in a partnership that owns one or more United States real property interests, see section 897(g) and the regulations thereunder.

(e) *Tiered partnerships*—(1) *Transfers of upper-tier partnerships*. Assets sold in a deemed sale described in paragraph (c)(1) of this section do not include interests in partnerships that are engaged in the conduct of a trade or business within the United States or interests in partnerships that hold, directly or indirectly, partnerships that are engaged in the conduct of a trade or business within the United States. Rather, if a foreign transferor transfers an interest in a partnership (upper-tier partnership) that owns, directly or indirectly, an interest in one or more partnerships that are engaged in the conduct of a trade or business within the United States, then—

(i) Beginning with the lowest-tier partnership that is engaged in the conduct of a trade or business within the United States in a chain of partnerships and going up the chain, each partnership that is engaged in the conduct of a trade or business within the United States is treated as selling its assets in a deemed sale in accordance with the principles of paragraph (c)(1) of this section; and

(ii) Each partnership must determine its deemed sale EC gain and deemed sale EC loss in accordance with the principles of paragraph (c)(2) of this section, and determine the distributive share of deemed sale EC gain and deemed sale EC loss for each partner that is either a partnership (in which the foreign transferor is a direct or indirect partner) or a foreign transferor, in accordance with the principles of paragraph (c)(3)(i) of this section.

(2) *Transfers by upper-tier partnerships*. If a foreign transferor is a direct or indirect partner in an upper-tier partnership and the upper-tier partnership transfers an interest in a partnership that is engaged in the conduct of a trade or business within the United States (including a partnership held indirectly through one or more partnerships), then the principles of this section (including paragraph (e)(1) of this section) apply with respect to the gain or loss on the transfer that is allocated to the foreign transferor by the upper-tier partnership.

(3) *Coordination with section 897*. For purposes of this paragraph (e), a lower-tier partnership that holds one or more United States real property interests is treated as engaged in the conduct of a trade or business within the United States.

(f) *Income tax treaties*—(1) *In general*. This paragraph (f) describes how the provisions of a U.S. income tax treaty apply to the transfer by a foreign transferor that is eligible for benefits under the treaty of an interest in a partnership that is engaged in the conduct of a trade or business within the United States.

(2) *Application of gains article*. Treaty provisions applicable to gains from the alienation of property forming part of a permanent establishment, including gains from the alienation of a permanent establishment in the United States, apply to the transfer by a foreign transferor of an interest in a partnership with a permanent establishment in the United States.

(3) *Coordination rule*. For purposes of applying paragraph (c) of this section to gains described in paragraph (f)(2) of this section, a foreign transferor's distributive share of deemed sale EC gain and deemed sale EC loss are determined with respect to the assets of the partnership that form part of the partnership's permanent establishment in the United States and that are not otherwise exempt from U.S. taxation under the treaty.

(g) *Definitions*. The following definitions apply for purposes of this section.

(1) *Effectively connected gain*. The term *effectively connected gain* means gain that is treated as effectively connected with the conduct of a trade or business within the United States.

(2) *Effectively connected loss*. The term *effectively connected loss* means loss treated as effectively connected with the conduct of a trade or business within the United States.

(3) *Foreign transferor*. The term *foreign transferor* means a nonresident alien individual or foreign corporation.

(4) *Section 751(a) property*. The term *section 751(a) property* means unrealized receivables described in section 751(c) and inventory items described in section 751(d).

(5) *Transfer*. The term *transfer* means a sale, exchange, or other disposition, and includes a distribution from a partnership

to a partner to the extent that gain or loss is recognized on the distribution, as well as a transfer treated as a sale or exchange under section 707(a)(2)(B).

(h) *Anti-stuffing rule*. If a foreign transferor (or a person that is related to a foreign transferor within the meaning of section 267(b) or 707(b)) transfers property (including another partnership interest) to a partnership in a transaction with a principal purpose of reducing the amount of gain treated as effectively connected gain, or increasing the amount of loss treated as effectively connected loss, under section 864(c)(8) or section 897, the transfer is disregarded for purposes of section 864(c)(8) or section 897, as appropriate, or otherwise recharacterized in accordance with its substance.

(i) *Examples*. This paragraph provides examples that illustrate the rules of this section. For purposes of this paragraph, unless otherwise provided, the following facts are presumed. FP is a foreign corporation. USP is a domestic corporation. PRS is a partnership that was formed on January 1, 2018, when FP and USP each contributed $100x in cash. PRS has made no distributions and received no contributions other than those described in paragraph (i)(1)(iii) of this section. FP's adjusted basis in its interest in PRS is $100x. X is a foreign corporation that is unrelated to FP, USP, or PRS. Upon the formation of PRS, FP and USP entered into an agreement providing that all income, gain, loss, and deduction of PRS will be allocated equally between FP and USP. PRS is engaged in the conduct of a trade or business within the United States (the U.S. Business) and an unrelated business in Country A (the Country A Business). In a deemed sale described in paragraph (c)(1) of this section, gain or loss on assets of the U.S. Business would be treated as effectively connected gain or effectively connected loss, and gain or loss on assets of the Country A Business would not be so treated (including by reason of paragraph (c)(2)(ii) of this section). PRS has no liabilities. FP does not qualify for the benefits of an income tax treaty between the United States and another country.

(1) *Example 1. Deemed sale limitation*—(i) *Facts*. On January 1, 2019, FP sells its entire interest in PRS to X for $105x. Immediately before the sale, PRS's balance sheet appears as follows:

	Adjusted Basis	*Fair Market Value*
U.S. Business capital asset	$100x	$104x
Country A Business capital asset	100x	106x
Total	$200x	$210x

(ii) *Analysis*—(A) *Outside gain or loss*. FP is a foreign transferor (within the meaning of paragraph (g)(3) of this section) and transfers (within the meaning of paragraph (g)(5) of this section) its interest in PRS to X. FP recognizes a $5x capital gain under section 741, which is an outside capital gain within the meaning of paragraph (b)(2)(i) of this section. Under paragraph (b)(1) of this section, FP's $5x capital gain is treated as effectively connected gain to the extent that it does not exceed the limitation described in paragraph (b)(3)(i) of this section, which is FP's aggregate deemed sale EC capital gain.

(B) *Deemed sale*. FP's aggregate deemed sale EC capital gain is determined according to the three-step process set forth in paragraph (c) of this section. First, the amount of gain or loss that PRS would recognize with respect to each of its assets upon a deemed sale described in paragraph (c)(1) of this section is a $4x gain with respect to the U.S. Business capital asset and a $6x gain with respect to the Country A Business capital asset. Second, under paragraph (c)(2) of this section, PRS's deemed sale EC gain is $4x. PRS recognizes no deemed sale EC gain or loss with respect to the Country A Business capital asset under section 864 and paragraph (c)(2)(ii) of this section. Third, under paragraph (c)(3)(ii)(B) of this section, FP's aggregate deemed sale EC capital gain is $2x (that is, the aggregate of its distributive share of deemed sale EC gain attributable to the deemed sale of assets that are not section 751(a) property, which is 50% of $4x).

(C) *Limitation*. Under paragraph (b)(3)(i) of this section, the $5x outside capital gain recognized by FP is treated as effectively connected gain to the extent that it does not exceed FP's $2x aggregate deemed sale EC capital gain. Accordingly, FP recognizes $2x of capital gain that is treated as effectively connected gain.

(2) *Example 2. Outside gain limitation*—(i) *Facts*. On January 1, 2019, FP sells its entire interest in PRS to X for $110x. Immediately before the sale, PRS's balance sheet appears as follows:

	Adjusted Basis	*Fair Market Value*
U.S. Business capital asset	$100x	$150x
Country A Business capital asset	100x	70x
Total	$200x	$220x

(ii) *Analysis*—(A) *Outside gain or loss*. FP is a foreign transferor (within the meaning of paragraph (g)(3) of this section) and transfers (within the meaning of paragraph (g)(5) of this section) its interest in PRS to X. FP recognizes a $10x capital gain under section 741, which is an outside capital gain within the meaning of paragraph (b)(2)(i) of this section. Under paragraph (b)(1) of this section, FP's $10x capital gain is treated as effectively connected gain to the extent that it does not exceed the limitation described in paragraph (b)(3)(i) of this section, which is FP's aggregate deemed sale EC capital gain.

(B) *Deemed sale*. FP's aggregate deemed sale EC capital gain is determined according to the three-step process set forth in paragraph (c) of this section. First, the amount of gain or loss that PRS would recognize with respect to each of its assets upon a deemed sale described in paragraph (c)(1) of this section is a $50x gain with respect to the U.S. Business capital asset and a $30x loss with respect to the Country A Business capital asset. Second, under paragraph (c)(2) of this section, PRS's deemed sale EC gain is $50x. PRS recognizes no deemed sale EC gain or loss with respect to the Country A Business capital asset under section 864 and paragraph (c)(2)(ii) of this section. Third, under paragraph (c)(3) of this section, FP's aggregate deemed sale EC capital gain is $25x (that is, the aggregate of its distributive share of deemed sale EC gain attributable to the deemed sale of assets that are not section 751(a) property, which is 50% of $50x).

(C) *Limitation*. Under paragraph (b)(3)(i) of this section, the $10x outside capital gain recognized by FP is treated as effectively connected gain to the extent that it does not exceed FP's $25x aggregate deemed sale EC capital gain. Accordingly, FP recognizes $10x of capital gain that is treated as effectively connected gain.

(3) *Example 3. Interaction with section 751(a)*—(i) *Facts*. On January 1, 2019, FP sells its entire interest in PRS to X for $95x. Through both its U.S. Business and its Country A Business, PRS holds inventory items that are section 751 property (as defined in §1.751-1(a)). Immediately before the sale, PRS's balance sheet appears as follows:

	Adjusted Basis	*Fair Market Value*
U.S. Business capital asset	$20x	$50x
U.S. Business inventory	30x	50x
Country A Business capital asset	100x	80x
Country A Business inventory	50x	10x
Total	$200x	$190x

(ii) *Analysis*—(A) *Outside gain or loss*. FP is a foreign transferor (within the meaning of paragraph (g)(3) of this section) and transfers (within the meaning of paragraph (g)(5) of this section) its interest in PRS to X. Under sections 741 and 751, FP recognizes a $10x ordinary loss and a $5x capital gain. See §1.751-1(a). Under paragraph (b)(2)(i) of this section, FP has outside ordinary loss equal to $10x and outside capital gain equal to $5x. Under paragraph (b)(1) of this section, FP's outside ordinary loss and outside capital gain are treated as effectively connected loss and effectively connected gain to the extent that each does not exceed the applicable limitation described in paragraph (b)(3) of this section. In the case of FP's outside ordinary loss, the applicable limitation is FP's aggregate deemed sale EC ordinary loss. In the case of FP's outside capital gain, the applicable limitation is FP's aggregate deemed sale EC capital gain.

(B) *Deemed sale*. FP's aggregate deemed sale EC ordinary loss and aggregate deemed sale EC capital gain are determined according to the three-step process set forth in paragraph (c) of this section.

(*1*) *Step 1*. The amount of gain or loss that PRS would recognize with respect to each of its assets upon a deemed sale described in paragraph (c)(1) of this section is as follows:

Asset	*Gain/(Loss)*
U.S. Business capital asset	$30x
U.S. Business inventory	20x
Country A Business capital asset	(20x)
Country A Business inventory	(40x)

(*2*) *Step 2*. Under paragraph (c)(2) of this section, PRS's deemed sale EC gain and deemed sale EC loss must be determined with respect to each asset. The amounts determined under paragraph (c)(2) of this section are as follows:

Asset	*Deemed Sale EC Gain/(Loss)*
U.S. Business capital asset	$30x
U.S. Business inventory	20x
Country A Business capital asset	0
Country A Business inventory	0

(*3*) *Step 3*. Under paragraph (c)(3) of this section, FP's aggregate deemed sale EC capital gain is $15x (that is, the aggregate of its distributive share of deemed sale EC gain that is attributable to the deemed sale of assets that are not section 751(a) property, which is 50% of $30x) and FP's aggregate deemed sale EC ordinary loss is $0 (that is, the aggregate of its distributive share of deemed sale EC loss that is attributable to the deemed sale of assets that are section 751(a) property).

(C) *Limitation*—(i) *Capital gain*. Under paragraph (b)(3)(i) of this section, the $5x outside capital gain recognized by FP is treated as effectively connected gain to the extent that it does not exceed FP's $15x aggregate deemed sale EC capital gain. Accordingly, the amount of FP's capital gain that is treated as effectively connected gain is $5x.

(ii) *Ordinary loss*. Under paragraph (b)(3)(iv) of this section, the $10x outside ordinary loss recognized by FP is treated as effectively connected loss to the extent that it does not exceed FP's $0 aggregate deemed sale EC ordinary loss. Accordingly, the amount of FP's ordinary loss that is treated as effectively connected loss is $0.

(j) *Applicability date*. This section applies to transfers occurring on or after November 27, 2017.

Par. 3. Section 1.897-7 is added to read as follows:

§1.897-7 Treatment of certain partnership interests, trusts and estates under section 897(g).

(a) through (b) [Reserved]. For further guidance, see § 1.897-7T(a) through (b).

(c) *Coordination with section 864(c)(8)*. Except as provided in §1.864(c)(8)-1, the amount of any money, and the fair market value of any property, received by a nonresident alien individual or foreign corporation in exchange for all or part of its interest in a partnership, trust, or estate shall, to the extent attributable to United States real property interests, be considered as an amount received from the sale or exchange in the United States of such property. See also §1.864(c)(8)-1(h) for an anti-stuffing rule that may apply to transactions subject to section 897. This paragraph applies to transfers occurring on or after November 27, 2017.

Par. 4. Section 1.897-7T is amended by adding paragraph (c) to read as follows:

§1.897-7T Treatment of certain partnership interests as entirely U.S. real property interests under sections 897(g) and 1445(e) (temporary).

* * * * *

(c) *Coordination with section 864(c)(8)*. [Reserved]. For further guidance, see §1.897-7(c).

Kirsten Wielobob,

Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on December 21, 2018, 4:15 p.m., and published in the issue of the Federal Register for December 27, 2018, 83 F.R. 66647)

Definition of Terms

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

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

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

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

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

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

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

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

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

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

Abbreviations

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

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

Numerical Finding List[1]

Bulletin 2019–22

Action on Decision:

2019-1, 2019-08 I.R.B. *569*

Announcements:

2019-1, 2019-06 I.R.B. *566*
2019-2, 2019-12 I.R.B. *910*
2019-3, 2019-15 I.R.B. *965*
2019-4, 2019-21 I.R.B. *1192*
2019-5, 2019-22 I.R.B. *1262*

Notices:

2019-01, 2019-02 I.R.B. *275*
2019-02, 2019-02 I.R.B. *281*
2019-03, 2019-03 I.R.B. *350*
2019-04, 2019-02 I.R.B. *282*
2019-05, 2019-02 I.R.B. *283*
2019-06, 2019-03 I.R.B. *353*
2019-07, 2019-09 I.R.B. *740*
2019-08, 2019-03 I.R.B. *354*
2019-09, 2019-04 I.R.B. *403*
2019-10, 2019-13 I.R.B. *913*
2019-11, 2019-05 I.R.B. *430*
2019-13, 2019-08 I.R.B. *580*
2019-16, 2019-10 I.R.B. *763*
2019-17, 2019-12 I.R.B. *907*
2019-18, 2019-13 I.R.B. *915*
2019-19, 2019-12 I.R.B. *907*
2019-20, 2019-14 I.R.B. *927*
2019-21, 2019-14 I.R.B. *927*
2019-22, 2019-14 I.R.B. *931*
2019-23, 2019-15 I.R.B. *941*
2019-24, 2019-14 I.R.B. *932*
2019-25, 2019-15 I.R.B. *942*
2019-26, 2019-15 I.R.B. *943*
2019-28, 2019-18 I.R.B. *1077*
2019-30, 2019-20 I.R.B. *1180*
2019-31, 2019-20 I.R.B. *1181*
2019-32, 2019-21 I.R.B. *1187*
2019-33, 2019-22 I.R.B. *1255*
2019-34, 2019-22 I.R.B. *1257*

Proposed Regulations:

REG-104259-18, 2019-02 I.R.B. *300*
REG-104352-18, 2019-03 I.R.B. *357*
REG-106089-18, 2019-05 I.R.B. *431*
REG-134652-18, 2019-09 I.R.B. *747*
REG-141739-08, 2019-09 I.R.B. *757*
REG-121694-16, 2019-16 I.R.B. *1032*
REG-135671-17, 2019-16 I.R.B. *1035*
REG-103083-18, 2019-17 I.R.B. *1046*
REG-113943-17, 2019-17 I.R.B. *1067*

Proposed Regulations:—Continued

REG-143686-07, 2019-17 I.R.B. *1072*
REG-124627-11, 2019-17 I.R.B. *1073*
REG-120186-18, 2019-21 I.R.B. *1193*
REG-113604-18, 2019-22 I.R.B. *1265*

Revenue Procedures:

2019-1, 2019-01 I.R.B. *1*
2019-2, 2019-01 I.R.B. *106*
2019-3, 2019-01 I.R.B. *130*
2019-4, 2019-01 I.R.B. *146*
2019-5, 2019-01 I.R.B. *230*
2019-6, 2019-02 I.R.B. *284*
2019-7, 2019-01 I.R.B. *268*
2019-8, 2019-03 I.R.B. *347*
2019-9, 2019-02 I.R.B. *293*
2019-10, 2019-02 I.R.B. *296*
2019-11, 2019-09 I.R.B. *742*
2019-12, 2019-04 I.R.B. *401*
2019-13, 2019-09 I.R.B. *744*
2019-14, 2019-15 I.R.B. *948*
2019-15, 2019-14 I.R.B. *939*
2019-17, 2019-17 I.R.B. *1045*
2019-18, 2019-18 I.R.B. *1077*
2019-20, 2019-20 I.R.B. *1182*
2019-21, 2019-21 I.R.B. *1190*
2019-22, 2019-22 I.R.B. *1260*
2019-25, 2019-22 I.R.B. *1261*

Revenue Rulings:

2019-03, 2019-02 I.R.B. *272*
2019-04, 2019-07 I.R.B. *567*
2019-05, 2019-11 I.R.B. *766*
2019-06, 2019-14 I.R.B. *919*
2019-07, 2019-10 I.R.B. *761*
2019-08, 2019-14 I.R.B. *923*
2019-09, 2019-14 I.R.B. *925*
2019-10, 2019-16 I.R.B. *1010*
2019-11, 2019-17 I.R.B. *1041*
2019-13, 2019-20 I.R.B. *1179*

Treasury Decisions:

9844, 2019-11 I.R.B. *781*
9845, 2019-08 I.R.B. *570*
9846, 2019-09 I.R.B. *583*
9847, 2019-09 I.R.B. *670*
9848, 2019-11 I.R.B. *897*
9850, 2019-12 I.R.B. *904*
9852, 2019-16 I.R.B. *1010*
9853, 2019-16 I.R.B. *1026*
9855, 2019-17 I.R.B. *1042*
9854, 2019-18 I.R.B. *1075*
9857, 2019-22 I.R.B. *1239*
9858, 2019-22 I.R.B. *1251*

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

Finding List of Current Actions on Previously Published Items[1]

Bulletin 2019–22

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

Internal Revenue Service
Washington, DC 20224

Official Business
Penalty for Private Use, $300

INTERNAL REVENUE BULLETIN

The Introduction at the beginning of this issue describes the purpose and content of this publication. The weekly Internal Revenue Bulletins are available at *www.irs.gov/irb/*.

We Welcome Comments About the Internal Revenue Bulletin

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