

HIGHLIGHTS OF THIS ISSUE

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

INCOME TAX

Rev. Rul. 2005-34, page 1098.

LIFO; price indexes; department stores. The March 2005 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, March 31, 2005.

Notice 2005-38, page 1100.

This document provides guidance under new section 965 of the Code generally concerning limitations described in sections 965(b)(1), (2), and (3) on the amount of dividends that a corporation that is a U.S. shareholder of a controlled foreign corporation (CFC) may treat as eligible for the dividends received deduction (DRD) under section 965(a), including the effects of certain corporate transactions on such limitations. In general, and subject to limitations and conditions, section 965(a) provides that a corporation that is a U.S. shareholder of a CFC may elect, for one taxable year, an 85 percent DRD with respect to certain cash dividends it receives from its CFCs. This document also addresses certain foreign tax credit and other consequences of elections under section 965. See also Notice 2005-10, 2005-6 I.R.B. 474, which primarily addresses requirements concerning domestic reinvestment plans described in section 965(b)(4). Notice 2005-10 modified.

Rev. Proc. 2005-30, page 1148.

This procedure extends the time for issuing authorities to make a carryforward election of unused private activity bond volume cap under section 146(f) of the Code, provided that the issuing authority meets the requirements of the revenue procedure.

Announcement 2005-39, page 1151.

This announcement provides supplemental information for the settlement initiative described in Announcement 2005-19 to resolve transactions that are the same as or substantially sim-

ilar to those described in Notice 2003-47. The transaction generally involved executives transferring compensatory stock options or restricted stock to a related person in exchange for a long-term, unsecured deferred payment obligation. It addresses (1) the penalty under the initiative for taxpayers with unexercised options or nonvested stock, (2) the application of section 6654 for a settlement of taxable year 2004, and (3) filing disclosure statements under regulations section 1.6011-4 for taxpayers that settle their transactions under the initiative. Taxpayers have until May 23, 2005, to notify the Service of their intent to participate in the settlement initiative.

EMPLOYMENT TAX

Announcement 2005-40, page 1152.

This document contains corrections to final and temporary regulations (T.D. 9196, 2005-19 I.R.B. 1000) that provide guidance for employers and employees relating to Form W-4, *Employee's Withholding Allowance Certificate*.

ADMINISTRATIVE

Rev. Proc. 2005-29, page 1118.

This procedure contains the latest revision of Publication 1516, *Specifications for Filing Form 8596, Electronically or Magnetically*.

Rev. Proc. 2005-30, page 1148.

This procedure extends the time for issuing authorities to make a carryforward election of unused private activity bond volume cap under section 146(f) of the Code, provided that the issuing authority meets the requirements of the revenue procedure.

Finding Lists begin on page ii.
Index for January through May begins on page vi.

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 146.—Volume Cap

What are the circumstances under which issuing authorities may obtain relief if they fail to make a timely carryforward election of unused private activity bond volume cap without requesting a private letter ruling? See Rev. Proc. 2005-30, page 1148.

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The March 2005 Bureau of Labor Statistics price indexes are accepted

for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, March 31, 2005.

Rev. Rul. 2005-34

The following Department Store Inventory Price Indexes for March 2005 were issued by the Bureau of Labor Statistics. The indexes are accepted by the Internal Revenue Service, under § 1.472-1(k) of the Income Tax Regulations and Rev. Proc. 86-46, 1986-2 C.B. 739, for ap-

propriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, March 31, 2005.

The Department Store Inventory Price Indexes are prepared on a national basis and include (a) 23 major groups of departments, (b) three special combinations of the major groups — soft goods, durable goods, and miscellaneous goods, and (c) a store total, which covers all departments, including some not listed separately, except for the following: candy, food, liquor, tobacco, and contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE
INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100, unless otherwise noted)

Groups	Mar 2004	Mar 2005	Percent Change from Mar 2004 to Mar 2005 ¹
1. Piece Goods	491.8	465.1	-5.4
2. Domestics and Draperies	537.6	536.8	-0.1
3. Women's and Children's Shoes	643.4	685.9	6.6
4. Men's Shoes	840.1	849.9	1.2
5. Infants' Wear	593.2	571.0	-3.7
6. Women's Underwear.....	493.6	547.7	11.0
7. Women's Hosiery	334.6	349.7	4.5
8. Women's and Girls' Accessories	561.7	607.0	8.1
9. Women's Outerwear and Girls' Wear	379.7	375.9	-1.0
10. Men's Clothing	539.2	564.8	4.7
11. Men's Furnishings.....	580.7	587.0	1.1
12. Boys' Clothing and Furnishings	451.9	445.9	-1.3
13. Jewelry.....	890.0	882.1	-0.9
14. Notions	798.5	777.7	-2.6
15. Toilet Articles and Drugs	982.7	991.4	0.9
16. Furniture and Bedding	620.3	604.2	-2.6
17. Floor Coverings.....	596.8	602.4	0.9
18. Housewares.....	714.4	712.2	-0.3
19. Major Appliances.....	205.2	205.0	-0.1
20. Radio and Television.....	43.1	39.5	-8.4
21. Recreation and Education ²	81.6	79.6	-2.5
22. Home Improvements ²	127.8	137.3	7.4
23. Automotive Accessories ²	112.3	114.4	1.9
Groups 1-15: Soft Goods	564.9	572.2	1.3
Groups 16-20: Durable Goods	387.2	381.1	-1.6
Groups 21-23: Misc. Goods ²	93.8	94.0	0.2
Store Total ³	501.0	504.0	0.6

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE
 INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
 (January 1941 = 100, unless otherwise noted)

Groups	Mar 2004	Mar 2005	Percent Change from Mar 2004 to Mar 2005 ¹
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¹Absence of a minus sign before the percentage change in this column signifies a price increase.

²Indexes on a January 1986 = 100 base.

³The store total index covers all departments, including some not listed separately, except for the following: candy, food, liquor, tobacco and contract departments.

DRAFTING INFORMATION

The principal author of this revenue ruling is Michael Burkom of the Office

of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue ruling, contact

Mr. Burkom at (202) 622-7924 (not a toll-free call).

Part III. Administrative, Procedural, and Miscellaneous

Section 965 — Limitations on Dividends Received Deduction and Other Guidance

Notice 2005-38

SECTION 1. OVERVIEW

This notice is the second in a series of items of published guidance regarding new section 965 of the Internal Revenue Code (Code). It supplements guidance previously set forth in Notice 2005-10, 2005-6 I.R.B. 474, which primarily addressed requirements regarding a domestic reinvestment plan described in section 965(b)(4). This notice primarily addresses the limitations, described in section 965(b)(1), (2), and (3), on the amount of dividends that a corporation that is a U.S. shareholder of a controlled foreign corporation may treat as eligible for the dividends received deduction under section 965(a) (DRD or section 965(a) DRD), including the effects of certain transactions on such limitations.

The Treasury Department and the Internal Revenue Service (IRS) intend to issue additional guidance concerning section 965 to address certain issues arising with respect to a U.S. corporation's computation of its tax liability, including the availability of foreign tax credits, when section 965 is applied. The Treasury Department and the IRS expect to issue regulations that incorporate the guidance provided in Notice 2005-10, this notice, and any subsequent guidance addressing section 965.

The remainder of this notice is divided into 14 sections. Section 2 provides background with respect to the issues addressed in this notice. Section 3 sets forth general principles that apply in determining the amount of cash dividends received by a U.S. shareholder that is considered extraordinary for purposes of section 965(b)(2). Section 4 sets forth general principles that apply in determining the maximum amount of dividends eligible under section 965(b)(1) to be taken into account under section 965(a). Section 5 addresses the taxable year to which sec-

tion 965 applies. Section 6 then addresses the effects of certain transactions on the determination of a U.S. shareholder's limitations determined under sections 3 and 4. Section 7 sets forth guidance and principles for determining under section 965(b)(3) the amount of related party indebtedness that reduces the amounts taken into account under section 965(a), including special adjustments made as a result of certain transactions. Section 8 provides guidance regarding the impact of certain transactions on domestic reinvestment plans. Section 9 addresses other issues arising under section 965, including the application of section 78, the expenses disallowed under section 965(d)(2), and the computation of the alternative minimum tax. Section 10 addresses reporting and other administrative requirements. Section 11 sets forth transition rules that apply to certain taxpayers that, prior to the issuance of this notice, either adopted a domestic reinvestment plan or filed a tax return for a taxable year to which section 965 applies. Section 12 describes the effect of this notice on other documents. Section 13 provides the effective date of this notice, and section 14 provides information required under the Paperwork Reduction Act of 1995. Finally, section 15 provides drafting information.

SECTION 2. BACKGROUND

.01 Section 965 — In General

The American Jobs Creation Act of 2004 (P.L. No. 108-357) (the Act), enacted on October 22, 2004, added new section 965 to the Code. In general, and subject to limitations discussed below, section 965(a) provides that a corporation that is a U.S. shareholder of a controlled foreign corporation (CFC) may elect, for one taxable year, an 85 percent DRD with respect to certain cash dividends it receives from its CFCs.

Section 951(b) defines the term "U.S. shareholder" with respect to any foreign corporation as a U.S. person who owns (within the meaning of section 958(a)), or is considered to own (under the construc-

tive ownership rules of section 958(b)), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation. Section 965(c)(5)(A) provides that all U.S. shareholders that are members of an affiliated group filing a consolidated return under section 1501 are treated as one U.S. shareholder. For purposes of this notice, the term "U.S. shareholder" means, unless otherwise indicated, a domestic corporation that, at any time after the beginning of the base period (defined below), is a U.S. shareholder (as defined in section 951(b)) with respect to a CFC and that owns (within the meaning of section 958(a)) stock of such CFC.

For purposes of section 965, the term "dividends" includes cash amounts included in gross income as dividends under sections 302 and 304, but does not include amounts treated as dividends under section 78 or 1248 or, in certain cases, section 367.¹ H.R. Conf. Rep. No. 108-755, at 314-15 (2004). Also for this purpose, a cash dividend includes a cash distribution from a CFC that is excluded from gross income under section 959(a) (regarding distributions of previously taxed income (PTI)) to the extent of inclusions under section 951(a)(1)(A) as a result of a cash dividend during the election year to: (1) such CFC from another CFC in a section 958(a) chain of ownership; or (2) any other CFC in such chain of ownership from another CFC in such chain of ownership, but only to the extent of cash distributions described in section 959(b) made during such year to the CFC from which such U.S. shareholder received such distribution.

Section 965(b) imposes four limitations on the section 965(a) DRD. These limitations are discussed in detail below in paragraphs .02 through .05 of this section.

Section 965(d) and (e) provide special rules that limit the use of foreign tax credits and the deduction of certain expenses to offset the nondeductible portion of section 965(a) dividends, respectively. See section 9.01 of this notice. These rules will be addressed in greater detail in a subsequent

¹ Dividends resulting from liquidations qualifying under section 332 to which section 367(b) applies qualify as cash dividends to the extent the U.S. shareholder actually receives cash as part of the liquidation. Section 965(c)(3). A deemed liquidation effectuated through an election under Treas. Reg. §301.7701-3(c), however, does not by itself result in an actual distribution of cash as required under section 965. See H.R. Conf. Rep. No. 108-755, at 315, n. 108 (2004).

notice that the Treasury Department and the IRS expect to issue soon.

Section 965(f) provides that taxpayers may elect the application of section 965 for either the taxpayer's last taxable year which begins before October 22, 2004, or the taxpayer's first taxable year which begins during the one-year period beginning on October 22, 2004. The election must be made on or before the taxpayer's due date (including extensions) for filing its Federal income tax return. See Notice 2005-10; see also H.R. Conf. Rep. No. 108-755, at 314, n. 107 (2004). The taxable year for which a taxpayer elects to apply section 965 will be referred to in this notice as the "election year."

.02 Extraordinary Dividends

Section 965(b)(2) provides that only those cash dividends (within the meaning of section 965(a)) received from CFCs during the U.S. shareholder's election year that are considered "extraordinary" are eligible for the section 965(a) DRD. Cash dividends received by the U.S. shareholder during the election year are considered extraordinary only to the extent such dividends exceed the annual average for the base period years of the following items reported on the U.S. shareholder's tax return as filed (including any amended returns that were filed on or before June 30, 2003): (1) dividends received during each base period year by such shareholder from CFCs²; (2) amounts includible in such shareholder's gross income for each base period year under section 951(a)(1)(B) (regarding investments in United States property under section 956) with respect to CFCs; and (3) amounts that would have been included for each base period year but for section 959(a) with respect to CFCs.³

The term "base period" in this notice means the five most recent taxable years of the U.S. shareholder that end on or before June 30, 2003. The term "base period inclusion" in this notice means any amount described in (1), (2), or (3) of the preceding paragraph, for any of the U.S. shareholder's taxable years in the base period. Under section 965(c)(2)(A), the term "base period years" generally in-

cludes only three taxable years in the U.S. shareholder's base period, determined by disregarding the years in the base period for which the base period inclusions are the highest and the lowest. However, if the taxpayer has fewer than five taxable years ending on or before June 30, 2003, then all taxable years ending on or before that date are considered base period years. The average of the U.S. shareholder's base period inclusions for its base period years is referred to in this notice as the "base period amount."

Section 965(c)(2)(C)(i) sets forth a general rule applicable to companies entering and exiting corporate groups, which provides that for purposes of determining the base period inclusions (and ultimately the base period amount), rules similar to the rules of section 41(f)(3)(A) and (B) apply. Section 41 generally provides for an incremental credit for qualified research activities, but only to the extent that current year research expenditures exceed the base amount for that year. For purposes of section 41, the base amount is computed by multiplying a measure of the taxpayer's qualified research expenses during a specified historical period by its average annual gross receipts for the four years immediately preceding the credit year. Section 41(f)(3)(A) and (B) generally provide that, as a result of certain acquisitions and dispositions, a taxpayer may increase or decrease the amount of its qualified research expenses and gross receipts to the extent that such amounts are attributable to the acquired or disposed of portion of a trade or business of the taxpayer.

In addition to the general references to section 41(f)(3)(A) and (B), section 965(c)(2)(C)(ii) provides a special rule for distributions during the base period of stock of a U.S. shareholder to which section 355 (or so much of section 356 that relates to section 355) applies. Under this special rule, the U.S. shareholder, the stock of which is distributed, is treated as having been in existence for the same period that the distributing corporation has been in existence. Further, the base period inclusions of the distributing and controlled corporations prior to the distribution are, in general, allocated between

such corporations on the basis of their respective interests in the CFCs giving rise to such inclusions immediately after such distribution. Section 965(c)(2)(C)(ii) also provides that this rule does not apply if neither the controlled corporation nor the distributing corporation is a U.S. shareholder of such CFCs immediately after the distribution.

.03 Maximum Amount Eligible for Section 965(a) — Greater of \$500 Million or Permanently Reinvested Earnings

Section 965(b)(1) limits the amount of dividends eligible for the section 965(a) DRD to the greatest of the following three amounts: (1) \$500 million (\$500 million limitation); (2) the amount shown on the taxpayer's applicable financial statement as earnings permanently reinvested outside the United States; or (3) in the case of an applicable financial statement that does not show a specific amount of earnings permanently reinvested outside the United States but that does show a specific amount of tax liability attributable to such earnings, the amount of such liability divided by 0.35. If the applicable financial statement does not show a specific earnings or tax liability amount, then the \$500 million limitation applies. The section 965(b)(1) amount shown on the taxpayer's applicable financial statement as earnings permanently reinvested outside the United States and the amount shown as a specific amount of tax liability attributable to such earnings divided by 0.35 is referred to in this notice as "APB 23 limitation."

Under section 965(c)(1), the term "applicable financial statement" means the most recently audited financial statement (including notes and other documents which accompany such statement) which is certified on or before June 30, 2003, as being prepared in accordance with generally accepted accounting principles, and which is used for the purposes of a statement or report to creditors or shareholders or for any other substantial nontax purpose. If the taxpayer is required to file with the Securities and Exchange Commission, the audited financial statement must be so filed on or before June 30,

² For this purpose, both cash and non-cash dividends received are taken into account. See section 965(b)(2)(B)(i).

³ For this purpose, distributions of PTI for any base period year do not include distributions excluded from gross income by reason of an amount described in section 965(b)(2)(B)(ii) (relating to investments in United States property) with respect to a prior taxable year.

2003, to qualify as an applicable financial statement. The legislative history states:

[APB 23 limitation] refers to elements of Accounting Principles Board Opinion 23 (“APB 23”), which provides an exception to the general rule of comprehensive recognition of deferred taxes for temporary book-tax differences. The exception is for temporary differences related to undistributed earnings of foreign subsidiaries and foreign corporate joint ventures that meet the indefinite reversal criterion in APB 23. H. R. Conf. Rep. No. 108–755, at 315, n. 111 (2004). The last day covered by the applicable financial statement is referred to in this notice as the “APB 23 determination date.”

Section 965(c)(5) provides special rules for applying section 965 to controlled groups of corporations. First, section 965(c)(5)(B) provides that all corporations treated as a single employer under section 52(a) (section 52(a) group) are limited to one \$500 million limitation, and the limitation must be divided among such corporations under regulations prescribed by the Secretary. A section 52(a) group includes all corporations that are members of a controlled group of corporations within the meaning of section 1563(a) substituting, however, “more than 50 percent” for “at least 80 percent” throughout section 1563(a)(1), and making the determination without regard to section 1563(a)(4) and (e)(3)(C). Second, section 965(c)(5)(C) provides that if a financial statement is an applicable financial statement for more than one U.S. shareholder, APB 23 limitation is divided among such shareholders under regulations prescribed by the Secretary.

.04 Increase in Related Party Indebtedness

Section 965(b)(3) provides that the amount of a U.S. shareholder’s dividends otherwise eligible for the deduction under section 965(a) are reduced by any increase in the indebtedness of the CFC to any related person (as defined in section 954(d)(3)) between October 3, 2004, and the close of the taxable year for which the election under section 965 is in effect.

For this purpose, all CFCs with respect to which the taxpayer is a U.S. shareholder are treated as a single CFC and, therefore, indebtedness between CFCs is disregarded for this purpose. See H.R. Conf. Rep. No. 108–755, at 314, n. 109 (2004). Section 965(b)(3) is intended to prevent a deduction from being claimed with respect to a section 965 dividend where the dividend is financed, directly or indirectly, by the U.S. shareholder. In such a case, there may be no net repatriation of funds, and thus it is inappropriate to allow a deduction under section 965(a). H.R. Conf. Rep. No. 108–755, at 315 (2004).

.05 Investment in the United States Pursuant to a Domestic Reinvestment Plan

Section 965(b)(4) requires a U.S. shareholder claiming a section 965(a) DRD with respect to a dividend to invest the amount of the dividend in the United States pursuant to a domestic reinvestment plan. The domestic reinvestment plan must be approved by the taxpayer’s president, chief executive officer, or comparable official before the payment of the dividend and subsequently approved by the taxpayer’s board of directors, management committee, executive committee, or similar body. The domestic reinvestment plan must provide for the investment of the dividend in the United States (other than as a payment for executive compensation), including as a source for the funding of worker hiring and training, infrastructure, research and development, capital investments, or the financial stabilization of the corporation for the purposes of job retention or creation. This list is not intended to be exclusive. H.R. Conf. Rep. No. 108–755, at 316 (2004). For additional guidance with respect to domestic reinvestment plans, see sections 8 and 9 of this notice and Notice 2005–10.

SECTION 3. BASE PERIOD AMOUNT — GENERAL PRINCIPLES

.01 Determination of Base Period Amount

(a) *In general.* A U.S. shareholder determines its base period inclusions and its

base period amount by applying the rules of section 965(b)(2)(B) and (c)(2) with respect to CFCs for which it was a U.S. shareholder at any time during its base period.

(b) *Consolidated groups.* A consolidated group⁴ determines its base period inclusions by first aggregating the base period inclusions of each of the members in its group. It then determines its base period amount by determining the average of such inclusions as provided under section 965(b)(2)(B) and (c)(2).

(c) *Short taxable years.* Taxable years of fewer than 12 months are taken into account as taxable years for purposes of determining the base period years pursuant to section 965(c)(2). In addition, base period inclusions in a taxable year of fewer than 12 months are not annualized or otherwise adjusted for purposes of calculating the base period amount.

(d) *Intermediary pass-through entities.* The Treasury Department and the IRS expect to issue guidance soon on the treatment of distributions to intermediary pass-through entities owned by U.S. shareholders for purposes of section 965(b)(2)(B)(i).

(e) *Example.* The following example illustrates the application of section 965(b)(2) and this section 3.01.

Example. (i) *Facts.* USP is the common parent of a consolidated group that includes USP’s wholly owned subsidiaries US1 and US2. US1 and US2 each wholly owns a foreign corporation, CFC1 and CFC2, respectively. The USP consolidated group maintains a taxable year ending July 31. US1 received a \$100x dividend from CFC1 in each of the consolidated taxable years ending July 31, 1996, 1997, and 1998. US2 received a dividend from CFC2 during each of the consolidated taxable years ending July 31, 1998, 1999, 2000, 2001, 2002, and 2003 in the amount of \$150x, \$150x, \$200x, \$100x, \$50x, and \$100x, respectively.

(ii) *Result.* USP first determines the base period inclusions of US1 and US2 to determine the consolidated group’s base period inclusions. Pursuant to section 965(c)(2), the base period includes the five most recent taxable years of the USP group that ended on or before June 30, 2003, which are the group’s taxable years ending July 31, 1998 (year 1) through July 31, 2002 (year 5). Accordingly, USP will have base period inclusions as follows:

⁴ The terms “consolidated group,” “member,” “subsidiary,” and “separate return year” are defined in Treas. Reg. §1.1502–1. In addition, the term “member” also refers, when the context so requires, to a member of a section 52(a) group.

Taxable year ending

July 31, 1998
July 31, 1999
July 31, 2000
July 31, 2001
July 31, 2002

USP group base period inclusions

\$250x
\$150x
\$200x
\$100x
\$50x

To determine its base period years pursuant to section 965(c)(2), USP disregards the taxable years in its base period with the highest and lowest base period inclusions, which are 1998 (\$250x) and 2002 (\$50x). To determine its base period amount, USP then averages the base period inclusions for the remaining three taxable years (that is, the base period years). Therefore, USP's base period amount is \$150x $((\$150x + \$200x + 100x)/3)$.

.02 Translation of Previously Taxed Income Distributed During the Base Period

For purposes of determining the dollar amount of base period inclusions attributable to distributions of PTI described in section 965(b)(2)(B)(iii), distributions of foreign currency are valued by multiplying the distributing CFC's foreign currency amount of the PTI distribution by the spot rate (as defined in Treas. Reg. §1.988-1(d)(1)) on the date of distribution.

SECTION 4. MAXIMUM AMOUNT ELIGIBLE FOR SECTION 965(a) — GENERAL PRINCIPLES

.01 Applicable Financial Statement

As noted above, the amount of dividends eligible for the section 965(a) DRD may be limited by section 965(b)(1)(B) or (C) to either: (1) the amount shown on the taxpayer's applicable financial statement as earnings permanently reinvested outside the United States; or (2) in the case of an applicable financial statement that does not show a specific amount of earnings permanently reinvested outside the United States but that does show a specific amount of tax liability attributable to such earnings, the amount of such liability divided by 0.35. Also as noted above, the term "applicable financial statement" means the most recently audited financial statement (including notes and other documents which accompany such statement) which is certified on or before June 30, 2003, as being prepared in accordance with generally accepted accounting principles, and which is used for the purposes of a

statement or report to creditors or shareholders or for any other substantial non-tax purpose. For purposes of determining an amount shown on a taxpayer's applicable financial statement pursuant to section 965(b)(1)(B) or (C), the parenthetical reference to notes and other documents accompanying the statement only includes notes and documents that form an integral part of the financial statement; it does not include work papers or other materials underlying or supporting the statement.

.02 Determination of APB 23 Limitation of a U.S. Shareholder

For purposes of section 965(b)(1)(B) and (C), the specific amount shown on the applicable financial statement that reflects the amount determined under paragraph 12 of APB 23 (or, in the case of section 965(b)(1)(C), a specific amount of tax liability) and that is disclosed as required under Financial Accounting Standards Board Statement 109, is treated as an amount of earnings permanently reinvested outside the United States (or, the amount of tax liability attributable to such earnings), regardless of the specific language used to describe such specific amount on the applicable financial statement.

.03 Amount of Tax Liability Attributable to Earnings Permanently Reinvested

If an applicable financial statement fails to show a specific amount of earnings permanently reinvested outside the United States, but instead shows a specific amount of tax liability attributable to such earnings, the APB 23 limitation under section 965(b)(1)(C) is the specific amount of such tax liability divided by 0.35. This amount may not be adjusted (for example, to take into account the foreign taxes imposed on such earnings).

The following example illustrates the application of section 965(b)(1)(C) and this section 4.03.

Example. (i) *Facts.* A CFC has earnings permanently reinvested outside the United States that have

been subject to foreign tax of \$10x. The applicable financial statement of the U.S. shareholder that wholly owns such CFC does not show a specific amount of earnings permanently reinvested outside the United States, but instead shows a \$25x tax liability attributable to such earnings.

(ii) *Result.* Although the applicable financial statement of the U.S. shareholder does not show an amount of permanently reinvested earnings, it does show a tax liability of \$25x attributable to earnings permanently reinvested. Thus, the amount described in section 965(b)(1)(C) is \$71.4x $(\$25x/0.35)$. This amount may not be adjusted to take into account the foreign taxes imposed on such earnings.

.04 Allocation of APB 23 Limitation

As noted above, section 965(c)(5)(C) provides that if a financial statement is an applicable financial statement for more than one U.S. shareholder, APB 23 limitation is divided among such shareholders under regulations prescribed by the Secretary. In such a case, the portion of the APB 23 limitation allocated to the U.S. shareholder is the amount from the separate company financial statements (or supporting work papers) of such U.S. shareholder that were prepared in connection with determining the amount described in section 965(b)(1)(B) or (C) shown on the applicable financial statement that included such U.S. shareholder.

Section 965(c)(5)(C) contemplates not only the situation where the financial statement reflects the operations of affiliated corporations that are not consolidated for tax purposes (for example, a U.S. corporation and a domestic subsidiary thereof that elects to apply section 936), but also the situation where the financial statement reflects the operations of corporations that were formerly affiliated and/or consolidated but are not in such relationship during a section 965 election year. See section 6 of this notice for rules regarding the allocation of APB 23 limitation in such a case.

The following example illustrates the application of section 965(b)(1) and this section 4.04.

Example. (i) *Facts.* USP is a domestic corporation that files a consolidated return with its

wholly-owned subsidiaries US1 and US2. USP also wholly owns US3, which does not join in the USP consolidated return because an election under section 936 is in effect with respect to US3. US1, US2 and US3 each wholly owns a foreign corporation, CFC1, CFC2, and CFC3, respectively. Even though US3 is not part of the USP consolidated group for U.S. tax purposes, US3 is consolidated with USP, US1, and US2 for financial accounting purposes. On USP's applicable financial statement, USP reported \$350x of earnings permanently reinvested outside the United States. The separate company financial statements of US1, US2, and US3 that were used in preparing the USP applicable financial statement reported earnings permanently reinvested by CFC1, CFC2, and CFC3 to be \$100x, \$50x and \$200x, respectively.

(ii) *Result.* The portion of the USP APB 23 limitation allocated to US1, US2, and US3 is that portion reflected on the separate company financial statements (or supporting work papers) of US1, US2, and US3 that were used in determining the USP APB 23 limitation on its applicable financial statement. Thus, US1 is allocated \$100x, US2 is allocated \$50x, and US3 is allocated \$200x of the \$350x APB 23 limitation. Because US1 and US2 are members of the USP consolidated group and such group is treated as one U.S. shareholder, the USP consolidated group's APB 23 limitation equals \$150x (\$50x + \$100x).

.05 Allocation of \$500 Million Limitation

As noted above, section 965(c)(5)(B) provides that all corporations which are included in a section 52(a) group are limited to one \$500 million limitation, which is divided among such corporations under regulations prescribed by the Secretary. Each qualified member of a section 52(a) group is allocated a portion of the section 52(a) group's single \$500 million limitation if it is a qualified member on the last day of the election year of the qualified member with the last election year to end (apportionment date). A "qualified member" is either: (1) a domestic corporation that files a separate tax return and is a member of a section 52(a) group; or (2) a consolidated group that is part of a section 52(a) group. Accordingly, if a consolidated group is not a part of a section 52(a) group, it has its own \$500 million limitation, and, if a consolidated group is part of a section 52(a) group, the portion of the \$500 million allocated to the consolidated group is not further allocated between and among the members of the consolidated group.

The section 52(a) group's single \$500 million limitation is allocated to all qualified members in proportion to the aggregate amount of total current and accumulated earnings and profits that are not previously taxed (non-PTI earnings

and profits) of all CFCs owned (within the meaning of section 958(a)) by such qualified members. For purposes of this rule, a consolidated group is treated as owning CFCs within the meaning of section 958(a), if any member of the group owns CFCs within the meaning of section 958(a). The amount of non-PTI earnings and profits of a CFC owned (within the meaning of section 958(a)) by a qualified member is the sum of the amounts of earnings and profits of such CFC appropriately reported on Schedule J, items 7(a) and 7(b), of the last Form 5471 filed by or on behalf of such qualified member on or before the apportionment date with respect to such CFC, translated into U.S. dollars at the average exchange rate for the CFC's taxable year (see section 989(b)(3)).

The following example illustrates the application of section 965(b)(1) and the rules of this section 4.05.

Example. (i) *Facts.* FP, a foreign corporation, wholly owns two domestic corporations, US1 and US2. US1 and US2 each wholly owns a foreign corporation, CFC1 and CFC2, respectively. US1 and US2 each has a taxable year ending July 31, and they each make an election under section 965 for the taxable year ending July 31, 2006. US1 and US2 have APB 23 limitations of zero. On US1's last Form 5471 filed on or before the July 31, 2006 apportionment date with respect to CFC1, US1 reported an amount of non-PTI earnings and profits for CFC1, translated into U.S. dollars using the average exchange rate, of \$100x. On US2's last Form 5471 filed on or before the July 31, 2006 apportionment date with respect to CFC2, US2 reported an amount of non-PTI earnings and profits for CFC2, translated into U.S. dollars using the average exchange rate, of \$300x.

(ii) *Result.* US1 and US2 do not have an APB 23 limitation and, thus, their maximum amount eligible for the section 965(a) DRD is \$500 million. Because US1 and US2 are members of the same section 52(a) group, they are limited to one \$500 million limitation, which is allocated between them. Pursuant to this section 4.05, the \$500 million limitation is allocated in proportion to the aggregate U.S. dollar amount of non-PTI earnings and profits reported on the last Form 5471 filed on or before the apportionment date by US1 and US2 with respect to CFC1 and CFC2, respectively. The apportionment date for the FP group is July 31, 2006. Consequently, US1 is allocated \$125 million of the \$500 million limitation ($\$100x/\$400x \times \$500$ million) and US2 is allocated \$375 million of the \$500 million limitation ($\$300x/\$400x \times \$500$ million).

SECTION 5. TAXABLE YEAR TO WHICH SECTION 965 APPLIES

.01 In General

Section 965(f) provides that a taxpayer may elect to apply section 965 to either the

taxpayer's last taxable year beginning before October 22, 2004, or the taxpayer's first taxable year starting during the one-year period beginning on October 22, 2004 (eligible year). Thus, assuming that the other requirements of section 965 are met, a taxpayer may elect to apply the section 965(a) DRD with respect to cash dividends (as defined for purposes of section 965(a)) received by a U.S. shareholder from its CFCs in an eligible year. Except as otherwise provided in this section 5, an eligible year may include a short taxable year.

.02 Consolidated Groups

For taxpayers that are members of a consolidated group, the common parent may elect on behalf of all the members to apply section 965 to one of the group's eligible years. The election applies to each member of the group that is included in the group's income tax return for that eligible year, but only for the portion of the eligible year during which such member is a member of the group. Further, every member can receive a cash dividend from a CFC that otherwise qualifies under section 965(a) during any period the recipient is a member of such group. This rule applies even if: (1) as a result of a subsidiary entering or leaving the group, the group's election year is, with respect to the particular subsidiary, neither the taxable year that includes October 22, 2004, nor the subsequent taxable year; or (2) a previous separate return year of the subsidiary also was an election year for the subsidiary. This rule also applies as a result of the acquisition of a consolidated group by an unrelated consolidated group, where the previous separate return year of the acquired group was an election year.

Under the rules of the preceding paragraph, if a subsidiary leaves the group during the group's election year, cash dividends received from the subsidiary's CFCs during its short taxable year that ends within the group's election year are eligible for the group's election. As a result, dividends received by the subsidiary during that initial short taxable year can be eligible for the section 965(a) DRD. Moreover, dividends received by the subsidiary during its next short taxable year as part of an acquiring group may also be eligible for the section 965(a) DRD.

In addition, if the departing subsidiary is not immediately thereafter a subsidiary member of another group, it may treat its next short taxable year as an eligible year and make an election under section 965 for that year, even if that next taxable year is neither the taxable year for that subsidiary that includes October 22, 2004, nor the subsequent taxable year, provided that the two short taxable years together do not exceed twelve months (or an equivalent 52–53 week year).

General consolidated return principles apply to reverse acquisitions as defined in Treas. Reg. §1.1502–75(d)(3), so that the taxable year of the continuing group governs its available eligible years and the terminating group members are subject to the general rules for members leaving and entering groups, with the common parent in effect treated as having become a subsidiary of the continuing group.

.03 Examples

The following examples illustrate the application of the rules of section 965(f) and this section 5.

Example 1. Member included in election year of different consolidated groups. (i) *Facts.* USP is the common parent of a calendar year consolidated group that elects to apply section 965 for its taxable year ending December 31, 2004. US1 is a member of the USP group and a U.S. shareholder. USB is the common parent of an unrelated consolidated group that elects to apply section 965 to its taxable year ending June 30, 2005. A member of the USB group acquires all the stock of US1 on November 15, 2004.

(ii) *Result.* Because US1 is included in the USP group during the USP group's section 965 election year (January 1, 2004, through December 31, 2004), US1's taxable year beginning January 1, 2004, and ending on November 15, 2004 is an election year during which cash dividends received from US1's CFCs may be eligible for the section 965(a) DRD. In addition, because US1 is included in the USB group during the USB group's election year (July 1, 2004 through June 30, 2005), cash dividends from US1's CFCs during US1's taxable year beginning on November 16, 2004 and ending June 30, 2005, may be eligible for the section 965(a) DRD of the USB group.

(iii) *Alternative facts.* If USB instead makes an election under section 965 for its taxable year ending June 30, 2006, cash dividends from US1's CFCs during the USB group's election year may still be eligible for the section 965(a) DRD. In this case, however, that election year is US1's taxable year from July 1, 2005, through June 30, 2006. Section 965 will not apply to US1's year beginning November 16, 2004, and ending June 30, 2005.

Example 2. Special rule for member departing but not joining a consolidated group. (i) *Facts.* Assume the same facts as in *Example 1*, except instead

of being acquired by an unrelated consolidated group, the stock of US1 is distributed to the shareholders of USP on November 15, 2004, and US1 becomes the common parent of a new consolidated group which also maintains a taxable year ending December 31.

(ii) *Result.* Because the taxable year ending December 31, 2004, is the USP group's election year, US1's taxable year beginning January 1, 2004, and ending on November 15, 2004, is an election year during which cash dividends received from US1's CFCs may be eligible for the section 965(a) DRD. Further, because US1 ceased to be a member of the USP group during its election year and did not become a subsidiary member of another consolidated group, US1 may make an election under section 965 for the subsequent short taxable year, which begins on November 16, 2004, and ends on December 31, 2004. This election will also apply to the other members of the US1 group during that short taxable year. US1 will not be able to make an election under section 965 for 2005.

Example 3. Acquisition of target resulting in single short election year. (i) *Facts.* USP is the common parent of a calendar year consolidated group that elects to apply section 965 for its taxable year ending December 31, 2004. US1 is a member of the USP group and a U.S. shareholder. On November 15, 2004, the stock of US1 is distributed to the shareholders of USP; after such distribution, US1 is not a member of a consolidated group and therefore files a separate return. USB is the common parent of an unrelated consolidated group that plans to apply section 965 to its taxable year ending December 31, 2005. On December 15, 2005, US1 purchases all the stock of USB for cash. US1 and its subsidiaries elect to file a consolidated return for the taxable year ending December 31, 2005.

(ii) *Result.* Because the taxable year ending December 31, 2004, is the USP group's election year, US1's taxable year beginning January 1, 2004, and ending on November 15, 2004, is an election year during which cash dividends received from US1's CFCs may be eligible for the section 965(a) DRD. Further, because US1 ceased to be a member of the USP group during its election year and did not become a subsidiary member of another consolidated group, US1 may make an election under section 965 for its short taxable year that begins on November 16, 2004, and ends on December 31, 2004. However, 2005 is not an eligible year for US1 or its consolidated group. The USB group's final taxable year ends on December 15, 2005, when it is acquired by US1. That short taxable year is an eligible year for which the USB group may make an election under section 965. Thereafter, the members of the former USB group will become members of the US1 group. Because the USB group was acquired after the US1 election year, the former USB group members may not participate in an election under section 965 for any period after December 15, 2005.

Example 4. Effect of reverse acquisition. (i) *Facts.* Assume the same facts as in *Example 3*, except that US1's acquisition of USB is for US1 stock rather than cash and the acquisition is a reverse acquisition described in Treas. Reg. §1.1502–75(d)(3).

(ii) *Result.* Under Treas. Reg. §1.1502–75(d)(3)(i), the USB group is treated as continuing to exist after the reverse acquisition with US1 as its common parent. The USB group's taxable year end-

ing December 31, 2005, is an eligible year for which the group may make an election under section 965. This election applies to cash dividends received by US1 after the acquisition when US1 was in the USB consolidated group (the period beginning December 16, 2005, and ending December 31, 2005), as well as to dividends received by the USB group members during the calendar year while USB was the common parent. As in *Example 3*, US1's short taxable year that begins on November 16, 2004 and ending on December 31, 2004, is an eligible year. However, US1's taxable year beginning January 1, 2005, and ending December 15, 2005, is not an eligible year for US1.

Example 5. Consolidated group included in election year of different consolidated groups. (i) *Facts.* Assume the same facts as in *Example 1* (i), except that a member of the USB group acquires the USP group on November 15, 2004, and the USP group makes an election under section 965(a) for the taxable year January 1, 2004 through November 15, 2004.

(ii) *Result.* Because the USP group's election year is January 1, 2004 through November 15, 2004, USP's taxable year beginning January 1, 2004, and ending on November 15, 2004, is an election year during which cash dividends received from the USP group's CFCs may be eligible for the section 965(a) DRD. In addition, because USP is included in the USB group during the USB group's election year (July 1, 2004 through June 30, 2005), cash dividends from the USP group's CFCs during USP's taxable year beginning on November 16, 2004 and ending June 30, 2005 may be eligible for the section 965(a) DRD of the USB group. If, in the alternative, USB elects to apply section 965 to its taxable year ending June 30, 2006, cash dividends from the USP consolidated group's CFCs during USP's taxable year beginning July 1, 2005, and ending June 30, 2006, may be eligible for the section 965 DRD of the USB consolidated group.

SECTION 6. EFFECTS OF CERTAIN TRANSACTIONS ON BASE PERIOD INCLUSIONS AND MAXIMUM AMOUNT ELIGIBLE FOR SECTION 965(a) DRD

.01 Base Period Inclusions and APB 23 Limitation as U.S. Shareholder Attributes

(a) *In general.* For purposes of section 965, base period inclusions and APB 23 limitation are historical amounts that are treated as tax attributes particular to a U.S. shareholder as of the date these amounts are fixed under section 965(b)(1) and (2). See section 2.01 of this notice for the definition of the term "U.S. shareholder" for this purpose. Consequently, base period inclusions and APB 23 limitation remain with a particular U.S. shareholder (for example, when a U.S. shareholder ceases to be a member of a consolidated group). See *Example 1* of section 6.01(d) of this notice. In addition, base period inclusions

and APB 23 limitation are treated in the same manner as items described in section 381(c). Therefore, if a corporation acquires the assets of a U.S. shareholder in a transaction described in section 381(a), the acquiring corporation succeeds to and takes into account the base period inclusions and APB 23 limitation of the transferor U.S. shareholder under the principles of section 381. See *Example 5* of section 6.01(d) of this notice. For exceptions to these general rules, see section 6.01(b) and (c) of this notice.

Because these amounts are not treated as tax attributes particular to a CFC, they are unaffected by a disposition of a CFC. Thus, these rules apply even if the U.S. shareholder no longer owns the CFC that gave rise to the base period inclusions or APB 23 limitation. Similarly, because these amounts are tax attributes of the U.S. shareholder rather than the CFC, a domestic corporation that acquires the assets of a CFC in a transaction described in section 381(a) does not succeed to and take into account base period inclusions and APB 23 limitation attributable to the transferor CFC under the principles of section 381. See *Example 1* of section 6.01(d) of this notice.

(b) *Adjustments for acquisitions and dispositions of U.S. shareholders that are included in consolidated returns.* (1) *In general.* Members of a consolidated group generally are treated as a single U.S. shareholder for the purpose of determining the group's base period amount or APB 23 limitation. However, when a member exits or enters a U.S. consolidated group, adjustments are required to the selling⁵ and/or acquiring group's base period inclusions and APB 23 limitation to reflect that base period inclusions and APB 23 limitation generally remain with a particular U.S. shareholder (that is, with the specific member rather than with the group itself). The selling group reduces its base period inclusions and APB 23 limitation by the amounts that are attributable to a departed member, and the acquiring group correspondingly increases its base period inclusions and APB 23 limitation to account for the new member. For exceptions to these general rules, see paragraph

(2), below, and *Examples 1, 4, 8 and 9* of section 6.01(d) of this notice. For specific rules addressing the determination of base period inclusions, see section 6.01(b)(3) of this notice.

When adjusting a consolidated group's base period inclusions to reflect the entry or exit of a U.S. shareholder, the consolidated group makes the adjustment to the specific base period inclusions (as opposed to the base period amount) for the group to reflect the particular base period inclusions of the acquired or disposed of U.S. shareholder or its successor. In the same way, the consolidated group makes an adjustment to its APB 23 limitation to reflect the APB 23 limitation attributable to the acquired or disposed of U.S. shareholder or its successor.

The rules of this paragraph that apply to dispositions or acquisitions of a member of a consolidated group also apply, as relevant, in the context of the acquisition of an entire consolidated group.

(2) *Special adjustment rules dependent upon timing of certain acquisitions or dispositions of U.S. shareholders.* Certain adjustments to base period inclusions and/or APB 23 limitation provided under paragraph (b)(1) of this section are not made if certain transactions occur during the selling group's election year, or certain transactions occur before or after a selling group's or acquiring group's⁶ APB 23 determination date. In addition, special rules are provided in section 6.01(c) of this notice with respect to certain spin-off transactions.

Specifically, under this paragraph (b)(2), when a U.S. shareholder ceases to be a member of a selling group during the selling group's election year, the selling group's base period inclusions and APB 23 limitation are not reduced by amounts attributable to the departing U.S. shareholder. Nonetheless, the acquiring group still increases its base period inclusions and, subject to the special rules of this paragraph (b)(2), its APB 23 limitation attributable to the acquired U.S. shareholder under the general rules of paragraph (b)(1) of this section. See *Example 1* of section 6.01(d) of this notice. In addition, dividends received by the U.S. shareholder

from its CFCs in any other election year may be taken into account in that year for purposes of section 965. See also section 5 of this notice for a discussion of taxable years to which section 965 applies.

This paragraph provides special rules to ensure that an acquiring consolidated group appropriately reflects an APB 23 limitation with respect to an acquired member when: (1) that member ceases to be a member of a selling consolidated group before the selling group's APB 23 determination date; and/or (2) that member joins an acquiring group before the acquiring group's APB 23 determination date. Specifically, if a U.S. shareholder joins a consolidated group before the acquiring group's APB 23 determination date, there is no adjustment to the acquiring group's APB 23 limitation because the U.S. shareholder's membership in the new group (and such U.S. shareholder's ownership of CFCs at the relevant time with permanently reinvested earnings) will be taken into account when determining the acquiring group's APB 23 limitation. Under the preceding sentence, if the selling group's APB 23 determination date has passed, the selling group reduces its APB 23 limitation to account for the departed U.S. shareholder. If a U.S. shareholder ceases to be a member of a consolidated group before the selling group's APB 23 determination date, there is no downward adjustment to the selling group's APB 23 limitation to reflect the departure because the selling group's APB 23 limitation will reflect such disposition. However, if a U.S. shareholder ceases to be a member of a consolidated group before the selling group's APB 23 determination date but after the acquiring group's APB 23 determination date, the acquiring group's APB 23 limitation is increased by the amount of the selling group's APB 23 limitation that would be allocated to the acquired U.S. shareholder under section 4 of this notice if the selling group substituted "the date of the acquisition" for "June 30, 2003" in applying section 965(c)(1).

The rules of this paragraph that apply to dispositions or acquisitions of a member of a consolidated group also apply, as

⁵ For purposes of this section 6, the term "selling group" also includes a group in which a U.S. shareholder ceases to be included as a member as a result of transactions other than sales (for example, through the distribution of the stock of the member).

⁶ For purposes of section 6, the term "acquiring group" includes a consolidated group that comes into existence after the acquisition of a corporation.

relevant, in the context of the acquisition of an entire consolidated group.

(3) *Determining the base period inclusions to be inherited.* When an acquiring group adjusts its base period inclusions to take into account an acquisition of a U.S. shareholder or consolidated group, the acquiring group takes into account five taxable years in the relevant base period for any acquired shareholder or group, assuming at least five taxable years are available. The inclusions are aggregated for taxable years one through five without regard to whether they are short or full taxable years on either side. An acquired U.S. shareholder or group cannot contribute more than five taxable years of inclusions to the base period history of the acquirer. The fifth taxable year in the acquiring group's base period is the last potential taxable year in its base period.

If the acquired U.S. shareholder or group joins the acquiring group after the end of the acquiring group's base period, the acquired U.S. shareholder's or acquired group's base period inclusions in its last five taxable years ending on or before June 30, 2003, are aggregated with the acquiring group's base period inclusions in its five base period taxable years, on a year-by-year basis.

Similarly, if an acquired U.S. shareholder or group joins the acquiring group before the end of the acquiring group's base period, the acquiring group inherits a base period inclusion history for the acquired U.S. shareholder or group for each of the taxable years in the acquiring group's base period that end on or before the date of the acquisition. The acquired U.S. shareholder's or acquired group's taxable year ending on the date of the acquisition shall correspond to the taxable year in the acquiring group's base period that ends on or before the date of the acquisition. The acquiring group then takes into account base period inclusions from the acquired U.S. shareholder's or group's taxable years prior to the taxable year ending with the date of the acquisition to the extent necessary to assemble a base period inclusion history for the inherited years. An acquired U.S. shareholder or acquired group may contribute five taxable years to the acquiring group's history even if the acquiring group did not itself exist for its full five taxable year base period. For

illustrations of these rules, see *Example 7* and *Example 8* of section 6.01(d).

(c) *Special rules for spin-offs.* (1) *In general.* Except as provided in paragraphs (c)(2) and (3) of this section, a distribution to which section 355 (or so much of section 356 as relates to section 355) applies is treated in the same manner as a disposition of the stock of the controlled corporation (controlled) by the distributing corporation (distributing) for purposes of section 965 and this notice. See sections 5, 6.01(a) and (b) of this notice and *Example 2* of section 6.01(d) of this notice.

(2) *Spin-off of a U.S. shareholder that occurs during the base period — allocation of base period inclusions.* In the case of a spin-off of the stock of a U.S. shareholder to which section 355 (or so much of section 356 that relates to section 355) applies that occurs during the base period, and after which either distributing or controlled is a U.S. shareholder of a CFC (applicable base period spin-off), any base period inclusions received by either distributing or controlled from such CFC are allocated as provided in section 965(c)(2)(C)(ii). For purposes of determining distributing's and controlled's base period inclusions and base period amounts under section 965(c)(2)(C)(ii), section 965(c)(2)(C)(ii)(I) treats controlled as having been in existence for the same period that distributing has been in existence. Further, section 965(c)(2)(C)(ii)(II) allocates base period inclusions that are received or includible by distributing and controlled from a CFC prior to an applicable base period spin-off of controlled based on the fair market values of distributing's and controlled's interests in such CFC immediately after such spin-off.

However, if stock of a member of a consolidated group is distributed pursuant to an applicable base period spin-off and, as a result of such distribution a controlled corporation leaves the consolidated group, the base period inclusions of the consolidated group with respect to each of the group's CFCs before the applicable base period spin-off are instead allocated between the members of the consolidated group that remain in the distributing corporation's group (distributing group) and the members, if any, that leave the group and thereafter file a consolidated return with the controlled corporation (controlled group) in proportion to the fair market

values of the distributing group's and the controlled group's respective interests in each CFC owned by the distributing group and the controlled group immediately after the applicable base period spin-off. The base period inclusions allocated to the distributing group and the controlled group are further allocated amongst the members of such groups in proportion to the fair market value of such members' respective interests in each CFC immediately after the applicable base period spin-off. See paragraph (c)(3) for the treatment of APB 23 limitations as a result of applicable base period spin-offs described in this paragraph (c)(2).

Section 965(c)(2)(C)(ii)(II) does not apply to any distribution that is not an applicable base period spin-off, such as a distribution that occurs after the base period; nor does it apply to allocate inclusions from CFCs with respect to which neither controlled nor distributing is a U.S. shareholder at the time of the spin-off. Instead, the rules of section 6.01(c)(1) of this notice apply to such distributions or inclusions.

(3) *Spin-off of a U.S. shareholder that occurs during the base period — allocation of APB 23 limitation.* If an applicable base period spin-off (as defined in paragraph (c)(2) of this section) occurs with respect to a U.S. shareholder that is not a member of a consolidated group after the APB 23 determination date of either distributing or controlled, the APB 23 limitation of distributing or controlled is adjusted to the extent that distributing's or controlled's APB 23 limitation is attributable to the stock of a CFC that is transferred between distributing and controlled in connection with the spin-off. Consistent with the treatment of base period inclusions, such adjustment is made by allocating the portion of any APB 23 limitation attributable to distributing or controlled with respect to the earnings of a CFC that is transferred between distributing and controlled in proportion to the fair market values of such corporations' respective interests as U.S. shareholders of such CFC immediately after the spin-off. If a spin-off occurs before the APB 23 determination dates of both distributing and controlled, the general rules of section 4 apply. See *Example 3* of section 6.01(d) of this notice.

If the stock of a member of a consolidated group is distributed pursuant to an applicable base period spin-off and, as a result of such distribution a controlled corporation leaves the consolidated group and, the spin-off occurs after the APB 23 determination date of the consolidated group, the APB 23 limitation that is attributable to each CFC owned by the consolidated group before the applicable base period spin-off is, instead, allocated between the distributing group and the controlled group in proportion to the fair market values of the distributing group's and the controlled group's respective interests in each CFC owned by the distributing group and the controlled group immediately after the applicable base period spin-off. The APB 23 limitation allocated to the distributing group and the controlled group is further allocated between and among the members of such groups in proportion to the fair market values of such members' respective interests in each CFC immediately after the applicable base period spin-off.

(d) *Examples.* The following examples illustrate the application of section 965(b)(1) and (2) and this section 6.01. Unless otherwise indicated, the following facts are assumed for purposes of these examples. All corporations and consolidated groups maintain calendar taxable years and were in existence prior to 1997. USP is a domestic corporation and the common parent of the USP consolidated group. USP wholly owns US1 and US2. US1 and US2 are U.S. shareholders and members of the USP consolidated group. US1 and US2 each wholly owns a foreign corporation, CFC1 and CFC2, respectively. USP elects to apply section 965 to its 2005 taxable year. USB is a domestic corporation and the common parent of the USB consolidated group, which is a consolidated group prior to any transactions described below. All domestic corporations acquired by the USB group that are eligible to do so elect to join in filing a consolidated return with the USB group. USB elects to apply section 965 for its 2005 taxable year. No elections are made under section 338 with respect to stock purchases.

Example 1. Sale of U.S. shareholder by consolidated group. (i) *Facts.* On December 31, 2003, USP sells the stock of US1 to an unrelated foreign person, FP. US1 files a separate return for the taxable years following such sale. On October 25, 2004, US2 sells CFC2 to USB for cash.

(ii) *Result.* On January 1, 2004, US1 is no longer a member of the USP consolidated group as a result of the sale of the US1 stock to FP. Accordingly, the USP group reduces its base period inclusions and APB 23 limitation attributable to US1. In addition, because US1 files a separate return after it ceases to be a member of the USP consolidated group, it takes into account its individual base period inclusions and APB 23 limitation. In contrast, US2's sale of CFC2 does not affect US2's base period inclusion history or APB 23 limitation, because base period inclusions and APB 23 limitation are not tax attributes of CFCs. Consequently, the USP group does not reduce its base period inclusions or APB 23 limitation as a result of the sale of CFC2. Similarly, USB does not make any adjustment to its base period inclusions or APB 23 limitation as a result of the acquisition of CFC2.

(iii) *Alternative Facts.* Assume the same facts as above, except that USP sells the stock of US1 to FP on February 15, 2005. On February 16, 2005, US1 is no longer a member of the USP consolidated group as a result of the sale of the US1 stock to FP. Because the transaction occurs within the USP election year, the USP group does not reduce its base period inclusions and APB 23 limitation attributable to US1. Further, US1 still takes into account its individual base period inclusions and APB 23 limitation should it make an election with respect to section 965(a) in its short taxable year following the acquisition (February 16, 2005 through December 31, 2005). The result with respect to USB is not changed under the alternative facts.

Example 2. Spin-off of U.S. shareholder by consolidated group. (i) *Facts.* The facts are the same as in *Example 1*, except that instead of USP selling the stock of US1, it distributes such stock in a distribution to which section 355 applies. US1 files a separate return for the taxable years following the distribution.

(ii) *Result.* The result is the same as that in *Example 1*. The special rules under section 965(c)(2)(C)(ii) and section 6.01(c)(2) of this notice do not apply because the distribution did not occur during USP's base period (which ended December 31, 2002).

Example 3. Section 368(a)(1)(D) reorganization/section 355 distribution. (i) *Facts.* USP owns CFC3. USP has base period inclusions and APB 23 limitation attributable to CFC3. On December 31, 2002, USP transfers the stock of CFC3 to controlled, a newly formed domestic corporation wholly-owned by USP, in a transaction to which section 368(a)(1)(D) applies, and immediately thereafter distributes the stock of controlled in a distribution to which section 355 applies.

(ii) *Result.* The distribution occurs during the USP group's base period and, therefore, the special rules under section 965(c)(2)(C)(ii) and section 6.01(c)(2) and (3) of this notice apply. As a result, USP's base period inclusions and APB 23 limitation that are attributable to CFC3 are allocated as provided in section 965(c)(2)(C)(ii) and section 6.01(c)(2) and (3) of this notice. Therefore, all of the base period inclusions and APB 23 limitation of USP attributable to CFC3 are allocated to controlled because controlled owns all the CFC3 stock immediately after the section 355 distribution.

(iii) *Alternative facts.* The facts are the same as in *Example 3*, except that the transaction occurs on December 31, 2003. Because the distribution does not occur during USP's base period, section

965(c)(2)(C)(ii) and section 6.01(c)(2) and (3) of this notice do not apply. Instead, the general rules of section 6.01(c)(1) of this notice apply. Therefore, none of the base period inclusions, and no portion of the APB 23 limitation, attributable to CFC3 are allocated to controlled; such amounts remain with USP.

Example 4. Internal spin-off of CFC followed by applicable base period spin-off. (i) *Facts.* US1 has base period inclusions with respect to CFC1. On June 30, 2002, US1 distributes the stock of CFC1 to USP in a transaction to which section 355 applies (first spin-off). On December 31, 2002, USP transfers the stock of CFC1 to controlled, a newly formed domestic corporation wholly owned by USP, in a transaction to which section 368(a)(1)(D) applies, and immediately thereafter distributes the stock of controlled in a distribution to which section 355 applies (second spin-off).

(ii) *Result.* The first and second spin-offs occur during the USP group's base period. Section 965(c)(2)(C)(ii)(II) does not apply to the first spin-off because CFC1 is not a United States shareholder. As a result US1's base period inclusions attributable to CFC1 are not allocated between US1 and USP in accordance with US1's and USP's proportional ownership of CFC1 after the first spin-off. However, in the second spin-off controlled is distributed out of USP's consolidated group. Accordingly, the USP group's base period inclusions with respect to each of its CFCs before the spin-off of controlled are allocated between the USP group and controlled (or controlled's group if controlled's affiliated group files a consolidated return) in proportion to the USP group's and controlled's (or the controlled group's) interests in each CFC owned by the USP group and controlled (or the controlled group) immediately after the second spin-off.

Example 5. Merger of a U.S. shareholder and other transactions. (i) *Facts.* On January 3, 2003, US1 sells its stock in CFC1 to USB for cash. On December 31, 2003, in an unrelated transaction US1 merges into US2. The merger of US1 into US2 is a reorganization under section 368(a)(1)(A). On December 31, 2004, in a transaction unrelated to the merger of US1 into US2, USP sells the shares of US2 to USB for cash. The APB 23 determination date for the USP and USB groups is December 31, 2002.

(ii) *Result.* The sale of CFC1 stock to USB has no effect on the USP group's base period inclusions and APB 23 limitation. The merger of US1 into US2 on December 31, 2003, is a transaction described in section 381(a), and US2 therefore succeeds to and takes into account US1's base period inclusions and APB 23 limitation.

Because US2 ceases to be a member of the USP consolidated group as a result of the sale of its stock to USB, the USP group reduces its base period inclusions and APB 23 limitation attributable to US2, including those amounts US2 succeeds to and takes into account as a result of the merger. Further, because US2 becomes a member of the USB consolidated group on January 1, 2005, USB's base period inclusions and APB 23 limitation are increased by the same amounts by which USP's base period inclusions and APB 23 limitation amount were decreased.

(iii) *Alternative facts.* The facts are the same as *Example 5* (i), except that instead of USP selling the shares of US2 to USB, US2 sells its assets to USB in

exchange for cash (and the assumption of any liabilities of US2) and distributes the cash proceeds to USP pursuant to a liquidation described in section 332.

Under the alternative facts, the result is the same as *Example 5* (ii), except as follows. USP does not make any adjustments to its base period inclusions or APB 23 limitation as a result of the sale of US2's assets to USB because the transaction with USB is not described in section 381(a) (this may not be the case, however, if the assets sold by US2 to USB include stock of a U.S. shareholder that is a member of the USP consolidated group). Further, USP continues to take into account the base period inclusions and APB 23 limitation attributable to US2 after the liquidation of US2 because the liquidation into USP is a transaction described in section 381(a). In addition, the USB consolidated group does not take into account the base period inclusions and APB 23 limitation attributable to US2, because US2 does not become a member of the USB consolidated group (nor does the USB consolidated group acquire the assets of US2 pursuant to a transaction described in section 381(a)).

(iv) *Alternative facts.* The facts are the same as *Example 5* (i), except that USP and USB make an election pursuant to section 338(h)(10) with respect to the sale of the stock of US2. The result under the alternative facts in this paragraph (iv) is the same as under the alternative facts of paragraph (iii) of this *Example 5*. This is the case regardless of whether an election under section 338 is made with respect to the CFC2 stock owned by US2.

Example 6. Acquisition of U.S. shareholder consolidated group. (i) *Facts.* USB acquires all the stock of USP on January 3, 2003, a date subsequent to the APB 23 determination dates for both the USP and USB groups. As a result of the acquisition, the USP group terminates and all the members of the USP group become members of USB consolidated group.

(ii) *Result.* USB's acquisition of all the stock of USP causes the USP consolidated group to cease to exist as of the end of January 3, 2003, a date after the end of the base periods of both the USP and USB groups. The USP group's base period inclusions for

each of the five taxable years in its base period is added to the USB group's base period inclusions for each corresponding taxable year in its base period to determine the USB group's base period amount. In addition, because the acquisition occurs after the APB 23 determination dates of both the USB and USP groups, the USB group's APB 23 limitation is increased by the USP group's APB 23 limitation.

Example 7. Taking into account base period inclusions of acquired U.S. shareholder transferred after the end of the acquirer's base period. (i) *Facts.* The USB consolidated group uses a taxable year ending March 31. The USB group elects to apply section 965 to its taxable year that begins on April 1, 2005 and ends on March 31, 2006. On May 31, 2005, USB acquires from USP 100% of the stock of US1 for cash.

(ii) *Result.* The acquisition of US1 occurs during the section 965 election year of the USP group and the section 965 election year of the USB group. Therefore, the special rules set forth in section 6.01(b)(2) apply. Under those rules, the USB consolidated group takes into account the base period inclusions of US1 for purposes of determining its base period amount under section 965(b)(2). Because US1 ceases to be a member of the USP consolidated group during the election year of such group, the USP consolidated group will also take into account the base period inclusions of US1 for purposes of determining its base period amount under section 965(b)(2). Accordingly, there is no corresponding decrease by the selling group for the increase by the buying group of base period inclusions and APB 23 amounts as a result of the transaction.

The USB consolidated group's base period includes the five taxable years ending on or before June 30, 2003 (that is, taxable years ending March 31, 1999 through March 31, 2003). Similarly, the base period of US1 and USP includes the five taxable years ending on or before June 30, 2003 (that is, the taxable years ending December 31, 1998 through December 31, 2002).

To determine the USB group's base period amount, US1's base period inclusions for each taxable year in its base period are added to the base

period inclusions for each corresponding taxable year in the USB group's base period. Thus, US1's base period inclusions for its taxable year ending December 31, 2002 are added to the base period inclusions for the USB group's year ended March 31, 2003, and US1's base period inclusions for the other four years in its base period are added to the USB group base period inclusions for the other four corresponding years in the USB group's base period.

Because the acquisition of US1 occurs during the election years of both the USP group and the USB group, both groups will also take into account the APB 23 limitation attributable to US1.

Example 8. Taking into account base period inclusions of acquired U.S. shareholder transferred before the end of the acquirer's base period. (i) *Facts.* The facts are the same as *Example 7*, except as follows. USB acquired US1 on February 15, 2002, a date prior to the APB 23 determination dates of both USP and USB. The USB group's base period includes the five taxable years ending March 31, 1999, through March 31, 2003. As a result of its acquisition, the base period of US1 includes its five taxable years that end on the following dates: February 15, 2002; December 31, 2001; December 31, 2000; December 31, 1999; and December 31, 1998.

(ii) *Result.* To determine the USB group's base period amount, US1's base period inclusions for each taxable year in US1's base period are added to the USB group's base period inclusions for each corresponding taxable year in the USB group's base period. US1's short taxable year ending February 15, 2002, corresponds to the last taxable year in the acquirer's base period that ends on or before the date of the acquisition (that is, the USB group's taxable year that ends March 31, 2001). The USB group also succeeds to that portion of US1's base period inclusion history for US1's taxable years that precede the short taxable year ending on February 15, 2002, that correspond to the USB group taxable years in its base period.

The corresponding taxable years in the respective base periods may be illustrated as follows:

<i>US1 base period year-ends</i>	<i>USB group base period year-ends</i>
3/31/03	3/31/03
3/31/02	3/31/02
2/15/02	3/31/01
12/31/01	3/31/00
12/31/00	3/31/99
12/31/99	
12/31/98	

US1's taxable years ending on December 31, 1999, and December 31, 1998, correspond to taxable years of the USB group that precede the USB group's base period. Accordingly, the USB group does not take into account the base period inclusions of US1 in those years. Nevertheless, the USP group will reduce its base period inclusions attributable to US1 for these taxable years.

US1's base period inclusions after February 15, 2002, are naturally taken into account by the USB group in determining its base period inclusions because such inclusions will occur during the time that

US1 is a part of the USB consolidated group. That is, US1 base period inclusions for its taxable year that ends March 31, 2002, and March 31, 2003, are taken into account in determining the USB group's inclusions for such taxable years.

US1 ceased being a member of the USP consolidated group and joined the USB consolidated group before the APB 23 determination dates of both the USP and USB consolidated groups. As a result, no adjustment is made to the APB 23 amount of the USP or USB consolidated groups as a result of the sale of

US1 stock as provided in section 6.01(a)(2) of this notice.

(iii) *Alternative facts.* The facts are the same as in *Example 8*, except that the USB group's first taxable year begins on April 1, 2000. The results are unchanged.

Example 9. Acquisition of U.S. shareholder stock before Acquirer's but after Seller's APB 23 determination date. (i) *Facts.* The USP group's applicable financial statement provides for an APB 23 limitation of \$700 million. The limitation is comprised of, as of the APB 23 determination date (December 31,

2002), earnings permanently reinvested in CFC1 of \$400 million and in CFC2 of \$300 million. The \$400 million of CFC1 earnings is attributable to US1, and the \$300 million of CFC2 earnings is attributable to US2. USB maintains a taxable year ending January 31. On January 3, 2003, USP sells to USB 81% of US1's outstanding stock and 60% of the outstanding stock of US2. The USB group's APB determination date is January 31, 2003.

(ii) *Result.* By reason of the transactions, US1 and US2 cease to be members of the USP consolidated group on January 3, 2003, a date that is after the USP group's APB 23 determination date. Therefore, the USP consolidated group reduces its APB 23 limitation by \$700 million because US1 and US2 are no longer members of the USP consolidated group. Similarly, the USP group reduces its base period inclusions to the extent they are attributable to US1 and US2. Further, the acquisition of US1 and US2 occurred prior to USB's APB 23 determination date. Therefore, the USB group does not increase its APB 23 limitation with respect to the transactions because the USB group will take into account permanently reinvested earnings of US1 and US2 for financial accounting purposes on its APB 23 determination date. Finally, USB inherits the relevant base period inclusion history of US1 because US1 joins the USB consolidated group. After the transaction, US2 is not a member of a consolidated group and therefore will file a separate return for subsequent taxable years. If US2 elects to apply section 965 in an eligible year, it will take into account its base period inclusion history and its APB 23 limitation.

(iii) *Alternative facts.* The facts are the same as in *Example 9* (i), except that US1 and US2 are sold on February 1, 2003. The USB group's reported APB 23 limitation is increased by \$400 million as a result of USB's purchase of 81% of the shares of US1 because US1 joins the USB consolidated group after the USB group's APB 23 determination date; it is not increased by the \$300 million attributable to US2 because US2 does not join the USB consolidated group. The base period inclusion results are unchanged.

.02 Allocated Portion of \$500 Million Limitation

Pursuant to section 4.05 of this notice, the \$500 million limitation described in section 965(b)(1)(A) is allocated among qualified members of a section 52(a) group on a single date, the apportionment date (as defined in section 4.05 of this notice), and only amongst the qualified members of the group on such date. A corporation or consolidated group is not allocated any of the \$500 million limitation and it has a \$0 limitation for an election year during which the corporation or consolidated group was a qualified member of a section 52(a) group if, on or after the end of its election year but before the section 52(a) group's apportionment date (or, if none, the date that would have been the apportionment date had the transaction not occurred), the corporation

or consolidated group becomes unrelated to the other qualified members of the section 52(a) group or ceases to exist.

Once an allocation occurs on an apportionment date, the allocated limit applies to a corporation or consolidated group that is a qualified member of the section 52(a) group for its election years ending while it is a qualified member of such group, including those years that end before the apportionment date. However, if a corporation or consolidated group becomes unrelated to the other qualified members of a section 52(a) group before the end of an election year of such corporation or consolidated group, the corporation or group is entitled to its own \$500 million limitation, unless it becomes part of a different section 52(a) group on or before that group's apportionment date. If it becomes part of a different section 52(a) group on or before that group's apportionment date, it may be allocated a portion of that section 52(a) group's \$500 million limitation. Accordingly, if a corporation or consolidated group is no longer a qualified member of a section 52(a) group, the former member does not retain any of the section 52(a) group's \$500 million limitation after it leaves such group.

The following examples illustrate the application of section 965(b)(1) and this section 6.02. Unless otherwise indicated, it is assumed in each example that all U.S. shareholders have APB 23 limitations of zero.

Example 1. Disposition of a member which joins an unrelated consolidated group. (i) *Facts.* A, an individual, wholly owns two domestic corporations, US1 and US2. US1 and US2 in turn each wholly own a foreign corporation, CFC1 and CFC2, respectively. US1 and US2 maintain the calendar year as their taxable year.

On September 30, 2005, A sells US1 to USB. USB is an unrelated domestic corporation and the common parent of a consolidated group that maintains a June 30 taxable year.

US1 elects section 965 for its taxable year ending September 30, 2005. US2 elects section 965 for its taxable year ending December 31, 2005. The USB group elects section 965 for its taxable year ending June 30, 2006.

(ii) *Result.* US2 is entitled to a full \$500 million limitation for its election year ending December 31, 2005, because it is not a member of a section 52(a) group on December 31, 2005. US1 has a limitation of \$0 for its election year ending September 30, 2005, because US1 and US2 would have been members of a section 52(a) group on an apportionment date, December 31, 2005, but for the disposition of US1 on or after the end of US1's election year but before December 31, 2005. The apportioned limitation does

not apply to US1's second election year as a member of the USB group. The USB group has its own \$500 million limitation, which is not adjusted upward as a result of the acquisition of US1.

Example 2. Disposition of a member which does not join an unrelated consolidated group. (i) *Facts.* The facts are the same as in *Example 1* except that the buyer of US1 is B, an individual unrelated to A. As in *Example 1*, US1 elects section 965 for its taxable year, which however ends on December 31, 2005.

(ii) *Result.* On December 31, 2005, there is no section 52(a) group, and the election year of neither corporation ended before that date. Therefore, US1 and US2 each has its own \$500 million limitation.

Example 3. Merger into unrelated corporation. (i) *Facts.* The facts are the same as in *Example 1* except that instead of the stock of US1 being sold, US1 merges into USB in a reorganization described in section 368(a)(1)(A).

(ii) *Result.* The result is the same as in *Example 1*.

Example 4. Merger into related corporation. (i) *Facts.* The facts are the same as in *Example 3* except that US1 merges into US2 in a reorganization described in section 368(a)(1)(A).

(ii) *Result.* US2 is entitled to a full \$500 million limitation for its election year ending December 31, 2005, because it is not a member of a section 52(a) group on December 31, 2005. US1 has a limitation of \$0 for its election year ending September 30, 2005, because US1 and US2 would have been members of a section 52(a) group on their apportionment date, December 31, 2005, but for the merger of US1 which results in the end of US1's election year before December 31, 2005.

Example 5. Spin-off resulting in unrelated corporation. (i) *Facts.* USP is a publicly held corporation and the parent of a consolidated group. C and US1 are wholly owned domestic subsidiaries of USP. US1 cannot be included in the USP consolidated group by virtue of section 1504(a)(3) (relating to the five-year period required to elapse before reconsolidation). The USP group and US1 each maintain the calendar year as their taxable years and USP, C, and US1 are each U.S. shareholders of CFCs.

On September 30, 2005, USP distributes the stock of C to its shareholders. Thereafter, USP and C are not members of the same section 52(a) group.

The USP group and US1 each elect section 965 for their taxable years ending December 31, 2005. C also elects section 965 for its short taxable year starting on October 1, 2005, and ending on December 31, 2005.

(ii) *Result.* December 31, 2005, is the apportionment date for the section 52(a) group that consists of the USP group and US1, and the \$500 million limitation is allocated between the USP group and US1 on that date. None of the limitation is allocated to C separately for its short taxable year ending September 30, 2005 (its limitation is \$0), but the apportionment does not apply to C's second election year, the short taxable year ending December 31, 2005. C has its own \$500 million limitation for that second election year.

Example 6. Spin-off resulting in related corporation. (i) *Facts.* The facts are the same as in *Example 5* except that all the stock of USP is owned by A, an individual, and A acquires all the stock of C in the

distribution. As a result, USP and C remain members of a single section 52(a) group after the distribution.

(ii) *Result.* December 31, 2005, is the apportionment date for the section 52(a) group that consists of the USP group, US1, and C, and the \$500 million limitation is allocated between the USP group, US1, and C on that date. C's allocation applies to its second election year, the short taxable year ending December 31, 2005. During the time that C is a member of the USP group, it is not separately allocated any of the \$500 million limitation of the section 52(a) group.

Example 7. Interaction of APB 23 limitation and \$500 million limitation. (i) *Facts.* The facts are the same as in *Example 1*, except that US1 has an APB 23 limitation of \$300 million, and USB has an APB 23 limitation of \$400 million.

(ii) *Result.* The result is the same as in *Example 1* with respect to the \$500 million limitation. The maximum repatriations allowed under section 965 for US1 in its election year ending September 30, 2005, is the greater of its allocated portion of the \$500 million limitation or its APB 23 limitation. US1's APB 23 limitation of \$300 million exceeds its portion of the \$500 million, which is \$0. Thus, US1's maximum amount under section 965(b)(1) is \$300 million. As in *Example 1*, the USB group's \$500 million limitation is not adjusted as a result of USB's acquisition of US1. However, the USB group's APB 23 limitation is adjusted upward to reflect the \$300 million APB 23 limitation attributable to US1. Because the maximum repatriations allowed under section 965 for the USB group is the greater of \$500 million or APB 23 limitation, the USB group's APB 23 limitation exceeds \$500 million as a result of the acquisition. Thus, USB's maximum amount under section 965(b)(1) is \$700 million (\$400 million + \$300 million).

SECTION 7. REDUCTION OF BENEFIT FOR INCREASES IN RELATED PARTY INDEBTEDNESS

.01 Background

(a) *General.* Section 965(b)(3) provides that a U.S. shareholder reduces the amount of dividends otherwise eligible for the deduction under section 965(a) by any increase in the indebtedness of its CFC to any related person (as defined in section 954(d)(3)) between October 3, 2004, and the close of the taxable year for which the election under section 965 is in effect. For purposes of section 965(b)(3), all CFCs with respect to which the taxpayer is a U.S. shareholder are treated as a single CFC.

(b) *Definitions.* For purposes of section 965(b)(3) and this section 7, the following definitions apply:

(i) The term "CFC" means all CFCs with respect to which the taxpayer is a U.S. shareholder, treating such CFCs as a single CFC pursuant to section 965(b)(3).

(ii) The term "individual CFC" is used to refer to a single CFC (for example, to identify a single CFC that is acquired or disposed of by a consolidated group U.S. shareholder).

(iii) The term "U.S. shareholder" as used in this section 7 is defined in section 951(b).

(iv) The term "related person" means a person that is related to a CFC within the meaning of section 954(d)(3).

(v) The term "related party indebtedness" means the amount of indebtedness of a CFC to a related person. However, indebtedness between individual CFCs of a U.S. shareholder is disregarded for purposes of section 965(b)(3).

(vi) The term "initial measurement date" means the close of October 3, 2004 or, if the U.S. shareholder so chooses, an alternative date which is provided as a matter of administrative convenience for taxpayers and the IRS. The alternative date is either: (i) the close of September 30, 2004, if such shareholder used a calendar year or a fiscal year as its taxable year; or (2) the close of the last day of such shareholder's fiscal-year month ending nearest October 3, 2004, if such shareholder used a 52–53 week taxable year. However, the U.S. shareholder uses the same date as its initial measurement date for all purposes of section 965.

(vii) The term "last measurement date" means the close of a U.S. shareholder's taxable year for which an election is in effect.

.02 Definition of Indebtedness

(a) *In general.* Except as provided in this section, for purposes of section 965(b)(3), "indebtedness" is defined under general Federal income tax principles. Further, the amount of indebtedness of a CFC to any related person pursuant to section 965(b)(3) is not reduced or otherwise offset by indebtedness of any related person to the CFC. Thus, for example, if on the initial measurement date or the last measurement date, there is \$100x of indebtedness of a CFC to its U.S. shareholder, and \$10x of indebtedness from such U.S. shareholder to the CFC, the amount of indebtedness under section 965(b)(3)(A) as of such date is \$100x (and not \$90x).

For purposes of section 965(b)(3), indebtedness of a CFC to a foreign disregarded entity that is owned for Federal tax purposes by a related person is treated as related party indebtedness. Thus, for example, if on the initial measurement date there is \$100x of indebtedness from a CFC to a foreign disregarded entity owned by a U.S. shareholder, which is a related person to the CFC, such amount is indebtedness described in section 965(b)(3)(B).

(b) *Exception for Intercompany Trade Payables.* For purposes of section 965(b)(3), the term "indebtedness" does not include indebtedness arising in the ordinary course of a business from sales, leases, or the rendition of services provided to or for a CFC by a related person, provided that such indebtedness is actually paid within 183 days.

.03 Determination of Related Party Indebtedness

A U.S. shareholder considers the indebtedness of its CFC to related persons only if the U.S. shareholder is a related person with respect to such CFC. For purposes of determining the related party indebtedness of a CFC pursuant to section 965(b)(3), the relationship between the CFC, its creditors, and any of its U.S. shareholders is determined independently on the initial measurement date and the last measurement date, respectively. For example, if on such date the creditor of the CFC is a related person and a U.S. shareholder is a related person with respect to such CFC, the U.S. shareholder has an amount of indebtedness that is considered under section 965(b)(3) and the rules of this section.

.04 Amount of Reduction under Section 965(b)(3)

(a) *In General.* Pursuant to section 965(b)(3) and the rules of this section, a U.S. shareholder reduces the amount of cash dividends that would otherwise be taken into account under section 965(a) by the excess (if any) of its last measurement date RPI (as determined under section 7.05(b)) over its initial measurement date RPI (as determined under sections 7.05(a) and 7.05(c)). If two or more U.S. shareholders may otherwise be considered to have an amount that is considered under

section 965(b)(3) attributable to the same CFC indebtedness, such shareholders take into account such indebtedness under the rules of 7.06 of this section.

(b) *Indirect Financing of Cash Dividend by a U.S. Shareholder.* Section 965(b)(3) is intended to prevent a U.S. shareholder from directly or indirectly financing a cash dividend qualifying under section 965(a). In addition to the application of the related party indebtedness rule under section 965(b)(3), general tax law principles such as the substance-over-form doctrine and circular cash-flow principles may apply to various financing structures. However, a related party guarantee of CFC indebtedness is not considered to be an indirect financing of a cash dividend for purposes of section 965(b)(3), provided that the CFC is treated as the obligor on the indebtedness for Federal income tax purposes. See *Plantation Patterns, Inc. v. Comm’r*, 462 F.2d 712 (5th Cir. 1972), cert. denied, 409 U.S. 1076 (1972).

.05 Amount of Related Party Indebtedness on the Initial Measurement Date and the Last Measurement Date

(a) *Initial Measurement Date RPI — General Rule.* A U.S. shareholder determines the amount of the related party indebtedness of its CFC on the initial measurement date and such amount is the “initial measurement date RPI” of such U.S. shareholder. The amount of the initial measurement date RPI is adjusted pursuant to section 7.05(c) of this notice in certain instances. See *Example 1* of section 7.08 of this notice.

(b) *Last Measurement Date RPI — General Rule.* A U.S. shareholder determines the amount of the related party indebtedness of its CFC on the last measurement date and such amount is the “last measurement date RPI” of such U.S. shareholder. Thus, to the extent that a CFC pays all or a portion of the principal on the related party indebtedness before the last measurement date and does not incur any new related party indebtedness before such date, the U.S. shareholder’s last measurement date RPI will be less than its initial measurement date RPI. See *Examples 4 and 6* of section 7.08 of this notice.

(c) *Special Adjustments to Initial Measurement Date RPI.* A U.S. shareholder

reduces its initial measurement date RPI to the extent the U.S. shareholder’s initial measurement date RPI is attributable to any individual CFC with respect to which such shareholder ceases to be a U.S. shareholder or a related person as the result of a transaction before the last measurement date. However, the prior sentence does not apply to the extent, before or as a result of such transaction, all or a portion of the principal on the indebtedness is paid by the debtor (for example, as a result of the liquidation of an individual CFC).

A domestic corporation that becomes a U.S. shareholder and a related person with respect to an individual CFC after such corporation’s initial measurement date, but before the last day of its election year (or a U.S. shareholder that files a separate return for its short taxable year immediately after a transaction during the same period), and that remains a U.S. shareholder and a related person with respect to such individual CFC on its last measurement date, increases its initial measurement date RPI by the amount of related party indebtedness of such individual CFC immediately after the transaction, excluding any indebtedness arising in connection with or as a result of the transaction (for example, as a result of the incorporation of a branch). See *Examples 3, 4, and 10* of section 7.08 of this notice.

If two or more U.S. shareholders may otherwise be considered to have an amount that is considered under section 965(b)(3) attributable to the same CFC indebtedness, such shareholders take into account such indebtedness under the rules of section 7.06 of this notice.

.06 Related Party Indebtedness — Multiple U.S. Shareholders

An increase in a CFC’s related party indebtedness may not reduce the total amount of dividends otherwise eligible for the section 965(a) DRD on anything but a dollar-for-dollar basis. Consequently, if more than one U.S. shareholder is a related person with respect to a CFC, then the effect of the increase in the related party indebtedness of the CFC pursuant to section 965(b)(3) is allocated among and between such U.S. shareholders. For this purpose, such increase is allocated on a dollar-for-dollar basis to cash dividends received by such U.S. shareholders that are

otherwise eligible for the section 965(a) DRD in the order that those dividends are received. If such dividends are received by more than one U.S. shareholder on the same day, each U.S. shareholder takes into account the remaining amount of the increase in related party indebtedness of such CFC based on the relative amount of cash dividends received on such day. The overall reduction in dividends of all U.S. shareholders eligible for the section 965(a) DRD under this rule may not exceed the total increase in related party indebtedness under section 965(b)(3). See *Examples 8 and 9* of section 7.08 of this notice.

.07 Translation of Foreign Currency-Denominated Related Party Indebtedness

The initial measurement date RPI and the last measurement date RPI of a U.S. shareholder is determined in U.S. dollars. The amount of any indebtedness on both the initial measurement date and the last measurement date is translated into U.S. dollars using the spot rate (as defined in Treas. Reg. §1.988-1(d)(1)) on the initial measurement date. See *Example 7* of section 7.08 of this notice.

.08 Examples

The following examples illustrate the application of section 965(b)(3) and this section 7. Unless otherwise indicated, the following facts are assumed for purposes of these examples. USP, a domestic corporation and the common parent of the USP consolidated group that uses the calendar year as its taxable year, wholly owns US1. US1 is a domestic corporation and a member of the USP consolidated group. US1 wholly owns CFC1, a foreign corporation that owes US1 \$100x at the close of September 30, 2004, evidenced by a note (\$100x note). USP wholly owns CFC2, a foreign corporation with no indebtedness owed to persons described in section 954(d)(3). The USP group chooses September 30, 2004, as its initial measurement date and it elects to apply section 965 to its 2005 calendar year tax year.

Example 1. Determination of the amount of initial measurement date RPI. (i) *Facts.* The general facts apply.

(ii) *Result.* US1 and USP are each U.S. shareholders with respect to CFC1 and CFC2 and are considered one U.S. shareholder for purposes of section 965(b)(3). Further, CFC1 and CFC2 are considered

one CFC for purposes of section 965(b)(3). The USP group's CFC (CFC1 and CFC2) has indebtedness of \$100x owed to the USP group (and directly to US1 as a member of that group), a related party. Therefore, the USP group has initial measurement date RPI of \$100x.

Example 2. Determination of initial and last measurement date RPI when CFC transferred or sold. (i) *Facts.* On December 31, 2004, US1 sells all the stock of CFC1 and the \$100x note to USB, an unrelated U.S. corporation that is the common parent of a consolidated group. Immediately after the transaction, CFC1 owes \$100x to USB. USB makes an election under section 965 for its calendar year ending December 31, 2005. As of USB's last measurement date, it is a U.S. shareholder and related person with respect to CFC1.

(ii) *Result.* Under section 965(b)(3) all CFCs of a U.S. shareholder are treated as one CFC. Moreover, for purposes of section 965(b)(3), all U.S. shareholders that are members of a consolidated group are considered one U.S. shareholder. Therefore, CFC1 and CFC2 are considered one CFC and US1 and USP are considered one U.S. shareholder (the USP group). Only the relationship between CFC1, CFC2 and the USP group is taken into account for purposes of determining the initial measurement date RPI of the USP group, while only the relationship between CFC1 and USB is taken into account for purposes of determining the last measurement date RPI of the USB group.

As of the initial measurement date the USP group's CFC (CFC1 and CFC2) owes \$100x to related parties. Therefore, under section 7.05(a), and without regard to the disposition of CFC1, the USP group's initial measurement date RPI is \$100x. Under section 7.05(c), however, the USP group reduces its initial measurement date RPI to account for the disposition of CFC1. Therefore, the USP group's initial measurement date RPI is \$0. As of the last measurement date, CFC1 is not related to the USP group. Accordingly, the USP group's last measurement date RPI is \$0.

With respect to the USB group, CFC1 is not related to the USB group on the USB group's initial measurement date. Therefore, the USB group's initial measurement date RPI, without consideration of the acquisition of CFC1 is \$0. Under section 7.05(c), however, the USB group increases its initial measurement date RPI by \$100x, the amount of the CFC1's related party indebtedness immediately after the acquisition. Therefore, the USB group has initial measurement date RPI of \$100x. Further, as of its last measurement date, CFC1 owes USB, a related party, \$100x. Therefore, the USB group's last measurement date RPI is \$100x.

(iii) *Alternative facts.* The facts are the same as in (i), except that USB does not purchase the \$100x note due from CFC1. Under section 7.05(c), the USP group reduces its initial measurement date RPI from \$100x to \$0, to account for the disposition of CFC1 (the same result reached in (ii)). Under section 7.05, the USP group's last measurement date RPI is \$0 (the same result reached in (ii)). Under the alternative facts, however, the USB group does not adjust its initial measurement date RPI to take into account the acquisition of CFC1 because immediately after the acquisition CFC1 will owe an indebtedness to US1, which is not a related person. As a result, the USB group has an initial measurement date RPI of \$0. Fur-

ther, the USB group has a last measurement date RPI of \$0.

(iv) *Alternative facts.* The facts are the same as in (i) except that CFC1 liquidates (whether by reason of an actual liquidation or by reason of an election under Treas. Reg. §301.7701-3) into US1 instead of being sold to USB. Under section 7.05(c), the USP group does not decrease its initial measurement date RPI to account for the liquidation. Consequently, the USP group's initial measurement date RPI is \$100x. Under section 7.05(b), the USP group's last measurement date RPI is \$0.

Example 3. Determination of initial and last measurement date RPI when a U.S. shareholder is transferred to an unrelated person. (i) *Facts.* The facts are the same as in *Example 1*, except that on December 31, 2004, all the stock of US1 (and indirectly CFC1), is sold to an unrelated U.S. shareholder, USB. US1 joins the USB consolidated group and USB makes an election under section 965 for the taxable year ending December 31, 2005. As of its last measurement date, USB is a U.S. shareholder and related person with respect to CFC1.

(ii) *Result.* Without regard to the disposition of US1, the USP group's initial measurement date RPI is \$100x. Under section 7.05(c), the USP group's initial measurement date RPI is decreased by \$100x, resulting in the USP group having initial measurement date RPI of \$0.

USP computes its last measurement date RPI under section 7.05(b) of this notice. As of the last measurement date, CFC1 owes an indebtedness to US1, a party that is not related within the meaning of section 954(d)(3) to USP. Therefore, the USP group's last measurement date RPI is \$0.

Without regard to the acquisition of US1, the USB group's initial measurement date RPI is \$0. However, under section 7.05(c), the USB group increases its initial measurement date RPI by \$100x, the amount of the related party indebtedness of its CFC (CFC1) immediately after the transaction. Further, the USB group's last measurement date RPI is \$100x because as of its last measurement date, CFC1 owed \$100x to US1, a related person.

(iii) *Alternative facts.* Assume that the stock of US1 is sold to USB on March 31, 2005, which is during the USP group's and the USB group's election year. The results are the same as set forth in (ii), above.

Example 4. Determination of initial and last measurement date RPI when a new CFC is formed. (i) *Facts.* The facts are the same as in *Example 1*, except that USP incorporates CFC2 on November 1, 2004, and during the USP election year USP acquires all the stock of USB (and indirectly all of USB's individual CFCs), an unrelated U.S. shareholder. Further, USB is a member of the USP consolidated group on the last day of the USP election year. In part, CFC2 is capitalized with \$100x of related party indebtedness and USP is a U.S. shareholder and a related person with respect to CFC2 on its last measurement date. USB has initial measurement date RPI of \$400x, attributable to its CFCs. Immediately after the acquisition, USB's CFCs continue to have indebtedness owed to USB in the amount of \$400x.

(ii) *Result.* Without regard to the acquisition of USB or the formation of CFC2, under section 7.05(a), the USP group has initial measurement date RPI of \$100x. Under section 7.05(c), the USP group in-

creases its initial measurement date RPI by the related party indebtedness of the USB CFCs immediately after the transaction. Note, however, that no adjustment is made to the USP group's initial measurement date RPI to account for CFC2's related party indebtedness under section 7.05(c). Thus, after adjustment, the USP group's initial measurement date RPI is \$500x. Under section 7.05(b), the USP group's last measurement date RPI is \$600x, which includes the indebtedness of CFC1 (\$100x), CFC2 (\$100x), and the acquired CFCs of USB (\$400x).

(iii) *Alternative facts.* The facts are the same as in *Example 6* (i), except that CFC1 pays US1 \$70x of the \$100x indebtedness on November 1, 2005. The USP group's initial measurement date RPI is \$500, the same as in (ii). Under section 7.05(b), the USP group's last measurement date RPI is \$530x, which includes the indebtedness of CFC1 (\$30x), CFC2 (\$100x), and the acquired CFCs of USB (\$400x). Under section 7.04 of this notice and section 965(b)(3), USP group reduces its dividends otherwise eligible for the section 965(a) DRD by \$30x.

Example 5. Determination of initial and last measurement date RPI when a U.S. shareholder and its CFC are transferred but the note due from the CFC is left behind. (i) *Facts.* The facts are the same as in *Example 1*, except that all the stock of US1 (and indirectly CFC1) is sold to an unrelated U.S. shareholder, USB, on December 31, 2004, before USP group's election year ending December 31, 2005. Assume that CFC1's related party indebtedness on the initial measurement date (\$100x) was the result of the indebtedness being owed to USP instead of US1. US1 is a member of the USB group on the USB group's last measurement date.

(ii) *Result.* Without regard to acquisitions and dispositions, the USP group has initial measurement date RPI of \$100x. Because USP was a U.S. shareholder and a related person with respect to CFC1 on the USP group's initial measurement date, but is not a U.S. shareholder or a related person on its last measurement date, section 7.05(c) requires the USP group to reduce its initial measurement date RPI from \$100x to \$0.

On the USP group's last measurement date, CFC1 is not a related person. Therefore, the USP group's last measurement date RPI is \$0.

USB has initial measurement date RPI of \$0, without regard to the acquisition of US1 (and CFC1). No adjustment is made to this amount under section 7.05(c) because immediately after the acquisition CFC1 owed an indebtedness to USP, an unrelated party. Further, the USB group's last measurement date RPI is \$0 because its CFC (CFC1) does not have an indebtedness to a related party on the last measurement date.

Example 6. Determination of initial and last measurement date RPI when a U.S. shareholder is transferred without the debtor CFC. (i) *Facts.* The facts are the same as in *Example 1*, except that on December 31, 2004, before the USP group's election year, US1 distributed CFC1 to USP, and then US1 was sold to USB. In addition, CFC1's related party indebtedness on the USP group's initial measurement date was owed to USP instead of US1. Finally, USB has initial measurement date RPI of \$0.

(ii) *Result.* Without regard to the distribution of CFC1 or the disposition of US1, the USP group

has initial measurement date RPI of \$100x. No adjustment is made under section 7.05(c) to the USP group's initial measurement date RPI as a result of the distribution of CFC1 because after the distribution the USP group is a U.S. shareholder and related person with respect to CFC1. Further, under section 7.05(c), the sale of US1 does not require the USP group to reduce its initial measurement date RPI because after the disposition USP is still a U.S. shareholder and related person with respect to CFC1. Therefore, USP has initial measurement date RPI of \$100x. The USP group's last measurement date RPI is also \$100x because on the last measurement date CFC1's indebtedness is owed to USP, a related party.

USB acquires US1, but US1 has no CFCs when it enters the USB consolidated group. Therefore, under section 7.05(c), the USB consolidated group does not increase its initial measurement date RPI. In addition, USB's last measurement date RPI is \$0.

(iii) *Alternative facts.* The facts are the same as in (i), except that the CFC1 indebtedness is owed to US1. Under the alternative facts, the USP group would still have initial measurement date RPI in the amount of \$100x. No adjustment is made to this amount under section 7.05(c) because on the USP group's initial measurement date and last measurement date the USP group was a U.S. shareholder and a related person with respect to CFC1. However, as of the last measurement date, CFC1 will owe an indebtedness to US1, an unrelated party. Therefore, the USP group's last measurement date RPI is \$0. The results with respect to the USB group are the same as set forth in (ii).

Example 7. Translating RPI denominated in a non-U.S. dollar currency. (i) *Facts.* CFC1's indebtedness to US1 is denominated in currency u. As of the close of September 30, 2004 (the initial measurement date), CFC1 owed 100u to US1. As of the close of December 31, 2005, CFC1 continued to owe 100u to US1. As of September 30, 2004, the spot rate is 1u/\$1. As of December 31, 2005, the spot rate is 1u/\$1.5.

(ii) *Result.* Pursuant to section 7.05 of this notice, the indebtedness of CFC1 to US1 on the initial measurement date and the last measurement date is converted into U.S. dollars on the spot rate on the initial measurement date. As a result, the indebtedness of CFC1 to US1 on both dates is \$100x.

Example 8. U.S. shareholder not related to CFC (i) *Facts.* FP, a foreign corporation, wholly owns US1, a domestic corporation. US1 owns 60% of CFC. US2, a domestic corporation that is unrelated to FP or US1, owns the remaining 40% of CFC. As of the initial measurement date of US1 and US2, CFC has related party indebtedness in the amount of \$100x that is owed to FP.

(ii) *Result.* US1 is a related person with respect to CFC on its initial measurement date. As a result, US1 takes into account the related party indebtedness of CFC for purposes of section 965(b)(3). Because US2 is not a related person with respect to CFC, the \$100x of related party indebtedness is not taken into account by US2 for purposes of section 965(b)(3).

Example 9. Application of Section 965(b)(3) reduction to multiple U.S. shareholders (i) *Facts.* USP is a domestic corporation and the common parent of a consolidated group. USP wholly owns US1, a domestic corporation that is not a member of the USP group because an election under section 936 is in ef-

fect with respect to US1. USP and US1 wholly own CFC1 and CFC2, respectively. The USP group and US1 both maintain a calendar taxable year and elect to apply section 965 to the taxable year ending December 31, 2005. USP receives a cash dividend of \$200x from CFC1 on February 1, 2005. US1 receives a cash dividend from CFC2 of \$300x on March 1, 2005. Both cash dividends received by USP and US1 during 2005 are otherwise eligible for the deduction under section 965(a). There is a \$300x increase in CFC1's related party indebtedness pursuant to section 965(b)(3). CFC2 does not have related party indebtedness at any time.

(ii) *Result.* Under section 965(d)(3), the USP group and US1 are both U.S. shareholders and related persons with respect to CFC1. Thus, both the USP group and US1 are required to take into account CFC1's increase in related party indebtedness. Based upon the rules set forth in section 7.06, above, CFC1's \$300x increase in related party indebtedness reduces the amount of the USP group's and US1's dividends eligible for the deduction under section 965(a) based on the earliest cash dividends eligible for the section 965(a) DRD received by the USP group and US1 during the election year. As a result, the USP group takes into account \$200x of the \$300x increase in RPI because it received a cash dividend of \$200x on February 1, 2005. US1 takes into account the remaining \$100x of such increase because it received its cash dividend on March 1, 2005.

(iii) *Alternative Facts.* The facts are the same as *Example 2*, except that USP and US1 received the cash dividends from CFC1 and CFC2, respectively, on the same day during the election year. Under section 7.06, the USP group and US1 take into account the \$300x increase in RPI attributable to CFC1 in proportion to their receipt of cash dividends on such date. Thus, the USP group takes into account \$120x of the increase $((\$200x/(\$200x + \$300x)) \times \$300x)$. US1 takes into account the remaining \$180x of the increase $((\$300x/(\$200x + \$300x)) \times \$300x)$.

Example 10. Determination of initial and last measurement date RPI when related party indebtedness arises in connection with or as a result of a transaction. (i) *Facts.* The facts are the same as in *Example 3*, except that in connection with or as a result of USB's purchase of the stock of US1 (and indirectly CFC1), US1 lends CFC1 \$50x.

(ii) *Result.* With respect to the USP group, the initial measurement date RPI and the last measurement date RPI are the same as in *Example 3*. The USB group's initial measurement date RPI and last measurement RPI are affected. Without regard to the acquisition of US1, the USB group's initial measurement date RPI is \$0. However, under section 7.05(c), the USB group increases its initial measurement date RPI by \$100x, the amount of the related party indebtedness of its CFC (CFC1) immediately after the transaction, but excluding the indebtedness arising in connection with, or as a result of, the transaction. The USB group's last measurement date RPI, however, is \$150x because as of its last measurement date, CFC1 owes \$150x to US1, a related person. Therefore, under section 7.04 of this notice and section 965(b)(3), the USB group reduces its dividends otherwise eligible for the section 965(a) DRD by \$50x.

SECTION 8. EFFECT OF CERTAIN TRANSACTIONS ON DOMESTIC REINVESTMENT PLANS

.01 In General

This section addresses the effect of certain transactions on domestic reinvestment plans adopted pursuant to section 965(b)(4) and Notice 2005-10. Section 8.02 of this notice addresses the effect of members entering and exiting a consolidated group. Section 8.03 addresses the effect of certain asset acquisitions. Section 8.04 then provides rules that apply to a corporation that may make permitted investments pursuant to more than one domestic reinvestment plan. Finally, section 8.05 of this notice provides reporting and administrative requirements for transactions addressed by this section 8.

.02 Members Entering and Exiting a Consolidated Group

A consolidated group may rely on any domestic corporation (regardless of whether such corporation is a U.S. shareholder) to fulfill the group's obligations to make permitted investments under a domestic reinvestment plan if that corporation is a member of the group at any time on or after the first day of the group's election year. For example, if a consolidated group adopts a domestic reinvestment plan and a member leaves the group during or after the group's election year, the group may rely on the former member's subsequent domestic investment activity to satisfy the group's obligations under its domestic reinvestment plan. Similarly, if a domestic corporation joins a consolidated group during or after the first day of the group's election year, the group may rely on the new member's domestic investment activity after it joins the group to satisfy the group's obligations under its domestic reinvestment plan. The rules of this paragraph apply regardless of the amount of cash or property held by the former member or new member at the time it leaves or joins the consolidated group, as the case may be.

In addition, a domestic corporation may rely on any other domestic corporation (regardless of whether such corporation is a U.S. shareholder) to fulfill its obligations to make permitted investments under a domestic reinvestment plan if both corpora-

tions are members of the same consolidated group at the time the investment is made, even if they were not members of the same consolidated group during the corporation's election year. For example, if a corporation adopts a domestic reinvestment plan and the corporation joins a consolidated group after the end of the corporation's election year, the acquired corporation may rely on the subsequent domestic investment activity of any member of the acquiring consolidated group to satisfy the corporation's obligations under its domestic reinvestment plan. Similarly, if a consolidated group adopts a domestic reinvestment plan and the group is acquired by another consolidated group after the acquired group's election year, the acquired group may rely on the subsequent domestic investment activity of any member of its new consolidated group to satisfy the acquired group's obligations under its domestic reinvestment plan.

.03 Asset Acquisitions

In general, if a corporation acquires assets of another corporation, the acquiring corporation will not succeed to the obligations of the transferor corporation under a domestic reinvestment plan, and investments made by the acquiring corporation therefore are not eligible to satisfy such domestic reinvestment plan. However, if the corporation acquires the assets of a transferor corporation in a transaction described in section 381(a), subsequent investments made by the acquiring corporation (or by members of the acquiring corporation's consolidated group) therefore may be eligible to satisfy the transferor's domestic reinvestment plan.

If, prior to the transaction described in section 381(a), the acquiring corporation was also required or permitted to make permitted investments in order to satisfy a domestic reinvestment plan, the acquiring corporation will continue to be required or permitted to satisfy obligations under that domestic reinvestment plan in addition to any obligations under the transferor's domestic reinvestment plan.

.04 Designation of Permitted Investment Activity

A single corporation may be able to make permitted investments in satisfaction of more than one domestic reinvestment

plan. However, the same expenditure of funds may not satisfy the investment requirement of more than one domestic reinvestment plan. For example, a single \$100x investment made by an acquired domestic corporation cannot be counted toward the investment requirements of both the selling consolidated group and the acquiring consolidated group. If a permitted investment by a corporation would satisfy the investment requirement of more than one domestic reinvestment plan, the corporation may designate which plan is being satisfied. If a corporation fails to so designate, its domestic investment activities will be treated as fulfilling domestic reinvestment plan obligations in the following order: first, under any plan adopted with respect to its own earliest election year; second, under any plan adopted with respect to its own subsequent election years, if any; and third, with respect to any plan adopted with respect to any other corporation (for example, a transferor in a transaction described in section 381(a) or a consolidated group the corporation later joined) in the order the corporation became required or permitted to make investments in satisfaction of such plan.

.05 Reporting and Other Administration Requirements under Section 8 of Notice 2005-10

If a former member of a consolidated group contributes to the completion of the group's domestic reinvestment plan (in whole or in part), the obligation to comply with the reporting and other administrative requirements contained in section 8 of Notice 2005-10 will remain with the group if such group continues to exist, or otherwise with the common parent (or successor agent) for the election year, or the common parent of any consolidated group that includes such former common parent (or successor agent).

.06 Examples

The following examples illustrate the application of section 965(b)(4) and this section 8. Unless otherwise indicated, the following facts are assumed for purposes of these examples: USP is a domestic corporation and the common parent of a consolidated group that uses the calendar year as its taxable year. USP wholly owns

US1 and US2, which are domestic corporations and members of the USP consolidated group. US1 and US2 each wholly owns a foreign corporation, CFC1 and CFC2, respectively. The USP group elects to apply section 965 for its taxable year ending December 31, 2005. The domestic reinvestment plan approved pursuant to section 965(b)(4) and Notice 2005-10 on behalf of the USP group requires that an amount of cash equal to the \$100x cash dividends that are received from the USP group's CFCs will be invested in the United States to fund research and development activities (performed in the United States) of the USP group over a two-year period. On December 31, 2005, CFC1 and CFC2 each distributes \$50x of dividends that are eligible for the section 965(a) DRD.

Example 1. Member exiting a consolidated group. (i) *Facts.* On July 1, 2006, all of the stock of US2 is acquired for cash by USB, a domestic corporation and the common parent of the USB consolidated group. Any permitted investments required to be made by the USB group under any domestic reinvestment plan (other than that of the USP group) are made prior to June 30, 2006. Between July 1, 2006 and December 31, 2007, US2 funds \$100x of research and development activities.

(ii) *Result.* Because US2 is a member of the USP group after the beginning of the USP group's election year, US2's funding of \$100x of research and development activities made while it is a member of the USB group will satisfy the USP group's obligations to make such permitted investments specified under the USP group's domestic reinvestment plan. However, the USP group satisfies the reporting and administrative requirements contained in section 8 of Notice 2005-10 with respect to such investment.

Example 2. Member entering a consolidated group. (i) *Facts.* On March 31, 2006, USP acquires for cash all the stock of US3, a domestic corporation that is not a member of a consolidated group. US3 elected to apply section 965 to its taxable year ending December 31, 2005. US3's domestic reinvestment plan requires that US3 expend \$5x to compensate existing employees for services performed in the United States over a two-year period. Between April 1, 2006 and December 31, 2007, US3 funds \$100x of research and development activities. During the same period, US2 expends \$5x to compensate existing employees for services performed in the United States.

(ii) *Result.* Because US3 is a member of the USP group after the beginning of the USP group's election year, US3's funding of \$100x of research and development activities after joining the group will satisfy the USP group's obligations to make such specified permitted investments under the USP group's plan. In addition, because US2 is a member of the same consolidated group as US3 when it expends \$5 to compensate existing employees for services performed in the United States (a permitted investment pursuant to section 965(b)(4) and Notice 2005-10),

US3 may rely on US2's expenditure to satisfy its obligation specified under its plan. USP is required to satisfy the administrative requirements with respect to investments under US3's plan.

Example 3. Asset acquisition of U.S. shareholder.

(i) *Facts.* The facts are the same as in *Example 2*, except that instead of USP acquiring the stock of US3, US3 merges into US2 in a reorganization under section 368(a)(1)(A) and (a)(2)(D) on March 31, 2006, after which US2 remains a member of the USP group. Between April 1, 2006 and December 31, 2007, US2 funds \$100x of research and development activities and pays \$5x to compensate existing employees for services performed in the United States.

(ii) *Result.* Because US2 acquired the assets of US3 in a transaction to which section 381(a) applies, US2 succeeded to US3's domestic reinvestment plan obligations. US2's payment of \$5x to compensate existing employees for services performed in the United States satisfies its obligation to make a permitted investment specified under US3's plan. The USP group may also rely on US2's funding of \$100x of research and development activities to satisfy the USP group's plan obligations. The result would be the same if, after the merger of US3 into US2, US1, instead of US2, paid \$5x to compensate existing employees for services performed in the United States, because US1 is a member of the same consolidated group as US2 and the compensation is a permitted investment pursuant to section 965(b)(4) and Notice 2005-10.

Example 4. Failure to designate sufficient investment activity to fulfill multiple domestic reinvestment plans.

(i) *Facts.* The facts are the same as in *Example 2*, except that US3's plan also required US3 to expend \$5x to fund research and development activities over a two-year period. The USP group fails to designate specific investment activities for purposes of section 8.04 of this notice to satisfy either the USP group domestic reinvestment plan or the US3 domestic reinvestment plan. Between March 31, 2006 and December 31, 2007, US3 funds \$5x of research and development activities and US2 funds \$95x of research and development activities.

(ii) *Result.* Because the USP group failed to designate specific investment activities to satisfy US3's and the USP group's domestic reinvestment plans, US3's permitted investments will first be taken into account under the US3 plan, and US2's permitted investments will first be taken into account under the USP group plan. Consequently, US3's \$5x expenditure will satisfy the US3 plan and cannot be taken into account by the USP group to satisfy its obligation to conduct \$100x of research and development activities. As a result, the USP group will have conducted only \$95x of research and development activities and the USP group's 2005 qualifying dividend is reduced by \$5x. If instead, US3 had merged into US2 on March 31, 2006, as in *Example 3*, and US2 spent the \$100x without designating, all \$100x would have satisfied the USP domestic reinvestment plan. In addition, the US3 plan would fail to have been satisfied, resulting in a \$5x reduction in US3's qualifying dividends.

SECTION 9. OTHER GUIDANCE

.01 Section 78 Gross-Up, Disallowance of Expenses Pursuant to Section 965(d)(2),

and Computation of Alternative Minimum Tax in Election Year

Section 78 does not apply to any tax which is not allowable as a credit under section 901 by reason of section 965(d).

The disallowance of expenses in section 965(d)(2) applies only to expenses that are "directly allocable" to the deductible portion described in section 965(d)(1).

For purposes of calculating alternative minimum tax for the election year under section 55(a) in accordance with section 965(e)(1)(B), the taxpayer's regular tax described in section 55(c) and tentative minimum tax determined under section 55(b)(1)(B) do not include tax attributable to nondeductible CFC dividends.

The IRS and Treasury will incorporate the rules in this section 9.01 into subsequent guidance. This subsequent guidance will provide detail regarding these and related rules.

.02 Contiguous Country Branches of Domestic Life Insurance Companies

Amounts added to the life insurance company taxable income of a domestic life insurance company by reason of section 814(e)(2) (dealing with contiguous country branches of a domestic life insurance company) are not eligible for the section 965(a) DRD.

.03 Cash Dividends in Excess of Amounts Covered by Domestic Reinvestment Plans

A domestic reinvestment plan may provide for the investment in the United States of an amount that is less than the entire amount of cash dividends that are otherwise eligible for the section 965(a) DRD. In such a case, the section 965(a) DRD applies only to the amount of eligible dividends that are reinvested pursuant to the plan (assuming that all the other requirements under section 965 are satisfied).

.04 Section 958(a) Chain of Ownership — Stock Deemed Issued Pursuant to Section 304(a)(1)

If stock of an acquiring CFC is deemed to be issued to another CFC pursuant to section 304(a)(1), the acquiring CFC is treated as being in a chain of ownership described in section 958(a) for purposes of applying section 965(a)(2).

The following example illustrates the application of section 965(a)(2) and this section 9.04:

Example. (i) *Facts.* USP, a domestic corporation, wholly owns two foreign corporations, CFC1 and CFC2. CFC1 wholly owns a foreign corporation, CFC3. CFC2 has \$100x of current and accumulated earnings and profits described in sections 304(b)(5)(A) and 959(c)(3). During USP's section 965 election year, CFC1 sells all its CFC3 stock to CFC2 for \$100x. Also during USP's election year, CFC1 distributes \$100x to USP that is excluded from gross income under section 959(a).

(ii) *Result.* Because CFC1 is in control of both CFC3 and CFC2 and receives property from CFC2 in exchange for its CFC3 stock, CFC1's sale of CFC3 stock to CFC2 is subject to section 304(a)(1). Accordingly, CFC1 is treated as receiving \$100x as a distribution in redemption of CFC2 stock. Because CFC1 actually owns 100% of CFC3 before the sale and is treated as owning 100% of CFC3 after the sale, pursuant to section 302(d), section 302(a) does not apply to the deemed redemption distribution and the proceeds of the deemed redemption are treated as a distribution to which section 301 applies. Therefore, CFC1 is treated as transferring its CFC3 stock to CFC2 in exchange for CFC2 stock in a transaction to which section 351(a) applies. The CFC2 stock CFC1 is treated as receiving in the deemed section 351 exchange is then treated as redeemed by CFC2 for \$100x. Under section 302, that redemption is treated as a distribution to which section 301 applies because CFC1 owns directly 100% of CFC3 before the redemption of the CFC2 stock that was deemed issued and is treated as owning 100% of CFC3 after the redemption. The deemed redemption proceeds are treated as a distribution to which section 301 applies, and CFC1 is treated as receiving a dividend of \$100x from the current and accumulated earnings and profits of CFC2. For purposes of section 965(a)(2), because CFC1 is treated under section 304(a)(1) as receiving CFC2 stock in the deemed section 351 exchange, CFC1 is treated as receiving the \$100x dividend from another CFC that is in a chain of ownership described in section 958(a).

.05 Acquisitions of Interests in Business Entities — Modification of Section 5.06 of Notice 2005-10

Section 5.06 of Notice 2005-10 provides, in part, that in valuing assets with respect to certain acquisitions of interests in business entities, the taxpayer must use the same methodology that it uses, under section 864(e) and Treas. Reg. §1.861-9T(g) (that is, tax book value, alternative tax book value, or fair market value), for purposes of allocating and apportioning its interest expense for the taxable year. Notwithstanding that section of Notice 2005-10, the Treasury Department and the IRS have decided that taxpayers may elect to use the fair market value methodology under Treas. Reg. §1.861-9T(g)

for purposes of valuing assets pursuant to section 5.06 of Notice 2005–10, even if they use the tax book value or alternative tax book value methodology for purposes of allocating and apportioning interest expense under section 864(e). Such election is made on the annual report (required under section 8.02(a) of Notice 2005–10) filed by the taxpayer for the taxable year of the acquisition.

.06 Distributions to Intermediary Disregarded Entities — Clarification of Section 3.02 of Notice 2005–10

Section 3.02 of Notice 2005–10 provides that for purposes of section 965(a), a cash dividend paid by a CFC to a pass-through entity that is owned by a U.S. shareholder is treated as received by such U.S. shareholder only if and to the extent that such shareholder receives cash in the amount of the CFC dividend during the taxable year for which such election is in effect. For this purpose, a disregarded entity need not actually distribute cash to a U.S. shareholder of the CFC, provided that the U.S. shareholder otherwise receives the cash from the disregarded entity and there is no legal obligation for the U.S. shareholder to repay the cash to the disregarded entity.⁷ For purposes of the preceding sentence, the term U.S. shareholder is defined in section 951(b).

Example. (i) *Facts.* USP, a domestic corporation, wholly owns DE, a disregarded entity. DE wholly owns CFC, a foreign corporation. Since Year 1, USP has held a \$200x obligation of DE. CFC pays a \$100x dividend to DE during Year 3, USP's election year. Also during Year 3, DE repays \$100x of its obligation to USP.

(ii) *Result.* The \$100x dividend paid by CFC is paid to DE, a pass-through entity that is owned by USP. As a result, pursuant to section 3.02 of Notice 2005–10, such dividend is treated as a cash dividend for purposes of section 965 only if and to the extent that USP receives \$100x from DE during Year 3 without an obligation to repay those funds to DE. DE's repayment of \$100x of its \$200x obligation held by USP satisfies this requirement, and the \$100x dividend paid by CFC during the election year therefore qualifies as a cash dividend for purposes of section 965. The result is the same regardless of whether the \$100x repayment by DE is of principal, accrued interest, or both.

(iii) *Alternative Facts.* The facts are the same except that instead of using the \$100x to satisfy a portion of an obligation held by USP, DE uses the \$100x cash to acquire an asset from USP. The result is the same.

SECTION 10. REPORTING AND OTHER ADMINISTRATIVE REQUIREMENTS

Pursuant to section 6001, the taxpayer must prepare, maintain, and, upon a request by the Commissioner, make available within 30 days of such request, a general description of any transaction that results in: (1) an adjustment to base period inclusions or APB 23 amounts pursuant to section 6 of this notice; (2) an adjustment to initial measurement date RPI pursuant to section 7 of this notice; or (3) a permitted investment being made by a U.S. shareholder that, at the time of such investment, is not a member of the consolidated group that adopted the domestic reinvestment plan pursuant to which such investment is made, as provided under section 8 of this notice. The description must include, as applicable, the name, address, and tax identification number (if available), of all parties relevant to the transaction (for example, selling group, departing or joining member, and acquiring group). In addition, it must include all relevant dates and the amount of adjustments resulting from the transactions.

In addition, pursuant to section 6001, the taxpayer must prepare, maintain, and, upon a request by the Commissioner, make available within 30 days of such request: (1) a list of investments that may satisfy more than one domestic reinvestment plan and the taxpayer designation of which plan the investment satisfies; and (2) those domestic corporations that have participated in more than one election year.

In the case of an adjustment to base period inclusions pursuant to section 6 of this notice, such adjustments may be determined by reference to the separate Form 1120 prepared for the departing U.S. shareholder for the base period years in question, without regard to the fact that the separate Form 1120 does not constitute a processed return, and was prepared to determine the consolidated return of the group of which it was a member.

SECTION 11. TRANSITION RULES

.01 Domestic Reinvestment Plans Approved Prior to May 10, 2005

If a domestic reinvestment plan is approved prior to May 10, 2005, the taxpayer may modify such plan to take into account the guidance herein not later than July 11, 2005, even if the dividend to which the domestic reinvestment plan relates has already been paid. Any plan that is so modified must be subsequently approved by the taxpayer's president, chief executive officer, or comparable official, and by the taxpayer's board of directors, management committee, executive committee, or similar body.

.02 Tax Returns filed Prior to May 10, 2005

If, prior to May 10, 2005, a taxpayer has filed its tax return for the taxable year for which it acquires an interest in a business entity that qualifies, in whole or in part, as a permitted investment pursuant to section 5.06 of Notice 2005–10, such taxpayer may make the election to use the fair market value methodology pursuant to section 9.05 of this notice with respect to such acquisition on an amended tax return that is filed on or before December 31, 2005.

SECTION 12. EFFECT OF THIS NOTICE ON OTHER DOCUMENTS

Sections 9.05 and 9.06 of this notice modify section 5.06 and clarify section 3.02 of Notice 2005–10, respectively. See also section 11 of this notice, pursuant to which domestic reinvestment plans approved prior to May 10, 2005 (including domestic reinvestment plans adopted or modified pursuant to the guidance included in Notice 2005–10), may be modified to take into account the guidance in this notice.

SECTION 13. EFFECTIVE DATE

This notice is effective for the taxable year for which taxpayers have elected section 965 to apply, and other taxable years as relevant.

⁷ See section 3.02 of Notice 2005–10 (providing that a loan of cash from the disregarded entity to the U.S. shareholder is not considered a distribution of cash for this purpose because there is a legal obligation for the U.S. shareholder to repay the cash to the disregarded entity).

SECTION 14. PAPERWORK REDUCTION ACT

The collections of information contained in this notice have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number [1545-1943].

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

The collections of information are in sections 5, 8, 9, 10, and 11 of this notice. This information is required to provide the IRS sufficient information to determine whether a taxpayer has properly elected to apply section 965 to a taxable year and whether the taxpayer has properly determined the maximum amount of cash dividends eligible for the DRD under section 965(a), taking into account the limitations on the DRD that are imposed by section 965(b)(1), (b)(2), and (b)(3). The collections of information are required to obtain the benefit of section 965 for a taxable year. The likely respondents are business corporations.

Estimated total annual reporting and/or recordkeeping burden: 1,250,000 hours.

Estimated average annual burden hours per respondent: 50 hours.

Estimated number of respondents: 25,000.

Estimated annual frequency of responses: on occasion and annually.

The collections of information contained in this notice 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 received by June 9, 2005. Comments are specifically requested concerning:

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

The accuracy of the estimated burden associated with the proposed collections of information (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 services to provide information.

Comments concerning the accuracy of the burden estimate and suggestions for reducing the burden of the final or temporary regulations 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, W:CAR:MP:T:T:SP, Washington, DC 20224.

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.

SECTION 15. DRAFTING INFORMATION

The principal authors of this notice are Jeffrey L. Vinnik of the Office of Associate Chief Counsel (International) and Krishna P. Vallabhaneni, formerly of the Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and the Treasury Department participated in its development. For further information regarding this notice, contact Mr. Vinnik at (202) 622-3840 (not a toll-free call).

NOTE: This revenue procedure will be reproduced as the next revision of IRS Publication 1516, *Specifications for Filing Form 8596, Electronically or Magnetically.*

Use this revenue procedure to prepare Tax Year 2005 and prior year information returns for submission to Internal Revenue Service (IRS) using any of the following:

- Electronic Filing
- Tape Cartridge

NOTE:

Following is a list of related forms for filing Information Returns Electronically/Magnetically:

Form 4419 — Application for Filing Information Returns Electronically/Magnetically

Form 4804 — Transmittal of Information Returns Reported Magnetically

Notice 210 — Preparation Instructions for Media Label

These forms can be obtained by calling 1-800-TAX-FORM (1-800-829-3676). You can also download forms and publications from the IRS Web Site at www.irs.gov.

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PART A. GENERAL

Sec. 1. Purpose

.01 Section 6050M of the Internal Revenue Code, which was added by section 1522 of the Tax Reform Act of 1986 (Public Law 99-514) and amended by section 1015(f) of the Technical and Miscellaneous Revenue Act of 1988 (Public Law 100-647), requires Federal Executive Agencies to file an information return with the Internal Revenue Service (IRS) reporting the name, address and Taxpayer Identification Number (TIN) of each person and/or corporation with whom the agency enters into a contract, together with any other information required by Treasury regulations.

.02 The purpose of this revenue procedure is to provide the specifications for filing Form 8596, Information Return for Federal Contracts, and Form 8596-A, Quarterly Transmittal of Information Returns for Federal Contracts, with IRS electronically through the Filing Information Returns Electronically (FIRE) System or magnetically, using IBM 3480, 3490, 3490E, 3590, or 3590E tape cartridges.

.03 *This revenue procedure applies to Federal Executive Agencies, United States Postal Service and the Postal Rate Commission with respect to reporting their contracts and contract increases in excess of \$25,000. Federal Executive Agencies may be required to report the same contract information to the Federal Procurement Data Center (FPDC) and therefore are permitted to make an election to have the FPDC file with the Internal Revenue Service on their behalf. If the election is made by the Federal Executive Agency it must be made by the head of the Agency (or his or her delegate). The agency must not file directly with IRS. See Part A, Section 5. Please read this revenue procedure carefully.*

.04 This Revenue Procedure supersedes Rev. Proc. 99-9, reprinted as Publication 1516 (Rev. 1-99), Specifications for Filing Forms 8596, Information Returns for Federal Contracts on Magnetic Tape, Tape Cartridge, 5¼ and 3½-inch Diskettes. Use this Revenue Procedure for filing Forms 8596 electronically or magnetically for the quarter beginning October 2005.

Sec. 2. Nature of Changes

a. General

.01 Extensive revisions were made to this publication. Please review the entire publication carefully. Only the major changes are listed here.

.02 The name Martinsburg Computing Center was changed to Enterprise Computing Center-Martinsburg (ECC-MTB).

.03 Electronic filing of Form 8596 is available on the internet at <http://fire.irs.gov>. Please review Part B to learn how to quickly and easily file Form 8596 electronically.

.04 Magnetic tape, 8mm, 4mm, Quarter Inch Tape Cartridges and diskettes are no longer acceptable media for submitting Form 8596 to IRS/ECC-MTB.

.05 Section 9, How to File Corrected Returns, was completely revised. Please read carefully.

.06 Section 12, Definition of Terms, was deleted. See current Instructions for Form 8596.

.07 Information in Section 11, Effect on Paper Document and Section 14, Effective Date was moved to other Sections. Sections 11 and 14 were deleted.

.08 The title of Publication 1516 was changed to Specifications for Filing Form 8596, Electronically/Magnetically.

b. Programming Changes

.01 A Record Sequence Number in positions 500 – 507 was added to all record layouts, “T”, “A”, “B”, “C”, “F”.

c. Programming Changes — Transmitter “T” Record

.01 Contact’s Email Address was added to positions 359-393.

.02 Magnetic Tape File Indicator was renamed Tape Cartridge File Indicator and was moved to positions 394-395.

.03 Electronic File Name for a Replacement File was added to positions 396-410.

.04 Transmitter’s Media Number was added to positions 411-416.

d. Programming Changes — Payer “A” Record

.01 Correction File Indicator was added to position 50.

e. Programming Changes — Payee “B” Record

.01 Corrected Return Indicator was added to position 6.

Sec. 3. Where to File and How to Contact the IRS Enterprise Computing Center-Martinsburg

.01 All information returns filed electronically or magnetically are processed at IRS/ECC-MTB. Files containing information returns and requests for IRS electronic and magnetic media filing information should be sent to the following address:

IRS-Enterprise Computing Center-MTB
Information Reporting Program
230 Murall Drive
Kearneysville, WV 25430

.02 Telephone inquiries for the Information Reporting Program Customer Service Section may be made between 8:30 a.m. and 4:30 p.m. Eastern time, Monday through Friday.

.03 The telephone numbers for magnetic media inquiries or electronic submissions are:

Information Reporting Program Customer Service Section

TOLL-FREE 1-866-455-7438 or outside the U.S. 1-304-263-8700

email at mccirp@irs.gov

**304-267-3367 — TDD
(Telecommunication Device for the Deaf)**

**304-264-5602 — Fax Machine
Electronic Filing — FIRE system**

<http://fire.irs.gov>

TO OBTAIN FORMS:

1-800-TAX-FORM (1-800-829-3676)

www.irs.gov — IRS Website access to forms

Sec. 4. Form 4419, Application for Filing Information Returns Electronically/Magnetically

.01 Transmitters are required to submit Form 4419, Application for Filing Information Returns Electronically/Magnetically, to request authorization to file information returns with IRS/ECC-MTB. A single Form 4419 should be filed no matter how many types of returns the transmitter will be submitting electronically/magnetically. For example, if a transmitter plans to file Forms 8596, one Form 4419 should be submitted. If, at a later date, another type of form (Forms 1098, 1099, 5498 and W-2G) is to be filed, the transmitter does not need to submit a new Form 4419.

Note: EXCEPTIONS — An additional Form 4419 is required for filing each of the following types of returns: Form 1042-S, Foreign Person’s U.S. Source Income Subject to Withholding, Form 8027, and Employer’s Annual Information Return of Tip Income and Allocated Tips. See the back of Form 4419 for detailed instructions.

.02 Tape cartridges and electronically filed returns may not be submitted to IRS/ECC-MTB until the application has been approved. Please read the instructions on the back of Form 4419 carefully. Forms may be obtained by calling **1-800-TAX-FORM (1-800-829-3676)**. The form is also available on the IRS website at **www.irs.gov**. This form may be photocopied.

.03 Upon approval, a five-character alpha/numeric Transmitter Control Code (TCC) will be assigned and included in an approval letter. The TCC **must** be coded in the Transmitter “T” Record. IRS/ECC-MTB uses the TCC to identify payers/transmitters and to track their files through the processing system. The same TCC can be used regardless of the method of filing. For example, a payer may send their production data on a tape cartridge and then later submit a correction file electronically. The same TCC can be used for each filing.

.04 Form 4419 may be submitted anytime during the year; however, it **must** be submitted to IRS/ECC-MTB at least 30 days before the due date of the return(s) for current year processing. This will allow IRS/ECC-MTB the minimum amount of time necessary to process and respond to applications.

.05 Once a transmitter is approved to file electronically/magnetically, it is not necessary to reapply **unless**:

- (a) The payer has discontinued filing electronically or magnetically for two consecutive years. The payer's TCC may have been reassigned by IRS/ECC-MTB. Payers who are aware that their TCC will no longer be used are requested to notify IRS/ECC-MTB so these numbers may be reassigned.
- (b) The payer's files were transmitted in the past by a service bureau using the service bureau's TCC, but now the payer has computer equipment compatible with that of IRS/ECC-MTB and wishes to prepare his or her own files. The payer must request a TCC by filing Form 4419.

.06 If **any** of the information (name, TIN or address) on Form 4419 changes, please notify IRS/ECC-MTB in writing so the IRS/ECC-MTB database can be updated. You may use our email address, mccirp@irs.gov, for basic name and address changes. Due to security concerns IRS/ECC-MTB discourages sending TIN information via email. A change in the method by which information returns are submitted is not information that needs to be updated (e.g., tape cartridge to electronic). The transmitter should include the TCC in all correspondence.

.07 Approval to file does not imply endorsement by IRS/ECC-MTB of any computer software or of the quality of tax preparation services provided by a service bureau or software vendor.

Sec. 5. Filing Requirements

.01 The requirements for Federal Contracts are governed by section 6011(e)(2)(A) and section 6050M of the Internal Revenue Code and Regulation section 1.6050M-1. *The term Federal Executive Agency means — (1) any Executive Agency (as defined in Section 105 of title 5, United States Code) other than the General Accounting Office; (2) any military department as defined in section 102 of such title; and (3) the United States Postal Service and the Postal Rate Commission.* A Federal Executive Agency that files 250 or more reportable contracts during a one year period, must file Form 8596 on an electronic/magnetic file for each quarter of that one year period.

.02 The information returns required by this section with respect to contracts of a Federal Executive Agency entered into on or after January 1, 1989, must be filed on a quarterly basis for the calendar quarters ending on the last day of March, June, September, and December, on or before the last day of the month following that quarter for which the returns are being made.

.03 The information returns required by this section may be made in one submission or in multiple submissions.

.04 If a Federal Executive Agency has reasonable expectations to enter into fewer than 250 reportable contracts during a one year period, the agency may file paper Forms 8596 and 8596-A with the IRS Kansas City Service Center, Kansas City, MO 64999-2222.

.05 Election to have the Director of the Federal Procurement Data Center file returns on behalf of an agency. Except for the U.S. Postal Service and the Postal Rate Commission, a Federal Executive Agency may elect to have the Director of the Federal Procurement Data Center (FPDC) file the required returns with IRS on behalf of the agency. The agency must comply with the requirements of the Federal Procurement Data System (FPDS) in submitting the information and must not file with the Internal Revenue Service.

.06 In order to make this election, the head of a Federal Executive Agency (or his or her delegate) shall attach a signed statement to its submission to the FPDC for that quarter stating the following:

- (a) The Director of the FPDC (or his or her delegate) is authorized to submit the required returns on behalf of the agency for contracts for that quarter in accordance with an election under 26 CFR, section 1.6050M-1(d)(5).
- (b) Under the penalties of perjury, the official has examined the information submitted by the agency to the FPDC who will submit the returns to IRS. The official certifies that information to be, to the best of his or her knowledge and belief, an accurate compilation of agency records maintained in the normal course of business for the purpose of making true, correct, and complete returns as required by section 6050M.

.07 An agency that elects to have the FPDC file its returns must not submit those same returns to the IRS.

.08 If a contract is increased by more than \$25,000 under one action, the action should be treated as a new contract and reported to IRS for the calendar quarter in which the increase occurs. This could occur through the exercise of an option contained in a basic or initial contract or under any other rule of contract law, expressed or implied, when the amount of money or other property obligated under the contract is increased by \$25,000.

.09 Special rules to filing requirements are as follows:

- (a) If a subcontract is entered into by the Small Business Administration (SBA) under a prime contract between SBA and a procuring agency pursuant to section 8(a) of the Small Business Act, the procuring agency, not the SBA, will be required to file Forms 8596 and 8596-A.
- (b) A Federal Supply Schedule Contract or an Automated Data Processing Schedule Contract entered into by the General Service Administration (GSA), or a scheduled contract entered into by the Department of Veterans Affairs (VA) on behalf of one or more Federal Executive Agencies, is not to be reported by the GSA or VA at the time of execution. When a Federal Executive Agency, including the GSA or the VA, places an order under a schedule contract, the Federal Executive Agency must file Forms 8596 and 8596-A.

.10 Exceptions: The following are not required to be reported under section 6050M:

- (a) Any contract action of \$25,000 or less;

- (b) Any contract which provides that all amounts payable under the contract by a Federal Executive Agency will be paid on or before the 120th day following the date of the contract action and for which it is reasonable to expect that all amounts will be so paid;
- (c) A license granted by a Federal Executive Agency;
- (d) An obligation of a contractor (other than a Federal Executive Agency) to a subcontractor;
- (e) Debt instruments of the U.S. Government or a Federal agency, such as Treasury Notes, Treasury Bonds, Treasury Bills, U.S. Savings Bonds, or similar instruments;
- (f) An obligation of a Federal Executive Agency to lend money, lease property to someone, or sell property;
- (g) A blanket purchase agreement. However, when an order is placed under a blanket purchase agreement, a contract then exists and Forms 8596 and 8596-A must be filed;
- (h) Any contract with a contractor who, in making the agreement, is acting in his or her capacity as an employee of a Federal Executive Agency (e.g., any contract of employment under which the employee is paid wages subject to Federal income tax withholding);
- (i) Any contract between a Federal Executive Agency and another Federal Governmental unit or any subsidiary agency;
- (j) Any contract with a foreign government or agency or any subsidiary agency;
- (k) Any contract with a state or local government or agency or any subsidiary agency;
- (l) Any contract with a person who is not required to have a taxpayer identification number, such as a nonresident alien, foreign corporation or foreign partnership, any of which does not have income effectively connected with the conduct of a trade or business in the United States and does not have an office or place of business as a fiscal or paying agent in the United States;
- (m) Certain confidential or classified contracts that meet the requirements of section 6050M(e);
- (n) Any contract that provides that all payments made after the 120th day after the date of the contract action will be made by someone other than a Federal Executive Agency or an agent of such an agency. For example, a contract under which the contractor will collect amounts owed to a Federal Executive Agency for the agency's debtor and will remit to the Federal Executive Agency the money collected less an amount for the contractor's consideration under the contract;
- (o) Contracts entered into using nonappropriated funds.

.11 All paper Forms 8596 and 8596-A for both original and corrected returns should be filed with the IRS Kansas City Service Center, Kansas City, MO 64999-2222. Forms 8596 and 8596-A may be obtained by calling 1-800-TAX-FORM (1-800-829-3676) and via www.irs.gov.

Sec. 6. Filing of Information Returns For Federal Contracts

.01 Form 4804, Transmittal of Information Returns Reported Magnetically, or a computer-generated substitute, must accompany all magnetic media shipments except for replacements, when Form 4804 is not always necessary. IRS/ECC-MTB allows for the use of computer-generated substitutes for Form 4804. The substitutes must contain all information requested on the original forms including the affidavit and signature line. Photocopies are acceptable; however, an original signature is required. When using computer-generated forms, be sure to clearly mark the tax year being reported. This will eliminate a telephone communication from IRS/ECC-MTB to question the tax year.

.02 Copies of Forms 4804 and requests for additional forms related to electronic/magnetic media processing may be obtained by calling 1-800-TAX-FORM (1-800-829-3676).

.03 Paper information returns must be sent to the IRS Kansas City Service Center using Form 8596 and Form 8596-A. **Returns filed on paper forms must not be sent to the IRS/ECC-MTB.**

.04 The affidavit on Form 4804 or the appropriate substitute affidavit set forth in this section must be signed by the head of the Federal Executive Agency (or his or her delegate), or if returns are being made on behalf of the agency by the FPDC, by the Director for the FPDC (or his or her delegate).

To use the substitute affidavit, the transmitter should attach the substitute to the Form 4804 and cross out the affidavit on the original form. The substitute affidavit must include the signature and title of the person signing and the date. The substitute affidavits follow:

(a) Returns made directly with the Internal Revenue Service by the Federal Executive Agency.

“Under the penalties of perjury, I declare that I have examined this transmittal, and accompanying documents, that they are prepared pursuant to the requirement of section 6050M, and, to the best of my knowledge and belief, they are compiled from agency records maintained in the normal course of business for the purpose of making a true, correct, and complete return as required by section 6050M.”

(b) Returns made by the Director of FPDC on an agency's behalf.

“Under the penalties of perjury, I declare that I have examined this transmittal, and accompanying documents, that they are prepared pursuant to the requirement of section 6050M and, to the best of my knowledge and belief, they are compiled from information submitted by the Federal Executive Agency to the FPDC pursuant to section 1.6050M-1(d)(5)(i) for the purpose of making a true, correct, and complete return as required by section 6050M.”

.05 If a Federal Executive Agency elects to have the FPDC make returns on its behalf, the FPDC shall attach a copy of that agency's signed statement, making the election, to the Form 4804 accompanying the magnetic media submission for that agency for that quarter. When filing electronically, mail or fax a copy of the affidavit to IRS/ECC-MTB (see Part A, Sec. 3.)

.06 **The transmitter must not report the same information on paper forms that is reported electronically/magnetically.** If part of the returns are reported on paper and part electronically/magnetically, the transmitter must be sure that duplicate information is not included on both. This does not mean that corrected documents should not be filed. If a return has been prepared and submitted improperly, a corrected return must be filed as soon as possible. See Part A, Sec. 8 for requirements and instructions on filing corrected returns.

.07 When a transmitter submits magnetic media files, the following items must be included:

- (a) A signed Form 4804 or computer generated substitute.
- (b) A self-adhesive external media label, created by the filer, must be affixed to each tape cartridge. For instructions on how to prepare an external media label, refer to Notice 210.
- (c) On the outside of the shipping container, affix or attach a label which reads **IRB Box _____ of _____** reflecting the number of containers in the shipment. If there is only one container, the outside of the package should be marked as Box 1 of 1. For multiple containers, include the sequence (for example, Box 1 of 3, 2 of 3, 3 of 3).

.08 Agencies are required to retain a copy of the information returns filed with IRS for at least three years or have the ability to reconstruct the data.

Sec. 7. Filing Dates

.01 The information returns required by this section must be filed on a quarterly basis for the calendar quarters as follows:

<u>QUARTER</u>	<u>DUE DATE</u>
January, February, March	April 30
April, May, June	July 31
July, August, September	October 31
October, November, December	January 31

.02 The director of the FPDC (or his or her delegate) shall submit the required return quarterly to IRS on or before the earlier date of:

- (a) 45 days following the date that the contract information is required to be submitted to the FPDC, or
- (b) 90 days following the end of the calendar quarter for which the election is made, except that, if the calendar quarter ends September 30, 105 days following the end of that quarter.

.03 If any due date falls on a Saturday, Sunday, or legal holiday, the filing deadline is extended to the next day that is not a Saturday, Sunday, or legal holiday.

Sec. 8. How to File Corrected Returns

- A **correction** is an information return submitted by the transmitter to correct an information return that was previously submitted to and processed by IRS/ECC-MTB, but contained erroneous information.
- **DO NOT SEND YOUR ENTIRE FILE AGAIN.** Only send the information returns in need of correction.
- Information returns omitted from the original file **must not** be coded as corrections. Submit them under a separate Payer "A" Record as original returns.
- Before creating your correction file, review the following guidelines chart carefully.

.01 When corrections are necessary, they must be filed in the next filing quarter. If the entire file that was submitted electronically/magnetically was in error, the IRS/ECC-MTB should be contacted immediately. (See Part A, Sec. 3 for the address)

.02 Corrections should be filed **as soon as possible**. All fields must be completed with the correct information, not just the data fields needing correction. Submit corrections only for the returns filed in error, not the entire file. Furnish corrected statements to recipients as soon as possible.

Note: Do NOT resubmit your entire file as corrections. This will result in duplicate filing and erroneous notices may be sent to payees. Submit only those returns which need to be corrected.

.03 There are numerous types of errors, and in some cases, more than one transaction may be required to correct the initial error. If the original return was filed as an aggregate, the filers must consider this in filing corrected returns.

.04 Corrected returns may be included on the same media as original returns; however, separate "A" Records are required. Corrected returns must be identified on Form 4804 and the external media label by indicating "Correction." If filers discover that certain information returns were omitted on their original file, they must not code these documents as corrections. The file must be coded and submitted as originals.

.05 Review the chart that follows. Errors normally fall under one of the two categories listed. Next to each type of error is a list of instructions on how to file the corrected return.

Guidelines for Filing Corrected Returns Electronically/Magnetically

Error Made on the Original Return

How To File the Corrected Return

Note: References to Form 4804 apply to magnetically filed media only. Form 4804 is not required for files submitted electronically through the FIRE System. One transaction is required to make the following corrections properly. (See Note.)

ERROR TYPE 1

1. Original return was filed with one or more of the following errors:
- (a) Incorrect dollar amount in the Payee "B" Record
 - (b) Incorrect payee address

CORRECTION

- A. Prepare a new Form 4804 that includes information relating to this new file.
 - B. Mark "Correction" in Block 1 of Form 4804.
 - C. Prepare a new file. The first record on the file will be the Transmitter "T" Record.
 - D. Make a separate "A" Record for each payer being reported. Information in the "A" Record may be the same as it was in the original submission. However, remove the "1" (one) in Field Position 48 and set the Correction File Indicator (Field Position, 50) to "1" (one).
 - E. The Payee "B" Records must show the correct record information as well as a Corrected Return Indicator Code of "G" in Field Position 6.
 - F. Corrected returns submitted to IRS/ECC-MTB using "G" coded "B" Records may be on the same file as those returns submitted without the "G" coded "B" Records; however, **separate "A" Records are required.**
 - G. Prepare a separate "C" Record for each payer being reported.
 - H. The last record on the file will be the End of Transmission "F" Record. Indicate "Correction" on the external media label.
-

File layout one step corrections

Transmitter "T" Record	Payer "A" Record	"G" coded Payee "B" Record	"G" coded Payee "B" Record	End of Payer "C" Record	End of Transmission "F" Record
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Guidelines for Filing Corrected Returns Electronically/Magnetically

Error Made on the Original Return

How To File the Corrected Return

Two (2) separate transactions are required to make the following corrections properly. Follow the directions for both Transactions 1 and 2. DO NOT use the two step correction process to correct money amounts.

ERROR TYPE 2

CORRECTION

1. Original return was filed with one or more of the following errors:

- (a) No payee TIN (SSN, EIN, ITIN)
- (b) Incorrect payee TIN
- (c) Incorrect payee name *and address*

Transaction 1: Identify incorrect returns

- A.** Prepare a new Form 4804 that includes information related to this new file.
- B.** Mark "Correction" in Block 1 of Form 4804.
- C.** Prepare a new file. The first record on the file will be the Transmitter "T" Record. Make a separate "A" Record for each type of return and each payer being reported. The information in the "A" Record will be **exactly** the same as it was in the original submission with one exception; remove the "1" from Field Position 48, and set the Correction File Indicator (Field Position 50) to "1" (one).
- D.** The Payee "B" Records must contain **exactly the same** information as submitted previously, **except**, insert a Corrected Return Indicator Code of "G" in Field Position 6 of the "B" Records, and enter "0" (zeros) in all payment amounts.
- E.** Corrected returns submitted to IRS/ECC-MTB using "G" coded "B" Records may be on the same file as those returns submitted with a "C" code; **however, separate "A" Records are required.**
- F.** Prepare a separate "C" Record for each type of return and each payer being reported.
- G.** Continue with Transaction 2 to complete the correction.

Transaction 2: Report the correct information.

- A.** Make a separate "A" Record for each type of return and each payer being reported. Remove the "1" in Field Position 48 and set the Correction File Indicator (Field Position 50), to "1" (one).
 - B.** The Payee "B" Records must show the correct information as well as a Corrected Return Indicator Code of "C" in Field Position 6.
-

Guidelines for Filing Corrected Returns Electronically/Magnetically (Continued)

Error Made on the Original Return	How To File the Corrected Return
	<p>C. Corrected returns submitted to IRS/ECC-MTB using “C” coded “B” Records may be on the same file as those returns submitted with “G” codes; however, separate “A” Records are required.</p> <p>D. Prepare a separate “C” Record for each type of return and each payer being reported.</p> <p>E. The last record on the file will be the End of Transmission “F” Record.</p> <p>F. Indicate “Correction” on the external media label.</p>

File layout **two** step corrections

Transmitter “T” Record	Payer “A” Record	“G” coded Payee “B” Record	“G” coded Payee “B” Record	End of Payer “C” Record	Payer “A” Record
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“C” coded Payee “B” Record	“C” coded Payee “B” Record	End of Payer “C” Record	End of Transmission “F” Record
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Note: If a filer is correcting the name and/or TIN in addition to any errors listed in item 2 of the chart, two transactions will be required. If a filer is reporting “G” coded, “C” coded, and/or “Non-coded” (original) returns on the same media, each category must be reported under separate “A” Records.

Sec. 9. Taxpayer Identification Numbers

.01 Contractors are required to furnish taxpayer identification numbers (TINs) to the agency under section 6109 of the Internal Revenue Code.

.02 The contractor’s TIN and name combination is used to associate information returns reported to IRS with corresponding information on tax returns. It is imperative that **correct** social security number (SSN) or employer identification number (EIN) for contractors be provided to IRS. **Do not enter hyphens or alpha characters.** Entering all zeros, ones, twos, etc., will have the effect of an incorrect TIN.

.03 IRS validates the SSN by using the Name Control of the surname of the individual who has been assigned this number. For this reason, the surname should be provided in the Payee Name Line and/or the Name Control in positions 7-10 of the “B” Record. It is imperative to provide correct information for IRS to validate the SSN. IRS validates an EIN by using the name control of the business to which the EIN has been assigned. If an EIN is reported for a contractor, the correct business name should be provided in the First Payee Name Line and/or Name Control in positions 7-10 of the “B” Record.

.04 For sole proprietors, the owner’s name (not the doing business as (DBA) name) must appear in the Payee Name Line. The TIN for a sole proprietor may be either an EIN or SSN.

.05 The TIN to be furnished to IRS depends primarily upon the manner in which the account is maintained or set up on the agency’s record. The payer and payee names and taxpayer identification numbers should be consistent with the names and numbers used on other tax returns. The TIN must be that of the contractor. If the contract is recorded in more than one name, the transmitter must furnish the TIN and name of one of the contractors. The TIN provided must be associated with the name of the contractor provided in the First Payee Name Line of the Payee “B” Record.

Sec. 10. State Abbreviations

.01 The following state and U.S. territory abbreviations are to be used when developing the state code portion of address fields.

State	Code	State	Code	State	Code
Alabama	AL	Kentucky	KY	No. Mariana Islands	MP
Alaska	AK	Louisiana	LA	Ohio	OH
American Samoa	AS	Maine	ME	Oklahoma	OK
Arizona	AZ	Marshall Islands	MH	Oregon	OR
Arkansas	AR	Maryland	MD	Pennsylvania	PA
California	CA	Massachusetts	MA	Puerto Rico	PR
Colorado	CO	Michigan	MI	Rhode Island	RI
Connecticut	CT	Minnesota	MN	South Carolina	SC
Delaware	DE	Mississippi	MS	South Dakota	SD
District of Columbia	DC	Missouri	MO	Tennessee	TN
Federated States of Micronesia	FM	Montana	MT	Texas	TX
Florida	FL	Nebraska	NE	Utah	UT
Georgia	GA	Nevada	NV	Vermont	VT
Guam	GU	New Hampshire	NH	Virginia	VA
Hawaii	HI	New Jersey	NJ	(U.S.) Virgin Islands	VI
Idaho	ID	New Mexico	NM	Washington	WA
Illinois	IL	New York	NY	West Virginia	WV
Indiana	IN	North Carolina	NC	Wisconsin	WI
Iowa	IA	North Dakota	ND	Wyoming	WY
Kansas	KS				

.02 Filers must adhere to the city, state, and ZIP Code format for U.S. addresses in the “B” Record. This also includes American Samoa, Federated States of Micronesia, Guam, Marshall Islands, Northern Mariana Islands, Puerto Rico, and the U.S. Virgin Islands.

.03 For foreign country addresses, filers may use a 51 position free format which should include city, province or state, postal code, and name of country in this order. This is allowable only if a “1” (one) appears in the Foreign Country Indicator, Field Position 247 of the “B” Record.

.04 When reporting APO/FPO addresses use the following format:

EXAMPLE:

Payee Name	PVT Willard J. Doe
Mailing Address	Company F, PSC Box 100 167 Infantry REGT
Payee City	APO (or FPO)
Payee State	AE, AA, or AP*
Payee ZIP Code	098010100

*AE is the designation for ZIPs beginning with 090–098, AA for ZIP 340, and AP for ZIPs 962–966.

PART B. ELECTRONIC FILING SPECIFICATIONS

Sec. 1. General

.01 Electronic filing of Form 8596 returns, originals, corrections, and replacements is offered as an alternative to magnetic media or paper filing. Filing electronically will fulfill the magnetic media requirements for those payers who are required to file magnetically. There is no minimum of number of forms filing requirement; therefore, any number of forms may be filed electronically. Payers who are under the filing threshold requirement are encouraged to file electronically. If the original file was sent magnetically, but IRS/ECC-MTB has requested a replacement file, the replacement may be transmitted electronically. Also, if the original file was submitted via magnetic media, any corrections may be transmitted electronically.

.02 All electronic filing of information returns are received at IRS/ECC-MTB via the FIRE (Filing Information Returns Electronically) System. To connect to the FIRE System, point your browser to <http://fire.irs.gov>. The system is designed to support the electronic filing of information returns only.

.03 The electronic filing of information returns is not affiliated with any other IRS electronic filing programs. Filers must obtain separate approval to participate in each of them. Only inquiries concerning electronic filing of information returns should be directed to IRS/ECC-MTB.

.04 Files submitted to IRS/ECC-MTB electronically must be in standard ASCII code. Do not send magnetic media with the same information as electronically submitted files. This would create duplicate reporting resulting in penalty notices.

.05 If a Federal Executive Agency elects to have the FPDC make returns on its behalf, the FPDC shall mail or fax a copy of that agency's signed statement, making the election, to IRS/ECC-MTB (see Part A, Sec. 3.)

.06 The record formats of the "T", "A", "B", "C", and "F" records are the same for both electronically or magnetically filed records. See Part D, Record Format Specifications and Record Layouts.

Sec. 2. Advantages of Filing Electronically

Some of the advantages of filing electronically are:

- (1) No Form 4804 requirements.
- (2) Security – Secure Socket Layer (SSL) 128-bit encryption.
- (3) Results available within 1-2 workdays regarding the acceptability of the data transmitted. It is the filer's responsibility to log into the system and check results.
- (4) Allows more attempts than magnetic media filing to replace bad files within a specific time frame before imposing penalties (refer to Part B, Sec. 4.05).
- (5) Better customer service due to on-line availability of transmitter's files for research purposes.

Sec. 3. Electronic Filing Approval Procedure

.01 Filers must obtain a Transmitter Control Code (TCC) prior to submitting files electronically. Filers who currently have a TCC for magnetic media filing may use their assigned TCC for electronic filing. Refer to Part A, Sec. 4, for information on how to obtain a TCC.

.02 Once a TCC is obtained, electronic filers assign their own user ID, password and PIN (Personal Identification Number) and do not need prior or special approval. See Part B, Sec. 5, for more information on the PIN.

.03 If a filer is submitting files for more than one TCC, it is not necessary to create a separate logon and password for each TCC.

.04 For all passwords, it is the user's responsibility to remember the password and not allow the password to be compromised. Passwords are user assigned at first logon and must be 8 alpha/numeric characters consisting of at least 1 uppercase, 1 lowercase, and 1 numeric. However, filers who forget their password or PIN, can call **toll-free 1-866-455-7438** for assistance. The FIRE System may require users to change their passwords on a yearly basis.

Sec. 4. Electronic Submissions

.01 Electronically filed information may be submitted to IRS/ECC-MTB 24 hours a day, 7 days a week. Technical assistance will be available Monday through Friday between 8:30 a.m. and 4:30 p.m. Eastern time by calling **toll-free at 1-866-455-7438**.

.02 **The FIRE System will be down from December 23, 2005, through January 3, 2006.** This allows IRS/ECC-MTB to update its system to reflect current year changes.

.03 If you are sending files larger than 10,000 records electronically, data compression is encouraged. If you are considering sending files larger than 5 million records, please contact IRS/ECC-MTB for specifics. WinZip and PKZip are the only acceptable compression packages. IRS/ECC-MTB cannot accept self-extracting zip files or compressed files containing multiple files. The time required to transmit information returns electronically will vary depending upon the type of connection to the internet and if data compression is used. **The time required to transmit a file can be reduced by as much as 95 percent by using compression.**

.04 Transmitters may create files using self assigned filename(s). Files submitted electronically will be assigned a new unique filename by the FIRE System. The file name assigned by the FIRE System will consist of submission type (ORIG [original], CORR [correction], and REPL [replacement]), the filer's TCC and a four-digit number sequence. The sequence number will be incremented for every file sent. For example, if it is your first original file for the calendar year and your TCC is 44444, the IRS assigned filename would be ORIG.44444.0001. **Record the filename.** This information will be needed by IRS/ECC-MTB to identify the file, if assistance is required.

.05 If a file was submitted timely and is unacceptable, the filer will have up to 60 days from the day the file to transmit an acceptable file. If an acceptable file is not received within 60 days, then the payer could be subject to late filing penalties. This only applies to files originally submitted electronically.

.06 The following definitions have been provided to help distinguish between a correction and a replacement:

- A **correction** is an information return submitted by the transmitter to correct an information return that was previously submitted to and successfully processed by IRS/ECC-MTB, but contained erroneous information. (See Note.)

☛ **Note: Corrections should only be made to records that have been submitted incorrectly, not the entire file.**

- A **replacement** is an information return file sent by the filer because the CHECK FILE STATUS option on the FIRE System indicated the original file was bad. After the necessary changes have been made, the file must be transmitted through the FIRE System. (See Note.)

☛ **Note: Filers should never transmit anything to IRS/ECC-MTB as a “Replacement” file unless the CHECK FILE STATUS option on the FIRE System indicates the file is bad.**

.07 The TCC in the Transmitter “T” Record must be the TCC used to transmit the file; otherwise, the file will be considered an error.

Sec. 5. PIN Requirements

.01 Form 4804 is not required for electronic files. Instead, the user will be prompted to create a PIN consisting of 10 numeric characters when establishing their initial logon name and password.

.02 The PIN is required each time an ORIGINAL, CORRECTION, or REPLACEMENT file is sent electronically and is permission to release the file. An authorized agent may enter their PIN, however, the payer is responsible for the accuracy of the returns. The payer will be liable for penalties for failure to comply with filing requirements. If you forget your PIN, please call **toll-free at 1-866-455-7438** for assistance.

.03 If the file is good, it is released for mainline processing after 10 calendar days from receipt. Contact us **toll-free at 1-866-455-7438** within this 10-day period if there is a reason the file should not be released for further processing. If the file is unacceptable, follow normal replacement procedures.

Sec. 6. Electronic Filing Specifications

.01 The FIRE System is designed exclusively for the filing of Forms 1042-S, 1098, 1099, 5498, 8027, 8596, and W-2G.

.02 A transmitter must have a TCC (see Part A, Sec. 4) before a file can be transmitted. A TCC assigned for magnetic media filing should also be used for electronic filing.

.03 The results of the electronic transmission will be available in the CHECK FILE STATUS area of the FIRE System within 1-2 business days. It is the filer’s responsibility to verify the acceptability of files submitted by selecting the CHECK FILE STATUS option. Forms 1042-S and 8027 require a longer processing time.

Sec. 7. Connecting to the FIRE System

.01 Point your browser to <http://fire.irs.gov> to connect to the FIRE System.

.02 When running Norton Internet Security or similar software, you may need to disable this feature if your file transfer does not complete properly.

.03 Before connecting, have your TCC and EIN available.

.04 Your browser must support SSL 128-bit encryption.

.05 Your browser must be set to receive “cookies”. Cookies are used to preserve your User ID status.

First time connection to The FIRE System (If you have logged on previously, skip to Subsequent Connections to the FIRE System.)

Click “*Create New Account*”.

Fill out the registration form and click “*Submit*”.

Enter your *User ID* (most users logon with their first and last name).

Enter and verify your *password* (the password is user assigned and must be 8 alpha/numerics, containing at least 1 uppercase, 1 lowercase and 1 numeric). FIRE may require you to change the password once a year.

Click “*Create*”.

If you receive the message “*Account Created*”, click “*OK*”.

Enter and verify your 10 digit self-assigned PIN (Personal Identification Number).

Click “*Submit*”.

First time connection to The FIRE System (If you have logged on previously, skip to Subsequent Connections to the FIRE System.)

If you receive the message **“Your PIN has been successfully created!”**, click **“OK”**.
Read the bulletin(s) and/or click **“Start the FIRE application”**.

Subsequent connections to The FIRE System

Click **“Log On”**.
Enter your **User ID** (most users logon with their first and last name).
Enter your **password** (the password is user assigned and is case sensitive).

Uploading your file to the FIRE System

At Menu Options:

Click **“Send Information Returns”**
Enter your **TCC**:
Enter your **EIN**:
Click **“Submit”**.

The system will then display the company name, address, city, state, ZIP code, phone number, contact and email address. This information will be used to contact or send correspondence (if necessary) regarding this transmission. Update as appropriate and/or Click **“Accept”**.

Click one of the following:

Original File
Correction File
Replacement File (if you select this option, select one of the following):
NEW FIRE Replacement (file was originally transmitted on this system)
Click the file to be replaced.

Magnetic Media Replacement
Enter the alpha character from Form 9267, Media Tracking Slip, that was sent with the request for replacement file. Click **“Submit”**.

Enter your 10-digit PIN.
Click **“Submit”**.
Click **“Browse”** to locate the file and open it.
Click **“Upload”**.

When the upload is complete, the screen will display the total bytes received and tell you the name of the file you just uploaded.

If you have more files to upload for that TCC:
Click **“File Another?”**; otherwise,
Click **“Main Menu”**.

It is your responsibility to check the acceptability of your file; therefore, be sure to check back into the system in 1-2 business days using the CHECK FILE STATUS option.

Checking your FILE STATUS

At the Main Menu:

Click **“Check File Status”**.
Enter your **TCC**:
Enter your **EIN**:
Click **“Search”**.

Checking your FILE STATUS

If “Results” indicate:

“Good, Not Released” and you agree with the “Count of Payees”, you are finished with this file. The file will automatically be released after 10 calendar days unless you contact us within this timeframe.

“Good, Released” — File has been released to our mainline processing.

“Bad” — Correct the errors and timely resubmit the file as a “replacement”.

“Not yet processed” — File has been received, but we do not have results available yet. Please check back in a few days.

Click on the desired file for a detailed report of your transmission.

When you are finished, click on **Main Menu**.

Click **“Log Out”**.

Close your Web Browser.

Sec. 8. Common Problems and Questions Associated with Electronic Filing

.01 The following are the major errors associated with electronic filing:

NON-FORMAT ERRORS

1. Transmitter does not check the FIRE System to determine file acceptability.

The results of your file transfer are posted to the FIRE System within two business days. It is your responsibility to verify file acceptability and, if the file contains errors, you can get an online listing of the errors. Date received and number of payee records are also displayed. If the file is good, but you do not want the file processed, you must contact IRS/ECC-MTB within 10 calendar days from the transmission of your file.

2. Incorrect file is not replaced timely.

If your file is bad, correct the file and timely resubmit as a replacement.

3. Transmitter compresses several files into one.

Only compress one file at a time. For example, if you have 10 uncompressed files to send, compress each file separately and send 10 separate compressed files.

4. Transmitter sends a file and CHECK FILE STATUS indicates that the file is good, but the transmitter wants to send a replacement or correction file to replace the original/correction/replacement file.

Once a file has been transmitted, you cannot send a replacement file unless CHECK FILE STATUS indicates the file is bad (1-2 business days after file was transmitted). If you do not want us to process the file, you must first contact us **toll-free at 1-866-455-7438** to see if this is a possibility.

5. Transmitter sends an original file that is good, and then sends a correction file for the entire file even though there are only a few changes.

The correction file, containing the proper coding, should only contain the records needing correction, not the entire file.

6. File is formatted as EBCDIC.

All files submitted electronically must be in standard ASCII code.

7. Transmitter has one TCC number, but is filing for multiple companies, which EIN should be used when logging into the system to send the file?

When sending the file electronically, you will need to enter the EIN of the company assigned to the TCC. When you upload the file, it will contain the EIN's for the other companies that you are filing for. This is the information that will be passed forward.

8. Transmitter sent the wrong file, what should be done?

Call us as soon as possible **toll-free at 1-866-455-7438**. We may be able to stop the file before it has been processed. **Please do not send a replacement for a file that is marked as a good file.**

PART C. MAGNETIC MEDIA SPECIFICATIONS

Sec. 1. General and Replacement Media

.01 All data received at the IRS/ECC-MTB for processing will be given the same protection as individual returns (Form 1040).

.02 Transmitters must ensure that the record format and specifications comply with this revenue procedure. If IRS/ECC-MTB is unable to process your media, replacement media will be requested. IRS/ECC-MTB no longer returns media in need of replacement.

.03 A replacement is an information return file sent by the filer **at the request of IRS/ECC-MTB** because of errors encountered while processing the filer's original file or correction file. After the necessary changes have been made, the entire file must be returned for processing along with the Media Tracking Slip (Form 9267) which was included in the correspondence from IRS/ECC-MTB. (See **Note**.)

Note: Filers should never send anything to IRS/ECC-MTB marked "Replacement" unless IRS/ECC-MTB has requested a replacement file in writing or via the FIRE System.

.04 Magnetic Media filers will receive a Media Tracking Slip (Form 9267), listing, and letter detailing the reason(s) their media could not be processed. It is imperative that filers maintain backup copies and/or recreate capabilities for their information return files. Open all correspondence from IRS/ECC-MTB immediately.

.05 When possible, sample records identifying errors encountered will be provided with the returned information. It is the responsibility of the transmitter to check the entire file for similar errors.

.06 Before sending replacement media, make certain the following items are in place:

- (a) Make the required changes noted in the enclosed correspondence and check entire file for other errors.
- (b) Code Transmitter "T" record, in positions 21–22 for replacement. See Part D, Sec. 2.
- (c) Code Payer "A" record in position 49 with "1" for replacement file. See Part D, Sec. 4.
- (d) Enclose Form 9267, Media Tracking Slip, with your replacement media.
- (e) Label your Media "**Replacement Data**" and indicate the appropriate Tax Year.
- (f) Complete a new Form 4804 **if any of your information has changed**.

.07 Replacement files must be corrected and returned to IRS/ECC-MTB within 45 days from the date of the letter. Refer to Part B, Sec. 4 .05, for procedures for files submitted electronically. A penalty for failure to return a replacement file will be assessed if the files are not corrected and returned within the 45 days **or if filers are notified by IRS/ECC-MTB of the need for a replacement file more than two times**. A penalty for intentional disregard of filing requirements will be assessed if a replacement file is not received.

Note: Replacing electronic files is detailed in Part B, Sec. 4.

.08 Transmitters should be consistent in the use of recording codes and density on files. If the media does not meet these specifications, IRS/ECC-MTB will request a replacement file. Contact IRS/ECC-MTB **toll-free at 1-866-455-7438, extension 5** for further information.

Sec. 2. Tape Cartridge Specifications

.01 In most instances, IRS/ECC-MTB can process tape cartridges that meet the following specifications:

- (a) Must be IBM 3480, 3490, 3490E, 3590, or 3590E.
- (b) Must meet American National Standard Institute (ANSI) standards, and have the following characteristics:
 - (1) Tape cartridges must be 1/2-inch tape contained in plastic cartridges that are approximately 4-inches by 5-inches by 1-inch in dimension.
 - (2) Magnetic tape must be chromium dioxide particle based 1/2-inch tape.

- (3) Cartridges must be 18-track, 36-track, 128-track or 256-track parallel (**See Note.**)
 - (4) Cartridges will contain 37,871 CPI, 75,742 CPI, or 3590 CPI (characters per inch).
 - (5) Mode will be full function.
 - (6) The data may be compressed using EDRC (Memorex) or IDRC (IBM) compression.
 - (7) Either EBCDIC (Extended Binary Coded Decimal Interchange Code) or ASCII (American Standard Coded Information Interchange) may be used.
- .02 The tape cartridge records defined in this Revenue Procedure may be blocked subject to the following:
- (a) A block **must not** exceed 32,250 tape positions.
 - (b) If the use of blocked records would result in a short block, all remaining positions of the block must be filled with 9s; however, the last block of the file may be filled with 9s or truncated. **Do not pad a block with blanks.**
 - (c) All records, except the header and trailer labels, may be blocked or unblocked. A record may not contain any control fields or block descriptor fields, which describe the length of the block or the logical records within the block. The number of logical records within a block (the blocking factor) must be constant in every block with the exception of the last block, which may be shorter (see item (b) above). The block length must be evenly divisible by 750.
 - (d) Records may not span blocks.
- .03 Tape cartridges may be labeled or unlabeled.
- .04 For the purposes of this Revenue Procedure, the following must be used:
- Tape Mark:
- (a) Signifies the physical end of the recording on tape.
 - (b) For even parity, use BCD configuration 001111 (8421).
 - (c) May follow the header label and precede and/or follow the trailer label.

Note: Filers should indicate on the external media label whether the cartridge is 18-track, 36-track, 128-track or 256-track.

PART D. RECORD FORMAT SPECIFICATIONS AND RECORD LAYOUTS

Sec. 1. General

.01 The specifications contained in this part of the Revenue Procedure define the required formation and contents of the records to be included in the electronic or magnetic media files.

.02 A provision is made in the "B" Records for entries which are optional. If the field is not used, enter blanks to maintain a fixed record length of 750 positions. Each field description explains the intended use of specific field positions.

Sec. 2. Transmitter "T" Record — General Field Descriptions

.01 The Transmitter "T" Record identifies the entity transmitting the electronic/magnetic media file and contains information which is critical if it is necessary for IRS/ECC-MTB to contact the filer.

.02 The Transmitter "T" Record is the first record on each file and is followed by a Payer "A" Record. A file format diagram is located at the end of Part D. A replacement file will be requested by IRS/ECC-MTB if the "T" Record is not present.

.03 For all fields marked "**Required**", the transmitter must provide the information described under Description and Remarks. For those fields not marked "**Required**", a transmitter must allow for the field, but may be instructed to enter blanks or zeros in the indicated field positions and for the indicated length.

.04 All records must be a fixed length of 750 positions.

.05 All alpha characters entered in the "T" Record must be upper-case, except email addresses which may be case sensitive. **Do not** use punctuation in the name and address fields.

Record Name: Transmitter "T" Record			
Field Position	Field Title	Length	Description and Remarks
1	Record Type	1	Required. Enter "T".
2-5	Payment Year	4	Required. Enter the 4-digit year in which the contract is signed.
6	Type of Return	1	Required. Enter "G".

Record Name: Transmitter "T" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
7-15	Transmitter's TIN	9	Required. Must be the valid nine-digit number TIN assigned by IRS to the Federal Executive Agency. Do not enter hyphens or alpha characters. Entering all zeros, ones, twos, etc., will have the effect of an incorrect TIN.
16-20	Transmitter Control Code	5	Required. Enter the five-character alpha/numeric Transmitter Control Code (TCC) assigned by IRS/ECC-MTB. A TCC must be obtained to file data within this program.
21-22	Replacement Alpha Character	2	Required for magnetic media replacement files only. Enter the alpha/numeric character which appears immediately following the TCC number on the Media Tracking Slip (Form 9267). The Form 9267 accompanies media that has been returned by IRS/ECC-MTB due to processing problems. This field must be blank unless media has been returned. If the file is being replaced magnetically, information is required in this field. Left-justify information and fill unused positions with blanks. If this is not a replacement file, enter blanks.
23-29	Blank	7	Enter blanks.
30-69	Transmitter Name	40	Required. Enter the name of the transmitter in the manner in which it is used in normal business. If someone other than the Federal Agency is transmitting data, enter the name of the transmitter. The name of the transmitter must be consistent through the entire file. Left-justify and fill unused positions with blanks.
70-109	Transmitter Name (Continuation)	40	Enter any additional information that may be part of the name. Left-justify information and fill unused positions with blanks
NOTE: All the information "Required" in Field Positions 110 thru 280 MUST contain the address information where correspondence relating to problem media can be sent.			
110-149	Agency Name	40	Required. Enter the name of the agency to be associated with the address where correspondence should be sent due to processing problems.
150-189	Agency Name (Continuation)	40	Enter any additional information that may be part of the name of the company where correspondence should be sent due to processing problems.
190-229	Agency Mailing Address	40	Required. Enter the mailing address where correspondence should be sent in the event IRS/ECC-MTB is unable to process.
230-269	Agency City	40	Required. Enter the city, town, or post office where correspondence should be sent.
270-271	Agency State	2	Required. Enter the valid U.S. Postal Service state abbreviation for states. Refer to the chart of valid state codes in Part A, Sec.10.
272-280	Agency ZIP Code	9	Required. Enter the valid nine-digit ZIP Code assigned by the U.S. Postal Service. If only the first five digits are known, left-justify information and fill unused positions with blanks
281-303	Blank	23	Enter blanks.
304-343	Contact Name	40	Required. Enter the name of the person to be contacted if IRS/ECC-MTB encounters problems with the file.
344-358	Contact Phone Number & Extension	40	Required. Enter the telephone number of the person to contact regarding electronic/magnetic files. Omit Extension hyphens. If no extension is available, left-justify information and fill unused positions with blanks. For example, the IRS/ECC-MTB Customer Service Section phone number of 866-455-7438 with an extension of 52345 would be 866455743852345.

Record Name: Transmitter "T" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
359-393	Contact Email Address	35	Required if available. Enter the email address of the person to contact regarding electronic or magnetic files. Left-justify information. If no email address is available, enter blanks.
394-395	Tape Cartridge File Indicator	2	Required for tape cartridge filer only. Enter the letters "LS" (in uppercase only). Use of this field by filers using other types of media will be acceptable but is not required. Otherwise, enter blanks.
396-410	Electronic File Name For a Replacement File	15	Required. Use for an electronic file which "FILE STATUS" has indicated was rejected. Enter the ORIGINAL or CORRECTION electronic file name assigned by the IRS electronic FIRE System. If you are sending an original, or correction, enter blanks.
411-416	Transmitter's Media Number	6	For magnetic media filers only. If your organization uses an in-house numbering system to identify media, enter that number; otherwise, enter blanks.
417-499	Blank	83	Enter blanks.
500-507	Record Sequence Number	8	Required. Enter the number of the record as it appears within your file. The record sequence number for the "T" record will always be "1" (one), since it is the first record on your file and you can have only one "T" record in a file. Each record, thereafter, must be incremented by one in ascending numerical sequence, i.e., 2, 3, 4, etc. Right-justify numbers with leading zeroes in the field. For example, the "T" record sequence number would appear as "00000001" in the field, the first "A" record would be "00000002", the first "B" record, "00000003", the second "B" record, "00000004" and so on until you reach the final record of the file, the "F" record.
508-748	Blank	241	Enter blanks.
749-750	Blank	2	Enter blanks, or carriage return/line feed (CR/LF) characters.

Sec. 3. Transmitter "T" Record — Record Layout

Record Type	Payment Year	Type of Return	Transmitter's TIN	Transmitter Control Code	Replacement Alpha Character
1	2-5	6	7-15	16-20	21-22

Blank	Transmitter Name	Transmitter Name (Cont'd.)	Agency Name	Agency Name (Cont'd.)	Agency Mailing Address
23-29	30-69	70-109	110-149	150-189	190-229

Agency City	Agency State	Agency ZIP Code	Blank	Contact Name	Contact Phone Number & Extension	Contact Email Address
230-269	270-271	272-280	281-303	304-343	344-358	359-393

Tape Cartridge File Indicator	Electronic File Name For a Replacement File	Transmitter's Media Number	Blank	Record Sequence Number	Blank	Blank or CR/LF
394-395	396-410	411-416	417-499	500-507	508-748	749-750

Sec. 4. Payer "A" Record — General Field Descriptions

.01 The Payer "A" Record identifies the payer of the file and provides parameters for the succeeding Payee "B" Records. IRS computer programs rely on the absolute relationship between the parameters and data fields in the "A" Record and the data fields in the "B" Record to which they apply.

.02 All records must be a fixed length of 750 positions.

.03 An "A" Record may be blocked with "B" Records; however, the initial record on a file must be a Transmitter "T" Record followed by a Payer "A" Record. IRS/ECC-MTB will accept an "A" Record after a "C" Record.

.04 The number of "A" Records appearing on the media will depend on the number of agencies being reported. A separate "A" Record is required for each agency followed by the Payee "B" Records for the agency. Each set of "B" Records is followed by a summary "C" Record. If more than one agency is being reported on a tape cartridge, an "A" Record may follow a "C" Record (i.e., The "A", "B", and "C" Records for one agency may be followed by "A", "B", and "C" Records for the next agency, etc.).

.05 All alpha characters entered in the "A" Record must be uppercase.

.06 Do not begin any record at the end of a block and continue the same record into the next block.

.07 For all fields marked "**Required**", the transmitter must provide the information described under Description and Remarks. For those fields not marked "**Required**", a transmitter must allow for the field, but may be instructed to enter blanks or zeros in the indicated media position(s) and for the indicated length.

Record Name: Payer "A" Record

Field Position	Field Title	Length	Description and Remarks
1	Record Type	1	Required. Enter an "A".
2-5	Payment Year	4	Required. Enter the 4-digit year in which the contract is signed.
6-11	Blank	6	Enter blanks.
12-20	Payer's Taxpayer Identification Number (TIN)	9	Required. Must be the valid nine-digit Taxpayer Identification Number assigned to the Federal Executive Agency. Do not enter blanks, hyphens, or alpha characters. All zeros, ones, twos, etc., will have the effect of an incorrect TIN.
21-24	Payer Name Control	4	Generally, the Name Control is the first four characters of the payer's name. The word "the" should be disregarded when it is the first word of the name, unless the name contains only two words. This field should be left blank if the name control is not determinable.
25-26	Blank	2	Enter blanks.
27	Type of Return	1	Required. Enter "G".
28	Amount Indicator	1	Required. Enter "8".
29-47	Blank	19	Enter blanks.
48	Original File Indicator	1	Required for original files only. Enter "1" (one) if the information is original data. Otherwise, enter a blank.
49	Replacement File Indicator	1	Required for replacement files only. Enter "1" (one) if the purpose of this file is to replace a file that IRS/ECC-MTB has informed you in writing can not be processed or the FIRE System indicated a FILE STATUS of bad. Otherwise, enter a blank.

Record Name: Payer "A" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
50	Correction File Indicator	1	Required for correction files only. Enter "1" (one) if this file is to correct information which was previously submitted to IRS/ECC-MTB, was processed, but contained erroneous information. Any information return which was inadvertently omitted from a file must be submitted as original. Otherwise, enter a blank.
51	Blank	1	Enter blanks.
52	Foreign Entity Indicator	1	Enter a "1" (one) if the payer is a foreign entity and income is paid by the foreign entity to a U.S. resident. If the payer is not a foreign entity, enter a blank.
53-92	First Payer Name Line	40	Required. Enter the name of the Federal Agency whose TIN appears in positions 12-20 of the "A" Record. The name of the agency must be entered in the manner in which it is used in normal business. Any extraneous information must be deleted. Left-justify information, and fill unused positions with blanks.
93-132	Second Payer Name Line	40	Required. Enter the name and title of the person to whom requests for an offset against any unpaid tax liability of the contractor can be sent. If necessary, please abbreviate.
133	Blank	1	Enter blank.
134-173	Payer Shipping Address	40	Required. Enter the address of the person to whom requests for an offset against any unpaid tax liability of the contract can be sent. The street address should include number, street, apartment or suite number (or P.O. Box if mail is not delivered to a street address). Left-justify and fill with blanks.
<p>For U.S. addresses, the payer city, state, and ZIP Code must be reported as a 40, 2, and 9 position field, respectively. Filers must adhere to the correct format for the payer city, state, and ZIP Code. For foreign addresses, filers may use the payer city, state, and ZIP Code as a continuous 51 position field. Enter information in the following order: city, province or state, postal code, and the name of the country. When reporting a foreign address, the Foreign Entity Indicator in position 52 must contain a "1" (one).</p>			
174-213	Payer City	40	Required. Enter the city of the person to whom requests for an offset against any unpaid tax liability of the contractor can be sent. Left-justify and fill with blanks.
214-215	Payer State	2	Required. Enter the valid U.S. Postal Service state abbreviations for states. Refer to the chart of valid state abbreviations in Part A, Sec.10.
216-224	Payer ZIP Code	9	Required. Enter the valid nine-digit ZIP Code assigned by the U.S. Postal Service. If only the first five digits are known, left-justify information and fill the unused positions with blanks.
225-239	Payer's Phone Number & Extension	15	Enter the payer's phone number and extension.
240-499	Blank	260	Enter blanks.
500-507	Record Sequence Number	8	Required. Enter the number of the record as it appears within your file. The record sequence number for the "T" record will always be "1" (one), since it is the first record on your file and you can have only one "T" record in a file. Each record, thereafter, must be incremented by one in ascending numerical sequence, i.e., 2, 3, 4, etc. Right-justify numbers with leading zeroes in the field. For example, the "T" record sequence number would appear as "00000001" in the field, the first "A" record would be "00000002", the first "B" record, "00000003", the second "B" record, "00000004" and so on until you reach the final record of the file, the "F" record.
508-748	Blank	241	Enter blanks.
749-750	Blank	2	Enter blanks or carriage return/line feed (CR/LF) characters.

Sec. 5. Payer “A” Record — Record Layout

Record Type	Payment Year	Blank	Payer’s TIN	Payer Name Control	Blank	Type of Return	Amount Indicator
1	2–5	6–11	12–20	21–24	25–26	27	28

Blank	Original File Indicator	Replacement File Indicator	Correction File Indicator	Blank	Foreign Entity Indicator	First Payer Name Line
29–47	48	49	50	51	52	53–92

Second Payer Name Line	Blank	Payer Shipping Address	Payer City	Payer State	Payer ZIP Code	Payer’s Phone & Extension
93–132	133	134–173	174–213	214–215	216–224	225–239

Blank	Record Sequence Number	Blank	Blank or CR/LF
240–499	500–507	508–748	749–750

Sec. 6. Payee “B” Record — General Field Descriptions

.01 The Payee “B” Record contains payment information from the individual contracts.

When filing information documents electronically/magnetically, the format for the Payee “B” Records will remain constant.

.02 All records must be a fixed length of 750 positions.

.03 The following specifications include a field in the payee records called “Name Control” in which the first four characters of the payee’s surname are to be entered by the filer.

(a) If filers are unable to determine the first four characters of the surname, the Name Control Field may be left blank. Compliance with the following will facilitate IRS computer programs in identifying the correct name control:

(1) The surname of the payee whose TIN is shown in the “B” Record should always appear first. If, however, the records have been developed using the first name first, the filer must leave a blank space between the first and last names.

(2) In the case of multiple payees, only the surname of the payee whose TIN (SSN, EIN or ITIN) is shown in the “B” Record must be present in the First Payee Name Line. Surnames of any other payees may be entered in the Second Payee Name Line.

.04 For all fields marked “**Required**”, the transmitter must provide the information described under Description and Remarks. For those fields not marked “**Required**”, the transmitter must allow for the field, but may be instructed to enter blanks or zeros in the indicated field position(s) and for the indicated length.

.05 All alpha characters entered in the “B” Record must be uppercase.

.06 Decimal points (.) cannot be used to indicate dollars and cents.

.07 **IRS strongly encourages filers to review data for accuracy before submission to facilitate the collection of delinquent federal tax liabilities from contractors. Filers should be especially careful that names, TINs and income amounts are correct.**

Record Name: Payee “B” Record

Field Position	Field Title	Length	Description and Remarks
1	Record Type	1	Required. Enter “B”.
2–5	Payment Year	4	Required. Enter the 4-digit year in which the contract is signed.

Record Name: Payee "B" Record (Continued)

Field Position	Field Title	Length	Description and Remarks								
6	Corrected Return Indicator (See Note.)	1	Required for corrections only. Indicates a corrected return.								
			<table border="0"> <thead> <tr> <th><u>Code</u></th> <th><u>Definition</u></th> </tr> </thead> <tbody> <tr> <td>G</td> <td>If this is a one-transaction correction or the first of a two-transaction correction</td> </tr> <tr> <td>C</td> <td>If this is the second transaction of a two transaction correction</td> </tr> <tr> <td>Blank</td> <td>If this is not a return being submitted to correct information already processed by IRS.</td> </tr> </tbody> </table>	<u>Code</u>	<u>Definition</u>	G	If this is a one-transaction correction or the first of a two-transaction correction	C	If this is the second transaction of a two transaction correction	Blank	If this is not a return being submitted to correct information already processed by IRS.
<u>Code</u>	<u>Definition</u>										
G	If this is a one-transaction correction or the first of a two-transaction correction										
C	If this is the second transaction of a two transaction correction										
Blank	If this is not a return being submitted to correct information already processed by IRS.										

Note: C, G, and non-coded records must be reported using separate Payer "A" Records. Refer to Part A, Sec. 8, for specific instructions on how to file corrected returns.

7-10	Name Control	4	If determinable, enter the first four (4) characters of the surname of the person whose TIN is being reported in positions 12-20 of the "B" Record; otherwise, enter blanks. This usually is the contractor. Surnames of less than four (4) characters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. In the case of a business, other than a sole proprietorship, use the first four significant characters of the business name. Disregard the word "the" when it is the first word of the name, unless there are only two words in the name. A dash (-) and an ampersand (&) are the only acceptable special characters. Surname prefixes are considered part of the surname, e.g., for Van Elm, the name control would be VANE.
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Note: Imbedded blanks, extraneous words, titles, and special characters (i.e., Mr., Mrs., Dr., period [.] , apostrophe [']) should be removed from the Payee Name Lines. This information may be dropped during subsequent processing at IRS/ECC-MTB. A dash (-) and an ampersand (&) are the only acceptable special characters.

The following examples may be helpful to filers in developing the Name Control:

<u>Name</u>	<u>Name Control</u>
Individuals:	
Jane Brown	BROW
John A. Lee	LEE*
James P. En , Sr.	EN*
John O'Neil	ONEI
Mary Van Buren	VANB
Juan De Jesus	DEJE
Gloria A. El-Roy	EL-R
Mr. John Smith	SMIT
Joe McCarthy	MCCA
Pedro Torres-Lopes **	TORR
Maria Lopez Moreno**	LOPE
Binh To La	LA*
Nhat Thi Pham	PHAM
Mark D'Allesandro	DALL

Record Name: Payee "B" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
Corporations:			
	The F irst National Bank	FIRS	
	T he H ideaway	THEH	
	A & B Cafe	A&BC	
	11TH Street Inc.	11TH	
Sole Proprietor:			
	Mark H emlock DBA The Sunshine Club	HEML	
Partnership:			
	Robert A spen and Bess Willow	ASPE	
	Harold F ir, Bruce Elm, and Joyce Spruce et al Ptr	FIR*	
Estate:			
	Frank W hite Estate	WHIT	
	Estate of Sheila B lue	BLUE	
Trusts and Fiduciaries:			
	D aisy Corporation Employee Benefit Trust	DAIS	
	Trust FBO The C herryblossom Society	CHER	
Exempt Organizations:			
	L aborer's Union, AFL-CIO	LABO	
	S t. B ernard's Methodist Church Bldg. Fund	STBE	

*Name Controls of less than four (4) significant characters must be left-justified and blank-filled.

**For Hispanic names, when two last names are shown for an individual, derive the name control from the first last name.

11	Type of TIN	1	This field is used to identify the Taxpayer Identification Number (TIN) in positions 12-20 as either an Employer Identification Number (EIN), a Social Security Number (SSN), or an Individual Taxpayer Identification Number (ITIN). Enter the appropriate code from the following table:															
			<table border="1"> <thead> <tr> <th><u>Code</u></th> <th><u>Type of TIN</u></th> <th><u>Type of Account</u></th> </tr> </thead> <tbody> <tr> <td>1</td> <td>EIN</td> <td>A business, organization, sole proprietor, or other entity</td> </tr> <tr> <td>2</td> <td>SSN</td> <td>An individual, including a sole proprietor or</td> </tr> <tr> <td>2</td> <td>ITIN</td> <td>An individual required to have a taxpayer identification number, but who is not eligible to obtain an SSN</td> </tr> <tr> <td>Blank</td> <td>N/A</td> <td>If the type of TIN is not determinable, enter a blank.</td> </tr> </tbody> </table>	<u>Code</u>	<u>Type of TIN</u>	<u>Type of Account</u>	1	EIN	A business, organization, sole proprietor, or other entity	2	SSN	An individual, including a sole proprietor or	2	ITIN	An individual required to have a taxpayer identification number, but who is not eligible to obtain an SSN	Blank	N/A	If the type of TIN is not determinable, enter a blank.
<u>Code</u>	<u>Type of TIN</u>	<u>Type of Account</u>																
1	EIN	A business, organization, sole proprietor, or other entity																
2	SSN	An individual, including a sole proprietor or																
2	ITIN	An individual required to have a taxpayer identification number, but who is not eligible to obtain an SSN																
Blank	N/A	If the type of TIN is not determinable, enter a blank.																

Record Name: Payee "B" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
12–20	Contractor's Taxpayer Identification Number (TIN)	9	Required. Enter the nine-digit Taxpayer Identification Number of the contractor (SSN, ITIN, or EIN). If an identification number has been applied for but not received, enter blanks . Do not enter hyphens or alpha characters. All zeros, ones, twos, etc., will have the effect of an incorrect TIN. If the TIN is not available, enter blanks.
21–29	Common Parent's Taxpayer Identification Number (TIN)	9	Required. If applicable, enter the valid nine-digit number assigned to the contractor's common parent; otherwise, enter blanks . Do not enter hyphens or alpha characters. All zeros, ones, twos, etc., will have the effect of an incorrect TIN.
30–54	Blank	25	Enter blanks.
55–138	Zero	84	Required. Enter zeros.
139–150	Total Amount Obligated Under Contract	12	Required. The amount reported in this field represents Total Amount Obligated Under the Contract. The Under Contract amount must be entered in U.S. dollars and cents . Dollar signs, commas, decimal points, or negative payments are not acceptable. Amount obligated must be right-justified and unused positions must be zero filled.
151–198	Zero	48	Required. Enter zeros.
199–246	Blank	48	Enter blanks.
247	Foreign Country Indicator	1	If the address of the payee is in a foreign country, enter a "1" (one) in this field; otherwise, enter blank . When filers use this indicator, they may use a free format for the payee city, state, and ZIP Code. Address information must not appear in the First or Second Payee Name Lines.
248–287	First Payee Name Line	40	Required. Enter the name of the contractor (preferably surname first) whose Taxpayer Identification Number (TIN) was provided in positions 12-20 of the "B" Record. Left-justify and fill unused positions with blanks. If more space is required for the name, utilize the Second Payee Name Line Field. If there are multiple payees, only the name of the payee whose TIN has been provided should be entered in this field. The names of the other payees may be entered in the Second Payee Name Line Field. If reporting information for a sole proprietor, the individual's name must always be present on the First Payee Name Line. The use of the business name is optional in the Second Payee Name Line Field.
288–327	Second Payee Name Line	40	If there are multiple payees, (e.g., partners or joint owners), use this field for those names not associated with the TIN provided in positions 12-20 of the "B" Record or if not enough space was provided in the First Payee Name Line, continue the name in this field (See Notes). Do not enter address information. It is important that filers provide as much payee information to IRS/ECC-MTB as possible to identify the payee associated with the TIN. Left-justify and fill unused positions with blanks.
<p>Note: End First Payee Name Line with a full word. Do not split words. Begin Second Payee Name Line with the next sequential word.</p> <p>Note: If applicable, enter the business name of the sole proprietor in this field.</p>			
328–367	Blank	40	Enter blanks.

Record Name: Payee "B" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
368-407	Payee Mailing Address	40	Required. Enter the mailing address of the contractor. The street address should include number, street, apartment or suite number (or P.O. Box if mail is not delivered to street address). Left-justify information and fill unused positions with blanks. This field must not contain any data other than the payee's mailing address.
<p>For U.S. addresses, the payee city, state, and ZIP Code must be reported as a 40, 2, and 9 position field, respectively. Filers must adhere to the correct format for the payee city, state, and ZIP Code. For foreign addresses, filers may use the payee city, state, and ZIP Code as a continuous 51 position field. Enter information in the following order: city, province or state, postal code, and the name of the country. When reporting a foreign address, the Foreign Country Indicator in position 247 must contain a "1" (one).</p>			
408-447	Blank	40	Enter blanks.
448-487	Payee City	40	Required. Enter the city, town or post office. Left-justify information and fill the unused positions with blanks. Enter APO or FPO if applicable. Do not enter state and ZIP Code information in this field.
488-489	Payee State	2	Required. Enter the valid U.S. Postal Service state abbreviations for states or the appropriate postal identifier (AA, AE, or AP) described in Part A, Sec. 10.
490-498	Payee ZIP Code	9	Required. Enter the valid nine-digit ZIP Code assigned by the U.S. Postal Service. If only the first five digits are known, left-justify information and fill the unused positions with blanks. For foreign countries, alpha characters are acceptable as long as the filer has entered a "1" (one) in the Foreign Country Indicator, located in position 247 of the "B" Record.
499	Blank	1	Enter blank.
500-507	Record Sequence Number	8	Required. Enter the number of the record as it appears within your file. The record sequence number for the "T" record will always be "1" (one), since it is the first record on your file and you can have only one "T" record in a file. Each record, thereafter, must be incremented by one in ascending numerical sequence, i.e., 2, 3, 4, etc. Right-justify numbers with leading zeroes in the field. For example, the "T" record sequence number would appear as "00000001" in the field, the first "A" record would be "00000002", the first "B" record, "00000003", the second "B" record, "00000004" and so on until you reach the final record of the file, the "F" record.
508-544	Blank	37	Enter blanks.
545	Filing Quarter	1	Required. Enter quarter; i.e., 1, 2, 3, or 4. See the chart below to determine the appropriate quarter.
<p align="center">Quarter</p> <p>1 January, February, March</p> <p>2 April, May, June</p> <p>3 July, August, September</p> <p>4 October, November, December</p>			
546-553	Blank	8	Enter blanks.

Record Name: Payee "B" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
554-568	Contract Number	15	Required (if available). Enter the contract number assigned by the Federal Executive Agency. Left-justify and fill the unused positions with blanks.
569	Blank	1	Enter blank.
570-573	Contract Modification Number	4	Required (if available). Enter the number assigned to the contract or order to designate a modification or termination. If this field is not utilized, enter blanks.
574	Blank	1	Enter blank.
575-589	Contract Office Order Number	15	Required (if available). Enter the number assigned by the contracting office. Left-justify and fill the unused positions with blanks.
590	Blank	1	Enter blank.
591-594	Reporting Agency Code	4	Required. Enter the four-digit agency and sub-agency code.
595	Blank	1	Enter blank.
596-600	Contract Office Number	5	Required (if available). Enter the number assigned by the Federal Executive Agency that identifies the purchasing or contracting office.
601	Blank	1	Enter blank.
602-609	Date of Contract Action	8	Required. Enter the date of the action. Use YYYYMMDD (e.g., 20050214).
610	Blank	1	Enter blank.
611-618	Contract Completion Date	8	Required. Enter the expected date of completion of contract such as the contract delivery date under the contract schedule. Use YYYYMMDD. If completion date is not available, enter blanks.
619-658	Name of Common Parent	40	Required (if applicable). If the contractor is a member of an affiliated group of corporations that files its income tax returns on a consolidated basis, enter the name of the common parent of the affiliated group. The name entered should match the EIN in positions 21-29. If this field is not utilized, enter blanks.
659-748	Blank	90	Enter blanks.
749-750	Blank	2	Enter blanks or carriage return line feed (CR/LF) characters.

Sec. 7. Payee "B" Record — Record Layout

Record Type	Payment Year	Corrected Return Indicator	Name Control	Type of TIN	Contractor's Taxpayer Identification Number (TIN)
1	2-5	6	7-10	11	12-20

Common Parent's Tayspayer Identification Number (TIN)	Blank	Zero	Total Amount Obligated Under Contract	Zero	Blank	Foreign Country Indicator
21-29	30-54	55-138	139-150	151-198	199-246	247

First Payee Name Line	Second Payee Name Line	Blank	Payee Mailing Address	Blank	Payee City	Payee State	Payee Zip Code
248-287	288-327	328-367	368-407	408-447	448-487	488-489	490-498

Blank	Record Sequence Number	Blank	Filing Quarter	Blank	Contract Number	Blank	Contract Modification Number
499	500-507	508-544	545	546-553	554-568	569	570-573

Blank	Contract Office Order Number	Blank	Reporting Agency Code	Blank	Contract Office Number	Blank
574	575-589	590	591-594	595	596-600	601

Date of Contract Action	Blank	Contract Completion Date	Name of Common Parent	Blank	Blank or (CR/LF)
602-609	610	611-618	619-658	659-748	749-750

Sec. 8. End of Payer "C" Record — General Field Descriptions and Record Layout

.01 The End of Payer "C" Record is a fixed record length of 750 positions.

.02 The control total field is 18 positions in length.

.03 The End of Payer "C" Record is a summary record for a given payer.

.04 The "C" Record will contain the total number of payees and total of the payment amounts of a given payer. The "C" Record must be written after the last Payee "B" Record for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record.

.05 Payers/Transmitters should verify the accuracy of the totals since data with missing or incorrect "C" Records will require a replacement.

Record Name: End of Payer "C" Record

Field Position	Field Title	Length	Description and Remarks
1	Record Type	1	Required. Enter "C".
2-9	Number of Payees	8	Required. Enter the total number of "B" Records covered by the preceding "A" Record. Right-justify information and fill unused positions with zeros.

Record Name: End of Payer "C" Record (Continued)

Field Position	Field Title	Length	Description and Remarks
10-15	Blank	6	Enter blanks.
16-141	Zero	126	Enter zeros.
142-159	Control Total	18	Required. Enter the total amount paid to contractors for all contracts present in the preceding Payee "B" Records. The Control Total must be entered in U.S. dollars and cents . Dollar signs, commas, decimal points, or negative payments are not acceptable. Total must be right-justified and unused positions must be zero filled.
160-231	Zero	72	Enter zeros.
232-499	Blank	268	Enter blanks.
500-507	Record Sequence Number	8	Required. Enter the number of the record as it appears within your file. The record sequence number for the "T" record will always be "1" (one), since it is the first record on your file and you can have only one "T" record in a file. Each record, thereafter, must be incremented by one in ascending numerical sequence, i.e., 2, 3, 4, etc. Right-justify numbers with leading zeroes in the field. For example, the "T" record sequence number would appear as "00000001" in the field, the first "A" record would be "00000002", the first "B" record, "00000003", the second "B" record, "00000004" and so on until you reach the final record of the file, the "F" record.
508-748	Blank	241	Enter blanks.
749-750	Blank	2	Enter blanks or carriage return/line feed (CR/LF) characters.

End of Payer "C" Record — Record Layout

Record Type	Number of Payees	Blank	Zero	Control Total	Zero
1	2-9	10-15	16-141	142-159	160-231

Blank	Record Sequence Number	Blank	Blank or CR/LF
232-499	500-507	508-748	749-750

Sec. 9. End of Transmission "F" Record — General Field Descriptions and Record Layout

- .01 The end of transmission "F" record is a fixed record length of 750 positions.
- .02 The "F" Record is a summary of the number of payers in the entire file.
- .03 This record should be written after the last "C" Record of the entire file.

Record Name: End of Transmission "F" Record

Field Position	Field Title	Length	Description and Remarks
1	Record Type	1	Required. Enter "F".
2-9	Number of "A" Records	8	Enter the total number of Payer "A" Records in the entire file (right-justify and zero fill) or enter all zeros.
10-30	Zero	21	Enter zeros.
31-499	Blank	469	Enter blanks.
500-507	Record Sequence Number	8	Required. Enter the number of the record as it appears within your file. The record sequence number for the "T" record will always be "1" (one), since it is the first record on your file and you can have only one "T" record in a file. Each record, thereafter, must be incremented by one in ascending numerical sequence, i.e., 2, 3, 4, etc. Right-justify numbers with leading zeroes in the field. For example, the "T" record sequence number would appear as "00000001" in the field, the first "A" record would be "00000002", the first "B" record, "00000003", the second "B" record, "00000004" and so on until you reach the final record of the file, the "F" record.
508-748	Blank	241	Enter blanks.
749-750	Blank	2	Enter blanks or carriage return/line feed (CR/LF) characters.

End of Transmission "F" Record — Record Layout

Record Type	Number of "A" Records	Zero	Blank	Record Sequence Number	Blank	Blank or CR/LF
1	2-9	10-30	31-499	500-507	508-748	749-750

File Format

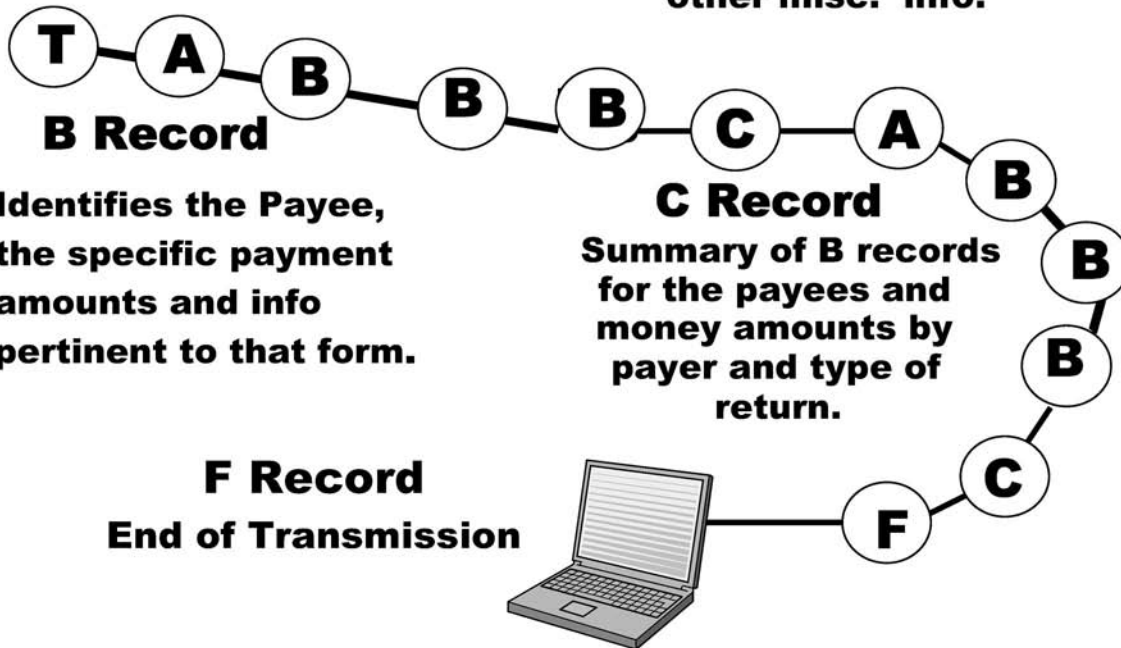
Each record must be 750 positions.

T Record

Identifies the Transmitter of electronic/magnetic file & information contained on Forms 4419 & 4804.

A Record

Identifies the Payer (the institution or person making payments) the type of document being reported, & other misc. info.



B Record

Identifies the Payee, the specific payment amounts and info pertinent to that form.

C Record

Summary of B records for the payees and money amounts by payer and type of return.

F Record

End of Transmission

26 CFR 601.601: Rules and regulations.
(Also Part 1, §§ 146; 1.103(n)-4T; 301.9100-1;
301.9100-3.)

Rev. Proc. 2005-30

SECTION 1. PURPOSE

This revenue procedure provides that an issuing authority that fails to make a timely carryforward election of unused private activity bond volume cap under § 146(f) of the Internal Revenue Code (the “Code”) is granted under § 301.9100-3 of the Procedure and Administration Regulations an automatic extension of six months from the due date of the carryforward election, to make the carryforward election, provided that the issuing authority meets the requirements of § 4 of this revenue procedure.

SECTION 2. LAW AND ANALYSIS

.01 Under § 103(a), except as provided in § 103(b), gross income does not include interest on any State or local bond. Section 103(b) provides, in part, that § 103(a) shall not apply to any private activity bond that is not a qualified bond (within the meaning of § 141). Section 141(e) provides, in part, that a qualified bond must meet the applicable requirements of § 146.

.02 Section 146(a) provides that a private activity bond issued as part of an issue meets the requirements of § 146 if the aggregate face amount of the private activity bonds issued pursuant to such issue, when added to the aggregate face amount of tax-exempt private activity bonds previously issued by the issuing authority during the calendar year, does not exceed such

authority’s volume cap for such calendar year.

.03 Section 146(f)(1) provides that if an issuing authority’s volume cap for any calendar year after 1985 exceeds the aggregate amount of tax-exempt private activity bonds the authority issued during such calendar year, such issuing authority may elect to treat all (or any portion) of such excess as a carryforward.

.04 Section 1.103(n)-4T, A-2, of the temporary Income Tax Regulations provides, in part, that an election to carry forward volume cap must be filed prior to the end of the calendar year with respect to which the issuing authority has the unused volume cap. These regulations, which were issued under the predecessor to § 146, generally continue to apply to the extent that they are not inconsistent with the Tax Reform Act of

1986. See Conf. Rep. 99-841 at II-686, 1986-3 (Vol. 4) C.B. 686. However, Notice 89-12, 1989-1 C.B. 633, which may be relied upon, provides that regulations to be issued under § 146 will require that the issuing authority file the carryforward election by the earlier of (1) February 15 of the calendar year following the year in which the excess amount arises, or (2) the date of issue of bonds issued pursuant to the carryforward election.

.05 Announcement 87-43, 1987-19 I.R.B. 15, provides that Form 8328 (*Carryforward Election of Unused Private Activity Bond Volume Cap*) should be used by issuers of tax-exempt bonds who wish to make a carryforward election under § 146(f).

.06 Sections 301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make a regulatory election (defined in § 301.9100-1(b) to include an election whose due date is prescribed by a regulation or notice). Section 301.9100-1(a) provides that an extension of time is available for elections that a taxpayer is otherwise eligible to make. However, the granting of an extension of time is not a determination that the taxpayer is otherwise eligible to make the election.

.07 Section 301.9100-3(a) generally provides, in part, that requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Federal Government.

.08 Section 301.9100-3(b)(1) provides, in part, that generally a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer requests relief under § 301.9100-3 before the failure to make the regulatory election is discovered by the Internal Revenue Service (the "IRS").

.09 Section 301.9100-3(b)(3) provides, in part, that for purposes of § 301.9100-3(b), a taxpayer is deemed to have not acted reasonably and in good faith if the taxpayer (1) was informed in all material respects of the required election and related tax consequences, but

chose not to file the election, or (2) uses hindsight in requesting relief. If specific facts have changed since the due date for making the election that make the election advantageous to a taxpayer, the IRS will not ordinarily grant relief. In such a case, the IRS will grant relief only when the taxpayer provides strong proof that the taxpayer's decision to seek relief did not involve hindsight.

.10 Section 301.9100-3(c) provides, in part, that the interests of the Federal Government are prejudiced if granting relief would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money). Similarly, if the tax consequences of more than one taxpayer are affected by the election, the Federal Government's interests are prejudiced if extending the time for making the election may result in the affected taxpayers, in the aggregate, having a lower tax liability than if the election had been timely made.

.11 The granting of an extension of time to file a Form 8328 under this revenue procedure will not prejudice the interests of the Federal Government.

SECTION 3. DESCRIPTION OF RELIEF

.01 An issuing authority that fails to make a timely carryforward election is granted under this revenue procedure an automatic extension of six months from the due date of the carryforward election (excluding extensions), to make the carryforward election, if that issuing authority meets the requirements of § 4 of this revenue procedure.

.02 The granting of an extension of time to make a carryforward election under this revenue procedure is not a determination that the issuing authority is otherwise eligible to make the election.

.03 If an issuing authority is not eligible for relief under this revenue procedure, such authority may request relief by applying for a letter ruling under § 301.9100-3, Rev. Proc. 2005-1, 2005-1 I.R.B. 1 (or its successor), and Rev. Proc. 96-16, 1996-1 C.B. 630.

SECTION 4. PROCEDURE

.01 An issuing authority is eligible for relief under this revenue procedure if it meets the following requirements—

(1) The issuing authority must file a Form 8328 within six months after the due date of the carryforward election (excluding extensions);

(2) The Form 8328 filed under this revenue procedure must have typed or printed on the top "FILED PURSUANT TO REV. PROC. 2005-30";

(3) The issuing authority must file the Form 8328 under this revenue procedure before it receives written notice from the IRS that it failed to make the carryforward election timely;

(4) The issuing authority must not have declined to make the carryforward election, after having been informed in all material respects of the required election and related tax consequences, on or before the due date for filing the election, and then have reversed that decision after the due date for filing the election;

(5) The issuing authority must not be filing the carryforward election in reaction to specific facts or circumstances that changed since the due date for making the carryforward election so as to make the filing of a carryforward election advantageous to the issuing authority; and

(6) The issuing authority must satisfy all of the requirements for making the carryforward election (other than the requirement to make the election timely).

.02 For carryforward elections made under this revenue procedure, by signing the Form 8328, the issuing authority is certifying that it has met all of the requirements in § 4.01 of this revenue procedure.

.03 This procedure is in lieu of the letter ruling procedure under § 301.9100-3 that is used to obtain relief for a failure to make a carryforward election timely. Accordingly, an issuing authority is not required to pay a user fee in order to benefit from the relief provided by this revenue procedure.

.04 A Form 8328 filed under this revenue procedure should be sent to the Internal Revenue Service Center, Ogden, Utah, 84201.

SECTION 5. EFFECT ON OTHER DOCUMENTS

Except as expressly provided in this revenue procedure, this revenue procedure has no effect on the application of any other document.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective as of May 11, 2005.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Zoran Stojanovic of the Of-

fice of Assistant Chief Counsel (Exempt Organizations/Employment Tax/Government Entities). For further information regarding this revenue procedure, contact Mr. Stojanovic at (202) 622-3980 (not a toll-free call).

Part IV. Items of General Interest

Supplemental Information for Notice 2003-47 and Announcement 2005-19, Executive Stock Option Transaction and Settlement Initiative

Announcement 2005-39

This document sets forth additional guidance relating to Notice 2003-47, 2003-2 C.B. 132, and Announcement 2005-19, 2005-11 I.R.B. 744. Notice 2003-47 identifies as a listed transaction for purposes of sections 6111 and 6112 of the Internal Revenue Code and section 1.6011-4 of the Income Tax Regulations a transaction (Transaction) in which an officer, director, or employee (Executive) to whom a compensatory nonstatutory stock option or restricted stock is granted in connection with the performance of services transfers the option or restricted stock to a related person in exchange for a deferred payment obligation. Announcement 2005-19 describes the terms under which the Internal Revenue Service will resolve listed transactions that are the same as, or substantially similar to, the transaction described in Notice 2003-47. Taxpayers have until May 23, 2005, to notify the Service of their intent to participate in the settlement described in the announcement.

A. Penalty for Executives with Unexercised Options or Unvested Stock

Under Section 3(c)(1) of Announcement 2005-19, if the option has not been exercised or the restricted stock has not vested, then the Executive recognizes compensation income in the year in which the option is exercised or the stock vests, and the Executive must pay an accuracy-related penalty under section 6662 equal to ten percent of the amount of the underpayment attributable to the Transaction. Specifically, Section 3(c)(1)(iv) of Announcement 2005-19 states that “the amount of the underpayment attributable

to the Transaction is equal to the increased tax resulting from the income recognized under Sections 3(a)(1) and (2).” Section 3(a)(1) determines the amount of compensation income the Executive must recognize, and Section 3(a)(2) determines the amount of gain the Executive must recognize.

To determine the amount of the penalty imposed under Section 3(c)(1)(iv), the underpayment attributable to the Transaction does not include the increased tax resulting from compensation income recognized in the year of exercise or vesting in excess of the amount of the deferred payment obligation received in exchange for the option or restricted stock.¹

B. Application of Section 6654 for a Settlement of Taxable Year 2004

Under Section 3(a) of Announcement 2005-19, an Executive generally must recognize the compensation income from the Transaction in the taxable year that the stock was disposed of or, if not yet disposed of, in the taxable year that includes December 31, 2004, except in the case of an unexercised option or unvested stock.

Section 6654(a) imposes an addition to the tax in the case of any underpayment of estimated tax by an individual, computed at the underpayment rate established under section 6621 on the amount of the underpayment for the period of the underpayment. Section 6654(b)(1) provides that the amount of the underpayment is the excess of the required installment over the amount (if any) of the installment paid on or before the due date of the installment. Section 6654(d)(1) generally provides that the required installment is 25 percent of the required annual payment, which is the lesser of (i) 90 percent of the tax shown on the return for the taxable year (or, if no return is filed, 90 percent of the tax for the year), or (ii) 100 percent (or 110 percent for adjusted gross income in excess of \$150,000) of the tax shown on the return for the individual for the preceding taxable year. Section 6654(e)(3) provides that no addition to tax shall be imposed under

section 6654(a) with respect to any underpayment to the extent the Secretary determines that by reason of casualty, disaster, or other unusual circumstances the imposition of an addition to tax would be against equity and good conscience.

In determining the amount of any addition to tax under section 6654, tax attributable to income that was recognized in the taxable year that includes December 31, 2004, as a result of settling the Transaction pursuant to Announcement 2005-19 and that otherwise would not have been included in income in 2004 will not be treated as “tax shown on the return for the taxable year.”

C. Effect of Settling on Filing Future Disclosure Statements Under Treas. Reg. § 1.6011-4

Under Treas. Reg. § 1.6011-4(e)(1), the disclosure statement for a reportable transaction, which includes a listed transaction, must be attached to the taxpayer’s tax return for each taxable year in which a taxpayer participates in a reportable transaction. Under section 6707A(a), any person who fails to include on any return or statement any information with respect to a reportable transaction that is required under section 6011 to be included with a return or statement shall pay a penalty in the amount determined under section 6707A(b).

A taxpayer who settles a Transaction pursuant to Announcement 2005-19 does not have to disclose that Transaction under Treas. Reg. § 1.6011-4 for the taxable year that includes December 31, 2004, or for any subsequent taxable year.

D. Contact Information

The principal author of this announcement is Nancy M. Galib of the Office of Associate Chief Counsel (Procedure & Administration). For further information regarding this announcement, contact Nancy M. Galib at (202) 622-4940 (not a toll-free call).

¹ For a discussion of the determination of the amount of the deferred payment obligation, see Announcement 2005-19 at n. 4.

Withholding Exemptions: Correction

Announcement 2005-40

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Correcting Amendment.

SUMMARY: This document corrects final and temporary regulations (T.D. 9196, 2005-19 I.R.B. 1000) that were published in the **Federal Register** on Thursday, April 14, 2005 (70 FR 19694). The document contains regulations providing guidance under section 3402(f) of the Internal Revenue Code (Code) for employers and employees relating to the Form W-4, “Employee’s Withholding Allowance Certificate.”

DATES: This document is effective on April 14, 2005.

FOR FURTHER INFORMATION CONTACT: Margaret A. Owens, (202) 622-0047 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

Background

The final and temporary regulations (T.D. 9196) that are the subject of these corrections are under section 3402 of the Internal Revenue Code.

Need for Correction

As published, T.D. 9196 contains errors that may prove to be misleading and are in need of clarification.

* * * * *

Correction of Publication

Accordingly, 26 CFR Part 31 is corrected by making the following correcting amendment:

Part 31 — Employment Taxes

Paragraph 1. The authority citation for part 31 continues to read in part as follows:

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

§31.3402(f)(2)-1T[Corrected]

1. Section 31.3402(f)(2)-1T(g)(4), the second sentence is amended by removing the date “April 14, 2008.” and adding “April 11, 2008.” in its place.

§31.3402(f)(5)-1T[Corrected]

2. Section 31.3402(f)(5)-1T(a)(2), the second sentence is amended by removing the date “April 14, 2008.” and adding “April 11, 2008.” in its place.

Cynthia Grigsby,
*Acting Chief, Publications
and Regulations Branch,
Legal Processing Division,
Associate Chief Counsel
(Procedure and Administration).*

(Filed by the Office of the Federal Register on May 16, 2005, 8:45 a.m., and published in the issue of the Federal Register for May 17, 2005, 70 F.R. 28211)

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.
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Key to Abbreviations:

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

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