Internal Revenue
bulletin

Bulletin No. 2006-43
October 23, 2006

HIGHLIGHTS OF THIS ISSUE

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

INCOME TAX

T.D. 9286, page 750.
REG–142270–05, page 791.

Temporary and proposed regulations under section 45G of the Code provide guidance regarding the railroad track maintenance credit determined for qualified railroad track maintenance expenditures paid or incurred by a Class II or Class III railroad and other eligible taxpayers during the taxable year. A public hearing on the proposed regulations is scheduled for January 9, 2007.

REG–105248–04, page 787.

Proposed regulations under section 853 of the Code would eliminate country-by-country reporting by a regulated investment company (RIC) to its shareholders of foreign source income received by the RIC and foreign taxes paid by the RIC. Under these regulations, the IRS and the Treasury Department would continue to require the reporting of per-country information by RICs to the IRS because this information remains relevant to monitoring compliance with the foreign tax credit provisions.

Notice 2006–79, page 763.

This notice sets forth additional transition relief under section 409A. The notice generally extends through December 31, 2007, the transition relief that previously had been provided through December 31, 2006, subject to certain exceptions.

Notice 2006–87, page 766.

This notice provides adjustments to the limitation on housing expenses for purposes of section 911 of the Code for specific locations, based on geographic differences in housing costs, relative to housing costs in the United States.

EMPLOYEE PLANS

Notice 2006–79, page 763.

This notice sets forth additional transition relief under section 409A. The notice generally extends through December 31, 2007, the transition relief that previously had been provided through December 31, 2006, subject to certain exceptions.

Notice 2006–89, page 772.

Section 906 of Pension Protection Act of 2006; transition rule. This notice provides transition relief for plans of Indian tribal governments to comply with the changes made by section 906 of the Pension Protection Act of 2006 under a reasonable and good faith standard, pending further guidance. The notice also provides for Indian tribal governments to implement a new plan for commercial employees by September 30, 2007, to satisfy this standard as a part of this transition relief.

Notice 2006–94, page 777.

Weighted average interest rate update; corporate bond indices; 30-year Treasury securities. The weighted average interest rate for October 2006 and the resulting permissible range of interest rates used to calculate current liability and to determine the required contribution are set forth.

EXCISE TAX

Rev. Rul. 2006–52, page 761.

Resellers of air transportation. This ruling explains the tax consequences under section 4261 of the Code when a traveler purchases a ticket for taxable transportation from a third party intermediary other than the airline. Rev. Ruls. 75–296 and 80–31 distinguished.

(Continued on the next page)

Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

Notice 2006–92, page 774.
This notice provides guidance on the alternative fuel and alternative fuel mixture credit and payments and the imposition of tax on alternative fuel and alternative fuel mixtures. The notice also provides guidance on the excise tax exemption for blood collector organizations.

ADMINISTRATIVE

Rev. Proc. 2006–41, page 777.
***Per diem* allowances.** This procedure provides optional rules for deeming substantiated the amount of certain business expenses of traveling away from home reimbursed to an employee or deductible by an employee or self-employed individual. Rev. Proc. 2005–67 superseded.

Announcement 2006–79, page 792.
This document contains corrections to a notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing (REG–112994–06, 2006–27 I.R.B. 47) relating to the determination of whether a foreign entity shall be treated as a surrogate foreign corporation under section 7874(a)(2)(B) of the Code.

The IRS Mission

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

Introduction

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

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

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

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

The Bulletin is divided into four parts as follows:

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

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

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

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

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

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

Section 45G.—Railroad Track Maintenance Credit

26 CFR 1.45G–1T: Railroad track maintenance credit (temporary).

T.D. 9286

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

Railroad Track Maintenance Credit

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations that provide rules for claiming the railroad track maintenance credit under section 45G of the Internal Revenue Code for qualified railroad track maintenance expenditures paid or incurred by a Class II railroad or Class III railroad and other eligible taxpayers during the taxable year. These temporary regulations reflect changes to the law made by the American Jobs Creation Act of 2004 and the Gulf Opportunity Zone Act of 2005. The text of these temporary regulations also serves as the text of the proposed regulations (REG–142270–05) set forth in the notice of proposed rulemaking on this subject in this issue of the Bulletin.

DATES: *Effective Date:* These regulations are effective on September 8, 2006.

Applicability Date: For dates of applicability, see §1.45G–1T(g).

FOR FURTHER INFORMATION CONTACT: Winston H. Douglas, (202) 622–3110 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

These temporary regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. 553). For this reason, the collection of information contained in these regulations has been reviewed, and pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545–2031. Responses to this collection of information are mandatory.

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

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden, and suggestions for reducing this burden, please refer to the preamble to the cross-referencing notice of proposed rulemaking published in this issue of the Bulletin.

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

Background

This document contains amendments to 26 CFR part 1 to provide regulations under section 45G of the Internal Revenue Code (Code). Section 45G was added to the Code by section 245(a) of the American Jobs Creation Act of 2004, Public Law 108–357 (118 Stat. 1418) (AJCA), and was modified by section 403(f) of the Gulf Opportunity Zone Act of 2005, Public Law 109–135 (119 Stat. 2577).

General Overview

Section 38 allows a credit for the taxable year for, among other things, the current year business credit. The current year business credit is the sum of the credits listed in section 38(b). Section 245(c)(1) of the AJCA amended section 38(b) of the Code to add to the list of credits the railroad track maintenance credit (RTMC) determined under section 45G(a).

Section 45G(a) provides that, for purposes of section 38, the RTMC for the taxable year is an amount equal to 50 percent of the qualified railroad track maintenance expenditures (QRTME) paid or incurred by an eligible taxpayer during the taxable year. Section 45G(d) defines the term QRTME to mean expenditures (whether or not chargeable to capital account) for maintaining railroad track owned by, or leased to, a Class II railroad or Class III railroad as of January 1, 2005. Section 45G(e) defines the terms Class II railroad and Class III railroad to have the respective meanings given those terms by the Surface Transportation Board (STB). Section 45G(c) defines an eligible taxpayer to mean any Class II railroad or Class III railroad, and any person who transports property using the rail facilities of such a railroad, or who furnishes railroad-related property or services to such a railroad, but only with respect to miles of railroad track assigned to such person by such a railroad.

Section 45G(b) imposes limitations on the amount of the RTMC for any taxable year. The credit allowed under section 45G(a) may not exceed $3,500 multiplied by the sum of (1) the number of miles of railroad track owned by, or leased to, the eligible taxpayer as of the close of the taxable year, and (2) the number of miles of railroad track assigned to the eligible taxpayer by a Class II railroad or Class III railroad that owns or leases the track as of the close of the taxable year.

Section 45G applies to QRTME paid or incurred during taxable years beginning after December 31, 2004, and before January 1, 2008.

Scope

The temporary regulations define several terms, including eligible taxpayer, QRTME, rail facilities, railroad-related property, and railroad-related services. The temporary regulations also instruct an eligible taxpayer how to determine the RTMC for the taxable year. Further, the temporary regulations provide guidance on assignments of miles of railroad track for purposes of section 45G, adjustments

to basis for the RTMC, and the treatment of controlled groups under section 45G.

Explanation of Provisions

Eligible Taxpayer

The temporary regulations provide that only an eligible taxpayer may claim the RTMC. An eligible taxpayer is defined in the temporary regulations as: (1) a Class II railroad or Class III railroad during the taxable year; (2) any person that transports property using the rail facilities of a Class II railroad or Class III railroad during the taxable year; or (3) any person that furnishes railroad-related property or railroad-related services to a Class II railroad or Class III railroad during the taxable year. A Class I railroad is an eligible taxpayer only if the Class I railroad is in the second or third category above and is assigned miles of railroad track for the taxable year by a Class II railroad or Class III railroad. A taxpayer in the second or third category is an eligible taxpayer only with respect to the miles of railroad track assigned to the person for the taxable year by a Class II railroad or Class III railroad.

Consistent with section 45G(e)(1), the temporary regulations provide that the terms Class II railroad and Class III railroad have the respective meanings given these terms by the STB. As determined by the STB, Class II railroads have annual carrier operating revenues of less than $250 million but in excess of $20 million after applying the railroad revenue deflator formula (Current Year's Revenues x (1991 Average Railroad Freight Price Index/Current Year's Average Railroad Freight Price Index)). 49 CFR Part 1201, Subpart A, §1–1(a). In general, Class III railroads have annual carrier operating revenues of $20 million or less after applying the railroad revenue deflator formula. 49 CFR Part 1201, Subpart A, §1–1(a).

The temporary regulations also provide that the rail facilities of a Class II railroad or Class III railroad include railroad yards, tracks, bridges, tunnels, wharves, docks, stations, and other related assets that are used in the transport of freight by a railroad and that are owned or leased by the Class II railroad or Class III railroad.

Railroad-related property is defined in the temporary regulations as meaning property that is provided directly to, and is unique to, a railroad. Further, this property must be property that, in the hands of a Class II railroad or Class III railroad, is described in asset classes 40.1 through 40.54 of Rev. Proc. 87–56, 1987–2 C.B. 674, with certain modifications, and is described in the STB property accounts for grading, tunnels and subways, and storage warehouses.

The temporary regulations define railroad-related services as meaning services that are provided directly to, and are unique to, a railroad. In addition, these services must relate to railroad shipping, loading and unloading of railroad freight, or repairs of rail facilities or railroad-related property. Examples of railroad-related services are the transport of freight by rail, the loading and unloading of freight transported by rail, locomotive leasing or rental, and maintenance of a railroad's right-of-way (including vegetation control). Examples of services that are not railroad-related services are general business services, cleaning services, banking services (including financing of railroad-related property), and office building rental.

Computation of Railroad Track Maintenance Credit

For purposes of section 38, the temporary regulations provide that the RTMC generally is equal to 50 percent of the QRTME paid or incurred by an eligible taxpayer during the taxable year. However, this credit amount cannot exceed the credit limitation provided by the temporary regulations. The credit limitation for a Class II railroad or Class III railroad differs from the credit limitation for other eligible taxpayers.

If an eligible taxpayer is a Class II railroad or Class III railroad, the temporary regulations provide that the RTMC cannot exceed $3,500 multiplied by the sum of: (1) the number of miles of railroad track owned or leased by the Class II railroad or Class III railroad within the United States at the close of its taxable year ("eligible railroad track"), reduced by the number of miles of eligible railroad track assigned by the Class II railroad or Class III railroad to another eligible taxpayer for that year; and (2) the number of miles of eligible railroad track owned or leased by another Class II railroad or Class III railroad that are assigned to the Class II railroad or Class III railroad for the taxable year.

If an eligible taxpayer is not a Class II railroad or Class III railroad, the temporary regulations provide that the RTMC cannot exceed $3,500 multiplied by the number of miles of eligible railroad track assigned to the eligible taxpayer by a Class II railroad or Class III railroad for the taxable year.

Determination of QRTME Paid or Incurred

The temporary regulations provide that QRTME is equal to the amount of expenditures paid or incurred during the taxable year by an eligible taxpayer for maintaining railroad track, roadbed, bridges, and related track structures that are located within the United States and owned or leased as of January 1, 2005, by a Class II railroad or Class III railroad. These expenditures may or may not be chargeable to a capital account. The regulations also define railroad track, roadbed, bridges, and related track structures as meaning property described in certain STB property accounts ("qualifying railroad structure").

The temporary regulations also define the term "paid or incurred" with respect to a taxpayer using an accrual method of accounting. In this case, paid or incurred means a liability incurred within the meaning of §1.446–1(c)(1)(ii). Consequently, a liability may not be taken into account under section 45G prior to the taxable year during which the liability is incurred. Further, the temporary regulations provide that QRTME is not paid or incurred during the taxable year to the extent that a taxpayer is entitled to reimbursement of any such expenditures. The temporary regulations provide that reimbursements may consist of amounts paid either directly or indirectly to the taxpayer. Examples of indirect reimbursements are discounted freight shipping rates, price markups of railroad-related property, debt forgiveness, or other similar arrangements. Thus, the temporary regulations limit the QRTME paid or incurred to the actual out-of-pocket expenditures paid or incurred by a taxpayer.

If an eligible taxpayer (assignee) pays a Class II railroad or Class III railroad (assignor) an amount in exchange for an assignment of one or more miles of eligible railroad track, the temporary regula-

tions provide that the amount is treated as QRTME paid or incurred by the assignee, and not the assignor railroad, at the time and to the extent the assignor pays or incurs QRTME. Consistent with the preceding paragraph, this QRTME would be reduced by any direct or indirect reimbursements made to the assignee during the taxable year with respect to that assignment.

Assignment of Railroad Track Miles

For purposes of section 45G, the temporary regulations provide that an assignment of a mile of railroad track is not a legal transfer of title, but merely a designation. This designation must be in writing and must include the names and taxpayer identification numbers of the Class II railroad or Class III railroad (assignor) making, and the eligible taxpayer (assignee) receiving, the assignment of eligible railroad track miles, the date of this assignment, and the number of miles of eligible railroad track that is assigned by the assignor to the assignee for a taxable year. The regulations also provide that the designation need not specify the location of the assigned mile of eligible railroad track and the assigned mile of eligible railroad track does not have to correspond to the mile of eligible railroad track on which the QRTME is paid or incurred by an eligible taxpayer.

Consistent with section 45G(b), the temporary regulations provide that only a Class II railroad or Class III railroad may assign a mile of eligible railroad track. Thus, if a Class II railroad or Class III railroad assigns a railroad track mile to an eligible taxpayer, the assignee is not permitted to reassign any eligible railroad track mile to another eligible taxpayer. The regulations also provide that the maximum number of miles of eligible railroad track that may be assigned by a Class II railroad or Class III railroad (assignor) for any taxable year are the total miles of eligible railroad track owned by, or leased to, the assignor reduced by the eligible railroad track miles that the assignor retains for itself in determining the RTMC.

The temporary regulations also provide that the assignment is treated as being made by the Class II railroad or Class III railroad at the close of Class II railroad's or Class III railroad's taxable year in which the assignment is made. The assignee takes the assignment into account for its taxable year that includes the date the assignment is treated as being made by the assignor railroad under the preceding sentence.

The temporary regulations require that a taxpayer must file Form 8900, "*Qualified Railroad Track Maintenance Credit*," with its timely filed (including extensions) Federal income tax return for the taxable year for which the taxpayer: (1) claims the RTMC; (2) assigns any miles of eligible railroad track; or (3) receives an assignment of any miles of eligible railroad track. Thus, for example, a Class II railroad or Class III railroad (assignor) that assigns all of its miles of eligible railroad track during a taxable year will need to file Form 8900 even though the assignor is not claiming any RTMC for that year.

As required by the temporary regulations, an assignor must attach to its Form 8900 an information statement identifying the name and taxpayer identification number (TIN) of each assignee, the total number of the assignor's eligible railroad track miles, the number of eligible railroad track miles assigned by the assignor to each assignee for the taxable year, and the total number of eligible railroad track miles assigned by the assignor to all assignees for the taxable year. Further, an eligible taxpayer (assignee) that received an assignment of railroad track miles during its taxable year from an assignor Class II railroad or Class III railroad and that claims the RTMC for that taxable year must attach to its Form 8900 a statement providing the total number of eligible railroad track miles assigned to the assignee for the taxable year and attesting that the assignee has in writing, and has retained as part of the assignee's records for purposes of §1.6001–1(a), information identifying the name and TIN of each assignor railroad, the date of each assignment, and the number of eligible railroad track miles assigned by each assignor railroad for the assignee's taxable year. If the Federal income tax return of a Class II railroad or Class III railroad, or another eligible taxpayer, for a taxable year ending after December 31, 2004, and ending before September 7, 2006, is filed before October 9, 2006, and the Class II railroad, Class III railroad, or other eligible taxpayer wants to apply the temporary regulations to that taxable year but did not include with that return the applicable information statement specified above, the regulations require the information statement to be attached to the taxpayer's next filed Federal income tax return or to the taxpayer's amended Federal income tax return filed pursuant to the effective date provisions in the temporary regulations (discussed later), provided this amended return is filed before the taxpayer's next filed Federal income tax return.

The temporary regulations also address situations in which a Class II railroad or Class III railroad (assignor) assigns more miles of eligible railroad track than the total number of miles that it owns or that are leased to it at the end of the taxable year in which the assignment is made. If the assignor does not own or have leased to it any eligible railroad track at the end of that year, the temporary regulations provide that any assignment made during that year is not valid, regardless of whether the assignment is properly reported. Similarly, if an assignor assigns more miles of eligible railroad track than it owned or are leased to it as of the end of the taxable year in which the assignment is made, the temporary regulations provide that the assignment is valid only with respect to the name of the assignee and the number of miles listed by the assignor on the information statement attached to its Form 8900 for that year and only to the extent of the maximum number of miles of eligible railroad track that may be assigned by the assignor Class II railroad or Class III railroad for the taxable year.

Special Rules

The temporary regulations provide rules for adjusting basis for the amount of the RTMC claimed by an eligible taxpayer. All or some of the QRTME paid or incurred by an eligible taxpayer during the taxable year may be required to be capitalized under section 263(a) as a tangible asset or as an intangible asset (see, for example, §1.263(a)–4(d)(8), which generally requires capitalization of amounts paid or incurred by a taxpayer to produce or improve real property owned by another). The basis of the tangible asset or intangible asset includes the capitalized amount of the QRTME. Thus, for purposes of section 45G(e)(3), the regulations provide that railroad track is qualifying

railroad structure (railroad track, roadbed, bridges, and related track structures) and intangible assets to which the QRTME is capitalized.

Consequently, if an eligible taxpayer claims the RTMC, the temporary regulations provide that the adjusted basis of these tangible and intangible assets must be reduced by the amount of the RTMC allowable. This reduction is taken into account at the time the QRTME is paid or incurred by an eligible taxpayer and before the depreciation deduction is determined for the taxable year for which the RTMC is allowable. If the amount of the QRTME is capitalized to more than one asset (for example, railroad track and bridges), whether tangible or intangible, the reduction to the basis of these assets is allocated among each of the assets subject to the reduction in proportion to the unadjusted basis of each asset at the time the QRTME is paid or incurred during that taxable year.

The temporary regulations also address the issue of how section 45G coordinates with section 61. Except as specifically provided in the Code, section 61 and §1.61–1(a) provide that gross income means all income from whatever source derived. Section 1.61–1(a) further provides that gross income includes income realized in any form, whether in money, property, or services. Section 45G does not provide, and its legislative history does not refer to, any exception to this rule. Accordingly, pursuant to section 61 and the regulations under section 61, the owner of the tangible assets (for example, railroad track and roadbed) with respect to which the QRTME is paid or incurred by another person that does not have a depreciable interest in those assets has gross income in the amount of that QRTME. However, the application of section 61 to QRTME paid or incurred with respect to eligible railroad track that is leased by a Class II railroad or Class III railroad raises a question as to under what circumstances the owner or lessee should recognize gross income with respect to QRTME. The IRS and Treasury Department request comments on this issue.

Finally, if an eligible taxpayer is a member of a controlled group of corporations, section 45G(e)(2) provides that rules similar to rules of section 41(f)(1) apply. Accordingly, the temporary regulations provide rules similar to those of §1.41–6T for determining the amount of the controlled group's RTMC, and rules for allocating the credit among members of the group.

Effective Date

These temporary regulations apply to taxable years ending on or after the date these regulations are filed in the **Federal Register** and beginning before January 1, 2008. However, a taxpayer may apply the temporary regulations to taxable years beginning after December 31, 2004, and ending before these regulations are filed in the **Federal Register**, provided that the taxpayer applies all provisions in these regulations to the taxable year.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. For the applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), please refer to the Special Analyses section of the preamble to the cross-reference notice of proposed rulemaking published in this issue of the Bulletin. Pursuant to section 7805(f), these temporary regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal author of these regulations is Winston H. Douglas, Office of the Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

Amendments to the Regulations

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

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.45G–0T is added to read as follows:

§1.45G–0T Table of contents for the railroad track maintenance credit rules (temporary).

This section lists the major paragraphs contained in §1.45G–1T.

§1.45G–1T Railroad track maintenance credit (temporary).

(a) In general.
(b) Definitions.
(1) Class II railroad and Class III railroad.
(2) Eligible railroad track.
(3) Eligible taxpayer.
(4) Qualifying railroad structure.
(5) Qualified railroad track maintenance expenditures.
(6) Rail facilities.
(7) Railroad-related property.
(8) Railroad-related services.
(9) Railroad track.
(10) Form 8900.
(11) Examples.
(c) Determination of amount of railroad track maintenance credit for the taxable year.
(1) General amount.
(2) Limitation on the credit.
(i) Eligible taxpayer is a Class II railroad or Class III railroad.
(ii) Eligible taxpayer is not a Class II railroad or Class III railroad.
(iii) Effect of double track.
(3) Determination of amount of QRTME paid or incurred.
(i) In general.
(ii) Effect of reimbursements.
(4) Examples.
(d) Assignment of track miles.
(1) In general.
(2) Assignment eligibility.
(3) Effective date of assignment.
(4) Assignment information statement.
(i) In general.
(ii) Assignor.
(iii) Assignee.
(iv) Special rule for 2005 returns.
(5) Special rules.
(i) Effect of subsequent dispositions of eligible railroad track during the assignment year.

(ii) Effect of multiple assignments of eligible railroad track miles during the same taxable year.

(6) Examples.

(e) Special rules.

(1) Adjustments to basis.

(i) In general.

(ii) Basis adjustment made to railroad track.

(iii) Examples.

(2) Coordination with section 61.

(f) Controlled groups.

(1) In general.

(2) Definitions.

(i) Trade or business.

(ii) Group and controlled group.

(iii) Group credit.

(iv) Consolidated group.

(v) Credit year.

(3) Computation of the group credit.

(4) Allocation of the group credit.

(i) In general.

(ii) Stand-alone entity credit.

(5) Special rules for consolidated groups.

(i) In general.

(ii) Special rule for allocation of group credit among consolidated group members.

(6) Tax accounting periods used.

(i) In general.

(ii) Special rule when timing of QRTME is manipulated.

(7) Membership during taxable year in more than one group.

(8) Intra-group transactions.

(i) In general.

(ii) Payment for QRTME.

(g) Effective date.

(1) In general.

(2) Application of regulation project REG–142270–05 to pre-effective date.

(3) Special rules for 2005 returns.

Par. 3. Section 1.45G–1T is added to read as follows:

§1.45G–1T Railroad track maintenance credit (temporary).

(a) *In general*. For purposes of section 38, the railroad track maintenance credit (RTMC) for qualified railroad track maintenance expenditures (QRTME) paid or incurred by an eligible taxpayer during the taxable year is determined under this section. A taxpayer claiming the RTMC must do so by filing Form 8900, "*Qualified Railroad Track Maintenance Credit*," with its timely filed (including extensions) Federal income tax return for the taxable year for which the RTMC is claimed. Paragraph (b) of this section provides definitions of terms. Paragraph (c) of this section provides rules for computing the RTMC, including rules regarding limitations on the amount of the credit. Paragraph (d) of this section provides rules for assigning miles of railroad track. Paragraph (e) of this section contains special rules. Paragraph (f) of this section contains rules for computing the amount of the RTMC in the case of a controlled group, and for the allocation of the group credit among members of the controlled group.

(b) *Definitions*. For purposes of section 45G and this section, the following definitions apply:

(1) *Class II railroad and Class III railroad* have the respective meanings given to these terms by the Surface Transportation Board (STB).

(2) *Eligible railroad track* is railroad track located within the United States that is owned or leased by a Class II railroad or Class III railroad at the close of its taxable year. For purposes of section 45G and this section, a Class II railroad or Class III railroad owns railroad track if the railroad track is subject to the allowance for depreciation under section 167 by the Class II railroad or Class III railroad.

(3) *Eligible taxpayer* is—

(i) A Class II railroad or Class III railroad during the taxable year;

(ii) Any person that transports property using the rail facilities of a Class II railroad or Class III railroad during the taxable year, but only with respect to the miles of eligible railroad track assigned to the person for that taxable year by that Class II railroad or Class III railroad under paragraph (d) of this section; or

(iii) Any person that furnishes railroad-related property or railroad-related services to a Class II railroad or Class III railroad during the taxable year, but only with respect to the miles of eligible railroad track assigned to the person for that taxable year by that Class II railroad or Class III railroad under paragraph (d) of this section.

(4) *Qualifying railroad structure* is property located within the United States that is described in the following STB property accounts in 49 CFR Part 1201, Subpart A:

(i) Property Account 3, Grading.

(ii) Property Account 4, Other right-of-way expenditures.

(iii) Property Account 5, Tunnels and subways.

(iv) Property Account 6, Bridges, trestles, and culverts.

(v) Property Account 7, Elevated structures.

(vi) Property Account 8, Ties.

(vii) Property Account 9, Rails and other track material.

(viii) Property Account 11, Ballast.

(ix) Property Account 13, Fences, snowsheds, and signs.

(x) Property Account 27, Signals and interlockers.

(xi) Property Account 39, Public improvements; construction.

(5) *Qualified railroad track maintenance expenditures (QRTME)* are expenditures for maintaining, repairing, and improving qualifying railroad structure that is owned or leased as of January 1, 2005, by a Class II railroad or Class III railroad. These expenditures may or may not be chargeable to a capital account.

(6) *Rail facilities* of a Class II railroad or Class III railroad are railroad yards, tracks, bridges, tunnels, wharves, docks, stations, and other related assets that are used in the transport of freight by a railroad and that are owned or leased by the Class II railroad or Class III railroad.

(7) *Railroad-related property* is property that is provided directly to, and is unique to, a railroad and that, in the hands of a Class II railroad or Class III railroad, is described in—

(i) The STB property accounts 3, Grading; 5, Tunnels and subways; and 22, Storage warehouses, in 49 CFR Part 1201, Subpart A; and

(ii) Asset classes 40.1 through 40.54 in the guidance issued by the Internal Revenue Service under section 168(i)(1) (for further guidance, for example, see Rev. Proc. 87–56, 1987–2 C.B. 674, and §601.601(d)(2)(ii)(*b*) of this chapter), except that any office building, any passenger train car, and any miscellaneous structure if such structure is not provided directly to, and is not unique to, a railroad are excluded from the definition of railroad-related property.

(8) *Railroad-related services* are services that are provided directly to, and are unique to, a railroad and that relate to rail-

road shipping, loading and unloading of railroad freight, or repairs of rail facilities or railroad-related property. Examples of railroad-related services are the transport of freight by rail; the loading and unloading of freight transported by rail; railroad bridge services; railroad track construction; providing railroad track material or equipment; locomotive leasing or rental; maintenance of railroad's right-of-way (including vegetation control); piggyback trailer ramping; rail deramping services; and freight train cars repair services. Examples of services that are not railroad-related services are general business services, such as, accounting and bookkeeping, marketing, legal services; cleaning services; office building rental; banking services (including financing of railroad-related property); and purchasing of, or services performed on, property not described in paragraph (b)(7) of this section.

(9) Except as provided in paragraph (e)(1) of this section, *railroad track* is property described in STB property accounts 8 (ties), 9 (rails and other track material), and 11 (ballast) in 49 CFR part 1201, Subpart A.

(10) *Form 8900*. If Form 8900 is revised or renumbered, any reference in this section to that form shall be treated as a reference to the revised or renumbered form.

(11) *Examples*. The application of this paragraph (b) is illustrated by the following examples. In all examples, the taxpayers use a calendar taxable year, and are not members of a controlled group:

Example 1. A is a manufacturer that in 2006, transports its products by rail using the railroad tracks owned by B, a Class II railroad that owns 500 miles of railroad track within the United States on December 31, 2006. B properly assigns for purposes of section 45G 100 miles of eligible railroad track to A in 2006. A is an eligible taxpayer for 2006 with respect to the 100 miles of eligible railroad track.

Example 2. C is a bank that loans money to several Class III railroads. In 2006, C loans money to D, a Class III railroad, who in turn uses the loan proceeds to purchase track material. Because providing loans is not a service that is unique to a railroad, C is not providing railroad-related services and, thus, C is not an eligible taxpayer, even if D assigns miles of eligible railroad track to C for purposes of section 45G.

Example 3. E leases locomotives directly to Class I, Class II, and Class III railroads. In 2006, E leases locomotives to F, a Class II railroad that owns 200 miles of railroad track within the United States on December 31, 2006. F properly assigns for purposes of section 45G 200 miles of eligible railroad track to E. Because locomotives are property that is unique to a railroad, and E leases these locomotives directly to F in 2006, E is an eligible taxpayer for 2006 with respect to the 200 miles of eligible railroad track assigned to E by F.

(c) *Determination of amount of railroad track maintenance credit for the taxable year*—(1) *General amount*. Except as provided in paragraph (c)(2) of this section, for purposes of section 38, the RTMC determined under section 45G(a) for the taxable year is equal to 50 percent of the QRTME paid or incurred (as determined under paragraph (c)(3) of this section) by an eligible taxpayer during the taxable year.

(2) *Limitation on the credit*—(i) *Eligible taxpayer is a Class II railroad or Class III railroad*. If an eligible taxpayer is a Class II railroad or Class III railroad, the RTMC determined under paragraph (c)(1) of this section for the Class II railroad or Class III railroad for any taxable year must not exceed $3,500 multiplied by the sum of—

(A) The number of miles of eligible railroad track owned or leased by the Class II railroad or Class III railroad, reduced by the number of miles of eligible railroad track assigned under paragraph (d) of this section by the Class II railroad or Class III railroad to another eligible taxpayer for that taxable year; and

(B) The number of miles of eligible railroad track owned or leased by another Class II railroad or Class III railroad that are assigned under paragraph (d) of this section to the Class II railroad or Class III railroad for the taxable year.

(ii) *Eligible taxpayer is not a Class II railroad or Class III railroad*. If an eligible taxpayer is not a Class II railroad or Class III railroad, the RTMC determined under paragraph (c)(1) of this section for the eligible taxpayer for any taxable year must not exceed $3,500 multiplied by the number of miles of eligible railroad track assigned under paragraph (d) of this section by a Class II railroad or Class III railroad to the eligible taxpayer for the taxable year.

(iii) *Effect of double track*. For purposes of this paragraph (c)(2), double track is treated as multiple lines of railroad track, rather than as a single line of railroad track. Thus, one mile of single track is one mile, but one mile of double track is two miles.

(3) *Determination of amount of QRTME paid or incurred*—(i) *In general*. The term *paid or incurred* means, in the case of a taxpayer using an accrual method of accounting, a liability incurred (within the meaning of §1.446–1(c)(1)(ii)). A liability may not be taken into account under section 45G and this section prior to the taxable year during which the liability is incurred.

(ii) *Effect of reimbursements*. The amount of QRTME treated as paid or incurred during the taxable year shall be reduced by any amount to which the taxpayer is entitled to be reimbursed, directly or indirectly, whether or not such reimbursement takes place during the taxable year in which the QRTME is, but for this sentence, paid or incurred by the taxpayer. Examples of indirect reimbursements include discounted freight shipping rates, markup of the price for track materials, and debt forgiveness. Similarly, any amount that an eligible taxpayer (assignee) pays a Class II railroad or Class III railroad (assignor) in exchange for an assignment of one or more miles of eligible railroad track under paragraph (d) of this section, is treated, for purposes of this section, as QRTME paid or incurred by the assignee, and not by the assignor, at the time and to the extent the assignor pays or incurs QRTME.

(4) *Examples*. The application of this paragraph (c) is illustrated by the following examples. In all examples, the taxpayers use an accrual method of accounting and a calendar taxable year, and are not members of a controlled group:

Example 1. Computation of RTMC; section 45G credit limitation is not exceeded. (i) G is a Class II railroad that owns or has leased to it 1,000 miles of railroad track within the United States on December 31, 2006. H is a manufacturer that in 2006, transports its products by rail using the rail facilities of G. In 2006, for purposes of section 45G, G assigns 100 miles of eligible railroad track to H and does not make any other assignments of railroad track miles. H did not receive any other assignments of railroad track miles in 2006. During 2006, G incurred QRTME in the amount of $2.5 million and H incurred QRTME in the amount of $200,000.

(ii) For 2006, G determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $1,250,000 (50% multiplied by $2,500,000 QRTME incurred by G during 2006). G further determines G's credit limitation under paragraph (c)(2)(i) of this section for 2006 to be $3,150,000 ($3,500 multiplied by 900 miles of eligible railroad track (1,000 miles owned by, or leased to, G on December 31, 2006, less 100 miles assigned by G to H in 2006)). Because G's tentative amount of RTMC does not exceed G's credit limitation amount for 2006, G may claim a RTMC for 2006 in the amount of $1,250,000.

(iii) For 2006, H determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $100,000 (50% multiplied by $200,000 QRTME

incurred by H during 2006). H further determines H's credit limitation under paragraph (c)(2)(ii) of this section for 2006 to be $350,000 ($3,500 multiplied by 100 miles of eligible railroad track assigned by G to H in 2006). Because H's tentative amount of RTMC does not exceed H's credit limitation amount for 2006, H may claim a RTMC in the amount of $100,000.

Example 2. Computation of RTMC; section 45G credit limitation is exceeded. (i) The facts are the same as in *Example 1*, except that G assigned for purposes of section 45G only 50 miles of railroad track to H in 2006 and, during 2006, H incurred QRTME in the amount of $400,000.

(ii) For 2006, G determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $1,250,000 (50% multiplied by $2,500,000 QRTME incurred by G during 2006). G further determines G's credit limitation under paragraph (c)(2)(i) of this section for 2006 to be $3,325,000 ($3,500 multiplied by 950 miles of eligible railroad track (1,000 miles owned by, or leased to, G on December 31, 2006, less 50 miles assigned by G to H in 2006)). Because G's tentative amount of RTMC does not exceed G's credit limitation amount for 2006, G may claim a RTMC in the amount of $1,250,000

(iii) For 2006, H determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $200,000 (50% multiplied by $400,000 QRTME incurred by H during 2006). H further determines H's credit limitation under paragraph (c)(2)(ii) of this section for 2006 to be $175,000 ($3,500 multiplied by 50 miles of eligible railroad track assigned by G to H in 2006). Because H's tentative amount of RTMC exceeds H's credit limitation amount for 2006, H may claim a RTMC in the amount of $175,000 (the credit limitation amount). There is no carryover of the amount of $25,000 (the tentative amount of $200,000 less the credit limitation amount of $175,000).

Example 3. Railroad track miles assigned for payment. (i) J is a Class II railroad that owns or has leased to it 1,000 miles of railroad track within the United States on December 31, 2006. K is a corporation that sells ties, ballast, and other track material to Class I, Class II, and Class III railroads. During 2006, K sold these items to J and J incurred QRTME in the amount of $1 million. Also, on December 6, 2006, J assigned for purposes of section 45G 150 miles of eligible railroad track to K and K paid J $800,000 for that assignment. K did not pay or incur any QRTME during 2006.

(ii) For 2006, in accordance with paragraph (c)(3)(ii) of this section, J is treated as having incurred QRTME in the amount of $200,000 ($1 million QRTME actually incurred by J less the $800,000 paid by K to J for the assignment of the railroad track miles in 2006). For 2006, J determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $100,000 (50% multiplied by $200,000 QRTME treated as incurred by J during 2006). J further determines J's credit limitation amount under paragraph (c)(2)(i) of this section for 2006 to be $2,975,000 ($3,500 multiplied by 850 miles of eligible railroad track (1,000 miles owned by, or leased to, J on December 31, 2006, less 150 miles assigned by J to K in 2006)). Because J's tentative amount of RTMC does not exceed J's credit limitation amount for 2006, J may claim a RTMC in the amount of $100,000.

(iii) For 2006, K is an eligible taxpayer because, during 2006, K provided railroad-related property to J and received an assignment of eligible railroad track miles from J. Under paragraph (c)(3)(ii) of this section, K is treated as having incurred QRTME in the amount of $800,000 (the amount paid by K to J for the assignment of the railroad track miles in 2006). For 2006, K determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $400,000 (50% multiplied by $800,000 QRTME treated as incurred by K during 2006). K further determines K's credit limitation amount under paragraph (c)(2)(ii) of this section for 2006 to be $525,000 ($3,500 multiplied by 150 miles of eligible railroad track assigned by J in 2006). Because K's tentative amount of RTMC does not exceed K's credit limitation amount for 2006, K may claim a RTMC in the amount of $400,000.

Example 4. Reimbursement of QRTME. (i) L is a Class III railroad that owns or has leased to it 500 miles of railroad track within the United States on December 31, 2006. M is a manufacturer that in 2006 transports its products by rail using the rail facilities of L. During 2006, L did not incur any QRTME. Also, in 2006, L assigned for purposes of section 45G 200 miles of eligible railroad track to M and agreed to reduce L's freight shipping rates to M by $250,000 in exchange for M upgrading these railroad track miles. Consequently, during 2006, M incurred QRTME of $500,000 to upgrade these 200 miles of railroad track and L reduced L's freight shipping rates for M by $250,000.

(ii) For 2006, M is an eligible taxpayer because, during 2006, M transported property using the rail facilities of L and received an assignment of eligible railroad track miles from L. Under paragraph (c)(3)(ii) of this section, the amount of QRTME paid or incurred by M during 2006 is $250,000 ($500,000 QRTME actually incurred by M, less the reimbursement of $250,000 by L to M). For 2006, M determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $125,000 (50% multiplied by $250,000 QRTME incurred by M during 2006). M further determines M's credit limitation amount under paragraph (c)(2)(ii) of this section for 2006 to be $700,000 ($3,500 multiplied by 200 miles of eligible railroad track assigned by L to M in 2006). Because M's tentative amount of RTMC does not exceed M's credit limitation amount for 2006, M may claim a RTMC in the amount of $125,000.

(d) *Assignment of track miles*—(1) *In general.* An assignment of any mile of eligible railroad track under this paragraph (d) is a designation by a Class II railroad or Class III railroad that is made solely for purposes of section 45G and this section of a specific number of miles of eligible railroad track as being assigned to another eligible taxpayer for a taxable year. A designation must be in writing and must include the name and taxpayer identification number of the assignee, and the information required under the rules of paragraph (d)(4)(iii)(B) of this section. A designation requires no transfer of legal title or other *indicia* of ownership of the eligible railroad track, and need not specify the location of any assigned mile of eligible railroad track. Further, an assigned mile of eligible railroad track need not correspond to any specific mile of eligible railroad track with respect to which the eligible taxpayer actually pays or incurs the QRTME. For purposes of this paragraph (d), double track is treated as multiple lines of railroad track, rather than as a single line of railroad track. Thus, one mile of single track is one mile, but one mile of double track is two miles.

(2) *Assignment eligibility.* Only a Class II railroad or Class III railroad may assign a mile of eligible railroad track. If a Class II railroad or Class III railroad assigns a mile of eligible railroad track to an eligible taxpayer, the assignee is not permitted to reassign any mile of eligible railroad track to another eligible taxpayer. The maximum number of miles of eligible railroad track that may be assigned by a Class II railroad or Class III railroad for any taxable year is its total miles of eligible railroad track less the miles of eligible railroad track that the Class II railroad or Class III railroad retains for itself in determining its RTMC for the taxable year.

(3) *Effective date of assignment.* If a Class II railroad or Class III railroad assigns a mile of eligible railroad track, the assignment is treated as being made by the Class II railroad or Class III railroad at the close of its taxable year in which the assignment was made. With respect to the assignee, the assignment of a mile of eligible railroad track is taken into account for the taxable year of the assignee that includes the date the assignment is treated as being made by the assignor Class II railroad or Class III railroad under this paragraph (d)(3).

(4) *Assignment information statement*—(i) *In general.* A taxpayer must file Form 8900, "*Qualified Railroad Track Maintenance Credit*," with its timely filed (including extensions) Federal income tax return for the taxable year for which the taxpayer assigns any mile of eligible railroad track, even if the taxpayer is not itself claiming the RTMC for that taxable year.

(ii) *Assignor.* Except as provided in paragraph (d)(4)(iv) of this section, a Class II railroad or Class III railroad (assignor)

that assigns one or more miles of eligible railroad track during a taxable year to one or more eligible taxpayers must attach to the assignor's Form 8900 for that taxable year an information statement providing—

(A) The name and taxpayer identification number of each assignee;

(B) The total number of miles of the assignor's eligible railroad track;

(C) The number of miles of eligible railroad track assigned by the assignor to each assignee for the taxable year; and

(D) The total number of miles of eligible railroad track assigned by the assignor to all assignees for the taxable year.

(iii) *Assignee*. Except as provided in paragraph (d)(4)(iv) of this section, an eligible taxpayer (assignee) that has received an assignment of miles of eligible railroad track during its taxable year from a Class II railroad or Class III railroad, and that claims the RTMC for that taxable year, must attach to the assignee's Form 8900 for that taxable year a statement—

(A) Providing the total number of miles of eligible railroad track assigned to the assignee for the assignee's taxable year; and

(B) Attesting that the assignee has in writing, and has retained as part of the assignee's records for purposes of §1.6001–1(a), the following information from each assignor:

(*1*) The name and taxpayer identification number of each assignor;

(*2*) The date of each assignment made by each assignor (as determined under paragraph (d)(3) of this section) to the assignee; and

(*3*) The number of miles of eligible railroad track assigned by each assignor to the assignee for the assignee's taxable year.

(iv) *Special rule for 2005 returns*. If an eligible taxpayer's Federal income tax return for a taxable year beginning after December 31, 2004, and ending before September 7, 2006, is filed before October 9, 2006, and the eligible taxpayer wants to apply paragraph (g)(2) of this section but did not include with that return the information specified in paragraph (d)(4)(ii) or (iii) of this section, as applicable, the eligible taxpayer must attach a statement containing the information specified in paragraph (d)(4)(ii) or (iii) of this section, as applicable, to either—

(A) The eligible taxpayer's next filed original Federal income tax return; or

(B) The eligible taxpayer's amended Federal income tax return that is filed pursuant to paragraph (g)(2) of this section, provided that amended Federal income tax return is filed by the eligible taxpayer before its next filed original Federal income tax return.

(5) *Special rules*—(i) *Effect of subsequent dispositions of eligible railroad track during the assignment year*. If a Class II railroad or Class III railroad assigns one or more miles of eligible railroad track that it owned or leased as of the actual date of the assignment, but does not own or lease any eligible railroad track at the close of the taxable year in which the assignment is made by the Class II railroad or Class III railroad, the assignment is not valid for that taxable year for purposes of section 45G and this section.

(ii) *Effect of multiple assignments of eligible railroad track miles during the same taxable year*. If a Class II railroad or Class III railroad assigns more miles of eligible railroad track than it owned or leased as of the close of the taxable year in which the assignment is made by the Class II railroad or Class III railroad, the assignment is valid for purposes of section 45G and this section only with respect to the name of the assignee and the number of miles listed by the assignor Class II railroad or Class III railroad on the statement required under paragraph (d)(4)(ii) of this section and only to the extent of the maximum miles of eligible railroad track that may be assigned by the assignor Class II railroad or Class III railroad as determined under paragraph (d)(2) of this section. If the total number of miles on this statement exceeds the maximum miles of eligible railroad track that may be assigned by the assignor Class II railroad or Class III railroad (as determined under paragraph (d)(2) of this section), the total number of miles on the statement shall be reduced by the excess amount of miles. This reduction is allocated among each assignee listed on the statement in proportion to the total number of miles listed on the statement for that assignee.

(6) *Examples*. The application of this paragraph (d) is illustrated by the following examples. In none of the examples are the taxpayers members of a controlled group:

Example 1. Assignor and assignee have the same taxable year. (i) N, a calendar year taxpayer, is a Class II railroad that owns 500 miles of railroad track within the United States on December 31, 2006. O, a calendar year taxpayer, is not a railroad, but is a taxpayer that provides railroad-related property to N during 2006. On November 7, 2006, N assigns for purposes of section 45G 300 miles of eligible railroad track to O. O receives no other assignment of eligible railroad track in 2006. O pays or incurs QRTME in the amount of $100,000 in November 2006, and $50,000 in February 2007. N and O each file Form 8900 with their timely filed Federal income tax returns for 2006 and attach the statement required by paragraph (d)(4)(ii) and (iii), respectively, of this section reporting the assignment of the 300 miles of eligible railroad track to O.

(ii) The assignment of the 300 miles of eligible railroad track made by N to O on November 7, 2006, is treated as made on December 31, 2006 (at the close of the N's taxable year). Consequently, the assignment is taken into account by O for O's taxable year ending on December 31, 2006. For 2006, O is an eligible taxpayer because, during 2006, O provides railroad-related property to N and receives an assignment of 300 eligible railroad track miles from N. For 2006, O determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $50,000 (50% multiplied by $100,000 QRTME paid or incurred by O during 2006). O further determines the credit limitation amount under paragraph (c)(2)(i) of this section for 2006 to be $1,050,000 ($3,500 multiplied by 300 miles of eligible railroad track assigned by N to O on December 31, 2006). Because O's tentative amount of RTMC does not exceed O's credit limitation amount for 2006, O may claim a RMTC for 2006 in the amount of $50,000.

Example 2. Assignor and assignee have different taxable years. (i) The facts are the same as in *Example 1*, except that O's taxable year ends on March 31.

(ii) The assignment of the 300 miles of eligible railroad track made by N to O on November 7, 2006, is treated as made on December 31, 2006. As a result, the assignment is taken into account by O for O's taxable year ending on March 31, 2007. Thus, for the taxable year ending on March 31, 2007, O determines the tentative amount of RMTC under paragraph (c)(1) of this section to be $75,000 (50% multiplied by $150,000 QRTME incurred by O during its taxable year ending March 31, 2007). Because O's tentative amount of RTMC does not exceed O's credit limitation amount for 2006, O may claim a RMTC for 2006 in the amount of $75,000.

Example 3. Assignment location differs from QRTME location. (i) P, a calendar-year taxpayer, is a Class III railroad that owns or has leased to it 200 miles of railroad track within the United States on December 31, 2006. P owns 50 miles of this railroad track and leases 150 miles of this railroad track from Q, a Class I railroad. On February 8, 2006, P assigns for purposes of section 45G 50 miles of eligible railroad track to R. R is not a railroad, but is a taxpayer that ships products using the 50 miles of eligible railroad track owned by P, and R paid $100,000 in 2006 to P to enable P to upgrade these 50 miles of eligible railroad track. In March 2006, P also assigns for purposes of section 45G 150 miles of eligible railroad track to S. S is not a railroad, but is a taxpayer that provides railroad-related property to P, and S paid $400,000 to P to enable P to upgrade P's 200 miles of eligible railroad track. For 2006, P

pays or incurs QRTME in the amount of $500,000 to upgrade the 150 miles of eligible railroad track that it leases from Q and pays or incurs no QRTME on the 50 miles of eligible railroad track that it owns. For 2006, P receives no other assignment of eligible railroad track miles and did not retain any eligible railroad track miles for itself. Also, R and S do not pay or incur any other amounts that would qualify as QRTME during 2006. P, R, and S each file Form 8900 with their timely filed Federal income tax returns for 2006 and attach the statement required by paragraph (d)(4)(ii) or (iii) of this section, whichever applies, reporting the assignment of eligible railroad track by P to R or S in 2006.

(ii) For 2006, in accordance with paragraph (c)(3)(ii) of this section, P is treated as having incurred QRTME in the amount of $0 ($500,000 QRTME actually incurred by P less the $100,000 paid by R to P for the assignment of the 50 miles of eligible railroad track and the $400,000 paid by S to P for the assignment of the 150 miles of eligible railroad track). Further, P assigned all of its eligible railroad track miles to R and S for 2006. Accordingly, for 2006, P may not claim any RTMC.

(iii) For 2006, R is an eligible taxpayer because, during 2006, R ships property using the rail facilities of P and receives an assignment of 50 eligible railroad track miles from P. In accordance with paragraph (c)(3)(ii) of this section, R is treated as having incurred QRTME in the amount of $100,000 (the amount paid by R to P for the assignment of the eligible railroad track miles in 2006) even though no work was performed on the 50 miles of eligible railroad track that was assigned by P to R. For 2006, R determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $50,000 (50% multiplied by $100,000 QRTME treated as incurred by R during 2006). R further determines the credit limitation amount under paragraph (c)(2)(ii) of this section to be $175,000 ($3,500 multiplied by 50 miles of eligible railroad track assigned by P to R in 2006). Because R's tentative amount of RTMC does not exceed R's credit limitation amount for 2006, R may claim a RTMC for 2006 in the amount of $50,000.

(iv) For 2006, S is an eligible taxpayer because, during 2006, S provides railroad-related property to P and receives an assignment of 150 eligible railroad track miles from P. In accordance with paragraph (c)(3)(ii) of this section, S is treated as having incurred QRTME in the amount of $400,000 (amount paid by S to P for the assignment of the eligible railroad track miles in 2006). For 2006, S determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $200,000 (50% multiplied by $400,000 QRTME treated as incurred by S during 2006). S further determines the credit limitation amount under paragraph (c)(2)(ii) of this section to be $525,000 ($3,500 multiplied by 150 miles of eligible railroad track assigned by P to S in 2006). Because S's tentative amount of RTMC does not exceed S's credit limitation amount for 2006, S may claim a RTMC for 2006 in the amount of $200,000.

Example 4. Multiple assignments of track miles. (i) T, a calendar-year taxpayer, is a Class III railroad that owns or has leased to it 200 miles of railroad track within the United States on December 31, 2006. T owns 75 miles of this railroad track and leases 125 miles of this railroad track from U, a Class I railroad. V and W are not railroads, but are both taxpayers that provide railroad-related services to T during 2006. On January 15, 2006, T assigns for purposes of section 45G 200 miles of eligible railroad track to V. V agrees to incur, in 2006, $1.4 million of QRTME to upgrade a portion of/segment of these 200 miles of eligible railroad track. Due to unexpected financial difficulties, V only incurs $250,000 of QRTME during 2006 and on May 15, 2006, T learns that V is unable to incur the remainder of the QRTME. On June 15, 2006, T assigns for purposes of section 45G the 200 miles of railroad track to W. In 2006, W incurs $1,100,000 of QRTME to upgrade a portion of/segment of the railroad track. For 2006, T receives no other assignment of eligible railroad track miles and did not retain any eligible railroad track miles for itself. V and W do not receive any other assignments of miles of eligible railroad track miles from a Class II railroad or Class III railroad during 2006. T and W each file Form 8900 with their timely filed Federal income tax returns for 2006, and attach the statement required by paragraph (d)(4)(ii) and (iii), respectively, of this section, reporting the assignment of 200 miles of eligible railroad track to W.

(ii) Because T did not retain any miles of eligible railroad track for itself for 2006, the maximum miles of eligible railroad track that may be assigned by T for 2006 is 200 miles pursuant to paragraph (d)(2) of this section. On the statement required by paragraph (d)(4)(ii) of this section, T assigned a total of 200 miles of eligible railroad track to W. Consequently, because T did not list V as an assignee on T's statement required by paragraph (d)(4)(ii) of this section, V did not receive an assignment of eligible railroad track miles from T during 2006 and V is not an eligible taxpayer for 2006. Thus, for 2006, V may not claim any RTMC even though V incurred QRTME in the amount of $250,000.

(iii) For 2006, W is an eligible taxpayer because, during 2006, W provides railroad-related services to T and receives an assignment of 200 eligible railroad track miles from T. W determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $550,000 (50% multiplied by $1,100,000 QRTME incurred by W during 2006). W further determines the credit limitation amount under paragraph (c)(2)(ii) of this section to be $700,000 ($3,500 multiplied by the 200 miles of eligible railroad track assigned by T to W in 2006). Because W's tentative amount of RTMC does not exceed W's credit limitation amount for 2006, W may claim a RTMC for 2006 in the amount of $550,000.

Example 5. Multiple assignments of track miles. (i) Same facts as in *Example 4*, except T, to its Form 8900 for 2006, attaches the statement required by paragraph (d)(4)(ii) of this section assigning 200 miles of eligible railroad track to W and 200 miles of eligible railroad track to V.

(ii) Because T did not retain any miles of eligible railroad track for itself for 2006, the maximum miles of eligible railroad track that may be assigned by T for 2006 is 200 miles pursuant to paragraph (d)(2) of this section. However, on the statement required by paragraph (d)(4)(ii) of this section, T assigned a total of 400 miles of eligible railroad track (200 miles to W and 200 miles to V). Consequently, the 400 miles of eligible railroad track on this statement must be reduced to the 200 maximum miles of eligible railroad track available for assignment for 2006. Because the statement reports 200 miles of eligible railroad track assigned to each W and V, the reduction of 200 miles (400 total miles of eligible railroad track on the statement less 200 maximum miles of eligible railroad track available for assignment) is allocated *pro-rata* between W and V and, therefore, 100 miles each to W and V. Thus, pursuant to paragraph (d)(5)(ii) of this section, the number of miles of eligible railroad track assigned by T to W and V for 2006 is 100 miles each.

(iii) For 2006, V is an eligible taxpayer because, during 2006, V provides railroad-related services to T and receives an assignment of 100 eligible railroad track miles from T. V determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $125,000 (50% multiplied by $250,000 QRTME incurred by V during 2006). V further determines the credit limitation amount under paragraph (c)(2)(ii) of this section to be $350,000 ($3,500 multiplied by the 100 miles of eligible railroad track assigned by T to V in 2006). Because V's tentative amount of RTMC does not exceed W's credit limitation amount for 2006, V may claim a RTMC for 2006 in the amount of $125,000.

(iv) For 2006, W is an eligible taxpayer because, during 2006, W provides railroad-related services to T and receives an assignment of 100 eligible railroad track miles from T. W determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $550,000 (50% multiplied by $1,100,000 QRTME incurred by W during 2006). W further determines the credit limitation amount under paragraph (c)(2)(ii) of this section to be $350,000 ($3,500 multiplied by the 100 miles of eligible railroad track assigned by T to W in 2006). Because W's tentative amount of RTMC exceeds W's credit limitation amount for 2006, W may claim a RTMC for 2006 in the amount of $350,000 (the credit limitation). There is no carryover of the amount of $200,000 (the tentative amount of $550,000 less the credit limitation amount of $350,000).

(e) *Special rules*—(1) *Adjustments to basis*—(i) *In general.* All or some of the QRTME paid or incurred by an eligible taxpayer during the taxable year may be required to be capitalized under section 263(a) as a tangible asset or as an intangible asset. See, for example, §1.263(a)–4(d)(8), which requires capitalization of amounts paid or incurred by a taxpayer to produce or improve real property owned by another (except to the extent the taxpayer is selling services at fair market value to produce or improve the real property) if the real property can reasonably be expected to produce significant economic benefits for the taxpayer. The basis of the tangible asset or intangible asset includes the capitalized amount of the QRTME.

(ii) *Basis adjustment made to railroad track.* An eligible taxpayer must reduce the adjusted basis of any railroad track with respect to which the eligible taxpayer claims the RTMC. For purposes of section 45G(e)(3) and this paragraph (e)(1), the

adjusted basis of any railroad track with respect to which the eligible taxpayer claims the RTMC is limited to the amount of QRTME, if any, that is required to be capitalized into the qualifying railroad structure or an intangible asset. The adjusted basis of the railroad track is reduced by the amount of the RTMC allowable (as determined under paragraph (c) of this section) by the eligible taxpayer for the taxable year, but not below zero. This reduction is taken into account at the time the QRTME is paid or incurred by an eligible taxpayer and before the depreciation deduction with respect to such railroad track is determined for the taxable year for which the RTMC is allowable. If all or some of the QRTME paid or incurred by an eligible taxpayer during the taxable year is capitalized under section 263(a) to more than one asset, whether tangible or intangible (for example, railroad track and bridges), the reduction to the basis of these assets under this paragraph (e)(1)(ii) is allocated among each of the assets subject to the reduction in proportion to the unadjusted basis of each asset at the time the QRTME is paid or incurred during that taxable year.

(iii) *Examples*. The application of this paragraph (e)(1) is illustrated by the following examples. In each example, all taxpayers use a calendar taxable year, and no taxpayers are members of a controlled group.

Example 1. (i) X is a Class II railroad that owns 500 miles of railroad track within the United States on December 31, 2006. During 2006, X incurs $1 million of QRTME for maintaining this railroad track. X uses the track maintenance allowance method for track structure expenditures (for further guidance, see Rev. Proc. 2002–65, 2002–2 C.B. 700, and §601.601(d)(2)(ii)(*b*) of this chapter). Assume all of the $1 million QRTME is track structure expenditures and none of it was expended for new track structure.

(ii) For 2006, X determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $500,000 (50% multiplied by $1 million QRTME incurred by X during 2006). X further determines the credit limitation amount under paragraph (c)(2)(i) of this section for 2006 to be $1,750,000 ($3,500 multiplied by 500 miles of eligible railroad track). Because X's tentative amount of RTMC does not exceed X's credit limitation amount for 2006, X may claim a RTMC for 2006 in the amount of $500,000.

(iii) Of the $1 million QRTME incurred by X during 2006, X determines under the track maintenance allowance method that $750,000 is the track maintenance allowance under section 162 and $250,000 is the capitalized amount for the track structure. In accordance with paragraph (e)(1)(ii) of this section, X reduces the capitalized amount of $250,000 by the RTMC of $500,000 claimed by X for 2006, but not below zero. Thus, the capitalized amount of $250,000 is reduced to zero. X also deducts under section 162 a track maintenance allowance of $750,000 on its 2006 Federal income tax return.

Example 2. (i) Y is a Class II railroad that owns or has leased to it 500 miles of eligible railroad track within the United States on December 31, 2006. Z is not a railroad, but is a taxpayer that, in 2006, transports its products using the rail facilities of Y. In 2006, Y assigns for purposes of section 45G 300 miles of eligible railroad track to Z. Z does not receive any other assignments of eligible railroad track miles in 2006. During 2006, Z incurs QRTME in the amount of $1 million, and Y does not incur any QRTME. Y and Z each file Form 8900 with their timely filed Federal income tax returns for 2006 and attach the statement required by paragraph (d)(4)(ii) and (iii), respectively, of this section reporting the assignment of the 300 miles of eligible railroad track to Z.

(ii) For 2006, Z determines the tentative amount of RTMC under paragraph (c)(1) of this section to be $500,000 (50% multiplied by $1 million QRTME incurred by Z during 2006). Z further determines the credit limitation amount under paragraph (c)(2)(ii) of this section for 2006 to be $1,050,000 ($3,500 multiplied by 300 miles of eligible railroad track assigned by Y to Z in 2006). Because Z's tentative amount of RTMC does not exceed Z's credit limitation amount for 2006, Z may claim a RTMC for 2006 in the amount of $500,000.

(iii) For 2006, Z also must determine the portion of the $1 million QRTME that Z incurs that is required to be capitalized under section 263(a), and the portion that is a section 162 expense. Because Z is not a Class II railroad or Class III railroad, Z cannot use the track maintenance allowance method. Assume that all of the QRTME constitutes an intangible asset under §1.263(a)–4(d)(8) and, therefore, is required to be capitalized by Z under section 263(a) as an intangible asset. In accordance with paragraph (e)(1)(ii) of this section, Z reduces the capitalized amount of $1 million by the RTMC of $500,000 claimed by Z for 2006. Thus, the capitalized amount of $1 million for the intangible asset is reduced to $500,000. Further, pursuant to §1.167(a)–3(b)(1)(iv), Z may treat this intangible asset with an adjusted basis of $500,000 as having a useful life of 25 years for purposes of the depreciation allowance under section 167(a).

(2) *Coordination with section 61*. Except as specifically provided in the Code and regulations under the Code, the owner of qualifying railroad structure has gross income if another person paid or incurred QRTME for the owner's qualifying railroad structure and that person does not have a depreciable interest in the tangible improvements made by the QRTME. See, for example, section 109, which excludes from gross income of the lessor, the value of property attributable to buildings or other improvements made by a lessee.

(f) *Controlled groups*—(1) *In general*. Pursuant to section 45G(e)(2), if an eligible taxpayer is a member of a controlled group of corporations, rules similar to the rules in §1.41–6T apply for determining the amount of the RTMC under section 45G(a) and this section. To determine the amount of RTMC (if any) allowable to a trade or business that at the end of its taxable year is a member of a controlled group, a taxpayer must—

(i) Compute the group credit in the manner described in paragraph (f)(3) of this section; and

(ii) Allocate the group credit among the members of the group in the manner described in paragraph (f)(4) of this section.

(2) *Definitions*. For purposes of section 45G(e)(2) and paragraph (f) of this section—

(i) A *trade or business* is a sole proprietorship, a partnership, a trust, an estate, or a corporation that is carrying on a trade or business (within the meaning of section 162). Any corporation that is a member of a commonly controlled group shall be deemed to be carrying on a trade or business if any other member of that group is carrying on any trade or business;

(ii) *Group* and *controlled group* means a controlled group of corporations, as defined in section 41(f)(5), or a group of trades or businesses under common control. For rules for determining whether trades or businesses are under common control, see §1.52–1(b) through (g);

(iii) *Group credit* means the RTMC (if any) allowable to a controlled group;

(iv) *Consolidated group* has the meaning set forth in §1.1502–1(h); and

(v) *Credit year* means the taxable year for which the member is computing the RTMC.

(3) *Computation of the group credit*. All members of a controlled group are treated as a single taxpayer for purposes of computing the RTMC. The group credit is computed by applying all of the section 45G computational rules (including the rules set forth in this section) on an aggregate basis.

(4) *Allocation of the group credit*—(i) *In general*. (A) To the extent the group credit (if any) computed under paragraph (f)(3) of this section does not exceed the sum of the stand-alone entity credits of all of the members of a controlled group, computed under paragraph (f)(4)(ii) of this section, such group credit shall be allocated among the members of the controlled group in proportion to the stand-alone en-

tity credits of the members of the controlled group, computed under paragraph (f)(4)(ii) of this section:

$$\text{group credit that does not exceed sum of all the members' stand-alone entity credits} \times \frac{\text{member's stand-alone entity credit}}{\text{Sum of all the members' stand-alone entity credits.}}$$

(B) To the extent that the group credit (if any) computed under paragraph (f)(3) of this section exceeds the sum of the stand-alone entity credits of all of the members of the controlled group, computed under paragraph (f)(4)(ii) of this section, such excess shall be allocated among the members of a controlled group in proportion to the QRTMEs of the members of the controlled group:

$$\text{(group credit less the sum of all the members' stand-alone entity credits)} \times \frac{\text{QRTMEs of members that are eligible taxpayers}}{\text{sum of QRTMEs of all members that are eligible taxpayers.}}$$

(ii) *Stand-alone entity credit*. The term *stand-alone entity credit* means the RTMC (if any) that would be allowable to a member of a controlled group if the credit were computed as if section 45G(e)(2) did not apply, except that the member must apply the rules provided in paragraphs (f)(5) (relating to consolidated groups) and (f)(8) (relating to intra-group transactions) of this section.

(5) *Special rules for consolidated groups*—(i) *In general*. For purposes of applying paragraph (f)(4) of this section, a consolidated group whose members are members of a controlled group is treated as a single member of the controlled group and a single stand-alone entity credit is computed for the consolidated group.

(ii) *Special rule for allocation of group credit among consolidated group members*. The portion of the group credit that is allocated to a consolidated group is allocated to the members of the consolidated group in accordance with the principles of paragraph (f)(4) of this section. However, for this purpose, the stand-alone entity credit of a member of a consolidated group is computed without regard to section 45G(e)(2).

(6) *Tax accounting periods used*—(i) *In general*. The credit allowable to a member of a controlled group is that member's share of the group credit computed as of the end of that member's taxable year. In computing the group credit for a group whose members have different taxable years, a member generally should treat the taxable year of another member that ends with or within the credit year of the computing member as the credit year of that other member. For example, Q, R, and S are members of a controlled group of corporations. Both Q and R are calendar year taxpayers. S files a return using a fiscal year ending June 30. For purposes of computing the group credit at the end of Q's and R's taxable year on December 31, S's fiscal year ending June 30, which ends within Q's and R's taxable year, is treated as S's credit year.

(ii) *Special rule when timing of QRTME is manipulated*. If the timing of QRTME by members using different tax accounting periods is manipulated to generate a credit in excess of the amount that would be allowable if all members of the group used the same tax accounting period, then the appropriate Internal Revenue Service official in the operating division that has examination jurisdiction of the return may require each member of the group to calculate the credit in the current taxable year and all future years as if all members of the group had the same taxable year and base period as the computing member.

(7) *Membership during taxable year in more than one group*. A trade or business may be a member of only one group for a taxable year. If, without application of this paragraph (f)(7), a business would be a member of more than one group at the end of its taxable year, the business shall be treated as a member of the group in which it was included for its preceding taxable year. If the business was not included for its preceding taxable year in any group in which it could be included as of the end of its taxable year, the business shall designate in its timely filed (including extensions) federal income tax return for the taxable year the group in which it is being included. If the business does not so designate, then the appropriate Internal Revenue Service official in the operating division that has examination jurisdiction of the return will determine the group in which the business is to be included. If the Federal income tax return for a taxable year beginning after December 31, 2004, and ending before September 7, 2006, is filed before October 9, 2006, and the business wants to apply paragraph (g)(2) of this section but did not designate its group membership in that return, the business must designate its group membership for that year either—

(i) In its next filed original Federal income tax return; or

(ii) In its amended Federal income tax return that is filed pursuant to paragraph (g)(2) of this section, provided that amended Federal income tax return is filed by the business before its next filed original Federal income tax return.

(8) *Intra-group transactions*—(i) *In general*. Because all members of a group under common control are treated as a single taxpayer for purposes of determining the RTMC, transfers between members of the group are generally disregarded.

(ii) *Payment for QRTME*. Amounts paid or incurred by the owner (or lessor) of eligible railroad track to another member of the group for QRTME shall be taken into account as QRTME by the owner (or

lessor) of the eligible railroad track for purposes of section 45G only to the extent of the lesser of—

(A) The amount paid or incurred to the other member; or

(B) The amount that would have been considered paid or incurred by the other member for the QRTME, if the QRTME was not reimbursed by the owner (or lessor) of the eligible railroad track.

(g) *Effective date*—(1) *In general.* (i) Except as provided in paragraphs (g)(2) and (g)(3) of this section, this section applies to taxable years ending on or after September 7, 2006, and beginning before January 1, 2008.

(ii) The applicability of this section expires on September 7, 2009.

(2) *Application of regulation project REG–142270–05 to pre-effective date.* A taxpayer may apply this section to taxable years beginning after December 31, 2004, and ending before September 7, 2006, provided that the taxpayer applies all provisions in this section to the taxable year.

(3) *Special rules for 2005 returns.* If a taxpayer's Federal income tax return for a taxable year beginning after December 31, 2004, and ending before September 7, 2006, is filed before October 9, 2006, and the taxpayer is not filing an amended Federal income tax return for that taxable year pursuant to paragraph (g)(2) of this section before the taxpayer's next filed original Federal income tax return, see paragraphs (d)(3)(iv) and (f)(7) of this section for the statements that must be attached to the taxpayer's next filed original Federal income tax return.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

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

Authority: 26 U.S.C. 7805.

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

§602.101 OMB control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
1.45G–1T	1545–2031
* * * * *	

Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

Approved August 24, 2006.

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

(Filed by the Office of the Federal Register on September 7, 2006, 8:45 a.m., and published in the issue of the Federal Register for September 8, 2006, 71 F.R. 53009)

Section 62.—Adjusted Gross Income Defined

26 CFR 1.62–2: Reimbursements and other expense allowance arrangements.

Rules are provided under which a reimbursement or other expense allowance arrangement for the cost of lodging, meal, and incidental expenses, or of meal and incidental expenses only, incurred by an employee while traveling away from home, satisfies the requirements of § 62(c) of the Code for substantiation of the amount of the expenses. See Rev. Proc. 2006-41, page 777.

Section 162.—Trade or Business Expenses

26 CFR 1.162–17: Reporting and substantiation of certain business expenses of employees.

Rules are provided for substantiating the amount of a deduction for an expense for meal and incidental expenses, or for incidental expenses only, incurred while traveling away from home. See Rev. Proc. 2006-41, page 777.

Section 4261.—Imposition of Tax

26 CFR 49.4261–2: Application of Tax (Also: 4291.)

Resellers of air transportation. This ruling explains the tax consequences under section 4261 of the Code when a traveler purchases a ticket for taxable transportation from a third party intermediary other than the airline. Rev. Ruls. 75–296 and 80–31 distinguished.

Rev. Rul. 2006–52

ISSUES

In the situation described below, what is the amount paid for taxable transportation for purposes of the tax imposed by § 4261 of the Internal Revenue Code, which person is liable for the tax, and which person is responsible for collecting the tax, filing the required return, and paying over the tax to the government?

FACTS

Traveler wants to travel between two cities in the United States on a scheduled commercial airline (Airline). Instead of contacting Airline directly for a ticket, Traveler contacts Intermediary, which is in the travel services industry. When Traveler orders a ticket, Traveler pays Intermediary Price *X* plus Fee *Y*. Traveler also pays Intermediary the amounts Airline charges on account of the tax imposed by § 4261 and the passenger facility charge (PFC) imposed under § 1113(e) of the Federal Aviation Act of 1958. (See Rev. Rul. 91–61, 1991–2 C.B. 377, for additional information regarding the PFC.) Traveler could have bought a ticket with the same itinerary and class of service from Airline without using Intermediary.

Intermediary is neither related to Airline nor under its supervision or control; thus, each transaction between Intermedi-

ary and Airline is made at arm's length. Intermediary neither operates nor charters aircraft. The amount of Fee *Y* is set solely by Intermediary. Fee *Y* compensates Intermediary for the service of facilitating Traveler's purchase of an airline ticket. Intermediary is not compensated by Airline for any services Intermediary provides.

Intermediary passes on to Airline Price *X* and the amounts Airline charges on account of the tax imposed by § 4261 and the PFC. Intermediary retains Fee *Y*. Price *X* and the amounts Airline charges on account of the tax imposed by § 4261 and the PFC are the only amounts required to be paid to Airline as a condition to Traveler receiving air transportation from Airline, and Airline issues a ticket to Traveler in exchange for Intermediary's payment of these amounts.

LAW AND ANALYSIS

Section 4261(a) imposes a tax on the amount paid for taxable transportation (as defined in § 4262) of any person by air and § 4261(b) imposes a tax on the amount paid for each domestic segment of taxable transportation. The § 4261(a) tax is a percentage of the amount paid and the § 4261(b) tax is a fixed dollar amount for each segment. "Taxable transportation" generally includes air transportation that begins and ends in the United States.

Section 4261(d) provides that the tax imposed by § 4261 shall be paid by the person making the payment subject to tax and § 4291 generally provides that any person receiving any payment for taxable air transportation must collect the amount of the tax from the person making the payment. The collector is generally required by regulations to make deposits, file returns, and pay over the tax to the government.

Rev. Rul. 75–296, 1975–2 C.B. 440, considers the application of the § 4261 tax to two situations involving travel agencies. One travel agency (Agency A) is an independent broker that charters an aircraft from an airline and sells tours to individuals and groups. The other travel agency (Agency B), which represents an airline and is under the supervision and control of that airline, is not licensed as a broker. When Agency B sells tours it retains a commission and remits the remainder of the amount collected to the airline. The ruling holds that Agency A is operating as a principal and is required to collect the tax and pay it over to the government. Agency B, because it operates under the control of the airline, is an agent of the airline. As the airline's agent, Agency B must collect the tax and remit it to the airline, which, in turn, must pay it over to the government.

Rev. Rul. 80–31, 1980–1 C.B. 251, considers the application of the § 4261 tax to a service charge added by an airline to the price of a ticket for the administrative costs involved in the use of that ticket by another person in another city. The ruling concludes that the charge was not an amount paid for taxable transportation because the service is optional, not reasonably necessary to the air transportation itself, and bears a reasonable relation to the cost of providing the service.

S. Rep. No. 105–33, at 158 (1997), 1997–4 C.B. 1067, 1238 (relating to the legislation that became Pub. L. 105–94, 1997–4 (Vol. 1) C.B. 1, which made numerous changes to the air transportation tax), notes that the "air passenger transportation excise taxes are imposed on passengers; transportation providers (generally airlines) are responsible for collecting and remitting the taxes to the Federal Government."

Under the facts of this revenue ruling, Airline is providing the transportation to Traveler. Intermediary is not providing transportation either directly or indirectly; it is simply facilitating the purchase of taxable transportation. Intermediary is simply a conduit through which Traveler pays Airline for taxable transportation. Thus, Traveler is the person that makes the payment subject to the § 4261 tax and Airline is the person that receives the taxable payment.

An airline's costs associated with selling tickets are generally necessary to the air transportation the airline provides. This includes the airline's costs of selling tickets through an unrelated third party. However, Intermediary's selling costs and profit, if any, are not charged by, or passed on to, Airline and are not reasonably necessary to the air transportation Airline provides to Traveler.

Fee *Y* is not received by Airline or by an agent of Airline, and is not an "amount paid" for taxable transportation. Rather, Fee *Y* compensates Intermediary for the service of facilitating Traveler's purchase of an airline ticket. Therefore, Price *X* is the amount paid for taxable transportation and is the base on which the § 4261(a) tax is calculated.

Rev. Rul. 75–296 is distinguishable from this case since that ruling addresses only situations in which a travel agent is either acting as a principal on its own behalf by chartering an entire aircraft or acting as an agent of the airline in selling individual tickets. It does not address the situation here in which Intermediary is not under the supervision or control of Airline and is acting on behalf of, and receiving compensation from, Traveler.

Rev. Rul. 80–31 is distinguishable from this case because that ruling did not involve amounts paid to an independent third party that is not under the airline's supervision or control.

HOLDINGS

Price *X* is the amount paid for taxable transportation, Traveler is liable for the tax imposed on Price *X*, and Airline is responsible for collecting the tax from Traveler, filing the required return, and paying over the tax to the government. Airline may collect the tax and the PFC through Intermediary as part of the transaction in which it receives payment of Price *X*.

EFFECT ON OTHER DOCUMENTS

Rev. Ruls. 75–296 and 80–31 are distinguished.

DRAFTING INFORMATION

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

Part III. Administrative, Procedural, and Miscellaneous

Additional Transition Relief Under Section 409A

Notice 2006–79

SECTION 1. PURPOSE

This notice provides transition relief under section 409A of the Internal Revenue Code (Code), applicable to nonqualified deferred compensation plans. The IRS and Treasury Department are currently in the process of finalizing the proposed regulations under section 409A that were published October 4, 2005. The proposed regulations contained a proposed effective date of January 1, 2007 for the final regulations. Although the IRS and Treasury Department expect to issue the final regulations before the end of 2006, commentators have expressed concern that there will not be sufficient time between the issuance of the final regulations and the proposed effective date for taxpayers to analyze the final regulations and come into compliance with them. Commentators have also raised questions and concerns about certain other aspects of the transition relief.

Accordingly, as described in more detail below, this notice provides further transition relief by:

- Announcing that the final regulations will not become effective until January 1, 2008
- Generally extending through 2007 the transition relief provided for 2006 in the preamble to the proposed regulations except with respect to certain discounted stock rights
- Providing additional transition relief for certain payment elections in linked plans and certain collective bargaining arrangements
- Extending the amendment date for certain plans that took advantage of transition relief provided for 2005

SECTION 2. BACKGROUND

Section 409A was added to the Code by section 885 of the American Jobs Creation Act of 2004, Public Law 108–357 (118 Stat. 1418). Section 409A generally provides that unless certain requirements are met, amounts deferred under a nonqualified deferred compensation plan for all taxable years are currently includible in gross income to the extent not subject to a substantial risk of forfeiture and not previously included in gross income. Section 409A also includes rules applicable to certain trusts or similar arrangements associated with nonqualified deferred compensation, where such arrangements are located outside of the United States or are restricted to the provision of benefits in connection with a decline in the financial health of the sponsor.

On December 20, 2004, the IRS issued Notice 2005–1, 2005–2 I.R.B. 274 (published as modified on January 6, 2005)), setting forth initial guidance with respect to the application of section 409A, and supplying transition guidance in accordance with the statutory provisions. A notice of proposed rulemaking (REG–158080–04, 2005–43 I.R.B. 786 [70 FR 57930]) was published in the Federal Register on October 4, 2005. The preamble to the proposed regulations clarified and extended certain provisions of the transition guidance provided in Notice 2005–1, generally through December 31, 2006.

Under the proposed regulations, the final regulations were proposed to become effective January 1, 2007. The Treasury Department and the IRS anticipate that the final regulations will be published in 2006. However, in order to allow sufficient time for taxpayers and their representatives to analyze the final regulations and come into compliance, the effective date for the final regulations is expected to be January 1, 2008. Accordingly, this notice provides additional transition relief applicable through December 31, 2007.

SECTION 3. TRANSITION RELIEF

.01. *Amendment and operation of plans adopted on or before December 31, 2007*

A plan adopted on or before December 31, 2007 will not be treated as violating section 409A(a)(2), (3) or (4) on or before December 31, 2007 if the plan is operated through December 31, 2007 in reasonable, good faith compliance with the provisions of section 409A and applicable provisions of Notice 2005–1 and any other generally applicable guidance published with an effective date prior to January 1, 2008, and the plan is amended on or before December 31, 2007 to conform to the provisions of section 409A and the final regulations with respect to amounts subject to section 409A. For such periods, to the extent an issue is not addressed in an applicable provision of Notice 2005–1 or other published guidance with an effective date prior to January 1, 2008, the plan must be operated consistent with a good faith, reasonable interpretation of section 409A, and, to the extent not inconsistent therewith, the plan's terms.

Compliance with the proposed regulations, or the final regulations prior to their effective date, is not required. However, for periods before January 1, 2008, compliance with the proposed regulations or the final regulations will constitute reasonable, good faith compliance with the statute. To the extent that a provision of either the proposed regulations or the final regulations is inconsistent with a provision of Notice 2005–1, or a provision of the proposed regulations is inconsistent with a provision of the final regulations, the plan may comply with the provision of the proposed regulations, the final regulations or Notice 2005–1.

A plan will not be operating in good faith compliance if discretion provided under the terms of the plan is exercised in a manner that causes the plan to fail to meet the requirements of section 409A. For example, if an employer retains the discretion under the terms of the plan to delay or extend payments under the plan in a manner that violates section 409A and exercises such discretion, the plan will not be considered to be operated in good faith compliance with section 409A with regard to any plan participant. However, an exercise of a right under the terms of the plan by a participant solely with respect to that participant's benefits under the plan, in a manner that causes the plan to fail to meet the requirements of section 409A, will not be considered to result in the plan failing to be operated in good faith compliance with respect to other participants. For example, the request for and receipt of an immediate

payment permitted under the terms of the plan if the participant forfeits 20 percent of the participant's benefits (a haircut) will be considered a failure of the plan to meet the requirements of section 409A with respect to that participant, but not with respect to all other participants under the plan.

.02. *Change in payment elections or conditions on or before December 31, 2007*

The transition relief provided in section XI.C. of the preamble to the proposed regulations generally continues to apply through December 31, 2007, with certain clarifications described below, and subject to limitations for certain discounted stock rights also described below. Accordingly, with respect to amounts subject to section 409A, a plan may provide, or be amended to provide, for new payment elections on or before December 31, 2007, with respect to both the time and form of payment of such amounts and the election or amendment will not be treated as a change in the time or form of payment under section 409A(a)(4) or an acceleration of a payment under section 409A(a)(3), provided that the plan is so amended and elections are made on or before December 31, 2007. With respect to an election or amendment to change a time and form of payment made on or after January 1, 2006 and on or before December 31, 2006, the election or amendment may apply only to amounts that would not otherwise be payable in 2006 and may not cause an amount to be paid in 2006 that would not otherwise be payable in 2006. With respect to an election or amendment to change a time and form of payment made on or after January 1, 2007 and on or before December 31, 2007, the election or amendment may apply only to amounts that would not otherwise be payable in 2007 and may not cause an amount to be paid in 2007 that would not otherwise be payable in 2007. So, for example, where an amount would otherwise be payable upon an event, such as a separation from service, an election in 2006 cannot change the amount that would be payable in 2006 if the service provider separated from service in 2006. In addition, a deferral election may be made with respect to an amount that is a short-term deferral within the meaning of proposed § 1.409A–1(b)(4), provided that the election is made before January 1, 2008 and before the year in which the amount would otherwise have been paid.

This provision applies to elections or amendments by a service provider, a service recipient, or both a service provider and a service recipient. A service provider or service recipient may make more than one change or amendment under this relief, provided that each such change or amendment is made in accordance with the deadlines and conditions set forth in the applicable transition relief. For example, a service provider that in 2005 elected to change the time and form of payment of deferred compensation to a lump sum payment in 2010, may elect again in 2006 or 2007 to change the time and form of payment in accordance with this paragraph. However, a service provider that in 2005 elected to be paid an amount in 2006 may not in 2006 change the time and form of payment to be paid in a later year.

Similarly, except as provided below with respect to certain discounted stock rights, an outstanding stock right that provides for a deferral of compensation subject to section 409A may be amended to provide for fixed payment terms consistent with section 409A, or to permit holders of such rights to elect fixed payment terms consistent with section 409A, and such amendment or election will not be treated as a change in the time and form of payment under section 409A(a)(4) or an acceleration of a payment under section 409A(a)(3), provided that the option or right is so amended and any elections are made, on or before December 31, 2007. For this purpose, a stock right will not be treated as payable in a year solely because the stock right is exercisable during that year, if the stock right is also reasonably expected to be exercisable in a subsequent year.

.03 *Payments linked to qualified plans*

The ability to link a payment election under a nonqualified deferred compensation plan to an election under a qualified plan has also been extended through 2007. In addition, this relief is extended to payment elections under nonqualified deferred compensation plans that are linked to certain additional employer plans, including section 403(b) annuities, section 457(b) eligible plans, and certain foreign broad-based plans. Accordingly, for periods ending on or before December 31, 2007, an election as to the time and form of a payment under a nonqualified deferred compensation plan that is controlled by a payment election made by the service provider or beneficiary of the service provider under a qualified employer plan described in proposed § 1.409A–1(a)(2), a plan that includes a trust described in section 402(d), a plan described in section 1022(i)(1) or (2) of the Employee Retirement Income Security Act, or a foreign broad-based plan described in proposed § 1.409A–1(a)(3)(v), will not violate the requirements of section 409A, provided that the determination of the time and form of the payment is made in accordance with the terms of the nonqualified deferred compensation plan that govern payment elections, as in effect on October 3, 2004. For example, where a nonqualified deferred compensation plan provides as of October 3, 2004, that the time and form of payment to a service provider or beneficiary will be the same time and form of payment elected by the service provider or beneficiary under a qualified plan, it will not be a violation of section 409A for the plan administrator to make or commence payments under the nonqualified deferred compensation plan on or after January 1, 2005, and on or before December 31, 2007, pursuant to the payment election under the qualified plan. Notwithstanding the foregoing, other provisions of the Internal Revenue Code and common law tax doctrines continue to apply to any election as to the time and form of a payment under a nonqualified deferred compensation plan.

.04 *Substitutions of non-discounted stock options and stock appreciation rights for discounted stock options and stock appreciation rights*

Notice 2005–1, Q&A–18(d) provides that it will not be a material modification to replace a stock option or stock appreciation right otherwise providing for a deferral of compensation under section 409A with a stock option or stock appreciation right that would not have constituted a deferral of compensation under section 409A if it had been granted upon the original date of grant of the replaced stock option or stock appreciation right, provided that the cancellation and reissuance occurs on or before December 31, 2005. Section XI.H. of the preamble to the proposed regulations extended the period during which the cancellation and reissuance may occur un-

til December 31, 2006, but only to the extent a cancellation and resissuance in 2006 does not result in the cancellation of a deferral in exchange for cash or vested property in 2006. Except with respect to certain discounted stock rights described in section 3.07 below, the period during which the cancellation and reissuance may occur is extended until December 31, 2007, but only to the extent such cancellation and reissuance in 2007 does not result in the cancellation of a deferral in exchange for cash or vested property in 2007. For example, a discounted option generally may be replaced through December 31, 2007 with an option that would not have provided for a deferral of compensation, although the exercise of such a discounted option in 2007 before the cancellation and replacement generally would result in a violation of section 409A.

Where replacement stock options or stock appreciation rights that would not constitute deferred compensation subject to section 409A are issued in accordance with the conditions set forth in Notice 2005–1, Q&A–18(d), the preamble to the proposed regulations and this notice, such replacement stock options or stock appreciation rights will be treated for purposes of section 409A as if granted on the grant date of the original stock option or stock appreciation right. For a discussion of certain methods that commentators proposed to use to compensate option holders for the value of a lost discount, see section XI.H. of the preamble to the proposed regulations.

.05 *Collectively bargained arrangements*.

A nonqualified deferred compensation arrangement maintained pursuant to one or more collective bargaining agreements in effect on October 3, 2004 is not required to comply with the provisions of section 409A on or before the earlier of the date on which the last of such collective bargaining agreements terminates (determined without regard to any extension thereof after October 3, 2004) or December 31, 2009.

.06 *Other transition issues*

Notice 2005–1, Q&A–21 provided relief with respect to certain initial deferral elections, generally providing that certain requirements would not be applicable to elections made on or before March 15, 2005. One of the conditions of the requirement was that the plan be amended to comply with the requirements of section 409A in accordance with Notice 2005–1, Q&A–19. Notice 2005–1, Q&A–19 generally required that plans be amended by December 31, 2005. The March 15, 2005 deadline for initial deferral elections was not extended in the preamble to the proposed regulations; however, the plan amendment requirement generally was extended to December 31, 2006. Although the initial deferral election relief contained in Notice 2005–1, Q&A–21 only referred to the requirements of Notice 2005–1, Q&A–19, the Treasury Department and the IRS have become aware that many taxpayers interpreted the extension of the plan amendment deadlines as flowing through to the requirements of Notice 2005–1, Q&A–21. To avoid unintentional noncompliance in this area, the deadline for a plan to be amended to reflect use of the relief provided in Notice 2005–1, Q&A–21 is extended to December 31, 2007. However, taxpayers retain the burden of demonstrating satisfaction of the requirement by showing that the deferral election was made by the March 15, 2005 deadline, in accordance with the plan terms in effect on or before December 31, 2005 (other than a requirement to make a deferral election on or before March 15, 2005). See Notice 2005–1, Q&A–21.

.07 *Transition relief not extended for certain discounted stock rights*

The transition relief provided in the preamble to the proposed regulations and described in this notice is not extended for any stock option or stock appreciation right (stock right) that:

(A) was granted with respect to stock of a corporation that as of the date of grant had issued any class of common equity securities required to be registered under section 12 of the Securities Exchange Act of 1934;

(B) was granted to a person who, as of the date of grant, was subject to the disclosure requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to such issuer; and

(C) with respect to the grant of such stock right, such corporation either has reported or reasonably expects to report a financial expense due to the issuance of a stock right with an exercise price lower than the fair market value of the underlying stock at the date of grant that was not timely reported on financial statements or reports for the period in which the related expense should have been reported under generally accepted accounting principles.

SECTION 4. APPLICATION OF FINAL REGULATIONS TO OUTSTANDING DEFERRALS

Commentators to the proposed regulations expressed concerns regarding the application of the final regulations, once effective, to outstanding deferrals such as, for example, outstanding stock rights. The Treasury Department and the IRS anticipate addressing these issues in connection with the issuance of the final regulations.

SECTION 5. EFFECT ON OTHER DOCUMENTS

Nothing in this notice is intended to limit the scope or applicability of the transition relief provided in Notice 2005–1 and the proposed regulations. In addition, this notice is not intended to limit the scope or applicability of the guidance provided in Notice 2005–94, 2005–52 I.R.B. 1208 (transition guidance with respect to 2005 reporting and withholding obligations); Notice 2006–4, 2006–3 I.R.B. 307 (transition guidance with respect to certain outstanding stock rights); Notice 2006–33, 2006–5 I.R.B. 754 (transition guidance with respect to the application of section 409A(b)); or Notice 2006–64, 2006–29 I.R.B. 88 (transition guidance with respect to the application of section 409A to accelerated payments necessary to meet federal ethics requirements).

SECTION 6. DRAFTING INFORMATION

The principal author of this notice is Stephen B. Tackney of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and the Treasury Department participated in its development. For further information regarding this notice, contact Mr. Tackney at (202) 927–9639 (not a toll-free call).

Determination of Housing Cost Amount Eligible for Exclusion or Deduction

Notice 2006–87

This notice provides adjustments to the limitation on housing expenses for purposes of section 911 of the Internal Revenue Code (Code) for specific locations, on the basis of geographic differences in housing costs relative to housing costs in the United States.

Section 911(a) of the Code allows a qualified individual to elect to exclude from U.S. gross income the foreign earned income and housing cost amount of such individual. Section 911(c)(1), as amended by section 515 of the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA), defines the term "housing cost amount" as an amount equal to the excess of (A) the housing expenses of an individual for the taxable year to the extent such expenses do not exceed the amount determined under section 911(c)(2), over (B) 16 percent of the exclusion amount (computed on a daily basis) in effect under section 911(b)(2)(D) for the calendar year in which such taxable year begins ($67.73 per day for 2006, or $82,400 for the full year), multiplied by the number of days of that taxable year within the applicable period described in section 911(d)(1). The applicable period is the period during which the individual meets the tax home requirement of section 911(d)(1) and either the *bona fide* residence requirement of section 911(d)(1)(A) or the physical presence requirement of section 911(d)(1)(B). Assuming that the entire taxable year of a qualified individual is within the applicable period, the section 911(c)(1)(B) amount for 2006 is $13,184 ($82,400 x .16).

Section 515 of TIPRA also added a new section 911(c)(2)(A) of the Code, which limits the housing expenses taken into account in section 911(c)(1)(A) to an amount equal to the product of — (i) 30 percent (adjusted as may be provided under the Secretary's authority under section 911(c)(2)(B)) of the amount in effect under section 911(b)(2)(D) for the calendar year in which the taxable year of the individual begins, multiplied by (ii) the number of days of that taxable year within the applicable period described in section 911(d)(1). Thus, for the year 2006, a qualified individual whose entire taxable year is within the applicable period is limited to maximum housing expenses of $24,720 ($82,400 x .30). Accordingly, the maximum housing cost amount a qualified individual may exclude from income in year 2006 is $11,536 ($24,720 – $13,184). The TIPRA changes apply to taxable years beginning after December 31, 2005.

To the extent the housing cost amount of any individual for any taxable year is not attributable to employer provided amounts, section 911(c)(4)(A) of the Code provides that such amount shall be treated as a deduction in computing adjusted gross income. Under section 911(c)(4)(B), however, the amount of this deduction is limited to the excess of the foreign earned income of the individual for the taxable year over the amount of such income excluded from gross income under section 911(a).

In addition, section 911(d)(7) of the Code prohibits the total amount excluded or deducted under section 911 for the taxable year from exceeding the individual's foreign earned income for such year. Further, section 911(b)(1)(B) excludes from the definition of foreign earned income certain amounts, including amounts paid by the United States or an agency thereof to an employee of the United States or an agency thereof. As a result, the exclusion or deduction from gross income of the housing cost amount under section 911 is not available to an individual whose earned income consists solely of amounts paid by the United States or an agency thereof to an employee of the United States or an agency thereof.

Section 911(c)(2)(B) of the Code authorizes the Secretary to issue regulations or other guidance to adjust the percentage under section 911(c)(2)(A)(i) based on geographic differences in housing costs relative to housing costs in the United States. The Joint Explanatory Statement of the Committee of Conference accompanying TIPRA states the conferees' intent that the Secretary be permitted to use publicly available data, such as the Quarterly Report Indexes published by the U.S. Department of State or any other information that the Secretary deems reliable, in making adjustments. See H.R. Conf. Rep. No. 304, 109th Cong., 1st Sess. 309 (2005).

Accordingly, the following table, which was derived from the Living Quarters Allowance table prepared by the Office of Allowances of the U.S. Department of State as of August 20, 2006, identifies locations within countries with high housing costs relative to housing costs in the United States, and provides an adjusted limitation on housing expenses for a qualified individual incurring housing expenses in one or more of these high cost localities in 2006 to use (in lieu of the otherwise applicable limitation of $24,720) in determining his or her housing expenses under section 911(c)(2)(A) of the Code. The table will be updated each year by administrative pronouncement (*e.g.*, through issuing a notice, amending Form 2555 or the instructions thereto, or by making a revised table available on the IRS website at *http://www.irs.gov*), beginning in 2007, based on the living quarters allowance for employees of the U.S. Department of State who are in Group 2, with family, contained in the first Living Quarters Allowance table released in that calendar year by the Office of Allowances of the U.S. Department of State.

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Argentina	Buenos Aires	120.27	43,900
Austria	Vienna	74.52	27,200
Bahamas, The	Nassau	136.16	49,700
Bahrain	Bahrain	120.55	44,000

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Barbados	Barbados	103.29	37,700
Belgium	Brussels	124.93	45,600
Belgium	SHAPE/Chievres	91.23	33,300
Bermuda	Bermuda	71.78	26,200
Bosnia-Herzegovina	Sarajevo	74.52	27,200
Brazil	Brasilia	86.30	31,500
Brazil	Rio de Janeiro	96.16	35,100
Brazil	Sao Paolo	127.40	46,500
Canada	Ottawa	107.40	39,200
Canada	Calgary	73.42	26,800
Canada	Halifax	68.49	25,000
Canada	London, Ontario	70.41	25,700
Canada	Montreal	138.90	50,700
Canada	Toronto	113.70	41,500
Canada	Vancouver	106.85	39,000
Canada	Victoria	76.71	28,000
Canada	Winnipeg	68.22	24,900
Chile	Santiago	96.71	35,300
Colombia	Bogota	148.22	54,100
Colombia	All cities other than Bogota and Barranquilla	123.01	44,900
Costa Rica	San Jose	71.78	26,200
Dominican Republic	Santo Domingo	110.96	40,500
Ecuador	Quito	81.92	29,900
Ecuador	Guayaquil	84.38	30,800
El Salvador	San Salvador	69.04	25,200
France	Paris	217.26	79,300
France	Le Havre	97.26	35,500
France	Lyon	139.45	50,900
France	Marseille	117.81	43,000
France	Montpellier	115.34	42,100
Germany	Berlin	132.05	48,200
Germany	Bad Aibling	92.05	33,600
Germany	Baumholder	98.08	35,800
Germany	Berchtesgaden	70.14	25,600
Germany	Darmstadt	107.67	39,300
Germany	Frankfurt am Main	112.88	41,200
Germany	Friedberg	86.03	31,400
Germany	Garmisch-Partenkirchen	93.15	34,000

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Germany	Geilenkirchen	73.97	27,000
Germany	Germersheim	81.64	29,800
Germany	Giessen	84.38	30,800
Germany	Grafenwoehr	69.86	25,500
Germany	Hanau	116.44	42,500
Germany	Hannover	80.55	29,400
Germany	Heidelberg	107.40	39,200
Germany	Kaiserslautern, Landkreis	121.64	44,400
Germany	Munich	115.62	42,200
Germany	Nuernberg	68.22	24,900
Germany	Stuttgart	113.97	41,600
Germany	Wiesbaden	129.04	47,100
Germany	Wuerzberg	93.42	34,100
Germany	All cities other than Augsburg, Bad Aibling, Bad Kreuznach, Baumholder, Berchtesgaden, Berlin, Bonn, Bremen, Bremerhaven, Cologne, Darmstadt, Duesseldorf, Flensburg, Frankfurt am Main, Friedberg, Garmisch-Partenkirchen, Geilenkirchen, Germersheim, Giessen, Grafenwoehr, Hamburg, Hanau, Hannover, Heidelberg, Heilbron, Kaiserslautern, Landkreis, Karlsruhe, Kerpen, Koblenz, Leipzig, Muenster, Munich, Nuernberg, Osterholz-Scharmbeck, Rheinberg, Stuttgart, Wiesbaden, Worms, and Wuerzburg.	92.60	33,800
Greece	Athens	86.85	31,700
Greece	Thessaloniki	84.11	30,700
Guatemala	Guatemala City	103.01	37,600
Holy See, The	Holy See, The	146.58	53,500
Hong Kong	Hong Kong	313.15	114,300
Hungary	Budapest	89.04	32,500
Ireland	Limerick	69.04	25,200
Italy	Rome	146.58	53,500
Italy	Catania	75.89	27,700
Italy	Genoa	103.29	37,700
Italy	Gioia Tauro	85.48	31,200

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Italy	Leghorn	91.78	33,500
Italy	Milan	218.63	79,800
Italy	Naples	120.82	44,100
Italy	Pordenone-Aviano	100.82	36,800
Italy	Sardinia	74.79	27,300
Italy	Turin	109.32	39,900
Italy	Verona	69.86	25,500
Italy	Vicenza	101.92	37,200
Italy	All cities other than Avellino, Brindisi, Catania, Florence, Gaeta, Genoa, Gioia Tauro, Leghorn, Milan, Naples, Nettuno, Pordenone-Aviano, Rome, Sardinia, Turin, Verona, and Vicenza.	84.11	30,700
Jamaica	Kingston	112.88	41,200
Japan	Tokyo	234.79	85,700
Japan	Akizuki	69.04	25,200
Japan	Gotemba	75.07	27,400
Japan	Misawa	69.32	25,300
Japan	Nagoya	80.00	29,200
Japan	Okinawa Prefecture	123.56	45,100
Japan	Osaka-Kobe	78.08	28,500
Japan	Sasebo	81.10	29,600
Japan	Tokyo-to	99.73	36,400
Japan	Yokohama	131.23	47,900
Japan	Yokosuka	113.42	41,400
Korea	Seoul	153.97	56,200
Korea	Chinhae	78.90	28,800
Korea	Chunchon	73.70	26,900
Korea	Kwangju	78.08	28,500
Korea	Osan AB	88.77	32,400
Korea	Pusan	81.92	29,900
Korea	Taegu	92.88	33,900
Korea	Tongduchon	72.33	26,400
Korea	Uijongbu	101.92	37,200
Korea	Waegwan	74.25	27,100

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Korea	All cities other than Changwon, Chinhae, Chunchon, Kunsun, Kwangju, Osan AB, Pusan, Seoul, Taegu, Tongduchon, Uijongbu, and Waegwan.	83.29	30,400
Kuwait	Kuwait City	163.84	59,800
Kuwait	All cities other than Kuwait City	146.85	53,600
Luxembourg	Luxembourg	120.27	43,900
Macedonia	Skopje	96.99	35,400
Malaysia	Kuala Lampur	96.71	35,300
Malaysia	All cities other than Kuala Lampur	92.33	33,700
Malta	Malta	100.00	36,500
Mexico	Mexico City	102.74	37,500
Netherlands	Hague, The	150.41	54,900
Netherlands	Amsterdam	144.93	52,900
Netherlands	Brunssum	83.01	30,300
Netherlands	Rotterdam	105.48	38,500
Netherlands	All cities other than Amsterdam, Brunssum, Coevorden, the Hague, Margraten, and Rotterdam.	76.71	28,000
Netherlands Antilles	Aruba	90.41	33,000
New Zealand	Wellington	73.15	26,700
New Zealand	Auckland	77.26	28,200
Norway	Oslo	70.96	25,900
Norway	Stavanger	90.41	33,000
Norway	All cities other than Oslo and Stavanger.	91.78	33,500
Panama	Panama City	88.22	32,200
Peru	Lima	74.79	27,300
Portugal	Lisbon	133.70	48,800
Russia	Moscow	75.34	27,500
Rwanda	Kigali	86.30	31,500
Singapore	Singapore	117.53	42,900
Spain	Madrid	99.18	36,200
Spain	Rota	85.48	31,200
Spain	Valencia	102.74	37,500
Switzerland	Bern	139.45	50,900
Switzerland	Geneva	192.60	70,300

Country	Location	Limitation on Housing Expenses (daily)	Limitation on Housing Expenses (full year)
Switzerland	All cities other than Bern and Geneva.	90.14	32,900
Thailand	Bangkok	100.27	36,600
Turkey	Ankara	84.93	31,000
Turkey	Izmir-Cigli	86.58	31,600
Ukraine	Kiev	76.99	28,100
United Kingdom	London	197.53	72,100
United Kingdom	Bath	103.84	37,900
United Kingdom	Bristol	78.08	28,500
United Kingdom	Cambridge	109.32	39,900
United Kingdom	Caversham	187.40	68,400
United Kingdom	Cheltenham	111.51	40,700
United Kingdom	Fairford	88.49	32,300
United Kingdom	Farnborough	130.14	47,500
United Kingdom	Felixstowe	110.96	40,500
United Kingdom	Harrogate	110.41	40,300
United Kingdom	High Wycombe	157.53	57,500
United Kingdom	Lakenheath	140.00	51,100
United Kingdom	Loudwater	133.42	48,700
United Kingdom	Oxfordshire	79.18	28,900
United Kingdom	Rochester	101.37	37,000
United Kingdom	Wiltshire	96.16	35,100
United Kingdom	All cities other than Bath, Belfast, Birmingham, Bristol, Brough, Bude, Cambridge, Caversham, Chelmsford, Cheltenham, Chicksands, Dunstable, Edinburgh, Edzell, Fairford, Farnborough, Felixstowe, Ft. Halstead, Glenrothes, Harrogate, High Wycombe, Hythe, Lakenheath, London, Loudwater, Nottingham, Oxfordshire, Rochester, Welford, West Byfleet, and Wiltshire.	96.16	35,100
Venezuela	Caracas	143.56	52,400
Vietnam	Hanoi	128.22	46,800

A qualified individual incurring housing expenses in one or more of the high cost localities identified above for the year 2006 may use the adjusted limit provided in the table (in lieu of $24,720) in determining his or her housing cost amount on Form 2555, *Foreign Earned Income*. A qualified individual who does not incur housing expenses in a locality identified above for the year 2006 is limited to maximum housing expenses of $67.73 per day ($24,720 per year) in determining his or her housing cost amount.

EFFECTIVE DATE

This notice is effective for taxable years beginning on or after January 1, 2006.

DRAFTING INFORMATION

The principal author of this notice is Paul J. Carlino of the Office of Associate Chief Counsel (International). For further information regarding this notice, contact Mr. Carlino at (202) 622–3840 (not a toll-free call).

Request for Comments

Comments are requested on the method identified in the notice for annual updates to the list contained in this notice. If a taxpayer believes that the average housing costs for a specific location differ significantly from the amount provided in this notice, the IRS and Treasury Department are particularly interested in information on housing costs that can be verified through publicly available data. Comments may be submitted to CC:PA:LPD:PR (Notice 2006–87), Room 5203, Internal Revenue Service, PO Box 7604, Washington, DC 20044. Submissions may also be hand-delivered Monday through Friday between the hours of 8 a.m. and 4:30 p.m. to Crystal Mall 4, room 108, 1901 South Bell Street, Arlington, VA 22202, Attn: CC:PA:LPD:PR (Notice 2006–87). Submissions may also be sent electronically via the internet to the following email address: *Notice.comments@irscounsel.treas.gov*. Include the notice number (Notice 2006–87) in the subject line.

Transition Relief for Indian Tribal Governmental Plans

Notice 2006–89

I. Purpose

This notice summarizes the changes made to § 414(d) of the Internal Revenue Code (the Code) by section 906 of the Pension Protection Act of 2006 (PPA '06) under which plans established and maintained by Indian tribal governments and certain related entities are governmental plans. This notice also provides transition relief under a reasonable and good faith standard with respect to compliance with the PPA '06 changes to § 414(d) pending further guidance, and invites comments from the public on whether additional transition issues need to be addressed. In addition, this notice provides approaches that give Indian tribal governments until September 30, 2007, to implement a new plan for commercial employees to satisfy the reasonable and good faith compliance standard as part of this transitional relief.

II. Background

Section 414(d) of the Code generally provides that a "governmental plan" includes a plan established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. A governmental plan is exempt from many of the plan qualification requirements under § 401(a) and other sections of the Code. For example, governmental plans are exempt from the minimum participation and vesting requirements under §§ 410 and 411, certain nondiscrimination and coverage requirements, funding requirements under § 412, and the joint and survivor annuity rules under § 417. See the last sentence of § 401(a) (the flush language following § 401(a)(36)).

PPA '06 changed § 414(d)[1] to amend the definition of "governmental plan" with respect to plans of an Indian tribal government, a subdivision of an Indian tribal government, or an agency or instrumentality thereof (ITG). Section 906(a)(1) of PPA '06 states:

> The term 'governmental plan' includes a plan which is established and maintained by an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), or an agency or instrumentality of either, and all of the participants of which are employees of such entity substantially all of whose services as such an employee are in the performance of essential governmental functions but not in the performance of commercial activities (whether or not an essential government function).

The Joint Committee on Taxation's Technical Explanation[2] provides that an employee all of whose services for an ITG are in the performance of essential governmental services and not in the performance of commercial activities (whether or not such activities are an essential governmental function) is an employee who can be covered under a governmental plan as described in § 414(d) of the Code. For example, a governmental plan includes a plan of a tribal government all of the participants of which are teachers in tribal schools, but a governmental plan does not include a plan covering tribal employees who are employed by a hotel, casino, service station, convenience store, or marina operated by a tribal government.

Section 906(c) of PPA '06 provides that the amendments made by section 906 apply to any year beginning on or after the date of enactment, which is August 17, 2006. The Joint Committee on Taxation's Technical Explanation (p. 244) states that the amendments apply to plan years beginning on or after the date of enactment.

Under section 1107 of PPA '06, a plan amendment made pursuant to any amendment made by PPA '06 may be retroactively effective, and does not violate the anti-cutback rules of § 411(d)(6) of the Code, except as provided by the Secretary of the Treasury, if, in addition to meeting the other applicable requirements, the amendment is made on or before the last day of the first plan year beginning on or after January 1, 2009 (2011 in the case of a governmental plan). Thus, an ITG must operate in accordance with the applicable changes to § 414(d) made by PPA '06 as of the related PPA '06 effective date, *i.e.*, the first day of the first plan year beginning on or after August 17, 2006. Further, a plan established and maintained by an ITG that is designed to be a governmental plan under § 414(d) as amended by PPA '06 must be amended to the extent necessary to reflect these changes by the last day of the first plan year beginning on or after January 1, 2011. This relief applies only if

[1] Section 906(a) of PPA '06 made similar amendments to section 3(32) and section 4021(b)(2) of the Employee Retirement Income Security Act of 1974 (ERISA).

[2] Joint Committee on Taxation, Technical Explanation of H.R. 4, the "Pension Protection Act of 2006" as passed by the House on July 28, 2006, and considered by the Senate on August 3, 2006 (JCX–38–06), August 3, 2006, 109th Cong., 2nd Sess. 244 (2006).

the amendment is effective as of the related PPA '06 effective date and the plan has been operated in accordance with the amendment.

III. Transition Relief

A. Reasonable Good Faith Compliance Pending Guidance

1. *In General*. The IRS and the Department of the Treasury anticipate issuing guidance on § 414(d) of the Code, including the amendment made by section 906 of PPA '06. Until such guidance is issued, a plan established and maintained by an ITG for its employees (ITG plan) will be treated as satisfying the requirements of section 906(a)(1) of PPA '06 to be a governmental plan under § 414(d) of the Code if it complies with those requirements based on a reasonable and good faith interpretation of the amendment made by section 906(a)(1) of PPA '06.

2. *Commercial Activities*. The reasonable and good faith interpretation standard extends to the question of whether activities are commercial for purposes of § 414(d) of the Code. However, for purposes of section III.A.1, it is not a reasonable and good faith interpretation of section 906(a)(1) of PPA '06 that an ITG plan is a governmental plan if employees who perform the following commercial activities continue to accrue benefits under the ITG plan. These are employees who are employed by a hotel, casino, service station, convenience store, or marina operated by the ITG from the first day of the first plan year beginning on or after August 17, 2006 (disregarding employees substantially all of whose services as an employee of the ITG are in the performance of essential governmental functions but not in the performance of services for a hotel, casino, service station, convenience store, or marina operated by the ITG).

B. Relief for Mixed ITG plans that Cover Both Governmental and Commercial Employees

Some ITG plans ("mixed ITG plans") provide benefits both to employees substantially all of whose work is in essential governmental functions that are not commercial activities ("governmental ITG employees") and to employees who perform commercial activities ("commercial ITG employees"). Furthermore, section 906(a)(1) of PPA '06 is effective for some ITG plans soon after its enactment. The IRS and the Department of the Treasury recognize that mixed ITG plans may have substantial difficulty in complying in operation with this provision by the provision's effective date. Accordingly, this section III.B provides guidance under which, until September 30, 2007, an ITG plan for commercial ITG employees will be treated as a continuation of the mixed ITG plan.

From the first day of the first plan year beginning on or after August 17, 2006, an existing mixed ITG plan will be treated for that plan year as satisfying the reasonable and good faith compliance standard for transitional relief under this notice if, by September 30, 2007, it takes the following steps to provide coverage for governmental ITG employees and commercial ITG employees under separate ITG plans. If an existing mixed ITG plan freezes benefits for the commercial ITG employees, and adopts a new plan covering those commercial ITG employees, in accordance with the steps below, the new ITG plan covering the commercial ITG employees will be treated as a continuation of the relevant portion of the mixed ITG plan that covered the commercial ITG employees prior to the first day of the first plan year beginning on or after August 17, 2006. These steps are:

(1) not later than September 30, 2007, the ITG adopts a separate plan covering commercial ITG employees and that plan complies with the applicable qualification rules under § 401(a) for plans that are not governmental plans under § 414(d) effective as of the first day of the first plan year beginning on or after August 17, 2006;

(2) the ITG takes action, not later than September 30, 2007, to freeze benefit accruals under the mixed ITG plan for commercial ITG employees (including commercial ITG employees who perform services for a hotel, casino, service station, convenience store, or marina operated by the ITG), effective as of the first day of the first plan year beginning on or after August 17, 2006; and

(3) there is no reduction in the benefit formula provided to participants in the continuing commercial ITG plan for the first plan year beginning on or after August 17, 2006 (*i.e.*, the level of accruals or nonelective contributions (including matching contributions) under that plan is not reduced for this year).

This relief applies even if benefits for commercial ITG employees for service before the first day of the first plan year beginning on or after August 17, 2006 are retained under the ITG plan covering governmental employees.

C. Example

The following example illustrates the relief provided in A. and B. of this section III.

Example. (i) Facts. An ITG maintains a mixed ITG plan (Plan A) for its employees. Plan A covers governmental ITG employees substantially all of whose services are in the performance of essential governmental functions that are not commercial activities, and also commercial ITG employees, *i.e.*, employees whose services are for commercial activities (such as a hotel, casino, service station, convenience store, or marina operated by the ITG). The first day of Plan A's plan year is October 1. Accordingly, section 906(a)(1) of PPA '06 is effective for Plan A on October 1, 2006.

(ii) *Reasonable and good faith compliance*. In order to comply with the requirements of section 906(a)(1) of PPA '06 to be a governmental plan, action is taken by the ITG on July 1, 2007, to freeze benefits under Plan A with respect to the commercial ITG employees, as of September 30, 2006, so that Plan A only provides benefits for the commercial ITG employees for years of service before October 1, 2006. A continuing plan (Plan B) is adopted on July 1, 2007, effective as of October 1, 2006, the terms of which are the same as Plan A, but which only applies to the commercial ITG employees. Since October 1, 2006, Plan B provides the same level of benefits as were provided under Plan A before October 1, 2006, and Plan B complies with the qualification requirements for plans that are not governmental plans (including the operations of Plan B being consistent with the terms of Plan B). Accordingly, Plan B is treated as a continuation of Plan A from and after October 1, 2006.

(iii) *Alternative reasonable and good faith compliance*. As an alternative to the action under (ii) of this Example, the ITG takes action on July 1, 2007, effective as of October 1, 2006, to spin off all (or a portion) of the assets and liabilities of Plan A with respect to commercial ITG employees as a separate Plan B for service from and after October 1, 2006. Since October 1, 2006, Plan B provides the same level of benefits as were provided under Plan A before October 1, 2006, and Plan B (including benefits for service before October 1, 2006) complies with the qualification requirements for plans that are not governmental plans beginning on October 1, 2006 (including the operations of Plan B being consistent with the terms of Plan B). Accordingly, Plan B is treated as a continuation of Plan A from and after October 1, 2006.

D. Definition of Essential Governmental Function

The definition of an essential governmental function under § 7871(e) of the Code for purposes of determining the availability of tax-exempt bond financing for an ITG (including the summary of which activities are considered an essential governmental function customarily performed by State and local governments) described in the advance notice of proposed rulemaking under § 7871 published by the IRS on August 9, 2006[3] will be considered a reasonable and good faith interpretation of what constitutes an essential government function under § 414(d).

E. Relief Only Applies Pending Further Guidance

The relief provided in this section III applies pending the issuance of further guidance relating to § 414(d), including the amendment made by section 906(a)(1) of PPA '06.

IV. Request for Comments

The IRS and the Department of the Treasury request public comments on issues relating to the amendment made by section 906(a)(1) of PPA '06, including transitional issues not addressed in this notice (such as issues for ITG plans with a cash or deferred arrangement under § 401(k)). Written comments should be submitted by January 22, 2007. Send submissions to: CC:PA:LPD:PR (Notice 2006–89), room 5203, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8:30 a.m. and 4:30 p.m. to: Crystal Mall 4 Building, 1901 S. Bell St., room 108, Arlington, VA 22202. Alternatively, taxpayers may submit comments electronically to *notice.comments@irscounsel.treas.gov* (Notice 2006–89).

Drafting Information

The principal author of this notice is Ingrid Grinde of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, please contact the Employee Plans taxpayer assistance telephone service at (877) 829–5500 (a toll-free number) between the hours of 8:30 am and 4:30 pm Eastern Time, Monday through Friday . Ms. Grinde may be reached at (202) 283–9888 (not a toll-free number).

Alternative Fuel and Alternative Fuel Mixtures; Blood Collector Organizations

Notice 2006–92

Section 1. PURPOSE

This notice provides guidance on: (1) the credit and payment provisions for alternative fuel and alternative fuel mixtures under §§ 34, 6426(d), 6426(e), and 6427(e) of the Internal Revenue Code; and (2) the imposition of tax on alternative fuel and alternative fuel mixtures under §§ 4041(a)(2), 4041(a)(3), and 4081(b). These provisions were added by the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (Pub. L. 109–59) and are effective October 1, 2006. This notice also provides guidance on the excise tax exemption for blood collector organizations added by the Pension Protection Act of 2006 (Pub. L. 109–280). References to regulations in this notice are to the Manufacturers and Retailers Excise Tax Regulations.

Section 2. DEFINITIONS

(a) *Alternative fuel* has the meaning given to the term by § 6426(d)(2). Section 6426(d)(2) provides that *alternative fuel* means liquefied petroleum gas, P Series Fuels (as defined by the Secretary of Energy under 42 U.S.C. 13211(2)), compressed or liquefied natural gas, liquefied hydrogen, any liquid fuel derived from coal (including peat) through the Fischer-Tropsch process, and liquid hydrocarbons derived from biomass (as defined in § 45K(c)(3)). The term does not include ethanol, methanol, biodiesel, or renewable diesel. (For the definition of biodiesel, see § 40A(d)(1). For the definition of renewable diesel and treatment of renewable diesel in the same manner as biodiesel, see § 40A(f).)

(b) *Alternative fuel mixture* means a mixture of alternative fuel and taxable fuel that contains at least 0.1 percent (by volume) of taxable fuel (as defined in § 4083(a)(1)).

(c) *Alternative fueler* means a person that—

(1) Is an alternative fueler (unmixed fuel); or

(2) Produces alternative fuel mixtures for sale or use in its trade or business.

(d) The *alternative fueler (unmixed fuel)* with respect to any alternative fuel is the person that—

(1) Is liable for tax on the alternative fuel imposed by § 4041(a)(2) or (3) (determined in the case of compressed natural gas after the application of § 48.4041–21 and in the case of any other alternative fuel after the application of rules similar to the rules of §§ 48.4041–3 and 48.4041–5); or

(2) Would be so liable for such tax but for the application of an exemption provided by § 4041(a)(3)(B), (b), (f), (g), or (h).

(e) *Motor vehicle* has the meaning given to the term by § 48.4041–8(c).

(f) *Use as a fuel*. The following definitions apply for purposes of section 4 of this notice (relating to alternative fuel mixtures):

(1) A mixture is *used as a fuel* when it is consumed in the production of energy. Thus, for example, a mixture is used as a fuel when it is consumed in an internal combustion engine to power a vehicle or in a furnace to produce heat. A mixture that is destroyed in a fire or other casualty loss is not used as a fuel.

(2) A mixture producer sells a mixture *for use as a fuel* if the producer has reason to believe that the mixture will be used as a fuel either by the person buying the mixture from the producer or by any later buyer of the mixture.

Section 3. ALTERNATIVE FUEL

(a) *Overview*. This section provides rules under which a credit or payment may be obtained under § 6426 (the alternative fuel excise tax credit), §§ 34 and 6427 (the alternative fuel income tax credit), or § 6427 (the alternative fuel payment) for

[3] Advance notice of proposed rulemaking, REG–118788–06, 71 Fed. Reg. 45474 (August 9, 2006).

alternative fuel that is sold for use or used as a fuel in a motor vehicle or motorboat. The amount of the credit or payment allowed with respect to alternative fuel is based on the amount of alternative fuel sold or used.

(b) *Conditions to allowance*—(1) *Excise tax credit*. A claim for the alternative fuel excise tax credit with respect to alternative fuel sold for use or used as a fuel in a motor vehicle or motorboat is allowed under § 6426 only if the claimant—

(i) Is the alternative fueler (unmixed fuel) with respect to the fuel;

(ii)(A) Is registered under § 4101 as an alternative fueler; or

(B) In the case of a claim made before July 1, 2007, is registered under § 4101 for any purpose;

(iii) Has made no other claim with respect to the alternative fuel;

(iv) Has filed a timely claim on Form 720, *Quarterly Federal Excise Tax Return*, and the claim contains all the information required by the claim form described in paragraph (c) of this section; and

(v) Has § 4041 liability for the period of the claim and the total amount of the alternative fuel excise tax credit claimed under § 6426 for the period of the claim does not exceed such liability.

(2) *Refundable income tax credit*—(i) *In general*. A claim for the alternative fuel income tax credit with respect to alternative fuel sold for use or used as a fuel in a motor vehicle or motorboat is allowed under §§ 34 and 6427(e)(2) only if—

(A) The conditions of paragraphs (b)(1)(i) and (ii) of this section are met;

(B) The sale or use of the alternative fuel is in the claimant's trade or business;

(C) The claimant has filed a timely claim for credit on Form 4136, *Credit for Federal Tax Paid on Fuels*, and the claim contains all the information required by the claim form described in paragraph (c) of this section; and

(D) The amount claimed under §§ 34 and 6427(e)(2) as an alternative fuel income tax credit is the amount that exceeds the claimant's § 4041 liability for the period of the claim.

(ii) *Estimated tax reduction*. For purposes of determining the amount of required estimated tax payments, the alternative fuel income tax credit claimed on Form 4136 is subtracted from total tax and reduces estimated tax payments. Thus, a taxpayer may benefit from the credit before filing an income tax return. See, for example, Form 1120–W, *Estimated Tax for Corporations*.

(3) *Payments*. A claim for the alternative fuel payment with respect to alternative fuel sold for use or used as a fuel in a motor vehicle or motorboat is allowed under § 6427(e)(2) only if—

(i) The claimant is—

(A) The United States;

(B) A State (as defined in § 48.4081–1(b)); or

(C) A § 501(a) exempt organization (other than an organization required to file a Form 990–T, *Exempt Organization Business Income Tax Return*);

(ii) The conditions of paragraphs (b)(1)(i) and (ii) of this section are met;

(iii) The sale or use of the alternative fuel is in the claimant's trade or business;

(iv) The claimant has filed a timely claim for payment on Form 8849, *Claim for Refund of Excise Taxes*, and the claim contains all of the information required by the claim form described in paragraph (c) of this section; and

(v) The amount claimed under § 6427(e)(2) as an alternative fuel payment is the amount that exceeds the claimant's § 4041 liability for the period of the claim.

(c) *Content of claim*. The claim form will provide that each claim for an alternative fuel credit or payment must contain the following information with respect to the alternative fuel covered by the claim:

(1) The amount of alternative fuel sold or used.

(2) A statement that the conditions to allowance described in paragraph (b) of this section have been met.

(3) A statement that the claimant either—

(i) Produced the alternative fuel it sold or used; or

(ii) Has in its possession the name, address, and employer identification number of the person(s) that sold the alternative fuel to the claimant, the date of purchase, and an invoice or other documentation identifying the alternative fuel.

(d) *Amount of the credit*. The amount of credit for any alternative fuel other than compressed natural gas is the product of $0.50 and the number of gallons of alternative fuel. The amount of the credit for compressed natural gas is $0.50 per 121 cubic feet.

Section 4. ALTERNATIVE FUEL MIXTURES

(a) *Overview*. This section provides rules under which a credit or payment may be obtained under § 6426 (the alternative fuel mixture excise tax credit), §§ 34 and 6427 (the alternative fuel mixture income tax credit), or § 6427 (the alternative fuel mixture payment) for an alternative fuel mixture that is sold for use or used as a fuel by the person producing the mixture. The amount of the credit or payment allowed with respect to an alternative fuel mixture is based on the amount of alternative fuel used to produce the mixture.

(b) *Conditions to allowance*—(1) *Excise tax credit*. A claim for the alternative fuel mixture excise tax credit with respect to an alternative fuel mixture is allowed under § 6426 only if the claimant—

(i) Produced the alternative fuel mixture for sale or use in the trade or business of the claimant;

(ii)(A) Sold the alternative fuel mixture for use as a fuel; or

(B) Used the alternative fuel mixture as a fuel;

(iii)(A) Is registered under § 4101 as an alternative fueler; or

(B) In the case of claims made before July 1, 2007, is registered under § 4101 for any purpose;

(iv) Has made no other claim with respect to the amount of alternative fuel in the mixture or, if a payment with respect to the amount of alternative fuel was erroneously claimed under § 6427 and received, claimant has repaid the government with interest;

(v) Has filed a timely claim on Form 720 and the claim contains all the information required by the claim form described in paragraph (c) of this section; and

(vi) Has § 4081 liability for the period of the claim and the total amount of the alternative fuel mixture excise tax credit claimed under § 6426 for the period of the claim does not exceed such liability.

(2) *Payment or income tax credit*. A claim for an alternative fuel mixture payment under § 6427 or an alternative fuel mixture income tax credit under §§ 34 and 6427 is allowed only if—

(i) The conditions of paragraphs (b)(1)(i), (ii), and (iii) of this section are met;

(ii) The claimant has filed a timely claim for payment on Form 8849 or Form 720 or for credit on Form 4136 and the claim contains all the information required by the claim form described in paragraph (c) of this section; and

(iii) The amount claimed under § 6427 as an alternative fuel mixture payment or under §§ 34 and 6427 as an alternative fuel mixture income tax credit is the amount that exceeds the claimant's § 4081 liability for the period of the claim.

(c) *Content of claim*. The claim form will provide that each claim for an alternative fuel mixture credit or payment must contain the following information with respect to the mixture covered by the claim:

(1) The amount of alternative fuel in the alternative fuel mixture.

(2) A statement that the conditions to allowance described in paragraph (b) of this section have been met.

(3) A statement that the claimant either—

(i) Produced the alternative fuel it used in the mixture; or

(ii) Has in its possession the name, address, and employer identification number of the person(s) that sold the alternative fuel to the claimant, the date of purchase, and an invoice or other documentation identifying the alternative fuel.

(d) *Amount of the credit or payment*. The amount of credit or payment for any alternative fuel mixture is the product of $0.50 and the number of gallons of alternative fuel used to produce the mixture.

Section 5. REGISTRATION

(a) *Application for registration*. Application for registration as an alternative fueler is made on Form 637, *Application for Registration (For Certain Excise Tax Activities)*, in accordance with the instructions for that form. As provided in § 48.4101–1(a)(2), a person is registered under § 4101 only if the Service has issued a registration letter to the person.

(b) *Requirements*. The Service will register an applicant as an alternative fueler only if the Service—

(1) Determines that the applicant is an alternative fueler or is likely to become an alternative fueler within a reasonable time after being registered under § 4101; and

(2) Is satisfied with the filing, deposit, payment, reporting, and claim history for federal taxes of the applicant and any related person (as defined in § 48.4101–1(b)(5)).

Section 6. TAXATION OF ALTERNATIVE FUEL AND ALTERNATIVE FUEL MIXTURES

(a) *Alternative fuels*—(1) *Liquids*. A liquid alternative fuel (that is, any alternative fuel other than compressed natural gas) is a liquid other than gas oil, fuel oil, or taxable fuel and is subject to the tax imposed by § 4041(a)(2) when it is sold for use or used as a fuel in a motor vehicle or motorboat. Rules similar to the rules of §§ 48.4041–3 and 48.4041–5 (relating to the application of the tax on sales of special motor fuels) apply. For exemptions from tax, see §§ 4041(b), (f), (g), and (h).

(2) *Compressed natural gas*. Compressed natural gas is subject to the tax imposed by § 4041(a)(3) when it is sold for use or used as a fuel in a motor vehicle or motorboat. The rules of § 48.4041–21 apply. For exemptions from tax, see §§ 4041(a)(3)(B), (b), (f), (g), and (h).

(b) *Alternative fuel mixtures*—(1) If an alternative fuel mixture is taxable fuel, the mixture is subject to tax imposed by § 4081 when it is removed, entered, or sold and the rules of §§ 48.4081–1 through 48.4081–8 apply.

(2) If an alternative fuel mixture is not a taxable fuel and is sold for use or used as a fuel in a diesel-powered highway vehicle or diesel-powered train, the mixture is subject to the tax imposed by § 4041(a)(1) at the time of such sale or use and the rules of § 48.4082–4 apply.

(3) If an alternative fuel mixture is not a taxable fuel and is sold for use or used as a fuel in a motor vehicle (other than a diesel-powered highway vehicle) or motorboat, the mixture is subject to the tax imposed by § 4041(a)(2) at the time of such sale or use and rules similar to the rules of §§ 48.4041–3 and 48.4041–5 (relating to the application of the tax on sales of special motor fuels) apply. For exemptions from tax, see §§ 4041(b), (f), (g), and (h).

(c) *Rate of tax*. For the rate of tax generally, see §§ 4041 and 4081. The rate of tax for compressed natural gas is $0.183 per 126.67 cubic feet.

Section 7. QUALIFIED BLOOD COLLECTOR ORGANIZATIONS

(a) *Overview*. Under the Pension Protection Act of 2006 (Pub. L. 109–280), qualified blood collector organizations are exempt from many federal excise taxes (or a credit or payment relating to the tax is available). These taxes include the taxes on fuel, tires, communications services, and heavy vehicles. This provision is effective after December 31, 2006, except that the exemption from the highway use tax applies after June 30, 2007.

(b) *Definition*. *Qualified blood collector organization* has the meaning given to the term by § 7701(a)(49). Section 7701(a)(49) provides that a *qualified blood collector organization* means an organization that is described in § 501(c)(3) and is exempt from tax under § 501(a), primarily engaged in the activity of the collection of human blood, registered with the Service for purposes of excise tax exemptions, and registered by the Food and Drug Administration to collect blood.

(c) *Registration*—(1) *In general*. Each blood collector organization must be registered by the Service as a condition for applying for the exemptions (or credit or payments) under the Code as a blood collector organization. Application for registration is made on Form 637, *Application for Registration (For Certain Excise Tax Activities)*, in accordance with the instructions for that form. As provided in § 48.4101–1(a)(2), a person is registered under § 4101 only if the Service has issued a registration letter to the person.

(2) *Requirements*. The Service will register an applicant as a blood collector organization only if the Service—

(i) Determines that the applicant is a person described in § 7701(a)(49)(A), (B), and (D); and

(ii) Is satisfied with the filing, deposit, payment, reporting, and claim history for all federal taxes of the applicant and any related person (as defined in § 48.4101–1(b)(5)).

Section 8. EFFECTIVE DATE

This notice is effective after September 30, 2006, except that section 7 of this notice is effective after December 31, 2006.

Section 9. DRAFTING INFORMATION

The principal authors of this notice are Susan Athy and Deborah Karet of the Office of the Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, please contact Ms. Athy (concerning alternative fuel and alternative fuel mixtures) and Ms. Karet (concerning qualified blood collector organizations) at (202) 622–3130 (not a toll-free call).

Weighted Average Interest Rates Update

Notice 2006–94

This notice provides guidance as to the corporate bond weighted average interest rate and the permissible range of interest rates specified under § 412(b)(5)(B)(ii)(II) of the Internal Revenue Code. In addition, it provides guidance as to the interest rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II).

CORPORATE BOND WEIGHTED AVERAGE INTEREST RATE

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

Notice 2004–34, 2004–1 C.B. 848, provides guidelines for determining the corporate bond weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability. That notice establishes that the corporate bond weighted average is based on the monthly composite corporate bond rate derived from designated corporate bond indices. The methodology for determining the monthly composite corporate bond rate as set forth in Notice 2004–34 continues to apply in determining that rate. See Notice 2006–75, 2006–36 I.R.B. 366.

The composite corporate bond rate for September 2006 is 5.95 percent. Pursuant to Notice 2004–34, the Service has determined this rate as the average of the monthly yields for the included corporate bond indices for that month.

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

Month	For Plan Years Beginning in: Year	Corporate Bond Weighted Average	90% to 100% Permissible Range
October	2006	5.79	5.21 to 5.79

30-YEAR TREASURY SECURITIES INTEREST RATE

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

The rate of interest on 30-year Treasury securities for September 2006 is 4.85 percent. The Service has determined this rate as the monthly average of the daily determination of yield on the 30-year Treasury bond maturing in February 2036.

Drafting Information

The principal authors of this notice are Paul Stern and Tony Montanaro of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, please contact the Employee Plans' taxpayer assistance telephone service at 877–829–5500 (a toll-free number), between the hours of 8:30 a.m. and 4:30 p.m. Eastern time, Monday through Friday. Mr. Stern may be reached at 202–283–9703. Mr. Montanaro may be reached at 202–283–9714. The telephone numbers in the preceding sentences are not toll-free.

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26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.

(Also Part I, §§ 62, 162, 267, 274; 1.62–2, 1.162–17, 1.267(a)–1, 1.274–5.)

Rev. Proc. 2006–41

SECTION 1. PURPOSE

This revenue procedure updates Rev. Proc. 2005–67, 2005–42 I.R.B. 729, and provides rules under which the amount of ordinary and necessary business expenses of an employee for lodging, meal, and incidental expenses, or for meal and incidental expenses, incurred while traveling away from home are deemed substantiated under § 1.274–5 of the Income Tax Regulations when a payor (the employer, its agent, or a third party) provides a *per diem* allowance under a reimbursement or other expense allowance arrangement to pay for the expenses. In addition, this revenue procedure provides an optional method for employees and self-employed individuals who are not reimbursed to use in computing the deductible costs paid or incurred for business meal and incidental expenses,

or for incidental expenses only if no meal costs are paid or incurred, while traveling away from home. Use of a method described in this revenue procedure is not mandatory, and a taxpayer may use actual allowable expenses if the taxpayer maintains adequate records or other sufficient evidence for proper substantiation. This revenue procedure does not provide rules under which the amount of an employee's lodging expenses will be deemed substantiated when a payor provides an allowance to pay for those expenses but not meal and incidental expenses.

SECTION 2. BACKGROUND AND CHANGES

.01 Section 162(a) of the Internal Revenue Code allows a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. Under that provision, an employee or self-employed individual may deduct expenses paid or incurred while traveling away from home in pursuit of a trade or business. However, under § 262, no portion of the travel expenses that is attributable to personal, living, or family expenses is deductible.

.02 Section 274(n) generally limits the amount allowable as a deduction under § 162 for any expense for food, beverages, or entertainment to 50 percent of the amount of the expense that otherwise would be allowable as a deduction. In the case of any expenses for food or beverages consumed while away from home (within the meaning of § 162(a)(2)) by an individual during, or incident to, the period of duty subject to the hours of service limitations of the Department of Transportation, § 274(n)(3) gradually increases the deductible percentage to 80 percent for taxable years beginning in 2008. For taxable years beginning in 2006 or 2007, the deductible percentage for these expenses is 75 percent.

.03 Section 274(d) provides, in part, that no deduction is allowed under § 162 for any travel expense (including meals and lodging while away from home) unless the taxpayer complies with certain substantiation requirements. Section 274(d) further provides that regulations may prescribe that some or all of the substantiation requirements do not apply to an expense that does not exceed an amount prescribed by the regulations.

.04 Section 1.274–5(g), in part, grants the Commissioner the authority to prescribe rules relating to reimbursement arrangements or *per diem* allowances for ordinary and necessary expenses paid or incurred while traveling away from home. Pursuant to this grant of authority, the Commissioner may prescribe rules under which these arrangements or allowances, if in accordance with reasonable business practice, are regarded (1) as equivalent to substantiation, by adequate records or other sufficient evidence, of the amount of travel expenses for purposes of § 1.274–5(c), and (2) as satisfying the requirements of an adequate accounting to the employer of the amount of travel expenses for purposes of § 1.274–5(f).

.05 For purposes of determining adjusted gross income, § 62(a)(2)(A) allows an employee a deduction for expenses allowed by Part VI (§ 161 and following), subchapter B, chapter 1 of the Code, paid or incurred by the employee in connection with the performance of services as an employee under a reimbursement or other expense allowance arrangement with a payor.

.06 Section 62(c) provides that an arrangement is not treated as a reimbursement or other expense allowance arrangement for purposes of § 62(a)(2)(A) if it—

(1) does not require the employee to substantiate the expenses covered by the arrangement to the payor, or

(2) provides the employee with the right to retain any amount in excess of the substantiated expenses covered under the arrangement.

Section 62(c) further provides that the substantiation requirements described therein do not apply to any expense to the extent that, under the grant of regulatory authority prescribed in § 274(d), the Commissioner has provided that substantiation is not required for the expense.

.07 Under § 1.62–2(c)(1), a reimbursement or other expense allowance arrangement satisfies the requirements of § 62(c) if it meets the requirements of business connection, substantiation, and returning amounts in excess of expenses as specified in the regulations. Section 1.62–2(e)(2) specifically provides that substantiation of certain business expenses in accordance with rules prescribed under the authority of §§ 1.274–5(g) or 1.274–5(j) is treated as substantiation of the amount of the expenses for purposes of § 1.62–2. Under § 1.62–2(f)(2), the Commissioner may prescribe rules under which an arrangement providing *per diem* allowances is treated as satisfying the requirement of returning amounts in excess of expenses, even though the arrangement does not require the employee to return the portion of the allowance that relates to days of travel substantiated and that exceeds the amount of the employee's expenses deemed substantiated pursuant to rules prescribed under § 274(d), provided the allowance is reasonably calculated not to exceed the amount of the employee's expenses or anticipated expenses and the employee is required to return within a reasonable period of time any portion of the allowance that relates to days of travel not substantiated.

.08 Section 1.62–2(h)(2)(i)(B) provides that, if a payor pays a *per diem* allowance that meets the requirements of § 1.62–2(c)(1), the portion, if any, of the allowance that relates to days of travel substantiated in accordance with § 1.62–2(e), that exceeds the amount of the employee's expenses deemed substantiated for the travel pursuant to rules prescribed under § 274(d) and § 1.274–5(g) or § 1.274–5(j), and that the employee is not required to return, is subject to withholding and payment of employment taxes. See §§ 31.3121(a)–3, 31.3231(e)–1(a)(5), 31.3306(b)–2, and 31.3401(a)–4 of the Employment Tax Regulations. Because the employee is not required to return this excess portion, the reasonable period of time provisions of § 1.62–2(g) (relating to the return of excess amounts) do not apply to this portion.

.09 Under § 1.62–2(h)(2)(i)(B)(4), the Commissioner has the discretion to prescribe special rules regarding the timing of withholding and payment of employment taxes on *per diem* allowances.

.10 Section 1.274–5(j)(1) grants the Commissioner the authority to establish a method under which a taxpayer may elect to use a specified amount for meals paid or incurred while traveling away from home in lieu of substantiating the actual cost of meals.

.11 Section 1.274–5(j)(3) grants the Commissioner the authority to establish a method under which a taxpayer may elect to use a specified amount for incidental

expenses paid or incurred while traveling away from home in lieu of substantiating the actual cost of incidental expenses.

.12 Sections 3.02(1)(a), 4.04(6), and 5.06 of this revenue procedure provide transition rules for the last 3 months of calendar year 2006.

.13 Section 5.02 of this revenue procedure contains revisions to the *per diem* rates for high-cost localities and for other localities for purposes of section 5.

.14 Section 5.03 of this revenue procedure contains the list of high-cost localities and section 5.04 of this revenue procedure describes changes to the list of high-cost localities for purposes of section 5.

SECTION 3. DEFINITIONS

.01 *Per diem allowance*. The term "*per diem* allowance" means a payment under a reimbursement or other expense allowance arrangement that is—

(1) paid with respect to ordinary and necessary business expenses incurred, or that the payor reasonably anticipates will be incurred, by an employee for lodging, meal, and incidental expenses, or for meal and incidental expenses, for travel away from home in connection with the performance of services as an employee of the employer,

(2) reasonably calculated not to exceed the amount of the expenses or the anticipated expenses, and

(3) paid at or below the applicable federal *per diem* rate, a flat rate or stated schedule, or in accordance with any other Service-specified rate or schedule.

.02 *Federal per diem rate and federal M&IE rate*.

(1) *In general*. The federal *per diem* rate is equal to the sum of the applicable federal lodging expense rate and the applicable federal meal and incidental expense (M&IE) rate for the day and locality of travel.

(a) *CONUS rates*. The rates for localities in the continental United States ("CONUS") are set forth in Appendix A to 41 C.F.R. ch. 301. However, in applying section 4.01, 4.02, or 4.03 of this revenue procedure, taxpayers may continue to use the CONUS rates in effect for the first 9 months of 2006 for expenses of all CONUS travel away from home that are paid or incurred during calendar year 2006 in lieu of the updated GSA rates. A taxpayer must consistently use either these rates or the updated rates for the period October 1, 2006, through December 31, 2006.

(b) *OCONUS rates*. The rates for localities outside the continental United States ("OCONUS") are established by the Secretary of Defense (rates for non-foreign localities, including Alaska, Hawaii, Puerto Rico, the Northern Mariana Islands, and the possessions of the United States) and by the Secretary of State (rates for foreign localities), and are published in the *Per Diem* Supplement to the Standardized Regulations (Government Civilians, Foreign Areas) (updated on a monthly basis).

(c) *Internet access to the rates*. The CONUS and OCONUS rates may be found on the Internet at *www.gsa.gov*.

(2) *Locality of travel*. The term "locality of travel" means the locality where an employee traveling away from home in connection with the performance of services as an employee of the employer stops for sleep or rest.

(3) *Incidental expenses*. The term "incidental expenses" has the same meaning as in the Federal Travel Regulations, 41 C.F.R. 300–3.1 (2006). Thus, based on the current definition of "incidental expenses" in the Federal Travel Regulations, "incidental expenses" means fees and tips given to porters, baggage carriers, bellhops, hotel maids, stewards or stewardesses and others on ships, and hotel servants in foreign countries; transportation between places of lodging or business and places where meals are taken, if suitable meals can be obtained at the temporary duty site; and the mailing cost associated with filing travel vouchers and payment of employer-sponsored charge card billings.

.03 *Flat rate or stated schedule*.

(1) *In general*. Except as provided in section 3.03(2) of this revenue procedure, an allowance is paid at a flat rate or stated schedule if it is provided on a uniform and objective basis with respect to the expenses described in section 3.01 of this revenue procedure. The allowance may be paid with respect to the number of days away from home in connection with the performance of services as an employee or on any other basis that is consistently applied and in accordance with reasonable business practice. Thus, for example, an hourly payment to cover meal and incidental expenses paid to a pilot or flight attendant who is traveling away from home in connection with the performance of services as an employee is an allowance paid at a flat rate or stated schedule. Likewise, a payment based on the number of miles traveled (such as cents per mile) to cover meal and incidental expenses paid to an over-the-road truck driver who is traveling away from home in connection with the performance of services as an employee is an allowance paid at a flat rate or stated schedule.

(2) *Limitation*. For purposes of this revenue procedure, an allowance that is computed on a basis similar to that used in computing the employee's wages or other compensation (such as the number of hours worked, miles traveled, or pieces produced) does not meet the business connection requirement of § 1.62–2(d), is not a *per diem* allowance, and is not paid at a flat rate or stated schedule, unless, as of December 12, 1989, (a) the allowance was identified by the payor either by making a separate payment or by specifically identifying the amount of the allowance, or (b) an allowance computed on that basis was commonly used in the industry in which the employee is employed. See § 1.62–2(d)(3)(ii).

SECTION 4. *PER DIEM* SUBSTANTIATION METHOD

.01 *Per diem allowance*. If a payor pays a *per diem* allowance in lieu of reimbursing actual lodging, meal, and incidental expenses incurred or to be incurred by an employee for travel away from home, the amount of the expenses that is deemed substantiated for each calendar day is equal to the lesser of the *per diem* allowance for that day or the amount computed at the federal *per diem* rate (see section 3.02 of this revenue procedure) for the locality of travel for that day (or partial day, see section 6.04 of this revenue procedure).

.02 *Meal and incidental expenses only per diem allowance*. If a payor pays a *per diem* allowance only for meal and incidental expenses in lieu of reimbursing actual meal and incidental expenses incurred or to be incurred by an employee for travel away from home, the amount of the expenses that is deemed substantiated for each calendar day is equal to the lesser of the *per diem* allowance for that day or the amount computed at the federal M&IE rate for the locality of travel for that day

(or partial day). A *per diem* allowance is treated as paid only for meal and incidental expenses if (1) the payor pays the employee for actual expenses for lodging based on receipts submitted to the payor, (2) the payor provides the lodging in kind, (3) the payor pays the actual expenses for lodging directly to the provider of the lodging, (4) the payor does not have a reasonable belief that lodging expenses were or will be incurred by the employee, or (5) the allowance is computed on a basis similar to that used in computing the employee's wages or other compensation (such as the number of hours worked, miles traveled, or pieces produced).

.03 *Optional method for meal and incidental expenses only deduction*. In lieu of using actual expenses in computing the amount allowable as a deduction for ordinary and necessary meal and incidental expenses paid or incurred for travel away from home, employees and self-employed individuals who pay or incur meal expenses may use an amount computed at the federal M&IE rate for the locality of travel for each calendar day (or partial day) the employee or self-employed individual is away from home. This amount will be deemed substantiated for purposes of paragraphs (b)(2) and (c) of § 1.274–5, provided the employee or self-employed individual substantiates the elements of time, place, and business purpose of the travel for that day (or partial day) in accordance with those regulations. See section 6.05(1) of this revenue procedure for rules related to the application of the limitation under § 274(n) to amounts determined under this section 4.03. See section 4.05 of this revenue procedure for a method for substantiating incidental expenses that may be used by employees or self-employed individuals who do not pay or incur meal expenses.

.04 *Special rules for transportation industry*.

(1) *In general*. This section 4.04 applies to (a) a payor that pays a *per diem* allowance only for meal and incidental expenses for travel away from home as described in section 4.02 of this revenue procedure to an employee in the transportation industry, or (b) an employee or self-employed individual in the transportation industry who computes the amount allowable as a deduction for meal and incidental expenses for travel away from home in accordance with section 4.03 of this revenue procedure.

(2) *Transportation industry defined*. For purposes of this section 4.04, an employee or self-employed individual is in the transportation industry only if the employee's or individual's work (a) is of the type that directly involves moving people or goods by airplane, barge, bus, ship, train, or truck, and (b) regularly requires travel away from home which, during any single trip away from home, usually involves travel to localities with differing federal M&IE rates. For purposes of the preceding sentence, a payor must determine that an employee or a group of employees is in the transportation industry by using a method that is consistently applied and in accordance with reasonable business practice.

(3) *Rates*. A taxpayer described in section 4.04(1) of this revenue procedure may treat $52 as the federal M&IE rate for any CONUS locality of travel, and $58 as the federal M&IE rate for any OCONUS locality of travel. A payor that uses either (or both) of these special rates with respect to an employee must use the special rate(s) for all amounts subject to section 4.02 of this revenue procedure paid to that employee for travel away from home within CONUS and/or OCONUS, as the case may be, during the calendar year. Similarly, an employee or self-employed individual that uses either (or both) of these special rates must use the special rate(s) for all amounts computed pursuant to section 4.03 of this revenue procedure for travel away from home within CONUS and/or OCONUS, as the case may be, during the calendar year. See section 4.04(6) of this revenue procedure for transition rules.

(4) *Periodic rule*. A payor described in section 4.04(1) of this revenue procedure may compute the amount of the employee's expenses that is deemed substantiated under section 4.02 of this revenue procedure periodically (not less frequently than monthly), rather than daily, by comparing the total *per diem* allowance paid for the period to the sum of the amounts computed either at the federal M&IE rate(s) for the localities of travel, or at the special rate described in section 4.04(3), for the days (or partial days) the employee is away from home during the period.

(5) *Examples*.

(a) *Example 1*. Taxpayer, an employee in the transportation industry, travels away from home on business within CONUS on 17 days (including partial days) during a calendar month and receives a *per diem* allowance only for meal and incidental expenses from a payor that uses the special rule under section 4.04(3) of this revenue procedure. The amount deemed substantiated under section 4.02 of this revenue procedure is equal to the lesser of the total *per diem* allowance paid for the month or $884 (17 days at $52 per day).

(b) *Example 2*. Taxpayer, a truck driver employee in the transportation industry, is paid a "cents-per-mile" allowance that qualifies as an allowance paid under a flat rate or stated schedule as defined in section 3.03 of this revenue procedure. Taxpayer travels away from home on business for 10 days. Based on the number of miles driven by Taxpayer, Taxpayer's employer pays an allowance of $500 for the 10 days of business travel. Taxpayer actually drives for 8 days, and does not drive for the other 2 days Taxpayer is away from home. Taxpayer is paid under the periodic rule used for transportation industry employers and employees in accordance with section 4.04(4) of this revenue procedure. The amount deemed substantiated and excludable from Taxpayer's income is the full $500 because that amount does not exceed $520 (ten days away from home at $52 per day).

(6) *Transition rules*. Under the calendar-year convention provided in section 4.04(3), a taxpayer who used the federal M&IE rates during the first 9 months of calendar year 2006 to substantiate the amount of an individual's travel expenses under sections 4.02 or 4.03 of Rev. Proc. 2005–67 may not use, for that individual, the special transportation industry rates provided in this section 4.04 until January 1, 2007. Similarly, a taxpayer who used the special transportation industry rates during the first 9 months of calendar year 2006 to substantiate the amount of an individual's travel expenses may not use, for that individual, the federal M&IE rates until January 1, 2007.

.05 *Optional method for incidental expenses only deduction*. In lieu of using actual expenses in computing the amount allowable as a deduction for ordinary and necessary incidental expenses paid or incurred for travel away from home, employees and self-employed individuals who do not pay or incur meal expenses for a calendar day (or partial day) of travel away from home may use, for each calendar day (or partial day) the employee or self-employed individual is away from home, an amount computed at the rate of $3 per day for any CONUS or OCONUS locality of travel. This amount will be deemed substantiated for purposes of paragraphs (b)(2) and (c) of § 1.274–5, provided the employee or

self-employed individual substantiates the elements of time, place, and business purpose of the travel for that day (or partial day) in accordance with those regulations. See section 4.03 of this revenue procedure for a method that may be used by employees or self-employed individuals who pay or incur meal expenses. The method authorized by this section 4.05 may not be used by payors that use section 4.01, 4.02, or 5.01 of this revenue procedure, or by employees or self-employed individuals who use the method described in section 4.03 of this revenue procedure. See section 6.05(4) of this revenue procedure for rules related to the application of the limitation under § 274(n) to amounts determined under this section 4.05.

SECTION 5. HIGH-LOW SUBSTANTIATION METHOD

.01 *In general*. If a payor pays a *per diem* allowance in lieu of reimbursing actual lodging, meal, and incidental expenses incurred or to be incurred by an employee for travel away from home and the payor uses the high-low substantiation method described in this section 5 for travel within CONUS, the amount of the expenses that is deemed substantiated for each calendar day is equal to the lesser of the *per diem* allowance for that day or the amount computed at the rate set forth in section 5.02 of this revenue procedure for the locality of travel for that day (or partial day, see section 6.04 of this revenue procedure). Except as provided in section 5.06 of this revenue procedure, this high-low substantiation method may be used in lieu of the *per diem* substantiation method provided in section 4.01 of this revenue procedure, but may not be used in lieu of the meal and incidental expenses only *per diem* substantiation method provided in section 4.02 of this revenue procedure.

.02 *Specific high-low rates*. Except as provided in section 5.06 of this revenue procedure, the *per diem* rate set forth in this section 5.02 is $246 for travel to any "high-cost locality" specified in section 5.03 of this revenue procedure, or $148 for travel to any other locality within CONUS. The high or low rate, as appropriate, applies as if it were the federal *per diem* rate for the locality of travel. For purposes of applying the high-low substantiation method and the § 274(n) limitation on meal expenses (see section 6.05(3) of this revenue procedure), the amount of the high and low rates that is treated as paid for meals is $58 for a high-cost locality and $45 for any other locality within CONUS.

.03 *High-cost localities*. The following localities have a federal *per diem* rate of $197 or more, and are high-cost localities for all of the calendar year or the portion of the calendar year specified in parentheses under the key city name:

Key City	*County or other defined location*
Arizona	
Phoenix/Scottsdale (January 1-March 31)	Maricopa
California	
San Francisco	San Francisco
Santa Barbara (July 1-August 31)	Santa Barbara
Santa Monica	City limits of Santa Monica
South Lake Tahoe (December 1-March 31)	El Dorado
Colorado	
Aspen (December 1-April 30)	Pitkin
Crested Butte/Gunnison (December 1-April 30)	Gunnison
Steamboat Springs (December 1-March 31)	Routt
Telluride (October 1-April 30)	San Miguel
Vail (December 1-March 31)	Eagle
District of Columbia	
Washington D.C. (also the cities of Alexandria, Falls Church, and Fairfax, and the counties of Arlington and Fairfax, in Virginia; and the counties of Montgomery and Prince George's in Maryland) (See also Maryland and Virginia)	

Key City	*County or other defined location*
Florida	
Fort Lauderdale (January 1-March 31)	Broward
Fort Walton Beach/DeFuniak Springs (June 1-July 31)	Okaloosa and Walton
Key West	Monroe
Miami (January 1-March 31)	Miami-Dade
Naples (February 1-March 31)	Collier
Palm Beach (February 1-March 31)	Boca Raton, Delray Beach, Jupiter, Palm Beach Gardens, Palm Beach, Palm Beach Shores, Singer Island and West Palm Beach
Stuart (February 1-March 31)	Martin
Illinois	
Chicago	Cook and Lake
Louisiana	
New Orleans (October 1-May 31)	Orleans, St. Bernard, Jefferson and Plaquemine Parishes
Maryland	
(For the counties of Montgomery and Prince George's, see District of Columbia)	
Baltimore	Baltimore City
Cambridge/St. Michaels (May 1-August 31)	Dorchester and Talbot
Ocean City (June 1-September 30)	Worcester
Massachusetts	
Boston/Cambridge	Suffolk, City of Cambridge
Martha's Vineyard (July 1-August 31)	Dukes
Nantucket (October 1-November 30 and June 1-September 30)	Nantucket
New York	
Floral Park/Garden City/Glen Cove/Great Neck/Roslyn	Nassau
Lake Placid (July 1-August 31)	Essex
Manhattan	The Boroughs of Manhattan, Brooklyn, the Bronx and Staten Island
Queens	Queens
Saratoga Springs/Schenectady (July 1-August 31)	Saratoga and Schenectady

Key City	*County or other defined location*
Pennsylvania	
Philadelphia	Philadelphia
Rhode Island	
Jamestown/Middletown/ Newport (October 1-November 30 and March 1-September 30)	Newport
Providence	Providence
Utah	
Park City (December 1-March 31)	Summit
Virginia	
(For the cities of Alexandria, Falls Church, and Fairfax, and the counties of Arlington and Fairfax, see District of Columbia)	
Washington	
Seattle	King

.04 *Changes in high-cost localities*. The list of high-cost localities in section 5.03 of this revenue procedure differs from the list of high-cost localities in section 5.03 of Rev. Proc. 2005–67 (changes listed by key cities).

(1) The following localities have been added to the list of high-cost localities: Santa Barbara, California; South Lake Tahoe, California; Fort Lauderdale, Florida; Fort Walton Beach/DeFuniak Springs, Florida; and Stuart, Florida.

(2) The portion of the year for which the following are high-cost localities has been changed: Aspen, Colorado; Miami, Florida; Chicago, Illinois; Cambridge/St. Michaels, Maryland; Nantucket, Massachusetts; and Jamestown/Middletown/Newport, Rhode Island.

(3) The following localities have been removed from the list of high-cost localities: Napa, California; San Diego, California; Silverthorne/Breckenridge, Colorado; Bar Harbor, Maine; Conway, New Hampshire; Cape May/Ocean City, New Jersey; Riverhead/Ronkonkoma/Melville/Smithtown/Huntington Station/Amagansett/East Hampton/Montauk/Southampton/Islandia/Commack/Medford/Stony Brook/Hauppauge/Centereach, New York; and Tarrytown/White Plains/New Rochelle/Yonkers, New York.

(4) The following localities have been redefined: Baltimore no longer includes Baltimore County; Manhattan, New York no longer includes Queens; and Washington, D.C. no longer includes Loudoun County, Virginia.

.05 *Specific limitation*.

(1) Except as provided in section 5.05(2) of this revenue procedure, a payor that uses the high-low substantiation method with respect to an employee must use that method for all amounts paid to that employee for travel away from home within CONUS during the calendar year. See section 5.06 of this revenue procedure for transition rules.

(2) With respect to an employee described in section 5.05(1) of this revenue procedure, the payor may reimburse actual expenses or use the meal and incidental expenses only *per diem* substantiation method described in section 4.02 of this revenue procedure for any travel away from home, and may use the *per diem* substantiation method described in section 4.01 of this revenue procedure for any OCONUS travel away from home.

.06 *Transition rules*. A payor who used the substantiation method of section 4.01 of Rev. Proc. 2005–67 for an employee during the first 9 months of calendar year 2006 may not use the high-low substantiation method in section 5 of this revenue procedure for that employee until January 1, 2007. A payor who used the high-low substantiation method of section 5 of Rev. Proc. 2005–67 for an employee during the first 9 months of calendar year 2006 must continue to use the high-low substantiation method for the remainder of calendar year 2006 for that employee. A payor described in the previous sentence may use the rates and high-cost localities published in section 5 of Rev. Proc. 2005–67, in lieu of the updated rates and high-cost localities provided in section 5 of this revenue procedure, for travel on or after October 1, 2006, and before January 1, 2007, if those rates and localities are used consistently during this period for all employees reimbursed under this method.

SECTION 6. LIMITATIONS AND SPECIAL RULES

.01 *In general*. The federal *per diem* rate and the federal M&IE rate described in section 3.02 of this revenue procedure for the locality of travel will be applied in the same manner as applied under the Federal Travel Regulations, 41 C.F.R. Part 301–11 (2006), except as provided in sections 6.02 through 6.04 of this revenue procedure.

.02 *Federal per diem rate*. A receipt for lodging expenses is not required in determining the amount of expenses deemed substantiated under section 4.01 or 5.01 of this revenue procedure. See section 7.01 of this revenue procedure for the requirement that the employee substantiate the time, place, and business purpose of the expense.

.03 *Federal per diem or M&IE rate*. A payor is not required to reduce the federal *per diem* rate or the federal M&IE rate for the locality of travel for meals provided in kind, provided the payor has a reasonable belief that meal and incidental expenses were or will be incurred by the employee during each day of travel.

.04 *Proration of the federal per diem or M&IE rate*. Pursuant to the Federal Travel Regulations, in determining the federal *per diem* rate or the federal M&IE rate for the locality of travel, the full applicable federal M&IE rate is available for a full day of travel from 12:01 a.m. to 12:00 midnight. The method described in section 6.04(1) of this revenue procedure must be used for purposes of determining the amount deemed substantiated under section 4.03 or 4.05 of this revenue procedure for partial days of travel away from home. For purposes of determining the amount deemed substantiated under section 4.01, 4.02, 4.04, or 5 of this revenue procedure for partial days of travel away from home, either of the following methods may be used to prorate the federal M&IE rate to determine the federal *per diem* rate or the federal M&IE rate for the partial days of travel:

(1) The rate may be prorated using the method prescribed by the Federal Travel Regulations. Currently the Federal Travel Regulations allow three-fourths of the applicable federal M&IE rate for each partial day during which the employee or self-employed individual is traveling away from home in connection with the performance of services as an employee or self-employed individual. The same ratio may be applied to prorate the allowance for incidental expenses described in section 4.05 of this revenue procedure; or

(2) The rate may be prorated using any method that is consistently applied and in accordance with reasonable business practice. For example, if an employee travels away from home from 9 a.m. one day to 5 p.m. the next day, a method of proration that results in an amount equal to two times the federal M&IE rate will be treated as being in accordance with reasonable business practice (even though only one and a half times the federal M&IE rate would be allowed under the Federal Travel Regulations).

.05 *Application of the appropriate § 274(n) limitation on meal expenses*. Except as provided in section 6.05(4), all or part of the amount of an expense deemed substantiated under this revenue procedure is subject to the appropriate limitation under § 274(n) (see section 2.02 of this revenue procedure) on the deductibility of food and beverage expenses.

(1) If an amount for meal and incidental expenses is computed pursuant to section 4.03 of this revenue procedure, the taxpayer must treat that amount as an expense for food and beverages.

(2) If a *per diem* allowance is paid only for meal and incidental expenses, the payor must treat an amount equal to the lesser of the allowance or the federal M&IE rate for the locality of travel for each day (or partial day, see section 6.04 of this revenue procedure) as an expense for food and beverages.

(3) If a *per diem* allowance is paid for lodging, meal, and incidental expenses, the payor must treat an amount equal to the federal M&IE rate for the locality of travel for each calendar day (or partial day) the employee is away from home as an expense for food and beverages. For purposes of the preceding sentence, if a *per diem* allowance for lodging, meal, and incidental expenses is paid at a rate that is less than the federal *per diem* rate for the locality of travel for each day (or partial day), the payor may treat an amount equal to 40 percent of the allowance as the federal M&IE rate for the locality of travel for each day (or partial day).

(4) If an amount for incidental expenses is computed under section 4.05 of this revenue procedure, none of the amount so computed is subject to limitation under § 274(n) on the deductibility of food and beverage expenses.

.06 *No double reimbursement or deduction*. If a payor pays a *per diem* allowance in lieu of reimbursing actual lodging, meal, and incidental expenses, or meal and incidental expenses, in accordance with section 4 or 5 of this revenue procedure, any additional payment with respect to those expenses is treated as paid under a nonaccountable plan, is included in the employee's gross income, is reported as wages or other compensation on the employee's Form W–2, "*Wage and Tax Statement*," and is subject to withholding and payment of employment taxes. Similarly, if an employee or self-employed individual computes the amount allowable as a deduction for meal and incidental expenses for travel away from home in accordance with section 4.03 or 4.04 of this revenue procedure, no other deduction is allowed to the employee or self-employed individual with respect to those expenses. For example, assume an employee receives a *per diem* allowance from a payor for lodging, meal, and incidental expenses, or for meal and incidental expenses, incurred while traveling away from home. During that trip, the employee pays for dinner for the employee and two business associates. The payor reimburses as a business entertainment meal expense the meal expense for the employee and the two business associates. Because the payor also pays a *per diem* allowance to cover the cost of the employee's meals, the amount paid by the payor for the employee's portion of the business entertainment meal expense is treated as paid under a nonaccountable plan, is reported as wages or other compensation on the employee's Form W–2, and is subject to withholding and payment of employment taxes.

.07 *Related parties*. Sections 4.01 and 5 of this revenue procedure do not apply if a payor and an employee are related within the meaning of § 267(b), but for this purpose the percentage of ownership interest referred to in § 267(b)(2) is 10 percent.

SECTION 7. APPLICATION

.01 If the amount of travel expenses is deemed substantiated under the rules provided in section 4 or 5 of this revenue procedure, and the employee substantiates to the payor the elements of time, place, and business purpose of the travel for that day (or partial day) in accordance with paragraphs (b)(2) and (c) (other than subparagraph (2)(iii)(A) thereof) of § 1.274–5, the employee is deemed to satisfy the adequate accounting requirements of § 1.274–5(f) as well as the requirement to substantiate by adequate records or other sufficient evidence for purposes of § 1.274–5(c). See § 1.62–2(e)(1) for the rule that an arrangement must require business expenses to be substantiated to the payor within a reasonable period of time.

.02 An arrangement providing *per diem* allowances will be treated as satisfying the requirement of § 1.62–2(f)(2) of returning amounts in excess of expenses if the

employee is required to return within a reasonable period of time (as defined in § 1.62–2(g)) any portion of the allowance that relates to days of travel not substantiated, even though the arrangement does not require the employee to return the portion of the allowance that relates to days of travel substantiated and that exceeds the amount of the employee's expenses deemed substantiated. For example, assume a payor provides an employee an advance *per diem* allowance for meal and incidental expenses of $250, based on an anticipated 5 days of business travel at $50 per day to a locality for which the federal M&IE rate is $39, and the employee substantiates 3 full days of business travel. The requirement to return excess amounts is treated as satisfied if the employee is required to return within a reasonable period of time (as defined in § 1.62–2(g)) the portion of the allowance that is attributable to the 2 unsubstantiated days of travel ($100), even though the employee is not required to return the portion of the allowance ($33) that exceeds the amount of the employee's expenses deemed substantiated under section 4.02 of this revenue procedure ($117) for the 3 substantiated days of travel. However, the $33 excess portion of the allowance is treated as paid under a nonaccountable plan as discussed in section 7.04 of this revenue procedure.

.03 An employee is not required to include in gross income the portion of a *per diem* allowance received from a payor that is less than or equal to the amount deemed substantiated under the rules provided in section 4 or 5 of this revenue procedure if the employee substantiates the business travel expenses covered by the *per diem* allowance in accordance with section 7.01 of this revenue procedure. See § 1.274–5(f)(2)(i). In addition, that portion of the allowance is treated as paid under an accountable plan, is not reported as wages or other compensation on the employee's Form W–2, and is exempt from the withholding and payment of employment taxes. See § 1.62–2(c)(2) and (c)(4).

.04 An employee is required to include in gross income only the portion of the *per diem* allowance received from a payor that exceeds the amount deemed substantiated under the rules provided in section 4 or 5 of this revenue procedure if the employee substantiates the business travel expenses covered by the *per diem* allowance in accordance with section 7.01 of this revenue procedure. See § 1.274–5(f)(2)(ii). In addition, the excess portion of the allowance is treated as paid under a nonaccountable plan, is reported as wages or other compensation on the employee's Form W–2, and is subject to withholding and payment of employment taxes. See § 1.62–2(c)(3)(ii), (c)(5), and (h)(2)(i)(B).

.05 If the amount of the expenses that is deemed substantiated under the rules provided in section 4.01, 4.02, or 5 of this revenue procedure is less than the amount of the employee's business expenses for travel away from home, the employee may claim an itemized deduction for the amount by which the business travel expenses exceed the amount that is deemed substantiated, provided the employee substantiates all the business travel expenses, includes on Form 2106, "*Employee Business Expenses*," the deemed substantiated portion of the *per diem* allowance received from the payor, and includes in gross income the portion (if any) of the *per diem* allowance received from the payor that exceeds the amount deemed substantiated. See § 1.274–5(f)(2)(iii). However, for purposes of claiming this itemized deduction with respect to meal and incidental expenses, substantiation of the amount of the expenses is not required if the employee is claiming a deduction that is equal to or less than the amount computed under section 4.03 of this revenue procedure minus the amount deemed substantiated under sections 4.02 and 7.01 of this revenue procedure. The itemized deduction is subject to the appropriate limitation (see section 2.02 of this revenue procedure) on meal and entertainment expenses provided in § 274(n) and the 2-percent floor on miscellaneous itemized deductions provided in § 67.

.06 An employee who pays or incurs amounts for meal expenses and does not receive a *per diem* allowance for meal and incidental expenses may deduct an amount computed pursuant to section 4.03 of this revenue procedure only as an itemized deduction. This itemized deduction is subject to the appropriate limitation on meal and entertainment expenses provided in § 274(n) and the 2-percent floor on miscellaneous itemized deductions provided in § 67. See section 7.07 of this revenue procedure for the treatment of an employee who does not pay or incur amounts for meal expenses and does not receive a *per diem* allowance for incidental expenses.

.07 An employee who does not pay or incur amounts for meal expenses and does not receive a *per diem* allowance for incidental expenses may deduct an amount computed pursuant to section 4.05 of this revenue procedure only as an itemized deduction. This itemized deduction is subject to the 2-percent floor on miscellaneous itemized deductions provided in § 67. See section 7.06 of this revenue procedure for the treatment of an employee who pays or incurs amounts for meal expenses and does not receive a *per diem* allowance for meal and incidental expenses.

.08 A self-employed individual who pays or incurs meal expenses for a calendar day (or partial day) of travel away from home may deduct an amount computed pursuant to section 4.03 of this revenue procedure in determining adjusted gross income under § 62(a)(1). This deduction is subject to the appropriate limitation on meal and entertainment expenses provided in § 274(n).

.09 A self-employed individual who does not pay or incur meal expenses for a calendar day (or partial day) of travel away from home may deduct an amount computed pursuant to section 4.05 of this revenue procedure in determining adjusted gross income under § 62(a)(1).

.10 If a payor's reimbursement or other expense allowance arrangement evidences a pattern of abuse of the rules of § 62(c) and the regulations thereunder, all payments under the arrangement will be treated as made under a nonaccountable plan. See § 1.62–2(k). Thus, these payments are included in the employee's gross income, are reported as wages or other compensation on the employee's Form W–2, and are subject to withholding and payment of employment taxes. See § 1.62–2(c)(3), (c)(5), and (h)(2).

SECTION 8. WITHHOLDING AND PAYMENT OF EMPLOYMENT TAXES

.01 The portion of a *per diem* allowance, if any, that relates to the days of business travel substantiated and that exceeds the amount deemed substantiated for those days under section 4.01, 4.02, or 5 of this revenue procedure is subject to withholding and payment of employment taxes. See § 1.62–2(h)(2)(i)(B).

.02 In the case of a *per diem* allowance paid as a reimbursement, the excess described in section 8.01 of this revenue procedure is subject to withholding and payment of employment taxes in the payroll period in which the payor reimburses the expenses for the days of travel substantiated. See § 1.62–2(h)(2)(i)(B)(2).

.03 In the case of a *per diem* allowance paid as an advance, the excess described in section 8.01 of this revenue procedure is subject to withholding and payment of employment taxes no later than the first payroll period following the payroll period in which the days of travel with respect to which the advance was paid are substantiated. See § 1.62–2(h)(2)(i)(B)(3). If some or all of the days of travel with respect to which the advance was paid are not substantiated within a reasonable period of time and the employee does not return the portion of the allowance that relates to those days within a reasonable period of time, the portion of the allowance that relates to those days is subject to withholding and payment of employment taxes no later than the first payroll period following the end of the reasonable period. See § 1.62–2(h)(2)(i)(A).

.04 In the case of a *per diem* allowance only for meal and incidental expenses for travel away from home paid to an employee in the transportation industry by a payor that uses the rule in section 4.04(4) of this revenue procedure, the excess of the *per diem* allowance paid for the period over the amount deemed substantiated for the period under section 4.02 of this revenue procedure (after applying section 4.04(4) of this revenue procedure), is subject to withholding and payment of employment taxes no later than the first payroll period following the payroll period in which the excess is computed. See § 1.62–2(h)(2)(i)(B)(4).

.05 For example, assume that an employer pays an employee a *per diem* allowance to cover business expenses for meals and lodging for travel away from home at a rate of 120 percent of the federal *per diem* rate for the localities to which the employee travels. The employer does not require the employee to return the 20 percent by which the reimbursement for those expenses exceeds the federal *per diem* rate. The employee substantiates 6 days of travel away from home: 2 days in a locality in which the federal *per diem* rate is $160 and 4 days in a locality in which the federal *per diem* rate is $120. The employer reimburses the employee $960 for the 6 days of travel away from home (2 x (120% x $160) + 4 x (120% x $120)), and does not require the employee to return the excess payment of $160 (2 days x $32 ($192-$160) + 4 days x $24 ($144-$120)). For the payroll period in which the employer reimburses the expenses, the employer must withhold and pay employment taxes on $160. See section 8.02 of this revenue procedure.

SECTION 9. EFFECTIVE DATE

This revenue procedure is effective for *per diem* allowances for lodging, meal and incidental expenses, or for meal and incidental expenses only, that are paid to an employee on or after October 1, 2006, with respect to travel away from home on or after October 1, 2006. For purposes of computing the amount allowable as a deduction for travel away from home, this revenue procedure is effective for meal and incidental expenses or for incidental expenses only paid or incurred on or after October 1, 2006.

SECTION 10. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 2005–67 is superseded.

DRAFTING INFORMATION

The principal author of this revenue procedure is Jeffrey T. Rodrick of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue procedure, contact Mr. Rodrick at (202) 622–4930 (not a toll-free call).

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Elimination of Country-by-Country Reporting to Shareholders of Foreign Taxes Paid by Regulated Investment Companies

REG–105248–04

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that would generally eliminate country-by-country reporting by a regulated investment company (RIC) to its shareholders of foreign source income that the RIC takes into account and foreign taxes that it pays. RICs will continue to report this information directly to the IRS. The regulations will affect certain RICs that pay foreign taxes and the shareholders of those RICs.

DATES: Written or electronic comments and requests for a public hearing must be received by December 18, 2006.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–105248–04), Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be sent electronically via the IRS Internet site at: *www.irs.gov/regs* or Federal eRulemaking Portal at *www.regulations.gov* (IRS REG–105248–04).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Susan Thompson Baker, (202) 622–3930; concerning submissions of comments and requests for a public hearing, Kelly Banks, (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collection of information should be received by November 17, 2006. Comments are specifically requested concerning:

The accuracy of the estimated burden associated with the proposed collection of information (see below);

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

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

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

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

The collection of information in this proposed regulation is in §1.853–4(c) and (d). A RIC is required to notify the IRS of amounts of income received from sources within foreign countries and possessions of the United States and taxes paid to each such foreign country or possession in order that the IRS may monitor shareholder compliance with the foreign tax credit provisions. The collection of information is required if a RIC elects to pass through the benefits of the foreign tax credit to its shareholders.

Estimated total annual reporting burden: 80 hours.

Estimated average annual burden hours per respondent: 2.

Estimated annual frequency of responses: 1.

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

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

Background

This document contains proposed amendments to 26 CFR part 1 under section 853 of the Internal Revenue Code (Code). Section 853 provides a foreign tax credit or deduction to shareholders of a RIC that makes an election under, and that meets the requirements set forth in, that section.

A RIC more than 50 percent of the value of whose total assets at the close of a taxable year consists of stock or securities in foreign corporations may make an election under section 853 (a "foreign tax passthrough election"). If the RIC makes this election for that taxable year, it forgoes a deduction or credit for certain taxes paid to foreign countries and possessions of the United States (collectively, "foreign taxes") (but the amount of the foreign taxes is allowed as an addition to the RIC's deduction for dividends paid for the year). Instead, the RIC passes through to its shareholders a credit or deduction for the foreign taxes it has paid during its taxable year. If the RIC makes this election, each shareholder includes the shareholder's proportionate share of these foreign taxes in gross income and treats this proportionate share as paid by the shareholder. Each shareholder of an electing RIC further treats as gross income from sources within foreign countries and possessions of the United States the sum of the shareholder's proportionate share of these taxes and the portion of any dividend paid by the RIC that represents income derived from sources within foreign countries and possessions of the United States. Each shareholder may then deduct or claim a credit for the payment of a proportionate share of these taxes.

A RIC electing this treatment must provide information to its shareholders and to the IRS. First, under section 853(c) of the Code, the RIC must designate, in a written notice mailed to shareholders not later than 60 days after the close of its taxable year, each shareholder's proportionate share of foreign taxes paid by the RIC and each shareholder's proportionate share of the RIC's gross income derived from sources within any foreign country or possession of the United States. Section 1.853–3(a) of the current Income tax regulations (the regulations) requires that this notice designate the shareholder's portion of foreign taxes paid to each such foreign country or possession of the United States and the portion of the dividend that represents income derived from sources within each foreign country or possession of the United States.

Second, under §1.853–4(a) of the regulations, the RIC must file with Form 1099–DIV, "*Dividends and Distributions*", and Form 1096, "*Annual Summary and Transmittal of U.S. Information Returns*", a statement as part of its income tax return (Form 1120–RIC or its successor) that sets forth the total amount of income received from sources within foreign countries and possessions of the United States; the total amount of foreign taxes paid; the date, form, and contents of the notice to its shareholders; and the proportionate share of this income received and these taxes paid during the taxable year attributable to one share of its stock. The RIC must also file as part of its return for the taxable year a Form 1118, "*Foreign Tax Credit—Corporations*", that has been modified so that it is a statement in support of the RIC's foreign tax passthrough election.

The requirement of §1.853–3(a) of the regulations that an electing RIC provide country-by-country information to its shareholders on foreign-source income received and foreign taxes paid was originally adopted at a time when many shareholders generally needed the information to apply a per-country limitation on the foreign tax credit. Because of changes to the foreign tax credit provisions, shareholders generally no longer need country-by-country information on the amounts of foreign-source income and foreign taxes paid.

The Treasury Department and the IRS have received comments suggesting that the section 853 regulations should be amended to eliminate per-country reporting to shareholders and that Form 1116, "*Foreign Tax Credit (Individual, Estate or Trust)*", should be modified to indicate that distributions from RICs are exempt from per-country shareholder reporting. According to these comments, eliminating the reporting of this information not only would reduce the time and expense required of RICs to compile and disseminate this tax information but also would reduce the confusion that their shareholders experience upon receipt of the extensive tables used to report this per-country information.

Even though the section 904 foreign tax credit limitation has been applied on a separate category of income basis, instead of on a per-country basis, since 1976, the Treasury Department and the IRS have continued to require the reporting of per-country information by RICs. This per-country information remains relevant to the IRS's monitoring compliance with the section 901 rules that disallow credits for refundable and noncompulsory payments and for taxes paid to certain countries. See §1.901–2(e)(2) and (5), providing that credit is not allowed for amounts that are in excess of final liability under foreign law for tax, and section 901(j), denying credit for tax paid to countries described in section 901(j)(2)(A) and subjecting income from sources in those countries to separate foreign tax credit limitations.

Although per-country information with respect to foreign income and foreign taxes is needed for the IRS to monitor compliance, the Treasury Department and the IRS believe that taxpayer burden can be reduced by continuing to require this information to be supplied with the RIC's tax return but generally not requiring it to be reported to the RIC's shareholders as well. Accordingly, the proposed regulations would revise §1.853–3 and §1.853–4 to require that a RIC provide aggregate per-country information on a statement filed with its tax return and would require that only summary foreign income and foreign tax amounts be reported to its shareholders. Once this proposed rule becomes final, the instructions to Forms 1116 and 1118 will be modified to permit summary reporting at the shareholder level similar to the summary reporting currently permitted with respect to "section 863(b) income" on Forms 1116 and 1118.

Explanation of Provisions

Proposed amendments to §1.853–1 of the regulations would update the regulations to reflect statutory amendments providing that the foreign tax passthrough election is not applicable to taxes for which the RIC would not be allowed a credit by reason of section 901(j) (denying credit for taxes paid to certain countries, including those with which the United States does not have diplomatic relations), section 901(k) and (l) (denying credit for withholding taxes paid on certain income where certain holding period requirements are not met), or any similar provision.

The proposed amendments would change in two ways the regulations that set forth requirements for a RIC seeking to make and to notify shareholders of a foreign tax passthrough election:

First, references in §1.853–3(a) and (b) of the regulations to required statements to shareholders of dollar amounts of taxes paid to specific countries, and to dollar amounts of income considered as received from specific countries, would be changed to require that a RIC (or a shareholder of record of the RIC who is a nominee acting as a custodian of a unit investment trust) state only the total amount of the shareholder's proportionate share of creditable foreign taxes paid, income from sources within countries described in section 901(j), if any, and income derived from sources within other foreign countries or possessions of the United States.

Second, proposed amendments to §1.853–3(b) extend various deadlines to reflect statutory changes since the regulations were issued. Thus the number of days following the close of its taxable year by which a RIC must notify its shareholders in writing of the making of a foreign tax passthrough election would be increased to 60. References to the number of days following the close of the taxable year by which a nominee acting as a custodian of a unit investment trust must notify holders of interests in the unit investment trust would be increased to 70. Similarly, references to the number of days following the close of a RIC's taxable year by which a statement that holders of interests in unit investment trusts have been directly no-

tified by the RIC (or a statement that the RIC has failed or is unable to notify these holders of interests) must be filed with the IRS and transmitted to a nominee would be increased to 60.

Section 1.853–4 of the regulations would be modified to create more flexibility in the references to specific forms. The current regulations require a RIC to file statements with Form 1099 and Form 1096 and to file, as a part of its return for the taxable year, a Form 1118, modified so that it becomes a statement in support of the election made by a RIC to pass through taxes paid to a foreign country or a possession of the United States. The first of these requirements, the requirement to file statements with Forms 1099 and 1096, is proposed to be eliminated. The proposed regulations would retain the general requirement that a RIC must file as part of its return a statement that elects the application of section 853 for the taxable year.

Section 1.853–4(a) of the regulations would also require that a RIC agree to provide certain information on foreign-source income received and foreign taxes paid. The information required to be provided is set forth in §1.853–4(c). Section 1.853–4(d) would provide that this required information is to be provided on or with a modified Form 1118 but would add that it may instead be provided in such other form or manner as may be prescribed by the Commissioner. This change would facilitate future changes in administrative practice if, for example, forms are renumbered or become obsolete.

Special Analyses

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

Comments and Requests for Public Hearing

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

The Treasury Department and the IRS invite suggestions regarding any provisions that should be added to the proposed regulations if the reporting of per-country information to shareholders is to be eliminated for calendar year 2006. In addition, the Treasury Department and the IRS invite comments both on the date by which final regulations should be published in order for a change in reporting practice to be practical for 2006 and on any effective date concerns regarding the reporting of per-country information to the IRS.

Drafting Information

The principal author of this regulation is Susan Thompson Baker of the Office of Associate Chief Counsel (Financial Institutions and Products).

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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 1.853–1 also issued under 26 U.S.C. 901(j).

Section 1.853–2 also issued under 26 U.S.C. 901(j).

Section 1.853–3 also issued under 26 U.S.C. 901(j).

Section 1.853–4 also issued under 26 U.S.C. 901(j) and 26 U.S.C. 6011. * * *

Par. 2. Section 1.853–1 is amended by adding a sentence at the end of paragraph (a) to read as follows:

§1.853–1 Foreign tax credit allowed to shareholders.

(a) *In general*. * * * In addition, the election is not applicable to any tax with respect to which the regulated investment company is not allowed a credit by reason of any provision of the Internal Revenue Code other than section 853(b)(1), including, but not limited to, section 901(j), section 901(k), or section 901(l).

* * * * *

Par. 3. Section 1.853–2 is amended by revising paragraph (d) to read as follows:

§1.853–2 Effect of election.

* * * * *

(d) *Example*. This section is illustrated by the following example:

Example. (i) *Facts*. X Corporation, a regulated investment company with 250,000 shares of common stock outstanding, has total assets, at the close of the taxable year, of $10 million ($4 million invested in domestic corporations, $3.5 million in Foreign Country A corporations, and $2.5 million in Foreign Country B corporations). X Corporation received dividend income of $800,000 from the following sources: $300,000 from domestic corporations, $250,000 from Country A corporations, and $250,000 from Country B corporations. All dividends from Country A corporations and from Country B corporations were properly characterized as income from sources without the United States. The dividends from Country A corporations were subject to a 10 percent withholding tax ($25,000) and the dividends from Country B corporations were subject to a 20 percent withholding tax ($50,000). X Corporation's only expenses for the taxable year were $80,000 of operation and management expenses related to both its U.S. and foreign investments. In this case, Corporation X properly apportioned the $80,000 expense based on the relative amounts of its U.S. and foreign source gross income. Thus, $50,000 in expense was apportioned to foreign source income ($80,000 × $500,000/$800,000, total expense times the fraction of foreign dividend income over total dividend income) and $30,000 in expense was apportioned to U.S. source income ($80,000 × $300,000/$800,000, total expense times the fraction of U.S. source dividend income over total dividend income). During the taxable year, X Corporation distributes to its shareholders the entire $645,000 income that is available for distribution

($800,000, less $80,000 in expenses, less $75,000 in foreign taxes withheld).

(ii) *Section 853 election.* X Corporation meets the requirements of section 851 to be considered a RIC for the taxable year and the requirements of section 852(a) for part 1 of subchapter M to apply for the taxable year. X Corporation notifies each shareholder by mail, within the time prescribed by section 853(c), that by reason of the election the shareholders are to treat as foreign taxes paid $0.30 per share of stock ($75,000 of foreign taxes paid, divided by the 250,000 shares of stock outstanding). The shareholders must report as income $2.88 per share ($2.58 of dividends actually received plus the $0.30 representing foreign taxes paid). Of the $2.88 per share, $1.80 per share ($450,000 of foreign source taxable income divided by 250,000 shares) is to be considered as received from foreign sources. The $1.80 consists of $0.30, the foreign taxes treated as paid by the shareholder and $1.50, the portion of the dividends received by the shareholder from the RIC that represents income of the RIC treated as derived from foreign sources ($500,000 of foreign source income, less $50,000 of expense apportioned to foreign source income, less $75,000 of foreign tax withheld, which is $375,000, divided by 250,000 shares).

Par. 4. Section 1.853–3 is amended by:

1. Revising paragraph (a).

2. Removing the number "55th" and adding the number "70th" in its place in the first sentence of paragraph (b).

3. Revising the second sentence of paragraph (b).

4. Removing the number "45" and adding the number "60" in its place in each place in which it appears in the fifth sentence of paragraph (b).

The revisions read as follows:

§1.853–3 Notice to shareholders.

(a) *General rule.* If a regulated investment company makes an election under section 853(a), in the manner provided in §1.853–4, the regulated investment company is required under section 853(c) to furnish its shareholders with a written notice mailed not later than 60 days after the close of its taxable year. The notice must designate the shareholder's portion of creditable foreign taxes paid to foreign countries or possessions of the United States and the portion of the dividend that represents income derived from sources within each country that is attributable to a period during which section 901(j) applies to such country, if any, and the portion of the dividend that represents income derived from other foreign countries and possessions of the United States. For purposes of section 853(b)(2) and paragraph (b) of §1.853–2, the amount that a shareholder may treat as the shareholder's proportionate share of foreign taxes paid and the amount to be included as gross income derived from any foreign country that is attributable to a period during which section 901(j) applies to such country or gross income from sources within other foreign countries or possessions of the United States shall not exceed the amount so designated by the regulated investment company in such written notice. If, however, the amount designated by the regulated investment company in the notice exceeds the shareholder's proper proportionate share of foreign taxes or gross income from sources within foreign countries or possessions of the United States, the shareholder is limited to the amount correctly ascertained.

(b) *Shareholder of record custodian of certain unit investment trusts.* * * * The notice shall designate the holder's proportionate share of the amounts of creditable foreign taxes paid to foreign countries or possessions of the United States and the holder's proportionate share of the dividend that represents income derived from sources within each country that is attributable to a period during which section 901(j) applies to such country, if any, and the holder's proportionate share of the dividend that represents income derived from other foreign countries or possessions of the United States shown on the notice received by the nominee identified as such. * * *

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Par. 5. Section 1.853–4 is amended by:

1. Revising paragraphs (a) and (b).

2. Adding paragraphs (c) and (d).

The revisions and additions read as follows:

§1.853–4 Manner of making election.

(a) *General rule.* To make an election under section 853 for a taxable year, a regulated investment company must file a statement of election as part of its Federal income tax return for the taxable year. The statement of election must state that the regulated investment company elects the application of section 853 for the taxable year and agrees to provide the information required by paragraph (c) of this section.

(b) *Irrevocability of the election.* The election shall be made with respect to all foreign taxes described in paragraph (c)(2) of this section, and must be made not later than the time prescribed for filing the return (including extensions). This election, if made, shall be irrevocable with respect to the dividend (or portion) and the foreign taxes paid with respect thereto, to which the election applies.

(c) *Required information.* A regulated investment company making an election under section 853 must provide the following information:

(1) The total amount of taxable income received in the taxable year from sources within foreign countries and possessions of the United States and the amount of taxable income received in the taxable year from sources within each such foreign country or possession.

(2) The total amount of income, war profits, or excess profits taxes (described in section 901(b)(1)) to which the election applies that were paid in the taxable year to such foreign countries or possessions and the amount of such taxes paid to each such foreign country or possession.

(3) The amount of income, war profits, or excess profits taxes paid during the taxable year to which the election does not apply by reason of any provision of the Internal Revenue Code other than section 853(b), including, but not limited to, section 901(j), section 901(k), or section 901(l).

(4) The date, form, and contents of the notice to its shareholders.

(5) The proportionate share of creditable foreign taxes paid to each such foreign country or possession during the taxable year and foreign income received from sources within each such foreign country or possession during the taxable year attributable to one share of stock of the regulated investment company.

(d) *Time and manner of providing information.* The information specified in paragraph (c) of this section must be provided at the time and in the manner prescribed by the Commissioner and, unless otherwise prescribed, must be provided on or with a modified Form 1118 filed as part of the RIC's timely filed Federal income tax return for the taxable year.

* * * * *

Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on September 15, 2006, 8:45 a.m., and published in the issue of the Federal Register for September 18, 2006, 71 F.R. 54598)

Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations and Notice of Public Hearing

Railroad Track Maintenance Credit

REG–142270–05

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing.

SUMMARY: In this issue of the Bulletin, the IRS is issuing temporary regulations (T.D. 9286) under section 45G of the Internal Revenue Code relating to the railroad track maintenance credit determined for qualified railroad track maintenance expenditures paid or incurred by a Class II or Class III railroad and other eligible taxpayers during the taxable year. The temporary regulations reflect changes to the law made by the American Jobs Creation Act of 2004 and the Gulf Opportunity Zone Act of 2005. The text of those temporary regulations also serves as the text of these proposed regulations. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written or electronic comments must be received by December 7, 2006. Outlines of topics to be discussed at the public hearing scheduled for Tuesday, January 9, 2007, at 10 a.m. must be received by December 8, 2006.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–142270–05), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Alternatively, submissions may be sent electronically, via the IRS Internet site at *http://www.irs.gov.regs* or via the Federal eRulemaking Portal at *http://www.regulations.gov* (IRS REG–142270–05). The public hearing will be held in the auditorium of the New Carrollton Federal Building, 5000 Ellin Road, Lanham, MD 20706.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Winston H. Douglas, (202) 622–3110; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Kelly D. Banks, (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collections of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collection of information should be received by November 7, 2006. Comments are specifically requested concerning:

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

The accuracy of the estimated burden associated with the proposed collection of information (see below);

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

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

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

The collections of information in this notice of proposed rulemaking are in §1.45G–1T(d). This information is required to verify the assignments of railroad track miles made under section 45G(b). This information will be used by the Service for examination purposes. The collection of information is required to obtain a benefit. The likely respondents are business or other for-profit institutions.

Estimated total annual reporting: 1,375 hours.

The estimated annual burden per respondent varies from 1 hour to 4 hours, depending on individual circumstances, with an estimated average of 2.5 hours.

Estimated number of respondents: 550.

Estimated frequency of responses: Annually.

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

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

Background

Temporary regulations in this issue of the Bulletin amend 26 CFR part 1 relating to section 45G of the Internal Revenue Code (Code). The temporary regulations contain rules for claiming the railroad track maintenance credit for qualified railroad track maintenance expenditures paid or incurred by a Class II or Class III railroad and other eligible taxpayers during the taxable year. The text of those temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations

and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they may be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for Tuesday, January 9, 2007, beginning at 10 a.m. in the auditorium of the New Carrollton Federal Building, 5000 Ellin Road, Lanham, MD 20706. Due to building security procedures, visitors must enter at the main front entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written or electronic comments and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by December 8, 2006. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Winston H. Douglas, Office of the Associate Chief Counsel (Passthroughs and Special Industries).

* * * * *

Proposed Amendments to the Regulations

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

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.45G–0 is added to read as follows:

§1.45G–0 Table of contents for the railroad track maintenance credit rules.

[The text of this proposed section is the same as the text of §1.45G–0T published elsewhere in this issue of the Bulletin].

Par. 3. Section 1.45G–1 is added to read as follows:

§1.45G–1 Railroad track maintenance credit.

[The text of this proposed section is the same as the text of §1.45G–1T published elsewhere in this issue of the Bulletin].

Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on September 7, 2006, 8:45 a.m., and published in the issue of the Federal Register for September 8, 2006, 71 F.R. 53052)

Guidance Under Section 7874 Regarding Expatriated Entities and Their Foreign Parents; Correction Notice

Announcement 2006–79

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing; correction.

SUMMARY: This document contains corrections to notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing (REG–112994–06, 2006–27 I.R.B. 47) that was published in the Federal Register on Tuesday, June 6, 2006 (71 FR 32495) relating to the determination of whether a foreign entity shall be treated as a surrogate foreign corporation under section 7874(a)(2)(B).

FOR FURTHER INFORMATION CONTACT: Milton Cahn at (202) 622–3918 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

The notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing (REG–112994–06) that is the subject of these corrections are under section 7874 of the Internal Revenue Code.

Need for Correction

As published, the notice of proposed rulemaking by cross-reference to temporary regulations and notice of public hearing (REG–112994–06) contains errors that may prove to be misleading and are in need of correction.

Correction of Publication

Accordingly, the notice of proposed rulemaking by cross reference to temporary regulations and notice of public hearing (REG–112994–06), that was the subject of FR Doc. E6–8698, is corrected as follows:

1. On page 32495, column 2, in the preamble, under the caption SUMMARY, line 8, the language "of the Code. The text of those'' is corrected to read "of the Internal Revenue Code. The text of those''.

2. On page 32495, column 2, in the preamble, under the caption DATES, lines 5 and 6, the language "24, 2006 at 10 a.m., must be received by October 3, 2006'' is corrected to read "31, 2006, at 10 a.m., must be received by October 10, 2006''.

3. On page 32495, column 2, in the preamble, under the caption ADDRESSES, lines 2–11, the language "CC:PA:LPD:PR (REG–112994–06), room 5203, Internal Revenue Service, PO Box 7604, Ben

Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG–112994–06), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC, or sent''. is corrected to read CC:PA:LPD (REG–112994–06), Internal Revenue Service, PO Box 7604 Ben Franklin Station, Washington, DC 20044 or sent''.

4. On page 32495, column 2, in the preamble, under the caption ADDRESSES, lines 1–3 from the bottom of the paragraph, the language, "held in the auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington DC'' is corrected to read "held in the auditorium, Internal Revenue Service, New Carrollton Federal Building (NCFB), 5000 Ellin Rd., Lanham, MD 20706''.

5. On page 32495, column 2, in the preamble, under the caption FOR FURTHER INFORMATION CONTACT, line 3, the language "Milton Cahn at (202) 622–3860;" is corrected to read "Milton Cahn at (202) 622–3860".

6. On page 32495, column 3, in the preamble, under the caption FOR FURTHER INFORMATION CONTACT, lines 2 and 3 from the top of the column, the language "Treena Garrett, (202) 622–7180 (not toll-free numbers)'' is corrected to read "Kelly Banks, (202) 622–0392 (not toll-free numbers)''.

7. On page 32495, column 3, in the preamble, under the paragraph heading "Background and Explanation of Provisions'', line 5 from the bottom of the paragraph, the language "7874(a)(2)(B) of the Code. The text of'' is corrected to read "7874(a)(2)(B) of the Internal Revenue Code. The text of''.

8. On page 32495, column 3, in the preamble, under the paragraph "Special Analyses'', line 5 from the bottom of the paragraph, the language "of the Code, this notice of proposed'' is corrected to read "of the Internal Revenue Code, this notice of proposed''.

9. On page 32496, column 1, in the preamble, under the paragraph heading "Comments and Public Hearing'', first paragraph of the column, lines 2 through 5, the language "for October 24, 2006, at 10 a.m. in the auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC.'' is corrected to read "for October 31, 2006, at 10 a.m. in the auditorium, Internal Revenue Service, New Carrollton Federal Building, 5000 Ellin Road, Lanham, MD 20706.''

10. On page 32496, column 1, in the preamble, under the paragraph heading "Comments and Public Hearing'', second paragraph of the column, lines 2 through 5, the language "for October 24, 2006, at 10 a.m. in the auditorium, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, DC. Due to building'' is corrected to read "for October 31, 2006, at 10 a.m. in the auditorium, Internal Revenue Service, New Carrollton Federal Building, 5000 Ellin Road, Lanham, MD 20706.''

Guy R. Traynor,
Chief, Publications and Regulations Branch, Legal Processing Division, Office of Associate Chief Counsel (Procedure and Administration).

(Filed by the Office of the Federal Register on August 15, 2006, 8:45 a.m., and published in the issue of the Federal Register for August 16, 2006, 71 F.R. 47158)

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.
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[1] A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2006–1 through 2006–26 is in Internal Revenue Bulletin 2006–26, dated June 26, 2006.

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