

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. 2009-3, page 382.

Insurance companies; interest rate tables. Prevailing state assumed interest rates are provided for the determination of reserves under section 807 of the Code for contracts issued in 2008 and 2009. Rev. Rul. 92-19 supplemented. Rev. Rul. 2008-19 modified.

Rev. Rul. 2009-4, page 408.

Section 1256 contracts marked to market. This ruling holds that Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code.

T.D. 9438, page 387.

REG-150066-08, page 423.

Final, temporary, and proposed regulations under section 954 of the Code relate to foreign base company sales income in cases in which personal property sold by a controlled foreign corporation is manufactured, produced, or constructed pursuant to a contract manufacturing arrangement or by one or more branches of the controlled foreign corporation. A public hearing on the proposed regulations is scheduled for April 20, 2009.

Notice 2009-10, page 419.

This notice serves to extend the application of the future regulations described in Notice 2008-91, 2008-43 I.R.B. 1001, to a third taxable year in certain cases and to extend Rev. Proc. 2008-26, 2008-21 I.R.B. 1014, to calendar year 2009.

EMPLOYEE PLANS

Notice 2009-9, page 419.

This notice provides guidance to financial institutions on the reporting rules applicable to required minimum distributions (RMDs) for 2009 in light of the enactment of the Worker, Retiree, and Employer Recovery Act of 2008. Section 201 of the Act waives any RMDs for 2009 from individual retirement arrangements (IRAs) and retirement plans that hold participant benefits in individual accounts. This notice modifies the reporting requirements applicable to RMDs from IRAs to reflect the waiver of the RMD rules for 2009. Notice 2002-27 modified.

EMPLOYMENT TAX

T.D. 9440, page 409.

REG-148568-04, page 421.

Final, temporary, and proposed regulations under sections 6011 and 6302 of the Code relate to the annual filing of federal employment tax returns and requirements for employment tax deposits. The regulations concern reporting and paying income taxes withheld from wages and reporting and paying taxes under the Federal Insurance Contributions Act (FICA) (collectively, "employment taxes"). The regulations generally allow certain employers to file a Form 944, *Employer's ANNUAL Federal Tax Return*, rather than Form 941, *Employer's QUARTERLY Federal Tax Return*.

(Continued on the next page)

Announcements of Disbarments and Suspensions begin on page 424.
Finding Lists begin on page ii.



Department of the Treasury
Internal Revenue Service

ADMINISTRATIVE

T.D. 9439, page 416.

Final regulations under section 6103 of the Code relate to disclosures of corporate tax return information to the Bureau of Economic Analysis. The regulations authorize the IRS to disclose certain items of corporate tax return information to the Secretary of Commerce for purposes of structuring United States national economic accounts and conducting related statistical activities authorized by law.

Notice 2009-11, page 420.

This notice provides that the February 17, 2009, due date for brokers to furnish Form 1099-B information to customers established under section 403 of the Energy Improvement and Extension Act of 2008 will apply to certain other tax information reportable for tax year 2008 if furnished to customers with Form 1099-B statements on an annual composite tax reporting statement.

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 446.—General Rule for Methods of Accounting

26 CFR 1.446-1: *General rule for methods of accounting.*

A revenue ruling holds that Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code. See Rev. Rul. 2009-4, page 408.

Section 481.—Adjustments Required by Changes in Method of Accounting

A revenue ruling holds that Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code. See Rev. Rul. 2009-4, page 408.

Section 807.—Rules for Certain Reserves

Insurance companies; interest rate tables. Prevailing state assumed interest rates are provided for the determination of reserves under section 807 of the Code for contracts issued in 2008 and 2009. Rev. Rul. 92-19 supplemented. Rev. Rul. 2008-19 modified.

Rev. Rul. 2009-3

For purposes of § 807(d)(4) of the Internal Revenue Code, for taxable years beginning after December 31, 2007, this ruling supplements the schedules of prevailing state assumed interest rates set forth in Rev. Rul. 92-19, 1992-1 C.B. 227. This information is to be used by insurance companies in computing their reserves for (1) life insurance and supplementary total and permanent disability benefits, (2) individual annuities and pure endowments, and (3) group annuities and pure endowments. As § 807(d)(2)(B) requires that the interest rate used to compute these reserves be the greater of (1) the applicable federal interest rate, or (2) the prevailing state assumed interest rate, the table of applicable federal interest rates in Rev. Rul. 92-19 is also supplemented.

Following are supplements to schedules A, B, C, and D to Part III of Rev. Rul. 92-19, providing prevailing state assumed interest rates for insurance products with different features issued in 2008 and 2009, and a supplement to the table in Part IV of Rev. Rul. 92-19, providing the applicable federal interest rates under § 807(d) for 2008 and 2009. This ruling does not supplement Parts I and II of Rev. Rul. 92-19.

This is the seventeenth supplement to the interest rates provided in Rev. Rul. 92-19. Earlier supplements were published in Rev. Rul. 93-58, 1993-2 C.B. 241 (interest rates for insurance products issued in 1992 and 1993); Rev. Rul. 94-11, 1994-1 C.B. 196 (1993 and 1994); Rev. Rul. 95-4, 1995-1 C.B. 141 (1994 and 1995); Rev. Rul. 96-2, 1996-1 C.B. 141 (1995 and 1996); Rev. Rul. 97-2, 1997-1 C.B. 134 (1996 and 1997); Rev. Rul. 98-2, 1998-1 C.B. 259 (1997 and 1998); Rev. Rul. 99-10, 1999-1 C.B. 671 (1998 and 1999); Rev. Rul. 2000-17, 2000-1 C.B. 842 (1999 and 2000); Rev. Rul. 2001-11, 2001-1 C.B. 780 (2000 and 2001); Rev. Rul. 2002-12, 2002-1 C.B. 624 (2001 and 2002); Rev. Rul. 2003-24, 2003-1 C.B. 557 (2002 and 2003); Rev. Rul. 2004-14, 2004-1 C.B. 511 (2003 and 2004); Rev. Rul. 2005-29, 2005-1 C.B. 1080 (2004 and 2005); Rev. Rul. 2006-25, 2006-1 C.B. 882 (May 15, 2006) (2005 and 2006); Rev. Rul. 2007-10, 2007-1 C.B. 660 (Mar. 5, 2007) (2006 and 2007); and Rev. Rul. 2008-19, 2008-13 I.R.B. 669 (Mar. 31, 2008) (2007 and 2008).

Part III. Prevailing State Assumed Interest Rates — Products Issued in Years After 1982.*

Schedule A

STATUTORY VALUATION INTEREST RATES
BASED ON THE 1980 AMENDMENTS TO THE
NAIC STANDARD VALUATION LAW

A. Life insurance valuation:

<u>Guarantee Duration (years)</u>	<u>Calendar Year of Issue</u>	
	<u>2009</u>	<u>2008***</u>
10 or fewer	4.50**	4.50
More than 10 but not more than 20	4.25**	4.25
More than 20	4.00**	4.00

Source: Rates calculated from the monthly averages, ending June 30, 2008, of Moody's Composite Yield on Seasoned Corporate Bonds.

*The terms used in the schedules in this ruling and in Part III of Rev. Rul. 92-19 are those used in the Standard Valuation Law; the terms are defined in Rev. Rul. 92-19.

**As these rates exceed the applicable federal interest rate for 2009 of 4.06 percent, the valuation interest rate to be used for this product under § 807 is the applicable rate specified in this table.

***The valuation interest rates for life insurance contracts issued in 2008 as set forth in Schedule A of Rev. Rul. 2008-19, 2008-13 I.R.B. 669 (Mar. 31, 2008) are corrected by the numbers set forth in this Schedule A.

Part III, Schedule B

STATUTORY VALUATION INTEREST RATES
BASED ON THE 1980 AMENDMENTS TO THE
NAIC STANDARD VALUATION LAW

B. Single premium immediate annuities and annuity benefits involving life contingencies arising from other annuities with cash settlement options and from guaranteed interest contracts with cash settlement options:

<u>Calendar Year of Issue</u>	<u>Valuation Interest Rate</u>
2008	5.50*

Source: Rates calculated from the monthly averages, ending June 30, 2008, of Moody's Composite Yield on Seasoned Corporate Bonds (formerly known as Moody's Corporate Bond Yield Average — Monthly Average Corporates). The terms used in this schedule are those used in the Standard Valuation Law as defined in Rev. Rul. 92-19.

*As this prevailing state assumed interest exceeds the applicable federal interest rate for 2008 of 4.06 percent, the valuation interest rate of 5.50 percent is to be used for this product under § 807.

Part III, Schedule C24 — 2008

**STATUTORY VALUATION INTEREST RATES
BASED ON NAIC STANDARD VALUATION LAW
FOR 2008 CALENDAR YEAR BUSINESS
GOVERNED BY THE 1980 AMENDMENTS**

C. Valuation interest rates for other annuities and guaranteed interest contracts that are valued on an issue year basis:

Cash Settlement Options?	Future Interest Guarantee?	Guarantee Duration (years)	Valuation Interest Rate (%) For Plan Type		
			A	B	C
Yes	Yes	5 or fewer	5.50*	5.00*	4.50*
		More than 5, but not more than 10	5.50*	5.00*	4.50*
		More than 10, but not more than 20	5.00*	4.50*	4.25*
		More than 20	4.25*	4.00	4.00
Yes	No	5 or fewer	5.75*	5.00*	4.75*
		More than 5, but not more than 10	5.50*	5.00*	4.75*
		More than 10, but not more than 20	5.00*	4.75*	4.50*
		More than 20	4.50*	4.25*	4.25*
No	Yes or No	5 or fewer	5.50*		
		More than 5, but not more than 10	5.50*	NOT APPLICABLE	
		More than 10, but not more than 20	5.00*		
		More than 20	4.50*		

Source: Rates calculated from the monthly averages, ending June 30, 2008, of Moody's Composite Yield on Seasoned Corporate Bonds.

*As these rates exceed the applicable federal interest rate for 2008 of 4.06 percent, the valuation interest rate to be used for this product under § 807 is the applicable rate specified in the above table.

Part III, Schedule D24 — 2008

STATUTORY VALUATION INTEREST RATES
 BASED ON NAIC STANDARD VALUATION LAW
 FOR 2008 CALENDAR YEAR BUSINESS
GOVERNED BY THE 1980 AMENDMENTS

D. Valuation interest rates for other annuities and guaranteed interest contracts that are contracts with cash settlement options and that are valued on a change in fund basis:

Cash Settlement Options?	Future Interest Guarantee?	Guarantee Duration (years)	Valuation Interest Rate For Plan Type		
			A	B	C
Yes	Yes	5 or fewer	6.00	5.75	4.75
		More than 5, but not more than 10	6.00	5.75	4.75
		More than 10, but not more than 20	5.50	5.50	4.50
		More than 20	5.00	5.00	4.25*
Yes	No	5 or fewer	6.25	6.00	5.00
		More than 5, but not more than 10	6.00	6.00	5.00
		More than 10, but not more than 20	5.75	5.50	4.75
		More than 20	5.00	5.00	4.50*

Source: Rates calculated from the monthly averages, ending June 30, 2008, of Moody's Composite Yield on Seasoned Corporate Bonds.

*As the applicable federal interest rate for 2008 of 4.06 percent is less than the prevailing state assumed interest rate, the valuation interest rate to be used for this product under § 807 is the applicable rate specified in the above table.

Part IV. Applicable Federal Interest Rates.

TABLE OF APPLICABLE FEDERAL INTEREST RATES FOR PURPOSES OF § 807

<u>Year</u>	<u>Interest Rate</u>
2008	4.06
2009	4.06

Sources: Rev. Rul. 2004–106, 2004–2 C.B. 893, for the 2005 rate; Rev. Rul. 2005–77, 2005–2 C.B. 1071, for the 2006 rate; Rev. Rul. 2006–61, 2006–2 C.B. 1028 (Dec. 11, 2006) for the 2007 rate; Rev. Rul. 2007–70, 2007–50 C.B. 1158 (Nov. 20, 2007) for the 2008 rate; and Rev. Rul. 2008–53, 2008–49 I.R.B. 1231 (Nov. 19, 2008) for the 2009 rate.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 92–19 is supplemented by the addition to Part III of that ruling of prevailing state assumed interest rates under § 807 for certain insurance products issued in 2008 and 2009 and is further supplemented by an addition to the table in Part IV of Rev. Rul. 92–19 listing applicable federal interest rates. Parts I and II of Rev. Rul. 92–19 are not affected by this ruling. Rev. Rul. 2008–19 is modified in that the valuation interest rates set forth in Schedule A of this ruling for contracts issued in 2008 correct and replace those set forth in Schedule A of Rev. Rul. 2008–19.

DRAFTING INFORMATION

The principal author of this revenue ruling is Josephine H. Firehock of the Office of Associate Chief Counsel (Financial Institutions and Products). For further information regarding this revenue ruling, contact her at (202) 622–3970 (not a toll-free call).

Section 954.—Foreign Base Company Income

26 CFR 1.954–3: Foreign base company sales income.

T.D. 9438

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 1

Guidance Regarding Foreign Base Company Sales Income

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains final and temporary regulations that provide guidance relating to foreign base company sales income in cases in which personal property sold by a controlled foreign corporation is manufactured, produced, or constructed pursuant to a contract manufacturing arrangement or by one or more branches of the controlled foreign corporation. These regulations modify the foreign base company sales income regulations to address current business structures and practices, particularly the growing importance of contract manufacturing and other manufacturing arrangements. These regulations, in general, will affect controlled foreign corporations and their United States shareholders. The text of the temporary regulations also serves

as the text of the proposed regulations (REG–150066–08) set forth in the notice of proposed rulemaking on this subject in this issue of the Bulletin.

DATES: *Effective Date:* These regulations are effective July 1, 2009.

Applicability Date: For dates of applicability, see §1.954–3(c) and §1.954–3T(e). The final regulations shall apply to taxable years of controlled foreign corporations beginning after June 30, 2009, and for taxable years of United States shareholders in which or with which such taxable years of the controlled foreign corporations end. The temporary regulations shall apply to taxable years of controlled foreign corporations beginning after June 30, 2009, and for taxable years of United States shareholders in which or with which such taxable years of the controlled foreign corporations end.

FOR FURTHER INFORMATION CONTACT: Ethan Atticks, (202) 622–3840 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

On February 28, 2008, the IRS and the Treasury Department published in the **Federal Register** proposed regulations (REG–124590–07, 2008–16 I.R.B. 801 [73 FR 10716], as corrected at 73 FR 20201), which provided proposed amendments to §1.954–3, addressing the treatment of contract manufacturing arrangements under the foreign base company sales income (FBCSI) rules.

Written comments were received in response to the notice of proposed rulemaking, and a public hearing on the proposed regulations was held on July 29, 2008.

Section 954(d)(1) defines *FBCSI* to mean income derived by a controlled foreign corporation (CFC) in connection with: (1) the purchase of personal property from a related person and its sale to any person, (2) the sale of personal property to any person on behalf of a related person, (3) the purchase of personal property from any person and its sale to a related person or (4) the purchase of personal property from any person on behalf of a related person, provided (in all these cases) that the property is manufactured, produced, grown or extracted outside of the CFC's country of organization and is sold for use, consumption or disposition outside of such country.

The existing regulations further define *FBCSI* and the applicable exceptions from *FBCSI*, including the exceptions to the *FBCSI* rules for personal property that is: (1) manufactured, produced, constructed, grown, or extracted within the CFC's country of organization (same country manufacture exception); (2) sold for use, consumption or disposition within the CFC's country of organization; and (3) manufactured, produced, or constructed by the CFC (the manufacturing exception). See §1.954-3(a)(2)-(4).

The existing regulations set forth certain tests to determine whether a CFC satisfies the manufacturing exception: the "substantial transformation test" of §1.954-3(a)(4)(ii) and the "substantive test" and safe harbor of §1.954-3(a)(4)(iii). For purposes of this preamble, the requirements of §1.954-3(a)(4)(ii) and 1.954-3(a)(4)(iii) will be referred to collectively as the "physical manufacturing test" and the satisfaction of either test will be described as "physical manufacturing."

The proposed regulations provide a third test for satisfying the manufacturing exception, which may apply when a CFC is involved in the manufacturing process but does not satisfy the physical manufacturing test. In particular, the proposed regulations provide that a CFC will satisfy the manufacturing exception if the facts and circumstances evince that the CFC makes a substantial contribution through

the activities of its employees to the manufacture, production, or construction of personal property (substantial contribution test). The proposed regulations also propose other modifications to the existing regulations to address the treatment of contract manufacturing arrangements under the *FBCSI* rules.

Written comments were received in response to the notice of proposed rulemaking, and a public hearing was held on July 29, 2008. After consideration of all the comments, the proposed regulations, as revised by this Treasury decision, are adopted as final and temporary regulations.

Summary of Comments and Explanation of Provisions

This Treasury decision contains final and temporary regulations relating to *FBCSI*. The temporary regulations contained in this Treasury decision also serve as the text of proposed regulations set forth in a notice of proposed rulemaking on this subject in this issue of the Bulletin. The preamble to this Treasury decision will refer to the proposed regulations published in the **Federal Register** on February 28, 2008, as the proposed regulations. The preamble will refer to the regulations that are published simultaneously as temporary regulations in this Treasury decision and as proposed regulations in this issue of the Bulletin as the temporary regulations.

A. Substantial Contribution Test

The proposed regulations provide that a CFC will satisfy the substantial contribution test with respect to personal property only if all the facts and circumstances evince that the CFC makes a substantial contribution through the activities of its employees to the manufacture of the property. Prop. Reg. §1.954-3(a)(4)(iv)(b) includes a non-exclusive list of activities (collectively, "*indicia* of manufacturing") to be considered in determining whether the CFC satisfies the substantial contribution test with respect to the manufacture, production, or construction of the personal property (manufacture of the personal property) under all the facts and circumstances.

1. General operation of substantial contribution test

In response to the proposed regulations, commentators requested further elaboration of the general operation of the substantial contribution test. For example, commentators requested guidance on the amount of activity performed by a CFC's employees that would be necessary to "satisfy" each individual activity listed among the *indicia* of manufacturing. Several commentators requested clarifications that suggested they believed that a certain threshold of employee activity was required before the activity would be considered in determining whether a CFC satisfied the substantial contribution test. Commentators requested, for example, clarification as to whether the "vendor selection" activity is satisfied if the CFC provides a contract manufacturer with an approved list of vendors but allows the contract manufacturer to make the final determination regarding the vendors to be used.

Commentators also requested guidance on how the *indicia* of manufacturing should be weighed in relation to one another and whether performing a certain minimum number of activities was required in order for the substantial contribution test to be satisfied. Others asked that the regulations explain whether a CFC must perform any particular activity in all cases to satisfy the substantial contribution test (for example, whether a CFC must always perform oversight and direction of the manufacturing process to satisfy the substantial contribution test). Some commentators requested that the regulations emphasize that the importance of each activity would vary by industry and by taxpayer. Commentators also requested that the regulations make clear that a CFC need not perform all of the *indicia* of manufacturing to establish a substantial contribution, and that the weight given to activities performed by employees of the CFC will depend on the economic significance of those activities to the business of the taxpayer with respect to the product being manufactured.

Although the proposed regulations provide guidance on many of these issues, the IRS and the Treasury Department believe that additional guidance with respect to the application of the substantial

contribution test is warranted in light of the comments received. Consequently, §1.954-3(a)(4)(iv)(c) is added to the final regulations to provide further clarification on the application of the substantial contribution test. First, §1.954-3(a)(4)(iv)(c) clarifies that all CFC employee functions contributing to the manufacture of the personal property will be considered in the aggregate when determining whether a substantial contribution is made to the manufacture of the personal property through the activities of a CFC's employees. Second, §1.954-3(a)(4)(iv)(c) clarifies that there is no single activity that will be accorded more weight than any other activity in every case or that will be required to be performed in all cases. Third, it clarifies that there is no minimum threshold with respect to functions performed by employees of a CFC before their functions with respect to a given activity may be taken into account as part of the substantial contribution test. Therefore, all functions performed by a CFC's employees are considered (and given appropriate weight) under the substantial contribution test, even if the CFC's employees perform only some of the functions in connection with any one activity (for example, some, but not all, of the vendor selection) considered under that test. The weight given to any functions performed by employees of the CFC with respect to any activity will be based on the economic significance of those functions to the manufacture, production, or construction of the relevant personal property. Corresponding amendments and additional examples have been added to the final regulations to illustrate further the application of the substantial contribution test. See §1.954-3(a)(4)(iv)(d).

Other commentators sought clarification as to the extent to which purely contractual assumptions of risk are considered in a substantial contribution analysis. The IRS and the Treasury Department believe that no further clarification in the final regulations is necessary to address this point. Both the proposed and final regulations provide that only activities of the CFC's employees are considered in the substantial contribution analysis and, consequently, purely contractual assumptions of risk are not considered in the substantial contribution analysis.

In addition, commentators requested that the regulations clarify that more than one person can provide a substantial contribution to the manufacturing process with respect to a given product. In response to this comment, the IRS and the Treasury Department amended the regulations to clarify that a CFC will not be precluded from making a substantial contribution to the manufacture of the personal property by the fact that other persons also make a substantial contribution to the manufacture, production, or construction of that property. Further, §1.954-3(a)(4)(iv)(d) *Example 9* is added to the final regulations to illustrate that more than one person can provide a substantial contribution to the manufacture of the same property.

2. *Indicia of manufacturing*

The IRS and the Treasury Department received numerous comments with respect to the specific activities listed in the proposed regulation that are considered in determining whether a CFC makes a substantial contribution through its employees to the manufacture, production, or construction of personal property.

a. *Oversight and Direction of Manufacturing*

Commentators requested that the IRS and the Treasury Department clarify certain issues related to the “oversight and direction of the activities or process” pursuant to which personal property is manufactured, produced, or constructed. Some commentators asked that the regulations provide that oversight and direction of the activities or process pursuant to which personal property is manufactured, produced, or constructed be a prerequisite for satisfying the substantial contribution test. Other commentators requested that the IRS and the Treasury Department clarify that in certain industries a substantial contribution can be made by a CFC without its employees engaging in significant oversight and direction of the activities or process pursuant to which personal property is manufactured, produced, or constructed. Some commentators focused on the fact that in an example in the proposed regulations the CFC was not treated as making a substantial contribution to the

manufacture of personal property when the CFC did not “regularly exercise” oversight and direction with respect to the contract manufacturer. See Prop. Reg. §1.954-3(a)(4)(iv)(c) *Example 1*.

The importance of oversight and direction of the activities or process pursuant to which personal property is manufactured, produced, or constructed will vary based on the facts and circumstances associated with the specific manufacture, production, or construction at issue. The IRS and the Treasury Department acknowledge that oversight and direction of the activities or process pursuant to which personal property is manufactured, produced, or constructed is likely to be an important element in many, but not all, substantial contribution analyses. Thus, to address taxpayer comments, the examples in the final regulations are amended to make clear that oversight and direction is not a prerequisite for satisfying the substantial contribution test and that in certain industries a substantial contribution could be made by a CFC without its employees engaging in oversight and direction of the activities or process pursuant to which personal property is manufactured, produced, or constructed. Finally, the examples in the final regulations do not use the potentially confusing reference to “regularly” exercising oversight.

b. *Material Selection, Vendor Selection, and Control of the Raw Materials, Work-in-process, and Finished Goods*

Some commentators asked if other activities listed among the *indicia* of manufacturing also represented means of exercising control of the raw materials, work-in-process and finished goods. The IRS and the Treasury Department acknowledge that some of the activities in the *indicia* of manufacturing may overlap with other activities in that list. The final regulations require a substantial contribution to the manufacture of the personal property through the activities of the CFC's employees and not satisfaction of any specific activity in the *indicia* of manufacturing. Therefore, the IRS and the Treasury Department determined that it was not necessary to clarify whether any particular function might reasonably be included under more than one heading in the *indicia* of manufacturing. However, to provide further clarity,

the final regulations group material selection, vendor selection, and control of the raw materials, work-in-process, and finished goods as a single activity in the *indicia* of manufacturing.

Commentators asked whether the control of the raw materials, work-in-process, and finished goods refers to the CFC having the contractual right to take possession of the personal property, to have title to the property, or to have economic risk of loss with respect to the property. These commentators requested clarification regarding whether tax ownership of raw materials, work-in-process and finished goods is required to have control of the raw materials, work-in-process, and finished goods. In connection with this question, commentators also asked whether a CFC can satisfy the substantial contribution test when the contract manufacturing arrangement is buy-sell or “turnkey” (that is, when the contract manufacturer purchases the raw materials).

Both the proposed and final regulations provide that only activities of the CFC’s employees are considered in the substantial contribution analysis. Thus, mere contractual rights, legal title, tax ownership, or assumption of economic risk are not considered in the substantial contribution analysis. To provide greater clarity, the final regulations revise Prop. Reg. §1.954–3(a)(4)(iv)(a), deleting the phrase “purchased by a controlled foreign corporation” in the first sentence of Prop. Reg. §1.954–3(a)(4)(iv)(a) to eliminate any inference that a CFC needs to own the raw materials that are used in the manufacturing process. In addition, examples in the final regulations clarify that buy-sell or turnkey contract manufacturing arrangements may satisfy the substantial contribution test. See §1.954–3(a)(4)(iv)(d) *Examples 3 and 9*.

c. *Management of Manufacturing Profits and Management of Risk of Loss*

Commentators requested clarification regarding which functions would qualify as “management of the manufacturing profits” or “management of the risk of loss.” Some commentators expressed concerns regarding the term “management of the manufacturing profits.” Other commentators suggested that it would add clarity if “management of the risk

of loss” were deleted from Prop. Reg. §1.954–3(a)(4)(iv)(b)(I) and included with “management of manufacturing profits” in a single item in the *indicia* of manufacturing. Some commentators expressed concern that the term “management of the risk of loss” implicitly excluded all other risk management functions. One commentator expressed the view that the *indicia* of manufacturing should include reference to management of enterprise risk, other than risks pertaining exclusively to sales and marketing functions. Some commentators suggested that management of the manufacturing profits might refer to such activities as the management of risks related to the raw materials and the utilization of plant capacity, but others thought it might encompass the finance function of a company.

The IRS and the Treasury Department agree that further clarification is needed as to the functions that are intended to be included within what was labeled “management of the manufacturing profits” and “management of the risk of loss” in the proposed regulations. The IRS and the Treasury Department intend that the substantial contribution test recognize contributions made by a CFC’s employees to the manufacturing process through functions which help to ensure that a plant is run in an economically efficient manner, such as optimization of plant capacity and reduction of waste (for example, waste of raw materials). On the other hand, not all corporate managerial decisions are intended to be considered in the substantial contribution test, because many such decisions are not directly related to the manufacture of the personal property with respect to which the substantial contribution analysis is being performed. For example, the IRS and the Treasury Department do not intend that corporate finance decisions be considered in the substantial contribution test. Similarly, the IRS and the Treasury Department do not intend that the general management of enterprise risk be considered in the substantial contribution test.

The IRS and the Treasury Department concluded that the term “management of the manufacturing costs or capacities” more accurately reflects the type of functions originally contemplated by “management of the manufacturing profits” in the proposed regulations and is also related to the types of functions contemplated

by the “management of the risk of loss.” Accordingly, the activity labeled “management of the manufacturing profits” in the proposed regulations is replaced in the final regulations with an activity entitled “management of manufacturing costs or capacities.” Further, the final regulations include a parenthetical list of functions (that is, managing the risk of loss, cost reduction or efficiency initiatives associated with the manufacturing process, demand planning, production scheduling, or hedging raw material costs) to elaborate on the meaning of the activity.

d. *Control of Logistics*

Commentators asked for clarification regarding the scope of logistical functions that will contribute towards a substantial contribution by a CFC. This activity is intended to include, for example, arranging for delivery of raw materials to a contract manufacturer, but to exclude, for example, delivery of finished goods to a customer. The final regulations provide further clarity on this issue by revising the activity to read “control of manufacturing related logistics.”

e. *Direction of the Development, Protection, and Use of Trade Secrets, Technology, Product Design, and Design Specifications, and Other Intellectual Property Used in Manufacturing the Product*

Commentators noted that the “and” in the description of this activity in the proposed regulations could be read to mean that directing the “development, protection, and use” of intellectual property are all required for this activity to be considered in the substantial contribution analysis. Commentators requested that these activities be stated in the disjunctive. The IRS and the Treasury Department adopted this comment, replacing “and” with “or” in the final regulations. This clarification is consistent with providing that all functions performed by a CFC’s employees are considered (and given appropriate weight) under the substantial contribution test. Thus, the CFC’s employees’ activities are considered regardless of whether the CFC’s employees perform all or only some of the functions listed in any enumerated item in the *indicia* of manufacturing.

The term “protection” is also deleted from the final regulations. The IRS and the Treasury Department were concerned that absent this clarification the final regulations could be read to provide that legal work performed by a CFC’s in-house legal staff was considered under the substantial contribution test, including in cases where, for example, litigation success could be heavily correlated to profitability or business failure with respect to a product. Further, the IRS and the Treasury Department modified the description of the activity in the final regulations to clarify that developing, or directing the use or development of, trade secrets, technology, or other intellectual property, are considered under the substantial contribution test, but only when activities of this nature are undertaken for the purpose of the manufacture of the personal property.

Commentators asked whether the intellectual property referred to in Prop. Reg. §1.954-3(a)(4)(iv)(b)(9) included marketing intangibles. The activity as described in both the proposed and final regulations is with respect to intellectual property used in the manufacture of the personal property. Thus, developing, or directing the use or development of, marketing intangibles is not intended to be considered in the substantial contribution test.

3. *Anti-abuse rule and safe harbor*

The IRS and the Treasury Department requested comments on whether the substantial contribution test should include an anti-abuse rule and safe harbor. In particular, comments were requested as to whether it would be appropriate to add an anti-abuse rule to prevent a CFC from satisfying the substantial contribution test in cases in which a significant portion of the direct or indirect contributions to the manufacture of personal property provided collectively by the CFC and any related U.S. persons are provided by one or more related U.S. persons. Commentators recommended that in determining whether a CFC makes a substantial contribution it should not be relevant whether other persons (whether U.S. or foreign, related or unrelated) contribute to the manufacturing process. The IRS and the Treasury Department agree with commentators that the substantial contribution test should focus on whether the activities of the CFC

itself are substantial without comparing those activities to those of other persons. Thus, the final regulations do not adopt such a rule. Examples in the final regulations also illustrate that the contributions of other persons to the manufacture of a product are not relevant to the analysis of whether a CFC makes a substantial contribution to the manufacturing process. See §1.954-3(a)(4)(iv)(d) *Examples 6, 7, and 9.*

The IRS and the Treasury Department also requested comments as to whether one or more safe harbors should be added to the substantial contribution test of the proposed regulations. Some commentators suggested that a CFC that contributes at least twenty percent of the costs of manufacturing personal property should be deemed to have substantially contributed to its manufacture. Other commentators suggested that a safe harbor was only appropriate if it were made clear that such a safe harbor would not function as a minimum standard and would be flexible enough to accommodate multiple industries. Many other commentators recommended that the IRS and the Treasury Department not adopt a safe harbor. The IRS and the Treasury Department concluded that no safe harbor could fairly apply across the range of industries potentially subject to §1.954-3, and therefore no safe harbor is provided in the final regulations.

4. *Definition of employee*

The IRS and the Treasury Department requested comments as to whether the requirement in the proposed regulations that the activities of the CFC be performed by its employees should take into account commercial arrangements where individuals performing services for the CFC while not on its payroll are nevertheless controlled by employees of the CFC. Commentators requested that the regulations expand the definition of the term “employee” to include various commercial or economic arrangements where individuals who perform services for a CFC under the CFC’s direction and control are not necessarily the CFC’s employees under local law. In particular, commentators suggested that the term “employee” could be defined for purposes of the substantial contribution test using section 3121(d)(2).

Other commentators asked that the term “employee” be defined more broadly to include anyone in an agency relationship with a CFC.

The IRS and the Treasury Department agree that clarification of the term “employee” will promote more effective application of these regulations. The IRS and the Treasury Department also agree that activities performed by certain non-payroll workers should be considered in determining whether the CFC provides a substantial contribution through “its employees.” However, the IRS and the Treasury Department concluded that it would be inappropriate to broaden the definition of employee to include anyone in an agency relationship with a CFC, because it could create unintended branch rule issues for taxpayers (for example, as a result of employees of a contract manufacturer being treated as employees of the CFC under such a definition). Thus, the final regulations provide that the term *employee* means any individual who, under §31.3121(d)-1(c), has the status of an employee for U.S. Federal tax purposes. This definition of the term “employee” may encompass certain seconded workers, part-time workers, workers on the payroll of a related employment company whose activities are directed and controlled by CFC employees, and contractors, so long as those individuals are deemed to be employees of the CFC under §31.3121(d)-1(c). Consistent with commentators’ request, this definition of the term employee may result in an individual being treated as an employee of two or more entities simultaneously.

5. *Product grouping*

Commentators requested that the determination of whether a CFC provides a substantial contribution to the manufacture of the personal property be made on the basis of a group or line of related products rather than on a product-by-product basis. The IRS and the Treasury Department believe that the substantial contribution test must be met with respect to each product. Whether manufactured goods are separate products or a single product for this purpose is determined by reference to the distinctions or lack thereof made by the CFC in its business operations and in its books and records, rather than by reference

to a third party's definition of a product or an industry product classification system, such as the Standard Industrial Classification Code. The IRS and the Treasury Department recognize that some activities taken into account under the substantial contribution test are not performed with respect to each individual unit of a particular product manufactured under a contract manufacturing arrangement. Section 1.954-3(a)(4)(iv)(d) *Example 11* has been added to the final regulations to address these comments.

6. Treatment of partnerships

Commentators requested that the regulations adopt principles to determine when the employees of a partnership should be treated as employees of the CFC for purposes of determining whether the CFC's relative economic interest in the partnership should be relevant in determining whether the CFC satisfies the substantial contribution test. The IRS and the Treasury Department concluded that this issue was beyond the scope of this regulatory project. However, the IRS and the Treasury Department continue to study this issue and welcome comments.

7. Rebuttable presumption

The proposed regulations provide a rebuttable presumption that the CFC does not satisfy the substantial contribution test when the activities of a branch of the CFC satisfy the physical manufacturing test. The presumption can only be rebutted if the taxpayer can prove to the satisfaction of the Commissioner that the CFC satisfied the substantial contribution test. Commentators suggested that satisfaction of the physical manufacturing test and satisfaction of the substantial contribution test should be treated equally under the regulations. Commentators also expressed the view that the standard required to rebut the presumption was either too subjective, imposed an improperly high standard, or both. They recommended that if a rebuttable presumption was retained, the standard required to rebut the presumption should be clear and convincing evidence.

In response to the comments received, the IRS and the Treasury Department reconsidered the ability to examine a CFC's claim that it substantially contributes to the manufacture of the personal property

when the activities of its branch satisfy the physical manufacturing test. Upon further study, the IRS and the Treasury Department concluded that the substantial contribution test can be administered without the benefit of a rebuttable presumption that a CFC does not satisfy the substantial contribution test when the activities of a branch of the CFC satisfy the physical manufacturing test. Thus, these final and temporary regulations do not contain a rebuttable presumption. The IRS and the Treasury Department took into account the request for parity of treatment with respect to satisfaction of the physical manufacturing test and the substantial contribution test in reaching this conclusion, as well as with respect to other aspects of the temporary regulations, as discussed further in Parts C and D of this preamble.

8. Documentation

Some commentators requested guidance on how taxpayers should document their activities for application of the substantial contribution test. Because the necessary documentation will vary by industry and by taxpayer, the IRS and the Treasury Department believe that creating general rules of documentation would prove impracticable and would not allow for enough flexibility in application of the substantial contribution test. Accordingly, the final regulations do not include documentation rules.

9. Automated manufacturing

Several comments were received concerning Prop. Reg. §1.954-3(a)(4)(iv)(c) *Example 4*. In *Example 4*, a CFC owns software and network systems that remotely and automatically (without human involvement) order raw materials for use by the contract manufacturer, take customer orders and route them to the contract manufacturer, and perform quality control. Although the CFC has a small number of computer technicians monitoring the software and network systems, the software and network systems were developed by employees of DP, the CFC's domestic parent corporation. Those DP employees supervise the CFC's computer technicians, evaluate the results of the automated manufacturing business, make ongoing operational decisions related to the performance of the manufacturing process,

redesign and update the products and the manufacturing process, and develop all of the upgrades and patches for the software and network systems owned by the CFC. The example concludes that the CFC does not provide a substantial contribution to the manufacture of Product X.

Commentators expressed concern that Prop. Reg. §1.954-3(a)(4)(iv)(c) *Example 4* did not recognize the importance of automated manufacturing in modern business practices. These commentators noted that manufacturing processes are increasingly automated and explained that in some high technology industries, automated manufacturing processes are the only way to manufacture and test the quality of certain products. In such industries, commentators noted that human involvement in various parts of the manufacturing process could be counterproductive. Some commentators were concerned that Prop. Reg. §1.954-3(a)(4)(iv)(c) *Example 4* penalized such automated manufacturing processes under the substantial contribution test.

The IRS and the Treasury Department agree that a CFC may provide a substantial contribution to a largely automated manufacturing process through its employees. Section 1.954-3(a)(4)(iv)(d) *Example 5* contains the same facts as Prop. Reg. §1.954-3(a)(4)(iv)(c) *Example 4*. Under those particular facts, substantial operational responsibilities and decision making by humans are required for the manufacturing process; however, they are not performed by the CFC. To provide additional guidance, the final regulations include an additional example, §1.954-3(a)(4)(iv)(d) *Example 6*, which illustrates that a CFC whose employees perform most of the functions that DP's employees perform in §1.954-3(a)(4)(iv)(d) *Example 5* makes a substantial contribution to the manufacturing process. This result applies even though DP's employees also contribute to the manufacturing process. Section 1.954-3(a)(4)(iv)(d) *Example 7* further illustrates that the CFC can make a substantial contribution through the activities of its employees regardless of whether the software and network systems were purchased by the CFC. These examples illustrate that the evaluation of whether a CFC makes a substantial contribution through its employees is determined based on whether industry-sufficient substantial

contribution activities are conducted by employees of the CFC.

B. The “Its” Argument

The proposed regulations clarify that for purposes of determining FBCSI a CFC qualifies for the manufacturing exception only if the CFC, acting through its employees, manufactured, produced, or constructed the relevant personal property within the meaning of §1.954-3(a)(4)(i). In response to the proposed regulations, some commentators maintained that a CFC need not satisfy the physical manufacturing test or the substantial contribution test to exclude a sale from FBCSI as long as the personal property sold is not the same as the property originally purchased by the CFC.

The IRS and the Treasury Department believe, as described in the preamble to the proposed regulations, that this position, commonly referred to as the “its” argument, is contrary to existing law, and represents an incorrect reading of section 954(d)(1). The final regulations accordingly maintain the rules provided in the proposed regulations regarding when personal property sold by a CFC will be considered to be other than the property purchased by the CFC.

C. Same Country Manufacture Exception

Commentators requested that the regulations incorporate the substantial contribution test in the same country manufacture exception. The IRS and the Treasury Department generally agree with commentators that if the substantial contribution test is sufficient to constitute the manufacture of the personal property where a CFC substantially contributes to the manufacture, production, or construction of that property, then it should be equally sufficient if those activities are performed by a related person (as defined in section 954(d)(3)) in the CFC’s country of organization. However, the IRS and the Treasury Department concluded that the same country manufacture exception would be difficult to administer and enforce in the case of a substantial contribution performed by an unrelated third party. Commentators suggested that these concerns could be ameliorated if taxpayers were required to maintain documentation with respect to a third party’s

substantial contribution. The IRS and the Treasury Department do not believe a documentation requirement adequately addresses these concerns because the IRS may be unable to audit the third party to verify if those substantial contribution activities in fact took place. Therefore, the final regulations provide that the same country manufacture exception is available to taxpayers in cases when a related person provides a substantial contribution to the manufacture of the personal property in the CFC’s country of organization. The final regulations also retain the rule provided in the proposed regulations modifying the application of the principles of §1.954-3(a)(4)(ii) and (a)(4)(iii) to reflect that the personal property manufactured, produced, or constructed in the country of organization of the selling corporation under the principles of §1.954-3(a)(4)(ii) and (a)(4)(iii) will qualify for the same country exception regardless of whose employees engage in qualifying manufacturing activities in that country.

D. Branch Rule

In addition to the amendments to §1.954-3(a), the proposed regulations also proposed amendments to the rules of §1.954-3(b) dealing with the application of the FBCSI rules to CFCs with branches or similar establishments (the branch rule), particularly the rules dealing with manufacturing branches. For the remainder of this preamble, the word “branch” will be used to refer to a “branch or similar establishment.”

1. Branch definition

Some commentators requested that the regulations define the term “branch” for purposes of the branch rule. These commentators suggested various definitions for the IRS and the Treasury Department to consider. Commentators suggested, for instance, that a branch be defined as a permanent establishment, as a business activity in a jurisdiction outside a CFC’s country of organization that has separate books and records, or as a trade or business outside a CFC’s country of organization. Commentators pointed to precedents in the section 367 and 987 regulations. Alternatively, some commentators requested that the regulations make clear that a *de minimis* amount of activity outside of a CFC’s

country of organization (for example, traveling employees) does not constitute a branch. Other commentators warned that requiring too high a level of activity outside of a CFC’s country of organization before a CFC was treated as having a “branch” would make it possible for a CFC organized in a lower-tax jurisdiction to contribute substantially to manufacturing activities in a higher-tax jurisdiction without causing the CFC to operate through a branch. Still other commentators suggested that courts have concluded that the IRS and the Treasury Department lack the regulatory authority to determine what constitutes a branch, and they may only address the consequences flowing from the existence of a branch.

The IRS and the Treasury Department determined that defining a branch was beyond the scope of this regulatory project. However, the temporary regulations retain an example similar to Prop. Reg. §1.954-3(b)(1)(ii)(c)(3)(f) *Example 3*, which illustrates that employees of a CFC that travel to a contract manufacturer’s location outside the CFC’s country of organization do not necessarily give rise to a branch in that location. See §1.954-3T(b)(1)(ii)(c)(3)(v) *Example 6*. See also Part D.3.b of this preamble.

2. Determination of hypothetical effective tax rate

Commentators requested that the regulations clarify that the tax rate disparity tests contained in §§1.954-3(b)(1)(i)(b) and (b)(1)(ii)(b) take into account incentive tax rates and other similar foreign tax relief available to a CFC in calculating the hypothetical effective tax rate of tax.

The IRS and the Treasury Department recognize that the tax rate disparity tests should take into account the actual tax rate paid with respect to the sales income by the selling branch or remainder and the hypothetical effective tax rate that would be paid by the manufacturing branch (or remainder) on that sales income under the laws of the country in which the manufacturing branch is located (or, in the case of a remainder, the country of organization of the CFC) if it were derived from sources within that country. Thus, the IRS and the Treasury Department agree that uniformly available tax incentives are to be considered in determining the hypotheti-

cal effective tax rate to be used in applying the tax rate disparity tests. In contrast, if a sales affiliate in the country of manufacturing can theoretically receive certain tax relief by taking certain actions, for example, by applying for special treatment pursuant to a ruling process, but the taxpayer has not affirmatively obtained such tax relief for the manufacturing branch (or remainder), then the hypothetical effective tax rate that would be paid by the manufacturing branch (or remainder) were it to derive the sales income should be the effective tax rate that would be applicable in that jurisdiction without such tax relief. The IRS and the Treasury Department believe that no change to the text of the existing regulations is necessary to address these points. However, §1.954-3T(b)(4) *Example (8)* is included in the temporary regulations to illustrate that uniformly applicable incentive tax rates are taken into account in determining the hypothetical effective tax rate.

The IRS and the Treasury Department concluded that other questions and requests in this area, including further clarification of the methodology for calculation of hypothetical tax rates, and for changes to the assumptions used in applying the tax rate disparity tests and determining the hypothetical effective tax rate, are beyond the scope of this regulatory project. However, the IRS and the Treasury Department continue to study these questions and welcome comments.

3. Multiple manufacturing branch rules

a. Determination of the Location of Manufacturing

Under Prop. Reg. §1.954-3(b)(1)(ii)(c)(3), the relevant tax rate disparity test is applied by giving satisfaction of the physical manufacturing test precedence over satisfaction of the substantial contribution test when multiple branches, or one or more branches and the remainder of the CFC, perform manufacturing activities with respect to the same item of personal property. If more than one branch (or one or more branches and the remainder of the CFC) each independently satisfies the physical manufacturing test, then the branch or the remainder of the CFC located or organized in the jurisdiction that would impose the lowest

effective rate of tax is treated as the location of manufacturing, producing, or constructing of the personal property for purposes of applying the tax rate disparity test (lowest-of-all-rates rule). If only one branch (or only the remainder of a CFC) independently satisfies the physical manufacturing test, then that branch (or remainder) is treated as the location of manufacturing, producing, or constructing of the personal property (location of manufacturing) for purposes of the tax rate disparity test.

If none of the branches or the remainder of the CFC independently satisfies the physical manufacturing test, but the CFC as a whole satisfies the substantial contribution test, then the location of manufacturing under the proposed regulations is the location of the branch or the remainder of the CFC that provides the predominant amount of the CFC's substantial contribution to the manufacture of the personal property (predominant place rule). If a predominant amount of the CFC's contribution to the manufacture of the personal property is not provided by any one location, then the location of manufacturing for purposes of applying the manufacturing branch tax rate disparity test under the proposed regulations is that place (either the remainder of the CFC or one of its branches) where manufacturing activity with respect to that property is performed and which would impose the highest effective rate of tax (highest-of-all-rates rule) when applying either §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b).

The IRS and the Treasury Department received multiple comments comparing and contrasting the highest- and lowest-of-all-rates rules. For example, commentators asked why the lowest-of-all-rates rule should apply when more than one branch (or one or more branches and the remainder of the CFC) independently satisfy the physical manufacturing test, whereas the highest-of-all-rates rule should apply when none of the branches or the remainder of the CFC independently satisfies the physical manufacturing test but the CFC as a whole satisfies the substantial contribution test. Commentators suggested that satisfaction of the physical manufacturing test and the substantial contribution test should be treated equally under the regulations, and therefore suggested having the same rule

in both circumstances. These commentators proposed a lowest-of-all-rates rule or the use of a weighted average of the tax rate of each branch or remainder of the CFC in both instances.

The IRS and the Treasury Department generally agreed with these comments. The IRS and the Treasury Department adopted taxpayers' comment that the same rule should apply consistently when a branch (or remainder) independently satisfies §1.954-3(a)(4)(i), regardless of whether it satisfies the physical manufacturing test or the substantial contribution test. Therefore the rules set forth in the proposed regulations are modified in the temporary regulations to provide that the lowest-of-all-rates rule will apply whenever a branch (or remainder) independently satisfies §1.954-3(a)(4)(ii), (iii), or (iv). However, providing parity of treatment for satisfaction of the physical manufacturing test and the substantial contribution test in respect of the lowest-of-all-rates rule is not sufficient to determine the location of manufacturing in cases where a CFC satisfies the substantial contribution test, yet no branch (or remainder) independently satisfies §1.954-3(a)(4)(iv).

Commentators questioned how to treat branches making contributions to the manufacture of the personal property through the activities of employees when no branch independently satisfies §1.954-3(a)(4)(iv). Some commentators expressed concern that it would be difficult to compare the relative contributions of various locations to determine which branch or remainder of the CFC made a predominant contribution under the predominant place rule. Other commentators requested greater guidance regarding the meaning of predominant contribution. Many commentators suggested that the highest-of-all-rates rule in the proposed regulations could lead to arbitrary results when no predominant contributor could be identified.

The IRS and the Treasury Department generally agreed with these comments. Consequently, the temporary regulations revise the rules for determining the location of manufacture of the personal property when more than one branch (or one or more branches and the remainder) contributes to the manufacture of the personal property but no branch (or

remainder) independently satisfies the physical manufacturing test or the substantial contribution test. The revised rules are based on the principle that the branch rule should apply in situations where purchase or sale activities with respect to the personal property are separated from manufacturing activities conducted by the CFC such that a demonstrably greater amount of manufacturing activity with respect to that property occurs in jurisdictions with tax rate disparity relative to the sales or purchase branch (or, in the case of a purchasing or selling remainder, the demonstrably greater amount of manufacturing activity with respect to the personal property occurs in jurisdictions with tax rate disparity relative to the purchasing or selling remainder).

Under the temporary regulations, if a demonstrably greater amount of manufacturing activity with respect to the personal property occurs in jurisdictions without tax rate disparity relative to the sales or purchase branch, the location of the sales or purchase branch will be deemed to be the location of manufacture of the personal property. In that case, the purchase or sales activities with respect to the property purchased or sold by or through the sales or purchase branch of the CFC will not, for purposes of determining FBCSI in connection with the sale of that property, be deemed to have substantially the same tax effect as if a branch were a wholly owned subsidiary corporation of the CFC. Otherwise, the location of manufacture of the personal property will be deemed to be the location of a manufacturing branch (or remainder) that has tax rate disparity relative to the sales or purchase branch. In that case, the purchase or sales activities with respect to the property purchased or sold by or through the sales or purchase branch of the CFC will be deemed to have substantially the same tax effect as if a branch were a wholly owned subsidiary corporation of the CFC, and that branch will be treated as a separate corporation for purposes of applying the regulations.

The temporary regulations apply analogous rules in the case of purchase or sales activity being conducted through the jurisdiction under the laws of which the CFC is organized. In such cases, however, the analysis focuses on whether the demonstrably greater amount of manufacturing activity with respect to the personal

property occurs in jurisdictions that do or do not have tax rate disparity relative to the jurisdiction under the laws of which the CFC is organized. The temporary regulations incorporate examples under §1.954-3T(b)(1)(ii)(c)(3)(v) to illustrate the application of these rules.

b. Location of Activities

The proposed regulations provide that for purposes of the multiple manufacturing branch rules the location of any activity with respect to the manufacture of the personal property is where the CFC's employees engage in such activity. Commentators suggested that in some cases the proposed regulations left it unclear, for purposes of determining the location of manufacturing, which jurisdiction was accorded credit for activities performed by an employee who is traveling temporarily to a foreign jurisdiction. Some commentators suggested that the location of activity rule should be removed or that the regulations should clarify that, for instance, the activities of employees of a CFC based in the jurisdiction under the laws of which the CFC is organized, even while traveling outside the CFC's country of organization, would generally be credited toward establishing that the jurisdiction under the laws of which the CFC is organized provided a predominant amount of a CFC's substantial contribution. The IRS and the Treasury Department believe the text of §1.954-3T(b)(1)(ii)(c)(3)(iv) makes clear that when an employee travels to perform activities, those activities are credited to the location in which the activities are conducted if there is a branch or remainder of the CFC in that jurisdiction. Section 1.954-3T(b)(1)(ii)(c)(3)(v) provides examples to further clarify this result.

Other commentators asked which location was accorded credit, if any, for activities performed by traveling employees of the CFC while located in a country in which there is no branch or remainder of the CFC. The temporary regulations provide that the location of any manufacturing activity is where the employees of the CFC perform that activity. Thus, the activities of employees while traveling to a country where the CFC does not maintain a branch or remainder are not credited to the branch or remainder where the traveling employees are regularly employed

for purposes of determining the location of manufacture of the personal property under the branch rule. Such activities, however, can be taken into account for purposes of satisfying the manufacturing exception and the substantial contribution test. See §1.954-3T(b)(1)(ii)(c)(3)(v) *Example 6*.

c. Clarifying Application of the Rule for Determining the Remainder of the CFC When Activities are Performed in Multiple Locations

Prop Reg. §1.954-3(b)(2)(ii)(a) provides that when treating the location of sales or purchase income as a separate corporation for purposes of determining whether FBCSI is realized, that separate corporation will exclude any branch or the remainder of the CFC that would be treated as a separate corporation, if the hypothetical tax rate imposed by the jurisdiction of each such branch or the remainder of the CFC were separately tested against the effective rate of tax imposed on the sales or purchase income under the relevant tax rate disparity test. Commentators suggested that the application of this rule for determining the remainder of the CFC when activities are performed in multiple locations is unclear. To clarify, the language from the proposed regulations is revised in the temporary regulations to describe what is included in the remainder, rather than what is excluded from the remainder, for purposes of determining whether there is FBCSI, after it is determined that a manufacturing branch should receive treatment as a separate corporation for purposes of applying the regulations. See §1.954-3T(b)(2)(ii)(a).

As with the rule provided in the proposed regulations, this rule is intended to provide that the activities of all branch locations (or, in the case of a remainder, the activities in the jurisdiction under the laws of which the CFC is organized) that do not have tax rate disparity relative to the sales or purchase branch location (or, in the case of a purchasing or selling remainder, the jurisdiction under the laws of which the CFC is organized) may be taken into account together with the activities of the sales or purchase branch (or, in the case of a purchasing or selling remainder, activities of the remainder of the CFC in the jurisdiction under the laws of

which the CFC is organized) for purposes of applying the separate corporation analysis required under the regulations and determining whether the sales income of the sales or purchase branch (or remainder) is FBCSI. Such determination will depend on whether the substantial contribution test is satisfied by the combined activities of the sales or purchase branch (or remainder) and the other locations aggregated with the sales or purchase branch (or remainder).

4. *Coordination of sales and manufacturing branch rules*

Commentators requested guidance on how the sales or purchase branch rules interact with the manufacturing branch rules. The current manufacturing branch rules contemplate the existence of a sales or purchase branch and a manufacturing branch. The rules provide that in such an instance the sales or purchase branch is treated as the remainder of the CFC for purposes of applying the tax rate disparity test. However, the sales or purchase branch rules of §1.954-3(b)(1)(i) of the existing regulations do not indicate that those rules do not apply in cases where the manufacturing branch rules are applied. Commentators were concerned that the manufacturing branch rules would be applied in addition to, rather than in lieu of, the sales or purchase branch rules.

The IRS and the Treasury Department agree that if one or more sales or purchase branches are used in addition to a manufacturing branch and §1.954-3T(b)(1)(ii)(c)(I) (use of one or more sales or purchases branches in addition to a manufacturing branch) is applied with respect to income from the sale of an item of personal property, then the sales or purchasing branch rules do not also apply to determine whether that income is FBCSI. Therefore, the temporary regulations clarify this point. See §1.954-3(b)(1)(i)(c).

5. *Unrelated to unrelated transactions*

Commentators suggested that there was uncertainty as to whether a substantial contribution to the manufacture, production, or construction of personal property by a CFC could cause the CFC to earn FBCSI in cases where, in the absence of the substantial contribution test, some taxpayers had taken the position that they

were outside the scope of the FBCSI rules. Some commentators expressed concern that transactions that are not currently subject to the existing regulations may become subject to the regulations as a result of the interaction of the substantial contribution test and the manufacturing branch rule. Other commentators suggested more generally that it was unclear if the substantial contribution test might create a branch through which a CFC carries on activities in a contract manufacturer's jurisdiction. Commentators suggested that taxpayers should be exempted from the branch consequences of the regulations by providing that the manufacturing branch rule only apply if the CFC was relying on the manufacturing exception for purposes of section 954(d)(1), or alternatively that the substantial contribution test should be elective. In this context, commentators noted that placing a CFC's substantial contribution activities, which are performed outside the country where the sales activities are performed, in a separately incorporated entity could prevent the CFC from having a branch that is subject to the manufacturing branch rule as a result of such activities.

The IRS and the Treasury Department agree that taxpayers may be subject to the FBCSI rules as a result of CFC employees performing *indicia* of manufacturing activities through a branch outside the country of organization of a CFC. The IRS and the Treasury Department believe this result is clear in the proposed regulations, and therefore no modifications are made to the text of the temporary regulations to clarify further this result. The IRS and the Treasury Department note that many commentators criticized the proposed regulations for drawing inappropriate distinctions between satisfaction of the physical manufacturing test and satisfaction of the substantial contribution test, and argued that updating the manufacturing exception in the context of modern business enterprise models required treating with equal importance and weight physical manufacturing and activities satisfying the substantial contribution test. The IRS and the Treasury Department adopted this comment in both the final regulations and the temporary regulations and, accordingly, did not incorporate in the temporary regulations an exception regarding activities performed through a branch located

outside the country of organization of a CFC for cases in which, in the absence of the substantial contribution test, some taxpayers had taken the position that they were outside the scope of the FBCSI rules.

One commentator noted that while there are strong policy reasons for the substantial contribution test and the branch rules to apply in the case of "unrelated to unrelated" transactions, the IRS and the Treasury Department should consider a special delayed effective date to allow taxpayers in this position time to restructure their operations in light of the regulations. The commentator argued that such taxpayers had been outside the scope of the FBCSI rules prior to these regulations and should be provided reasonable time to restructure. For a discussion of the effective date of the final and temporary regulations, see Part F of this preamble.

6. *Branch rule examples*

Commentators expressed concern that the facts of Prop. Reg. §1.954-3(b)(1)(ii)(c)(3)(f) *Example 4* ascribed most substantial contribution activities to the remainder, but determined that the remainder had not met the substantial contribution test. In the example, the remainder performs seven activities listed in the *indicia* of manufacturing of the proposed regulations, whereas Branch A performs only one activity (design) and Branch B performs only two activities. The example was intended to show that in a CFC's particular industry, the weight accorded to the activities performed by each branch can be comparable, even though a different number of activities occur in different locations, because the economic significance of the activities conducted in each location is comparable. However, the IRS and the Treasury Department recognize that the example may have caused confusion for taxpayers. Therefore, the allocation of activities in *Example 4* of Prop. Reg. §1.954-3(b)(1)(ii)(c)(3)(f) has been revised in §1.954-3T(b)(1)(ii)(c)(3)(v) *Example 3*. Moreover, *Examples 4, 5, and 6* of Prop. Reg. §1.954-3(b)(1)(ii)(c)(3)(f) have been restructured in the temporary regulations to be consistent with the revisions to the branch rules.

Commentators also noted that *Example 4* and *Example 5* of Prop. Reg. §1.954-3(b)(1)(ii)(c)(3)(f) suggest that

income other than sales or purchasing income may be FBCSI. These examples are amended in the temporary regulations to be consistent with section 954(d)(2), which provides that income attributable to the carrying on of purchase or sales activities by a branch may be FBCSI.

Commentators requested that the IRS and the Treasury Department add an example to the regulations to illustrate how the substantial contribution test and the branch rules operate in cases involving multiple manufacturing branches and multiple sales branches. The temporary regulations include such an example. See §1.954-3T(b)(1)(ii)(c)(3)(v) *Example 5*.

The temporary regulations also include an example illustrating the operation of the location of manufacture rules under §1.954-3T(b)(1)(ii)(c)(3) and the application of the substantial contribution test when a tested manufacturing location has been determined to have tax rate disparity with a tested sales location. See §1.954-3T(b)(4) *Example (9)*. *Example (9)* illustrates that a tested sales location can satisfy the substantial contribution test for purposes of determining FBCSI once it has been determined that a tested manufacturing location should be treated as a separate corporation for purposes of determining FBCSI. Although a branch that has tax rate disparity with the tested sales location is the tested manufacturing location, *Example (9)* concludes that the CFC does not have FBCSI from the sale of the personal property because, after applying the aggregation rules of §1.954-3T(b)(2)(ii)(a), the tested sales location satisfies §1.954-3(a)(4)(iv).

E. Conforming Amendments

Sections 1.954-3(a)(1)(i) and (c) of the existing regulations contain cross-references to foreign base company shipping income under §1.954-6. Section 954 was amended by Public Law 108-357 in 2004, and foreign base company shipping income was removed as a separate category of foreign base company income. The final regulations are amended by deleting both references to foreign base company shipping income to reflect the 2004 amendment to section 954.

Section 1.954-3(a)(1)(i) of the existing regulations defines “related person” and “unrelated person” by an obsolete cross

reference to §1.954-1(e). The final regulations are amended to define “related person” and “unrelated person” with reference to §1.954-1(f).

F. Effective Date

Several commentators requested that the new regulations provide for a delayed effective date to allow taxpayers to implement supply chain and structural changes that may be required to satisfy the substantial contribution test and the branch rules. The IRS and the Treasury Department agree that a delayed effective date is appropriate for taxpayers whose structures require modification to accommodate the new regulations. Accordingly, these final and temporary regulations will apply to taxable years of CFCs beginning after June 30, 2009, and for taxable years of United States shareholders in which or with which such taxable years of the CFCs end. Thus, the final and temporary regulations will become applicable January 1, 2010, for CFCs whose taxable year is the calendar year. The temporary regulations will expire on or before December 23, 2009. In addition, a taxpayer may choose to apply these final and temporary regulations retroactively with respect to its open taxable years. The taxpayer may so choose if and only if the taxpayer and all members of the taxpayer’s affiliated group apply both the final and temporary regulations, in their entirety, to the earliest taxable year of each controlled foreign corporation that ends with or within an open taxable year of the taxpayer and to all subsequent taxable years. A taxpayer that chose, prior to December 24, 2008, to apply Prop. Reg. §1.954-3 (73 FR 10716 as corrected at 73 FR 20201) in its entirety to all of the taxpayer’s open taxable years in which or with which a taxable year of a controlled foreign corporation of the taxpayer ended, may continue to apply Prop. Reg. §1.954-3 (73 FR 10716 as corrected at 73 FR 20201) in its entirety with respect to all of the taxpayer’s open taxable years that begin prior to July 1, 2009.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment

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

Drafting Information

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

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for 26 CFR part 1 continues to read in part as follows:

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

Par. 2. Section 1.954-3 is amended by:

1. Revising paragraphs (a)(1)(i), (a)(1)(iii) *Examples 1* and 2, (a)(2), (a)(4)(i), (a)(4)(ii), (a)(4)(iii), (a)(6)(i), and (c).

2. Adding paragraphs (a)(4)(iv) and (d).

3. Removing and reserving paragraphs (b)(1)(i)(c), (b)(1)(ii)(a), (b)(1)(ii)(c), (b)(2)(i)(b), (b)(2)(i)(d), (b)(2)(ii)(a), (b)(2)(ii)(b), (b)(2)(ii)(e) and (b)(4) *Example (3)*.

The additions and revisions read as follows:

§1.954-3 Foreign base company sales income.

(a) * * *

(1) *In general*—(i) *General rules*. Foreign base company sales income of a controlled foreign corporation shall, except

as provided in paragraphs (a)(2), (a)(3) and (a)(4) of this section, consist of gross income (whether in the form of profits, commissions, fees or otherwise) derived in connection with the purchase of personal property from a related person and its sale to any person, the sale of personal property to any person on behalf of a related person, the purchase of personal property from any person and its sale to a related person, or the purchase of personal property from any person on behalf of a related person. See section 954(d)(1). For purposes of the preceding sentence, except as provided in paragraphs (a)(2) and (a)(4) of this section, personal property sold by a controlled foreign corporation will be considered to be the same property that was purchased by the controlled foreign corporation regardless of whether the personal property is sold in the same form in which it was purchased, in a different form than the form in which it was purchased, or as a component part of a manufactured product. This section shall apply to the purchase and / or sale of personal property, whether or not such property was purchased and / or sold in the ordinary course of trade or business, except that income derived in connection with the sale of tangible personal property will not be considered to be foreign base company sales income if such property is sold to a person that is not a related person, as defined in §1.954-1(f), after substantial use has been made of the property by the controlled foreign corporation in its trade or business. This section shall not apply to the excess of gains over losses from sales or exchanges of securities or from futures transactions, to the extent such excess gains are includible in foreign personal holding company income of the controlled foreign corporation under §1.954-2; nor shall it apply to the sale of the controlled foreign corporation's property (other than its stock in trade or other property of a kind which would properly be included in its inventory if on hand at the close of the taxable year, or property held primarily for sale to customers in the ordinary course of its business) if substantially all the property of such corporation is sold pursuant to the discontinuation of the trade or business previously carried on by such corporation. The term "any person" as used in this paragraph (a)(1)(i) includes a related person as defined in §1.954-1(f).

* * * * *

(iii) * * *

Example 1. Controlled foreign corporation A, incorporated under the laws of foreign country X, is a wholly owned subsidiary of domestic corporation M. Corporation A purchases from M Corporation, a related person, articles manufactured in the United States and sells the articles to P, an unrelated person, for delivery and use in foreign country Y. Gross income of A Corporation derived from the purchase and sale of the personal property is foreign base company sales income.

Example 2. Corporation A in *Example 1* also purchases from P, an unrelated person, articles manufactured in country Y and sells the articles to foreign corporation B, a related person, for use in foreign country Z. Gross income of A Corporation derived from the purchase and sale of the personal property is foreign base company sales income.

* * * * *

(2) *Property manufactured, produced, constructed, grown, or extracted within the country in which the controlled foreign corporation is created or organized.* Foreign base company sales income does not include income derived in connection with the purchase and sale of personal property (or purchase or sale of personal property on behalf of a related person) in a transaction described in paragraph (a)(1) of this section if the property is manufactured, produced, constructed, grown, or extracted in the country under the laws of which the controlled foreign corporation which purchases and sells the property (or acts on behalf of a related person) is created or organized. See section 954(d)(1)(A). The principles set forth in paragraphs (a)(4)(ii) and (a)(4)(iii) of this section apply under this paragraph (a)(2) in determining what constitutes the manufacture, production, or construction of personal property, excluding the requirement set forth in paragraph (a)(4)(i) of this section that the provisions of paragraphs (a)(4)(ii) and (a)(4)(iii) of this section may only be satisfied through the activities of employees of the corporation manufacturing, producing, or constructing the personal property. The principles of paragraph (a)(4)(iv) of this section apply under this paragraph (a)(2) in determining what constitutes the manufacture, production, or construction of personal property but only when the personal property is manufactured, produced, or constructed by a person related to the controlled foreign corporation within the meaning of §1.954-1(f). The application of this paragraph (a)(2)

may be illustrated by the following examples:

* * * * *

(4) *Property manufactured, produced, or constructed by the controlled foreign corporation—(i) In general.* Foreign base company sales income does not include income of a controlled foreign corporation derived in connection with the sale of personal property manufactured, produced, or constructed by such corporation. A controlled foreign corporation will have manufactured, produced, or constructed personal property which the corporation sells only if such corporation satisfies the provisions of paragraph (a)(4)(ii), (a)(4)(iii), or (a)(4)(iv) of this section through the activities of its employees (as defined in §31.3121(d)-1(c) of this chapter) with respect to such property. A controlled foreign corporation will not be treated as having manufactured, produced, or constructed personal property which the corporation sells merely because the property is sold in a different form than the form in which it was purchased. For rules of apportionment in determining foreign base company sales income derived from the sale of personal property purchased and used as a component part of property which is not manufactured, produced, or constructed, see paragraph (a)(5) of this section.

(ii) *Substantial transformation of property.* If personal property purchased by a foreign corporation is substantially transformed by such foreign corporation prior to sale, the property sold by the selling corporation is manufactured, produced, or constructed by such selling corporation. The application of this paragraph (a)(4)(ii) may be illustrated by the following examples:

* * * * *

(iii) *Manufacture of a product when purchased components constitute part of the property sold.* If purchased property is used as a component part of personal property which is sold, the sale of the property will be treated as the sale of a manufactured product, rather than the sale of component parts, if the assembly or conversion of the component parts into the final product by the selling corporation involves activities that are substantial in nature and generally considered to constitute the manufacture, production, or

construction of property. Without limiting this substantive test, which is dependent on the facts and circumstances of each case, the operations of the selling corporation in connection with the use of the purchased property as a component part of the personal property which is sold will be considered to constitute the manufacture of a product if in connection with such property conversion costs (direct labor and factory burden) of such corporation account for 20 percent or more of the total cost of goods sold. In no event, however, will packaging, repackaging, labeling, or minor assembly operations constitute the manufacture, production, or construction of property for purposes of section 954(d)(1). The application of this paragraph (a)(4)(iii) may be illustrated by the following examples:

* * * * *

(iv) *Substantial contribution to manufacturing of personal property—(a) In general.* If an item of personal property would be considered manufactured, produced, or constructed (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) prior to sale by the controlled foreign corporation had all of the manufacturing, producing, and constructing activities undertaken with respect to that property prior to sale been undertaken by the controlled foreign corporation through the activities of its employees, then this paragraph (a)(4)(iv) applies. If this paragraph (a)(4)(iv) applies and if the facts and circumstances evince that the controlled foreign corporation makes a substantial contribution through the activities of its employees to the manufacture, production, or construction of the personal property sold, then the personal property sold by the controlled foreign corporation is manufactured, produced, or constructed by such controlled foreign corporation.

(b) *Activities.* The determination of whether a controlled foreign corporation makes a substantial contribution through the activities of its employees to the manufacture, production, or construction of the personal property sold involves, but will not necessarily be limited to, consideration of the following activities:

(1) Oversight and direction of the activities or process pursuant to which the property is manufactured, produced, or con-

structed (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section).

(2) Activities that are considered in, but that are insufficient to satisfy, the tests provided in paragraphs (a)(4)(ii) and (a)(4)(iii) of this section.

(3) Material selection, vendor selection, or control of the raw materials, work-in-process or finished goods.

(4) Management of manufacturing costs or capacities (for example, managing the risk of loss, cost reduction or efficiency initiatives associated with the manufacturing process, demand planning, production scheduling, or hedging raw material costs).

(5) Control of manufacturing related logistics.

(6) Quality control (for example, sample testing or establishment of quality control standards).

(7) Developing, or directing the use or development of, product design and design specifications, as well as trade secrets, technology, or other intellectual property for the purpose of manufacturing, producing, or constructing the personal property.

(c) *Application of substantial contribution test.* When considering whether a controlled foreign corporation makes a substantial contribution to the manufacture, production, or construction of the personal property, the performance of any activity in paragraph (a)(4)(iv)(b) of this section will be taken into account. The performance or lack of performance of any particular activity in paragraph (a)(4)(iv)(b) of this section, or of a particular number of activities in (a)(4)(iv)(b) of this section, is not determinative. The weight accorded to the performance of any quantum of any activity (whether or not specified in paragraph (a)(4)(iv)(b) of this section) will vary with the facts and circumstances of the particular business. See paragraph (a)(4)(iv)(d) *Examples 8, 10 and 11* of this section. In determining whether the activities of the controlled foreign corporation constitute a substantial contribution, there is no minimum performance threshold before an activity can be considered. The fact that other persons make a substantial contribution to the manufacture, production, or construction of the personal property prior to sale does not preclude the controlled foreign corporation from making a substantial contribution to the manufacture, construction, or production of that

property through the activities of its employees. See paragraph (a)(4)(iv)(d) *Example 9* of this section.

(d) *Examples.* The rules of this paragraph (a)(4)(iv) are illustrated by the following examples:

Example 1. No substantial contribution to manufacturing. (i) *Facts.* FS, a controlled foreign corporation, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. Under the terms of the contract, FS retains the right to control the raw materials, work-in-process, and finished goods, and the right to oversee and direct the activities or process pursuant to which Product X is manufactured by CM. FS owns the intellectual property used in the manufacturing process. However, FS does not exercise, through its employees, its powers to control the raw materials, work-in-process, or finished goods, and FS does not exercise its powers of oversight and direction. Likewise, FS does not, through its employees, develop or direct the use or development of the intellectual property for the purpose of manufacturing Product X.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. FS does not satisfy the test under this paragraph (a)(4)(iv) because it does not make a substantial contribution through the activities of its employees to the manufacture of Product X. Mere contractual rights to control materials, contractual rights to oversee and direct the manufacturing activities or process pursuant to which the property is manufactured, and ownership of intellectual property are not sufficient to satisfy this paragraph (a)(4)(iv). Therefore, under the facts and circumstances of the business, FS is not considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 2. Substantial contribution to manufacturing. (i) *Facts.* Assume the same facts as in *Example 1*, except for the following. FS, through its employees, engages in product design and quality control and controls manufacturing related logistics. Employees of FS exercise the right to oversee and direct the activities of CM in the manufacture of Product X.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section. The analysis

and conclusion would be the same if CM were related to FS because the relationship between CM and FS is irrelevant for purposes of applying paragraph (a)(4) of this section.

Example 3. Raw materials procured by contract manufacturer. (i) *Facts.* FS, a controlled foreign corporation, enters into a contract with CM to manufacture (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) Product X. CM physically performs the substantial transformation, assembly, or conversion required to manufacture Product X outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. Employees of FS select the materials that will be used to manufacture Product X. FS does not own the materials or work-in-process during the manufacturing process. FS, through its employees, exercises oversight and direction of the manufacturing process and provides quality control. FS manages the manufacturing costs and capacities with respect to Product X by managing the risk of loss and engaging in demand planning and production scheduling.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 4. Physical conversion by employees of a person other than the contract manufacturer. (i) *Facts.* FS, a controlled foreign corporation organized in Country M, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion required to manufacture Product X outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. CM contracts with another corporation for its employees in order to operate CM's manufacturing plant and transform, assemble, or convert the raw materials into Product X. Apart from the physical performance of the substantial transformation, assembly, or conversion of the raw materials into Product X, employees of FS perform all of the other manufacturing activities required in connection with the manufacture of Product X (for example, oversight and direction of the manufacturing process; vendor selection; control of raw materials, work-in-process, and finished goods; control of manufacturing related logistics; and quality control).

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a sub-

stantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 5. Automated manufacturing supervised by another person. (i) *Facts.* FS, a controlled foreign corporation, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation selected by FS, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion outside of FS's country of organization. Product X is sold by FS to related and unrelated persons for use outside of FS's country of organization. At all times, FS retains ownership of the raw materials, work-in-process, and finished goods. FS retains the right to oversee and direct the activities or process pursuant to which Product X is manufactured by CM, but does not exercise, through its employees, its powers of oversight and direction. FS is the owner of sophisticated software and network systems that remotely and automatically (without human involvement) take orders, route them to CM, order raw materials, and perform quality control. FS has a small number of computer technicians who monitor the software and network systems to ensure that they are running smoothly and apply any necessary patches or fixes. The software and network systems were developed by employees of DP, the U.S. corporate parent of FS. DP's employees supervise the computer technicians, evaluate the results of the automated manufacturing business, and make ongoing operational decisions, including decisions related to acceptable performance of the manufacturing process, stoppages of that process, and decisions related to product and manufacturing process design. DP's employees develop and provide to FS all of the upgrades to the software and network systems. DP also has employees who direct and control other aspects of the manufacturing process such as vendor and material selection, management of the manufacturing costs and capacities, and the selection of CM. The need for DP's employees to direct the activities of the FS employees and otherwise contribute to the manufacturing process evinces that substantial operational responsibilities and decision making are required to be exercised by parties other than CM in order to manufacture Product X.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstance of the business, FS does not satisfy the test under this paragraph (a)(4)(iv) because it does not make a substantial contribution through the activities of its employees to the manufacture of Product X. Mere ownership of materials and intellectual property along with contractual rights to exercise powers of direction and control are not sufficient to satisfy this paragraph (a)(4)(iv). The employees of FS do not perform the amount of activity necessary to constitute a substantial contribution. FS is not considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 6. Automated manufacturing supervised by FS. (i) *Facts.* Assume the same facts as in *Example 5*, except for the following. FS, through its employees, engages in the activities undertaken by DP's employees in *Example 5*. DP's employees also contribute to product and manufacturing process design, and provide support and oversight to FS in connection with functions performed by FS through its employees.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. This determination does not require a comparison between the activities of FS and the activities of DP. Selection of the contract manufacturer, even though not specifically identified in paragraph (a)(4)(iv)(b) of this section, is considered under paragraph (a)(4)(iv)(c) of this section in determining whether FS makes a substantial contribution to the manufacture of Product X through its employees. FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 7. Automated manufacturing supervised by FS with purchased intellectual property. (i) *Facts.* Assume the same facts as in *Example 6*, except for the following. The software and network systems, and the upgrades to those systems, were purchased by FS rather than developed by employees of FS.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. The lack of performance of software and network system development activities is not determinative under the facts and circumstances of the business. Therefore, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. This determination does not require a comparison between the activities of FS and the activities of DP. FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 8. Manufacture without intellectual property. (i) *Facts.* FS, a controlled foreign corporation, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. At all times, FS controls the raw materials, work-in-process, and finished goods. FS controls the manufacturing related logistics, manages the manufacturing costs and capacities, and provides quality control with respect to CM's manufacturing process

and product. No intellectual property of significant value is required to manufacture Product X. FS does not own any intellectual property underlying Product X, or hold an exclusive or non-exclusive right to manufacture Product X.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Because use of intellectual property plays little or no role in the manufacture of Product X, it is irrelevant to the substantial contribution analysis under paragraph (a)(4)(iv) of this section. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 9. Substantial contribution by more than one CFC. (i) *Facts.* FS1 and FS2, unrelated controlled foreign corporations, contract with CM, an unrelated corporation, to manufacture (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) Product X. CM physically performs the substantial transformation, assembly, or conversion required to manufacture Product X outside of FS1's and FS2's respective countries of organization. Neither FS1 nor FS2 owns the materials or work-in-process during the manufacturing process. Product X is sold by FS1 and FS2 to persons related to FS1 and FS2, respectively, for disposition outside of FS1's and FS2's respective countries of organization. FS1, through its employees, designs Product X. FS1 directs the use of the product design and design specifications, and other intellectual property, for the purpose of manufacturing Product X. Employees of FS1 also select the materials that will be used to manufacture Product X, and the vendors that provide those materials. FS2, through its employees, designs the process for manufacturing Product X. FS2, through its employees, manages the manufacturing costs and capacities with respect to Product X. FS1 and FS2 each provide quality control and oversight and direction of CM's manufacturing activities with respect to different aspects of the manufacture of Product X.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS1 or FS2 through the activities of their employees, FS1 or FS2 would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. The fact that other persons make a substantial contribution to the manufacture of personal property does not preclude a controlled foreign corporation from making a substantial contribution to the manufacture of personal property through the activities of its employees. In the analysis of whether FS1 or FS2 make a substantial contribution to the manufacture of Product X, each company takes into account its individual activities, including those of providing quality control and oversight and direction of the manufacture of Product X. In addition, no threshold level of activity is required, including with respect to providing quality control or oversight and direction of the

activities or process pursuant to which Product X is manufactured, before FS1 and FS2 can take into account their respective activities. Under the facts and circumstances of the business, both FS1 and FS2 satisfy the test under this paragraph (a)(4)(iv) because each independently makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS1 and FS2 are each considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 10. Manufacture of products designed by CFC. (i) *Facts.* FS, a controlled foreign corporation, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. Products in the X industry are distinguished (and vary widely in value) based on the raw materials used to make the product and the product design. FS designs the product and selects the materials that CM will use to manufacture Product X. FS also manages the manufacturing costs and capacities. Product X can be manufactured from the raw materials to FS's design specifications without significant oversight and direction, quality control, or control of manufacturing related logistics. The activities most relevant to the substantial contribution analysis under these facts are material selection, product design and management of the manufacturing costs and capacities.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS makes a substantial contribution through the activities of its employees to the manufacture of Product X. FS satisfies the test under this paragraph (a)(4)(iv) because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

Example 11. Direction and oversight of manufacturing and quality control through periodic visits. (i) *Facts.* FS, a controlled foreign corporation, purchases raw materials from a related person. The raw materials are manufactured (under the principles of paragraph (a)(4)(ii) or (a)(4)(iii) of this section) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion outside of FS's country of organization. Product X is sold by FS for use outside of FS's country of organization. FS controls the raw material, work-in-process, and finished goods, manages the manufacturing costs and capacities, and provides oversight and direction of the manufacture of Product X. Employees of FS visit CM's manufacturing facility for one week each quarter and perform quality control tests on a random sample of the units of Product X produced during the week. In the X industry, quarterly visits to a manufacturing facility by qual-

ified persons are sufficient to control the quality of manufacturing.

(ii) *Result.* If the manufacturing activities undertaken with respect to Product X prior to sale were undertaken by FS through the activities of its employees, FS would have satisfied the manufacturing exception contained in paragraph (a)(4)(ii) or (a)(4)(iii) of this section with respect to Product X. Therefore, this paragraph (a)(4)(iv) applies. Under the facts and circumstances of the business, FS satisfies the test under this paragraph (a)(4)(iv) with respect to Product X because it makes a substantial contribution through the activities of its employees to the manufacture of Product X. Therefore, FS is considered to have manufactured Product X under paragraph (a)(4)(i) of this section.

* * * * *

(6) *Special rule applicable to distributive share of partnership income—(i) In general.* To determine the extent to which a controlled foreign corporation's distributive share of any item of gross income of a partnership would have been foreign base company sales income if received by it directly, under §1.952-1(g), the property sold will be considered to be manufactured, produced, or constructed by the controlled foreign corporation, within the meaning of paragraph (a)(4)(i) of this section, only if the manufacturing exception of paragraph (a)(4)(i) of this section would have applied to exclude the income from foreign base company sales income if the controlled foreign corporation had earned the income directly, determined by taking into account only the activities of the employees of, and property owned by, the partnership.

* * * * *

(b) * * *

(1) * * *

(i) * * *

(c) [Reserved]. For further guidance, see §1.954-3T(b)(1)(i)(c).

(ii) * * *

(a) [Reserved]. For further guidance, see §1.954-3T(b)(1)(ii)(a).

* * * * *

(c) [Reserved]. For further guidance, see §1.954-3T(b)(1)(ii)(c).

(2) * * *

(i) * * *

(b) [Reserved]. For further guidance, see §1.954-3T(b)(2)(i)(b).

* * * * *

(d) [Reserved]. For further guidance, see §1.954-3T(b)(2)(i)(d).

* * * * *

(ii) * * *

(a) [Reserved]. For further guidance, see §1.954-3T(b)(2)(ii)(a).

(b) [Reserved]. For further guidance, see §1.954-3T(b)(2)(ii)(b).

* * * * *

(e) [Reserved]. For further guidance, see §1.954-3T(b)(2)(ii)(e).

* * * * *

(4) * * *

Example (3). [Reserved]. For further guidance, see §1.954-3T(b)(4) *Example (3)*.

* * * * *

(c) *Effective/applicability date*. Paragraphs (a)(1)(i), (a)(1)(iii) *Example 1*, (a)(1)(iii) *Example 2*, (a)(2), (a)(4)(i), (a)(4)(ii), (a)(4)(iii), (a)(4)(iv) and (a)(6)(i) shall apply to taxable years of controlled foreign corporations beginning after June 30, 2009, and for taxable years of United States shareholders in which or with which such taxable years of the controlled foreign corporations end.

(d) *Application of regulations to earlier taxable years*. A taxpayer may choose to apply these regulations and the regulations under §1.954-3T retroactively with respect to its open taxable years. The taxpayer may so choose if and only if the taxpayer and all members of the taxpayer's affiliated group (within the meaning of §1504(a)) apply both these regulations and the regulations under §1.954-3T, in their entirety, to the earliest taxable year of each controlled foreign corporation that ends with or within an open taxable year of the taxpayer and to all subsequent taxable years of the taxpayer.

Par. 3. Section 1.954-3T is added to read as follows:

§1.954-3T Foreign base company sales income (temporary).

(a) through (b)(1)(i)(b) [Reserved]. For further guidance, see §1.954-3(a) through (b)(1)(i)(b).

(c) *Use of more than one branch*. If a controlled foreign corporation carries on purchasing or selling activities by or through more than one branch or similar establishment located outside the country under the laws of which such corporation is created or organized, then §1.954-3(b)(1)(i)(b) shall be applied separately to the income derived by each

such branch or similar establishment (by treating such purchasing or selling branch or similar establishment as if it were the only branch or similar establishment of the controlled foreign corporation and as if any such other branches or similar establishments were separate corporations) in determining whether the use of such branch or similar establishment has substantially the same tax effect as if such branch or similar establishment were a wholly owned subsidiary corporation of the controlled foreign corporation. See paragraph (b)(1)(ii)(c)(I) of this section for rules applicable to a controlled foreign corporation that carries on purchase or sales activities by or through one or more branches or similar establishments in addition to carrying on manufacturing activities by or through one or more branches or similar establishments.

(ii) *Manufacturing branch—(a) In general*. If a controlled foreign corporation carries on manufacturing, producing, constructing, growing, or extracting activities by or through a branch or similar establishment located outside the country under the laws of which such corporation is created or organized and the use of the branch or similar establishment for such activities with respect to personal property purchased or sold by or through the remainder of the controlled foreign corporation has substantially the same tax effect as if the branch or similar establishment were a wholly owned subsidiary corporation of such controlled foreign corporation, the branch or similar establishment and the remainder of the controlled foreign corporation will be treated as separate corporations for purposes of determining foreign base company sales income of such corporation. See section 954(d)(2). The provisions of this paragraph (b)(1)(ii) and §1.954-3(b)(1)(ii)(b) will apply only if the controlled foreign corporation (including any branches or similar establishments of such controlled foreign corporation) manufactures, produces, or constructs such personal property within the meaning of §1.954-3(a)(4)(i), or carries on growing or extracting activities with respect to such personal property.

(b) [Reserved]. For further guidance, see §1.954-3(b)(1)(ii)(b).

(c) *Use of more than one branch—(I) Use of one or more sales or purchase branches in addition to a manufacturing*

branch. If, with respect to personal property manufactured, produced, constructed, grown, or extracted by or through a branch or similar establishment located outside the country under the laws of which the controlled foreign corporation is created or organized, purchasing or selling activities are carried on by or through more than one branch or similar establishment, or by or through one or more branches or similar establishments located outside such country, of such corporation, then §1.954-3(b)(1)(ii)(b) shall be applied separately to the income derived by each such purchasing or selling branch or similar establishment (by treating such purchasing or selling branch or similar establishment as though it alone were the remainder of the controlled foreign corporation) for purposes of determining whether the use of such manufacturing, producing, constructing, growing, or extracting branch or similar establishment has substantially the same tax effect as if such branch or similar establishment were a wholly owned subsidiary corporation of the controlled foreign corporation. If this rule applies, the sales or purchase branch rules contained in paragraph (b)(1)(i)(c) of this section and §1.954-3(b)(1)(i) do not apply. The application of this paragraph (b)(1)(ii)(c)(I) is illustrated by the following example:

Example. All activities of controlled foreign corporation conducted through sales branches and manufacturing branch. (i) *Facts*. FS, a controlled foreign corporation organized under the laws of country M, operates three branches. Branch A, located in country A, manufactures Product X under the principles of §1.954-3(a)(4)(i). Branch B, located in Country B, sells Product X manufactured by Branch A to customers for use outside of Country B. Branch C, located in Country C sells Product X manufactured by Branch A to customers for use outside of Country C. FS does not conduct any manufacturing or selling activities apart from the activities of Branches A, B and C. Country M imposes an effective rate of tax on sales income of 0%. Country A imposes an effective rate of tax on sales income of 20%. Country B imposes an effective rate of tax on sales income of 20%. Country C imposes an effective rate of tax on sales income of 18%.

(ii) *Result*. Pursuant to this paragraph (b)(1)(ii)(c)(I), §1.954-3(b)(1)(ii)(b) is applied to the sales income derived by Branch B by treating Branch B as though it alone were the remainder of the controlled foreign corporation. The use of Branch B does not have the same tax effect as if Branch B were a wholly owned subsidiary of FS because the tax rate applicable to the income allocated to Branch B under §1.954-3(b)(1)(ii)(b) (20%) is not less than 90 percent of, and at least 5 percentage points less than, the effective rate of tax which would apply to such income under the laws of Country A (20%),

the country in which Branch A is located. Section 1.954-3(b)(1)(ii)(b) is applied separately to the sales income derived by Branch C by treating Branch C as though it alone were the remainder of the controlled foreign corporation. The use of Branch C does not have the same tax effect as if Branch C were a wholly owned subsidiary of FS because the tax rate applicable to the income allocated to Branch C under §1.954-3(b)(1)(ii)(b) (18%) is not less than 90 percent of, and at least 5 percentage points less than, the effective rate of tax which would apply to such income under the laws of Country A (20%), the country in which Branch A is located. Pursuant to this paragraph (b)(1)(ii)(c)(1), the rules under paragraph (b)(1)(i)(c) of this section and §1.954-3(b)(1)(i) for determining whether a sales or purchase branch is treated as a separate corporation from the remainder of the controlled foreign corporation do not apply.

(2) *Use of more than one branch to manufacture, produce, construct, grow, or extract separate items of personal property.* If a controlled foreign corporation carries on manufacturing, producing, constructing, growing, or extracting activities with respect to separate items of personal property by or through more than one branch or similar establishment located outside the country under the laws of which such corporation is created or organized, then paragraph (b)(1)(ii)(c) of this section and §1.954-3(b)(1)(ii)(b) will be applied separately to each such branch or similar establishment (by treating such manufacturing branch or similar establishment as if it were the only such branch or similar establishment of the controlled foreign corporation and as if any other such branches or similar establishments were separate corporations) for purposes of determining whether the use of such branch or similar establishment has substantially the same tax effect as if such branch or similar establishment were a wholly owned subsidiary corporation of the controlled foreign corporation. The application of this paragraph (b)(1)(ii)(c)(2) is illustrated by the following example:

Example. Multiple branches that satisfy §1.954-3(a)(4)(i). (i) *Facts.* FS is a controlled foreign corporation organized in Country M. FS operates two branches, Branch A and Branch B located in Country A and Country B, respectively. Branch A and Branch B each manufacture separate items of personal property (Product X and Product Y, respectively) within the meaning of §1.954-3(a)(4)(ii) or (iii). Raw materials used in the manufacture of Product X and Product Y are purchased by FS from an unrelated person. FS engages in activities in Country M to sell Product X and Product Y to a related person for use, disposition or consumption outside of Country M. Employees of FS located in Country M perform only sales functions. The effective rate imposed in Country M on the income from the sales

of Product X and Product Y is 10%. Country A imposes an effective rate of tax on sales income of 20%. Country B imposes an effective rate of tax on sales income of 12%.

(ii) *Result.* Pursuant to this paragraph (b)(1)(ii)(c)(2), §1.954-3(b)(1)(ii)(b) is applied separately to Branch A and Branch B with respect to the sales income of FS attributable to Product X (manufactured by Branch A) and Product Y (manufactured by Branch B). Because the effective rate of tax on FS's sales income from the sale of Product X in Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in the country in which Branch A is located (20%), the use of Branch A to manufacture Product X has substantially the same tax effect as if Branch A were a wholly owned subsidiary corporation of FS. Because the effective rate of tax on FS's sales income from the sale of Product Y in Country M (10%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in the country in which Branch B is located (12%), the use of Branch B to manufacture Product Y does not have substantially the same tax effect as if Branch B were a wholly owned subsidiary corporation of FS. Consequently, only Branch A is treated as a separate corporation apart from the remainder of FS for purposes of determining foreign base company sales income from the sales of Product X.

(3) *Use of more than one manufacturing branch, or one or more manufacturing branches and the remainder of the controlled foreign corporation, to manufacture, produce, or construct the same item of personal property—(i) In general.* This paragraph (b)(1)(ii)(c)(3) applies to determine the location of manufacture, production, or construction of personal property for purposes of applying §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b) where more than one branch (or similar establishment) of a controlled foreign corporation, or one or more branches (or similar establishments) of a controlled foreign corporation and the remainder of the controlled foreign corporation, each engage in manufacturing, producing, or constructing activities with respect to the same item of personal property which is then sold by the controlled foreign corporation. The location of manufacture, production, or construction is determined under paragraph (b)(1)(ii)(c)(3)(ii) of this section if one or more branches (or similar establishments), or the remainder of the controlled foreign corporation, independently satisfies §1.954-3(a)(4)(i) with respect to an item of personal property. The location of manufacture, production, or construction is determined under paragraph (b)(1)(ii)(c)(3)(iii) of this section if

none of the branches (or similar establishments), or the remainder of the controlled foreign corporation, independently satisfies §1.954-3(a)(4)(i) with respect to an item of personal property, but the controlled foreign corporation as a whole makes a substantial contribution to the manufacture, production or construction of that property within the meaning of §1.954-3(a)(4)(iv). For purposes of this paragraph (b)(1)(ii)(c)(3), the location of any activity with respect to the manufacture, production, or construction of an item of personal property is determined under paragraph (b)(1)(ii)(c)(3)(iv) of this section. For purposes of this paragraph (b)(1)(ii)(c)(3), if multiple branches (or similar establishments) are located in a single jurisdiction, then the activities of those branches will be aggregated for purposes of determining whether a branch or remainder of the controlled foreign corporation satisfies §1.954-3(a)(4)(i).

(ii) *Manufacture, production, or construction in one or more locations.* If only one branch (or similar establishment), or only the remainder of a controlled foreign corporation, independently satisfies §1.954-3(a)(4)(i) with respect to an item of personal property, then that branch (or similar establishment) or the remainder of the controlled foreign corporation will be the location of manufacture, production, or construction of that property for purposes of applying §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b) to the income from the sale of that property. See paragraph (b)(1)(ii)(c)(3)(v) *Example 1* of this section. If more than one branch (or similar establishment), or one or more branches (or similar establishments) and the remainder of the controlled foreign corporation, each independently satisfy §1.954-3(a)(4)(i) with respect to an item of personal property, then the location of manufacture, production, or construction of that property for purposes of applying §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b) will be the location of that branch (or similar establishment) or the jurisdiction under the laws of which the remainder of the controlled foreign corporation is organized that satisfies §1.954-3(a)(4)(i) and that would, after applying §1.954-3(b)(1)(ii)(b) to such branch (or similar establishment) or §1.954-3(b)(1)(i)(b) to the remainder of the controlled foreign corporation, im-

pose the lowest effective rate of tax on the income allocated to such branch or the remainder of the controlled foreign corporation under such section (that is, either §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b)). See paragraph (b)(1)(ii)(c)(3)(v) *Example 2* of this section.

(iii) *No location independently satisfies manufacturing test.* If none of the branches (or similar establishments) or the remainder of the controlled foreign corporation independently satisfies §1.954-3(a)(4)(i) with respect to an item of personal property but the controlled foreign corporation as a whole makes a substantial contribution to the manufacture, production, or construction of that property within the meaning of §1.954-3(a)(4)(iv), then for purposes of applying §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b), the location of manufacture, production, or construction with respect to that property will be the “tested manufacturing location” unless the “tested sales location” provides a demonstrably greater contribution to the manufacture, production, or construction of the property. The tested manufacturing location is the location of any branch (or similar establishment) or remainder of the controlled foreign corporation that contributes to the manufacture, production, or construction of the personal property, if any, and that would, after applying §1.954-3(b)(1)(ii)(b) to such branch (or similar establishment) or §1.954-3(b)(1)(i)(b) to the remainder of the controlled foreign corporation, be treated as a separate corporation and would impose the lowest effective rate of tax on the income allocated to such branch (or similar establishment) or to the remainder of the controlled foreign corporation under such section (that is, either §1.954-3(b)(1)(ii)(b) or (b)(1)(i)(b)). The tested sales location is the location where the branch (or similar establishment) or the remainder of the controlled foreign corporation purchases or sells the personal property. For purposes of this paragraph (b)(1)(ii)(c)(3)(iii), the contribution to the manufacture, production, or construction of the personal property by the tested sales location will be deemed to include the activities of any branch (or similar establishment) or remainder of the controlled foreign corporation that would not be treated as a corporation separate

from the tested sales location after the application of §1.954-3(b)(1)(ii)(b) or (b)(1)(i)(b). For purposes of this paragraph (b)(1)(ii)(c)(3)(iii), the contribution of the tested manufacturing location to the manufacture, production, or construction of the personal property will be deemed to include any activities of any branch (or similar establishment) or remainder of the controlled foreign corporation that would be treated as a corporation separate from the tested sales location after the application of §1.954-3(b)(1)(ii)(b) or (b)(1)(i)(b). Whether the tested sales location provides a demonstrably greater contribution to the manufacture, production, or construction of the personal property is determined by weighing the relative contributions to the manufacture, production, or construction of that property by the tested sales location and the tested manufacturing location under the facts and circumstances test provided in §1.954-3(a)(4)(iv). See paragraph (b)(1)(ii)(c)(3)(v) *Examples 4, 5, and 6* of this section. If the tested sales location provides a demonstrably greater contribution to the manufacture, production, or construction of the personal property than the tested manufacturing location or if there is no tested manufacturing location, then the tested sales location is the location of manufacture, production, or construction of that property and the rules of paragraph (b)(1)(ii)(a) of this section and §1.954-3(b)(1)(i)(a) will not apply with respect to the sales income related to that property and the use of the purchasing or selling branch (or similar establishment) or the purchasing or selling remainder will not result in a branch being treated as a separate corporation for purposes of paragraph (b)(2)(ii) of this section or §1.954-3(b)(2)(ii).

(iv) *Location of activity.* For purposes of paragraph (b)(1)(ii)(c)(3) of this section, the location of any activity with respect to the manufacture, production, or construction of an item of personal property is the location where the employees of the controlled foreign corporation perform such activity. For example, the location of any activity concerning intellectual property is determined based on where employees of the controlled foreign corporation develop, or direct the use or development of, the intellectual property, not on the formal assignment of that intellectual property.

(v) *Examples.* The following examples illustrate the application of this paragraph (b)(1)(ii)(c)(3):

Example 1. Multiple branches contribute to the manufacture of a single product, only one branch satisfies §1.954-3(a)(4)(i). (i) *Facts.* FS is a controlled foreign corporation organized in Country M. FS operates three branches, Branch A, Branch B, and Branch C, located respectively in Country A, Country B, and Country C. Branch A, Branch B, and Branch C each performs different manufacturing activities with respect to the manufacture of Product X. Branch A, through the activities of employees of FS located in Country A, designs Product X. Branch B, through the activities of employees of FS located in Country B, provides quality control and oversight and direction. Branch C, through the activities of employees of FS located in Country C, manufactures Product X (within the meaning of §1.954-3(a)(4)(ii) or (a)(4)(iii)) using the designs developed by Branch A and under the oversight of the quality control personnel of Branch B. The activities of Branch A and Branch B do not independently satisfy §1.954-3(a)(4)(i). Employees of FS located in Country M purchase the raw materials used in the manufacture of Product X from a related person and control the work-in-process and finished goods throughout the manufacturing process. Employees of FS located in Country M also manage the manufacturing costs and capacities related to Product X. Further, employees of FS located in Country M oversee the coordination between the branches. Employees of FS located in Country M sell Product X to unrelated persons for use outside of Country M. The sales income from the sale of Product X is taxed in Country M at an effective rate of tax of 10%. Country C imposes an effective rate of tax of 20% on sales income.

(ii) *Result.* Country C is the location of manufacture for purposes of applying §1.954-3(b)(1)(ii)(b) because only the activities of Branch C independently satisfy §1.954-3(a)(4)(i). The use of Branch C has substantially the same tax effect as if Branch C were a wholly owned subsidiary corporation of FS because the effective rate of tax on the sales income (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in the country in which Branch C is located (20%). Therefore, sales of Product X by the remainder of FS are treated as sales on behalf of Branch C. In determining whether the remainder of FS will qualify for the manufacturing exception under §1.954-3(a)(4)(iv), the activities of FS will include the activities of Branch A or Branch B, respectively, if each of those branches would not be treated as a separate corporation under §1.954-3(b)(1)(ii)(b), if that paragraph were applied independently to each of Branch A and Branch B. See paragraph (b)(2)(ii)(a) of this section.

Example 2. Multiple branches satisfy §1.954-3(a)(4)(i) with respect to the same product sold by the controlled foreign corporation. (i) *Facts.* Assume the same facts as in *Example 1*, except for the following. In addition to the design of Product X, Branch A also performs in Country A other manufacturing activities, including those ascribed to FS in *Example 1*, that are sufficient to qualify as manufacturing under §1.954-3(a)(4)(iv) with respect

to Product X. Country A imposes an effective rate of tax of 12% on sales income.

(ii) *Result.* Branch A and Branch C through their activities each independently satisfy the requirements of §1.954-3(a)(4)(i). Therefore, §1.954-3(b)(1)(ii)(b) is applied by comparing the effective rate of tax imposed on the income from the sales of Product X against the lowest effective rate of tax that would apply to the sales income in either Country A or Country C if §1.954-3(b)(1)(ii)(b) were applied separately to Branch A and Branch C. Country A imposes the lower effective rate of tax, and therefore, Branch A is treated as the location of manufacture for purposes of applying §1.954-3(b)(1)(ii)(b). The effective rate of tax in Country B is not considered because Branch B does not satisfy §1.954-3(a)(4)(i). Neither Branch A nor Branch C is treated as a separate corporation because the effective rate of tax on the sales income of FS from the sale of Product X (10%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in the country in which Branch A is located (12%). Sales of Product X by the remainder of the controlled foreign corporation are not treated as made on behalf of any branch.

Example 3. Determining the location of manufacture when manufacturing activities performed by multiple branches and no branch independently satisfies §1.954-3(a)(4)(i). (i) *Facts.* FS, a controlled foreign corporation organized in Country M, purchases raw materials from a related person. The raw materials are manufactured (under the principles of §1.954-3(a)(4)(ii) or (a)(4)(iii)) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion of the raw materials in Country C. FS has two branches, Branch A and Branch B, located in Country A and Country B respectively. Branch A, through the activities of employees of FS located in Country A, designs Product X. Branch B, through the activities of employees of FS located in Country B, controls manufacturing related logistics, provides oversight and direction during the manufacturing process, and controls the raw materials and work-in-process. FS manages the manufacturing costs and capacities related to the manufacture of Product X through employees located in Country M. Further, employees of FS located in Country M oversee the coordination between the branches. Employees of FS located in Country M also sell Product X to unrelated persons for use outside of Country M. Country M imposes an effective rate of tax on sales income of 10%. Country A imposes an effective rate of tax on sales income of 20%, and Country B imposes an effective rate of tax on sales income of 24%. Neither the remainder of FS, nor any branch of FS independently satisfies §1.954-3(a)(4)(i). However, under the facts and circumstances of the business, FS as a whole provides a substantial contribution to the manufacture of Product X within the meaning of §1.954-3(a)(4)(iv).

(ii) *Result.* Based on the facts, neither the remainder of FS (through the activities of its employees in Country M) nor any branch of FS independently satisfies §1.954-3(a)(4)(i) with respect to Product X, but FS, as a whole, provides a substantial contribution through the activities of its employees

to the manufacture of Product X. The remainder of FS, Branch A, and Branch B each provides a contribution through the activities of employees to the manufacture of Product X. Therefore, FS must determine the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. The tested sales location is Country M because the remainder of FS performs the selling activities with respect to Product X. The location of Branch A is the tested manufacturing location because the effective rate of tax imposed on FS's sales income by Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country A (20%), and Country A has the lowest effective rate of tax among the manufacturing branches that would, after applying §1.954-3(b)(1)(ii)(b), be treated as a separate corporation. The activities of Branch B will be included in the contribution of Branch A for purposes of determining the location of manufacture of Product X because the effective rate of tax imposed on the sales income by Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country B (24%). Under the facts and circumstances of the business, the activities of the remainder of FS would not provide a demonstrably greater contribution to the manufacture of Product X than the activities of Branch A and Branch B, considered together. Therefore, the location of manufacture is Country A, the location of Branch A.

Example 4. Manufacturing activities performed by multiple branches, no branch independently satisfies §1.954-3(a)(4)(i), selling activities performed by remainder of the controlled foreign corporation, remainder contribution includes branch manufacturing activities. (i) *Facts.* The facts are the same as *Example 3*, except that the effective rate of tax on sales income in Country B is 12%. In addition, under the facts of the particular business, the activities of employees of FS located in Country B and Country M, if considered together, would provide a demonstrably greater contribution to the manufacture of Product X than the activities of employees of FS located in Country A.

(ii) *Result.* Based on the facts, neither the remainder of FS (through activities of its employees in Country M) nor any branch of FS independently satisfies §1.954-3(a)(4)(i) with respect to Product X, but FS, as a whole, provides a substantial contribution through the activities of its employees to the manufacture of Product X. The remainder of FS, Branch A, and Branch B each provide a contribution through the activities of their employees to the manufacture of Product X. Therefore, FS must determine the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. The tested sales location is Country M because the remainder of FS performs the selling activities with respect to Product X. The location of Branch A is the tested manufacturing location because the effective rate of tax imposed on FS's sales income by Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country A (20%), and Branch A is the only branch that would, after applying §1.954-3(b)(1)(ii)(b), be treated as a separate corporation. The activities of Branch B will be included in the contribution of the remainder of FS for purposes of determining the location of manufac-

ture of Product X because the effective rate of tax imposed on the sales income by Country M (10%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country B (12%). Under a facts and circumstances analysis, considered together, the activities of Branch B and the remainder of FS would provide a demonstrably greater contribution to the manufacture of Product X than the activities of Branch A. Therefore, the rules of paragraph (b)(1)(ii)(a) of this section will not apply and neither Branch A nor Branch B will be treated as a separate corporation for purposes of paragraph (b)(2)(ii) of this section and §1.954-3(b)(2)(ii).

Example 5. Manufacturing activities performed by multiple branches, no branch independently satisfies §1.954-3(a)(4)(i), selling activities performed by remainder of the controlled foreign corporation and a sales branch. (i) *Facts.* The facts are the same as *Example 3*, except that selling activities are also performed by Branch D in Country D, and Country D imposes a 16% effective rate of tax on sales income. In addition, under the facts and circumstances of the business, the activities of employees of FS located in Country A and Country M, considered together, would provide a demonstrably greater contribution to the manufacture of Product X than the activities of employees of FS located in Country B.

(ii) *Result.* Based on the facts, neither the remainder of FS nor any branch of FS independently satisfies §1.954-3(a)(4)(i) with respect to Product X, but FS, as a whole, provides a substantial contribution through the activities of its employees to the manufacture of Product X. The remainder of FS, Branch A, and Branch B each provide a contribution through the activities of their employees to the manufacture of Product X. Therefore, FS must determine the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. Further, pursuant to paragraph (b)(1)(ii)(c)(1) of this section, paragraph (b)(1)(ii)(c)(3)(iii) of this section must be applied separately to the sales income derived by the remainder of FS and Branch D respectively. The results with respect to the remainder of FS in this *Example 6* are the same as in *Example 3*. However, paragraph (b)(1)(ii)(c)(3)(iii) of this section must also be applied with respect to Branch D because Branch D performs selling activities with respect to Product X. Thus, for purposes of that sales income, the location of Branch D is the tested sales location. The location of Branch B is the tested manufacturing location because the effective rate of tax imposed on the Branch D's sales income by Country D (16%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country B (24%), and Branch B is the only branch that would, after applying §1.954-3(b)(1)(ii)(b), be treated as a separate corporation. The manufacturing activities performed in Country M by the remainder of FS and the manufacturing activities performed in Country A by Branch A will be included in Branch D's contribution to the manufacture of Product X for purposes of determining the location of manufacture of Product X with respect to Branch D's sales income because the effective rate of tax imposed on the sales income by Country D (16%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country M (10%) and Country A (20%). Under the

facts and circumstances of the business, the activities of Branch D, Branch A, and the remainder of FS, considered together, would provide a demonstrably greater contribution to the manufacture of Product X than the activities of Branch B. Therefore, the rules of paragraph (b)(1)(ii)(a) of this section will not apply to Branch D and neither Branch A nor Branch D will be treated as a separate corporation for purposes of paragraph (b)(2)(ii) of this section and §1.954-3(b)(2)(ii).

Example 6. Determining the location of manufacture when employees of remainder of controlled foreign corporation travel to location of unrelated contract manufacturer to perform manufacturing activities. (i) *Facts.* FS, a controlled foreign corporation organized in Country M, purchases raw materials from a related person. The raw materials are manufactured (under the principles of §1.954-3(a)(4)(ii) or (a)(4)(iii)) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion of the raw materials in Country C. Employees of FS located in Country M sell Product X to unrelated persons for use outside of Country M. Employees of FS located in Country M engage in product design, manage the manufacturing costs and capacities with respect to Product X, and direct the use of intellectual property for the purpose of manufacturing Product X. Quality control and oversight and direction of the manufacturing process are conducted in Country C by employees of FS who are employed in Country M but who regularly travel to Country C. Branch A, located in Country A, is the only branch of FS. Product design with respect to Product X conducted by employees of FS located in Country A is supplemental to the bulk of the design work, which is done by employees of FS located in Country M. At all times, employees of Branch A control the raw materials, work-in-process and finished goods. Employees of FS located in Country A also control manufacturing related logistics with respect to Product X. Country M imposes an effective rate of tax on sales income of 10%. Country A imposes an effective rate of tax on sales income of 20%. Neither the remainder of FS nor Branch A independently satisfies §1.954-3(a)(4)(i). However, under the facts and circumstance of the business, FS as a whole (including Branch A) provides a substantial contribution to the manufacture of Product X within the meaning of §1.954-3(a)(4)(iv).

(ii) *Result.* Based on the facts, neither the remainder of FS nor Branch A independently satisfies §1.954-3(a)(4)(i) with respect to Product X, but FS, as a whole, provides a substantial contribution through the activities of its employees to the manufacture of Product X. The remainder of FS and Branch A each provide a contribution through the activities of employees to the manufacture of Product X. Therefore, FS must determine the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. The tested sales location is Country M because the remainder of FS performs the selling activities with respect to Product X. The tested manufacturing location is the location of Branch A because the effective rate of tax imposed on the remainder of FS's sales income by Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country A (20%), and Branch A is the only branch

that would, after applying §1.954-3(b)(1)(ii)(b), be treated as a separate corporation. Although the activities of traveling employees are considered in determining whether FS, as a whole, makes a substantial contribution to the manufacture of Product X under §1.954-3(a)(4)(iv), the activities of the employees of FS that are performed in Country C are not taken into consideration in determining whether Country M, the jurisdiction under the laws of which FS is organized, is the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. Activities of employees performed outside the jurisdiction in which the controlled foreign corporation is organized and outside a location in which the controlled foreign corporation maintains a branch or similar establishment, are not considered in determining the location of manufacture. Under the facts and circumstances of the business, the activities of employees of FS performed in Country M do not provide a demonstrably greater contribution to the manufacture of Product X than the activities of employees of FS performed in Country A. Therefore, the location of manufacture is Country A, the location of Branch A.

(4) *Use of more than one branch to manufacture, produce, construct, grow, or extract separate items of personal property.* For purposes of paragraphs (b)(1)(ii)(c)(2) and (b)(1)(ii)(c)(3) of this section, an *item* of personal property refers to an individual unit of personal property rather than a type or class of personal property.

(2) [Reserved]. For further guidance, see §1.954-3(b)(2).

(i) [Reserved]. For further guidance, see §1.954-3(b)(2)(i).

(a) *Treatment as separate corporations.* [Reserved]. For further guidance, see §1.954-3(b)(2)(i)(a).

(b) *Activities treated as performed on behalf of the remainder of corporation.* With respect to purchasing or selling activities performed by or through the branch or similar establishment, such purchasing or selling activities will—

(1) With respect to personal property manufactured, produced, or constructed by the remainder of the controlled foreign corporation (or any branch treated as the remainder of the controlled foreign corporation); or

(2) With respect to personal property (other than property described in paragraph (b)(2)(i)(b)(1) of this section) purchased or sold, or purchased and sold, by the remainder of the controlled foreign corporation (or any branch treated as the remainder of the controlled foreign corporation), be treated on behalf of the remainder of the controlled foreign corporation.

(c) [Reserved]. For further guidance, see §1.954-3(b)(2)(i)(c).

(d) *Determination of hypothetical tax.* To the extent applicable, the principles of §1.954-1(d)(2) shall be used in determining, under paragraph (b)(1)(i) of this section and §1.954-3(b)(1)(i), the effective rate of tax which would apply to the income of the branch or similar establishment under the laws of the country in which the controlled foreign corporation is created or organized, or in determining, under paragraph (b)(1)(ii) of this section and §1.954-3(b)(1)(ii), the effective rate of tax which would apply to the income of the branch or similar establishment under the laws of the country in which the manufacturing, producing, constructing, growing, or extracting branch or similar establishment is located.

(e) [Reserved]. For further guidance, see §1.954-3(b)(2)(i)(e).

(ii) [Reserved]. For further guidance, see §1.954-3(b)(2)(ii).

(a) *Treatment as separate corporations.* The branch or similar establishment will be treated as a wholly owned subsidiary corporation of the controlled foreign corporation, and such branch or similar establishment will be deemed to be incorporated in the country in which it is located. For purposes of applying the rules of this paragraph (b)(2)(ii) and §1.954-3(b)(2)(ii), a branch or similar establishment of a controlled foreign corporation treated as a separate corporation purchasing or selling on behalf of the remainder of the controlled foreign corporation under paragraph (b)(2)(ii)(b) of this section, or the remainder of the controlled foreign corporation treated as a separate corporation purchasing or selling on behalf of a branch or similar establishment of the controlled foreign corporation under §1.954-3(b)(2)(ii)(c), will include any other branch or similar establishment or remainder of the controlled foreign corporation that would not be treated as a separate corporation (apart from the branch or similar establishment of a controlled foreign corporation that is treated as performing purchasing or selling activities on behalf of the remainder of the controlled foreign corporation under paragraph (b)(2)(ii)(b) of this section or the remainder of the controlled foreign corporation that is treated as performing purchasing or selling activities on behalf

of the branch or similar establishment under §1.954-3(b)(2)(ii)(c) if the effective rate of tax imposed on the income of the purchasing or selling branch or similar establishment, or purchasing or selling remainder of the controlled foreign corporation, were tested under the principles of §1.954-3(b)(1)(i)(b) or (b)(1)(ii)(b) against the effective rate of tax that would apply to such income if it were considered derived by such other branch or similar establishment or the remainder of the controlled foreign corporation.

(b) *Activities treated as performed on behalf of the remainder of corporation.* With respect to purchasing or selling activities performed by or through the branch or similar establishment, such purchasing or selling activities will—

(1) With respect to personal property manufactured, produced, or constructed by the remainder of the controlled foreign corporation (or any branch treated as the remainder of the controlled foreign corporation); or

(2) With respect to personal property (other than property described in paragraph (b)(2)(ii)(b)(1) of this section) purchased or sold, or purchased and sold, by the remainder of the controlled foreign corporation (or any branch treated as the remainder of the controlled foreign corporation), be treated as performed on behalf of the remainder of the controlled foreign corporation.

(c) and (d) [Reserved]. For further guidance, see §1.954-3(b)(2)(ii)(c) and (d).

(e) *Comparison with ordinary treatment.* Income derived by a branch or similar establishment, or by the remainder of the controlled foreign corporation, shall not be determined to be foreign base company sales income under paragraph (b) of this section or §1.954-3(b) if the income would not be so considered if it were derived by a separate controlled foreign corporation under like circumstances.

(f) [Reserved]. For further guidance, see §1.954-3(b)(2)(ii)(f).

(3) [Reserved]. For further guidance, see §1.954-3(b)(3).

(4) *Illustrations.* The application of this paragraph (b)(4) may be illustrated by the following examples:

Examples (1) and (2). [Reserved]. For further guidance, see §1.954-3(b)(4) *Examples (1) and (2).*

Example (3). (i) *Facts.* Corporation E, a controlled foreign corporation incorporated under the laws of foreign Country X, is a wholly owned subsidiary of Corporation D, also a controlled foreign corporation incorporated under the laws of Country X. Corporation E maintains Branch B in foreign Country Y. Both corporations use the calendar year as the taxable year. In 1964, Corporation E's sole activity, carried on through Branch B, consists of the purchase of articles manufactured in Country X by Corporation D, a related person, and the sale of the articles through Branch B to unrelated persons. One hundred percent of the articles sold through Branch B are sold for use outside Country X and 90 percent are also sold for use outside of Country Y. The income of Corporation E derived by Branch B from such transactions is taxed to Corporation E by Country X only at the time Corporation E distributes such income to Corporation D and is taxed on the basis of what the tax (a 40 percent effective rate) would have been if the income had been derived in 1964 by Corporation E from sources within Country X from doing business through a permanent establishment therein. Country Y levies an income tax at an effective rate of 50 percent on income derived from sources within such country, but the income of Branch B for 1964 is effectively taxed by Country Y at a 5 percent rate since under the laws of such country, only 10 percent of Branch B's income is derived from sources within such country. Corporation E makes no distributions to Corporation D in 1964.

(ii) *Result.* In determining foreign base company sales income of Corporation E for 1964, Branch B is treated as a separate wholly owned subsidiary corporation of Corporation E, the 5 percent rate of tax being less than 90 percent of, and at least 5 percentage points less than the 40 percent rate. Income derived by Branch B, treated as a separate corporation, from the purchase from a related person (Corporation D), of personal property manufactured outside of Country Y and sold for use, disposition, or consumption outside of Country Y constitutes foreign base company sales income. If, instead, Corporation D were unrelated to Corporation E, none of the income would be foreign base company sales income because Corporation E would be purchasing from and selling to unrelated persons and if Branch B were treated as a separate corporation it would likewise be purchasing from and selling to unrelated persons. Alternatively, if Corporation D were related to Corporation E, but Branch B manufactured the articles prior to sale under the principles of §1.954-3(a)(4)(iv), the income would not be foreign base company sales income because Branch B, treated as a separate corporation, would qualify for the manufacturing exception under §1.954-3(a)(4).

Examples (4) through (7) [Reserved]. For further guidance, see §1.954-3(b)(4) *Examples (4) through (7).*

Example (8). *Uniformly applicable incentive tax rate in one country.* (i) *Facts.* FS is a controlled foreign corporation organized in Country M. FS operates one branch, Branch A, located in Country A. Branch A manufactures Product X within the meaning of §1.954-3(a)(4)(ii) or (a)(4)(iii). Raw materials used in the manufacture of Product X are purchased by FS from an unrelated person. FS engages in activities in Country M to sell Product X to a related person for use outside of Country M. Employees of FS

located in Country M perform only sales functions. The effective rate imposed in Country M on the income from the sale of Product X is 10%. Country A generally imposes an effective rate of tax on income of 20%, but imposes a uniformly applicable incentive rate of tax of 10% on manufacturing income and related sales income.

(ii) *Result.* The use of Branch A to manufacture Product X does not have substantially the same tax effect as if Branch A were a wholly owned subsidiary corporation of FS because the effective rate of tax on FS's sales income from the sale of Product X in Country M (10%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in the country in which Branch A is located (10%). Consequently, pursuant to §1.954-3(b)(1)(ii)(b), Branch A is not treated as a separate corporation apart from the remainder of FS for purposes of determining foreign base company sales income.

Example (9). *Manufacturing activities performed by multiple branches, no branch independently satisfies §1.954-3(a)(4)(i), selling activities performed by remainder of the controlled foreign corporation, branch manufacturing activities included in remainder contribution.* (i) *Facts.* FS, a controlled foreign corporation organized in Country M, has two branches, Branch A and Branch B, located in Country A and Country B respectively. FS purchases raw materials from a related person. The raw materials are manufactured (under the principles of §1.954-3(a)(4)(ii) or (a)(4)(iii)) into Product X by CM, an unrelated corporation, pursuant to a contract manufacturing arrangement. CM physically performs the substantial transformation, assembly, or conversion required to manufacture Product X outside of FS's country of organization. FS manages the manufacturing costs and capacities with respect to the manufacture of Product X through employees located in Country M. Further, employees of FS located in Country M oversee the coordination between the branches. Branch A, through the activities of employees of FS located in Country A, designs Product X, controls manufacturing related logistics, and controls the raw materials and work-in-process during the manufacturing process. Branch B, through the activities of employees of FS located in Country B, provides quality control and oversight and direction during the manufacturing process. Employees of FS located in Country M sell Product X to unrelated persons for use outside of Country M. Country M imposes an effective rate of tax on sales income of 10%. Country A imposes an effective rate of tax on sales income of 12%, and Country B imposes an effective rate of tax on sales income of 24%. None of the remainder of FS, Branch A, or Branch B independently satisfies §1.954-3(a)(4)(i). However, under the facts and circumstances of the business, FS, as a whole, provides a substantial contribution to the manufacture of Product X within the meaning of §1.954-3(a)(4)(iv). Under the facts and circumstances of the business, the activities of the remainder of FS and Branch A, if considered together, would not provide a demonstrably greater contribution to the manufacture of Product X than the activities of Branch B. Under the facts and circumstances of the business, however, the activities of the employees of the remainder of FS and Branch A, if considered

together, would constitute a substantial contribution to the manufacture of Product X.

(ii) *Result.* Based on the facts, neither the remainder of FS (through activities of its employees in Country M) nor any branch of FS independently satisfies §1.954-3(a)(4)(i) with respect to Product X, but FS, as a whole, provides a substantial contribution through the activities of its employees to the manufacture of Product X. The remainder of FS, Branch A, and Branch B each provide a contribution through the activities of employees to the manufacture of Product X. Therefore, FS must determine the location of manufacture under paragraph (b)(1)(ii)(c)(3)(iii) of this section. The tested sales location is Country M because the remainder of FS performs the selling activities with respect to Product X. The location of Branch B is the tested manufacturing location because the effective rate of tax imposed on FS's sales income by Country M (10%) is less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country B (24%); and Branch B is the only manufacturing branch that would, after applying §1.954-3(b)(1)(ii)(b), be treated as a separate corporation. The manufacturing activities performed in Country A will be included in the contribution of the remainder of FS for purposes of determining the location of manufacture of Product X because the effective rate of tax imposed on the sales income by Country M (10%) is not less than 90% of, and at least 5 percentage points less than, the effective rate of tax that would apply to such income in Country A (12%). Under the facts and circumstances of the business, the manufacturing activities of the remainder of FS and Branch A, considered together, would not provide a demonstrably greater contribution to the manufacture of Product X than the activities of Branch B. Therefore, the location of manufacture is Country B, the location of Branch B. In determining that Country B is the location of manufacture, it was determined that after applying §1.954-3(b)(1)(ii)(b) Branch B would be treated as a separate corporation under paragraph (b)(1)(ii)(a) of this section for purposes of determining foreign base company sales income. To determine whether income from the sale of Product X is foreign base company sales income, the remainder of FS takes into account the activities of Branch A because, under paragraph (b)(2)(ii)(a) of this section, Branch A would not be treated as a separate corporation apart from FS. The remainder of FS is considered to have manufactured Product X under §1.954-3(a)(4)(i) because the manufacturing activities of the remainder of FS and Branch A, considered together, would make a substantial contribution to the manufacture of Product X within the meaning of §1.954-3(a)(4)(iv). Therefore, income derived from the sale of Product X by the remainder of FS does not constitute foreign base company sales income.

(c) [Reserved]. For further guidance, see §1.954-3(c).

(d) [Reserved]. For further guidance, see §1.954-3(d).

(e) *Effective/applicability date of temporary regulations.* Paragraphs (b)(1)(i)(c), (b)(1)(ii)(a), (b)(1)(ii)(c), (b)(2)(i)(b), (b)(2)(ii)(a), (b)(2)(ii)(b),

(b)(2)(ii)(e), and (b)(4) *Example (3)*, *Example (8)*, and *Example (9)* of this section shall apply to taxable years of controlled foreign corporations beginning after June 30, 2009, and for taxable years of United States shareholders in which or with which such taxable years of the controlled foreign corporations end.

(f) *Application of temporary regulations to earlier taxable years.* For the application of these temporary regulations retroactively with respect to taxable years of controlled foreign corporations and to open taxable years of United States shareholders in which or with which such taxable years of the controlled foreign corporations end, see §1.954-3(d).

(g) *Expiration date.* The applicability of this section expires on or before December 23, 2011.

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

Approved December 18, 2008.

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

(Filed by the Office of the Federal Register on December 24, 2008, 8:45 a.m., and published in the issue of the Federal Register for December 29, 2008, 73 F.R. 79334)

Section 1256.—Section 1256 Contracts Marked to Market

(Also §§ 446, 481, 7805; 1.446-1, 301.7805-1.)

Section 1256 contracts marked to market. This ruling holds that Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code.

Rev. Rul. 2009-4 ISSUE

Is Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Internal Revenue Code?

LAW

Section 1256(g)(7) of the Code provides that the term “qualified board or exchange” means:

(A) a national securities exchange which is registered with the Securities and Exchange Commission,

(B) a domestic board of trade designated as a contract market by the Commodity Futures Trading Commission, or

(C) any other exchange, board of trade, or other market which the Secretary determines has rules adequate to carry out the purposes of section 1256.

HOLDING

The Internal Revenue Service determines that Dubai Mercantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code.

EFFECTIVE DATE

Under the authority of section 7805(b)(8) of the Code, this revenue ruling is effective for Dubai Mercantile Exchange Contracts (commodity futures contracts and futures contract options) entered into on or after February 1, 2009.

CHANGE IN METHOD OF ACCOUNTING

A change in the treatment of Dubai Mercantile Exchange Contracts to comply with this revenue ruling is a change in method of accounting within the meaning of sections 446 and 481 of the Code and the regulations thereunder. The Commissioner grants consent to taxpayers to change to the section 1256 mark to market method for the first taxable year during which the taxpayer holds a Dubai Mercantile Exchange Contract that was entered into on or after February 1, 2009. Such a taxpayer need not file a Form 3115, *Application for Change in Accounting Method*. Dubai Mercantile Exchange Contracts that were entered into before February 1, 2009, are not covered by the change in method for which consent is granted. Because the change is being made on a “cut-off” basis, there is no potential omission or duplication of income or deductions, and

therefore no adjustment under section 481 is required.

DRAFTING INFORMATION

The principal author of this revenue ruling is K. Scott Brown of the Office of Associate Chief Counsel (Financial Institutions and Products). For further information regarding this revenue ruling, contact Mr. Brown at (202) 622-7454 (not a toll-free call).

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 31.6011(a)-1: Returns under Federal Insurance Contributions Act.

T.D. 9440

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 31

Employer's Annual Federal Tax Return and Modifications to the Deposit Rules

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains temporary regulations relating to the annual filing of Federal employment tax returns and requirements for employment tax deposits. These temporary regulations relate to sections 6011 and 6302 of the Internal Revenue Code (Code) concerning reporting and paying income taxes withheld from wages and reporting and paying taxes under the Federal Insurance Contributions Act (FICA) (collectively, "employment taxes"). These temporary regulations generally allow certain employers to file a Form 944, "Employer's ANNUAL Federal Tax Return," rather than Form 941, "Employer's QUARTERLY Federal Tax Return." In addition to rules related to Form 944, the temporary regulations provide an additional method for

employers who file Form 941 to determine whether the amount of accumulated employment taxes is considered *de minimis*. The portions of this document that are final regulations provide necessary cross-references to the temporary regulations. The text of these temporary regulations also serves as the text of the proposed regulations (REG-148568-04) set forth in this issue of the Bulletin.

DATES: Effective Date: These regulations are effective on December 29, 2008.

Applicability Date: For dates of applicability, see §§31.6011(a)-1T(g), 31.6011(a)-4T(d), and 31.6302-1T(n).

FOR FURTHER INFORMATION CONTACT: Audra Dineen, (202) 622-4910 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

These temporary regulations amend the Regulations on Employment Taxes and Collection of Income Tax at Source (26 CFR part 31) under section 6011 relating to the Federal employment tax return filing requirements and section 6302 relating to the employment tax deposit requirements. These temporary regulations are part of the IRS's effort to reduce taxpayer burden by permitting certain employers to file one return annually to report their employment tax liabilities instead of four quarterly returns. These temporary regulations affect taxpayers that file Form 941, "Employer's QUARTERLY Federal Tax Return," Form 944, "Employer's ANNUAL Federal Tax Return," and any related Spanish-language returns or returns for U.S. possessions.

On January 3, 2006, a temporary regulation (T.D. 9239, 2006-1 C.B. 401) relating to Form 944 (the 2006 temporary regulation) was published in the **Federal Register** (71 FR 11). A notice of proposed rulemaking (REG-148568-04, 2006-1 C.B. 417) cross-referencing the temporary regulations was published in the **Federal Register** for the same day (71 FR 46) (the 2006 proposed regulation). A correction to the 2006 temporary regulation was published in the Federal Register on March 17, 2006 (71 FR 13766). No requests for a public hearing were received; therefore,

no public hearing was held. Comments responding to the notice of proposed rulemaking were received.

Those comments requested that use of Form 944 be changed from mandatory to voluntary and that the amount of the employment tax liability used to determine whether employers are eligible to file Form 944 (the "eligibility threshold") be increased. The Treasury Department and the IRS agree with the suggestion to make Form 944 voluntary. The Treasury Department and the IRS will continue to consider whether to increase the eligibility threshold. The final regulations allow the eligibility threshold to be increased through future guidance.

These temporary regulations continue to permit most employers who file Form 944 to pay accumulated employment taxes annually when they file their returns and modify the lookback period and *de minimis* deposit rule for these employers. In addition to the rules related to Form 944, these temporary regulations provide an additional method for employers who file Forms 941 quarterly to determine whether the amount of accumulated employment taxes is considered *de minimis*. This safe harbor was originally proposed in the 2006 proposed regulation.

Explanation of Provisions

Form 944 — Regulations Concerning Filing Requirements Under Section 6011

These temporary regulations allow certain employers to file an annual employment tax return, Form 944, to report their social security, Medicare, and withheld Federal income taxes rather than the quarterly Form 941. For these employers, Form 944 will replace Form 941 and reduce their burden by reducing the number of returns they are required to file each year. Form 944 will not replace Form 943, "Employer's Annual Federal Tax Return for Agricultural Employees," or Schedule H (Form 1040), "Household Employment Taxes." However, if an employer files Form 944, the employer may choose to report wages with respect to household employees on Form 944, instead of reporting such wages on Schedule H (Form 1040). Form 944 is generally due January 31 of the year following the tax year for which the return is filed. If the employer

timely deposits all accumulated employment taxes on or before January 31 of the year following the tax year for which the return is filed, the employer will have 10 extra calendar days to file Form 944 pursuant to §31.6071(a)-1(a).

Under the 2006 proposed and temporary regulations, the IRS sent a notification letter to qualified employers with an estimated employment tax liability of \$1,000 or less requiring them to participate in the Employers' Annual Federal Tax Program (Form 944) (hereinafter referred to as the Form 944 Program). Employers were eligible to opt out only if they estimated that their employment tax liability would exceed the \$1,000 threshold or if they wanted to e-file Forms 941 quarterly instead. New employers who estimated that their employment tax liability would be \$1,000 or less also were eligible to file Form 944. These employers were identified by their responses on Form SS-4, *Application for Employer Identification Number*, and notified that they were required to file Form 944 in the letter advising them of their employer identification number. Employers that were not identified by the IRS in either manner were able to contact the IRS if they thought they were qualified. If the IRS determined they were qualified, it would send confirmation to these employers. Once employers received this letter, they were required to file Form 944 instead of Forms 941.

Commentators suggested that Form 944 should be voluntary instead of mandatory. This benefits taxpayers because it allows them to choose the filing requirement they prefer and to change from year to year more easily. In addition, commentators suggested that the threshold should be increased in order to allow more employers to take advantage of Form 944 and to bring the threshold in line with the *de minimis* deposit rule amount, which is less than \$2,500 as discussed more fully in this preamble. Sections 31.6011(a)-1T(a)(5) and 31.6011(a)-4T(a)(4) have been revised to incorporate the suggestion to make the program voluntary. Although these temporary regulations do not adopt the suggestion to increase the eligibility threshold, the Treasury Department and the IRS will continue to consider this suggestion and may increase the threshold in the future. To accommodate any potential increase to the threshold amount before fi-

nal regulations are issued, these temporary regulations contain a provision that allows the IRS to increase the eligibility threshold by guidance published in the Internal Revenue Bulletin. See §601.601(d)(2)(ii)(b).

Under §§31.6011(a)-1T(a)(5) and 31.6011(a)-4T(a)(4) in effect for taxable years beginning on or after January 1, 2009, employers who estimate that their annual employment tax liability will be \$1,000 or less can contact the IRS to express their desire to file Form 944 instead of Forms 941 for a taxable year. Only upon such a request will the IRS send a notification letter to qualified employers confirming that they may file Form 944 for that taxable year. Once employers receive this notice they must file Form 944 and cannot file Forms 941 instead for a taxable year until they contact the IRS to change their filing requirement to Form 941 for that taxable year and receive confirmation that their filing requirement has been changed.

The IRS will issue guidance published in the Internal Revenue Bulletin informing employers how they can contact the IRS to participate in the Form 944 Program and how they can elect out if they later decide that they want to file Forms 941 instead of Form 944. Under the 2006 regulations, employers were only eligible to opt out if they estimated that their employment tax liability would exceed the \$1,000 threshold or if they wanted to e-file Forms 941 quarterly instead. Because the program is being made voluntary, beginning in tax year 2010, employers will be able to opt out for any reason if they follow procedures to be provided in future guidance. Employers that have received notification of their qualification to file Form 944, even if the notification was received prior to the publication of these regulations, must continue to file Form 944 unless they properly opt out of the Form 944 program.

In addition, a few clarifying revisions were made to the regulations under section 6011. First, §§31.6011(a)-1T(a) and 31.6011(a)-4T(a) were clarified by adding references to §§31.6011(a)-1T(a)(5) and 31.6011(a)-4T(a)(4) to account for Form 944 in §§31.6011(a)-1T(a)(1) and 31.6011(a)-4T(a)(1). Second, §§31.6011(a)-1(a)(5) and 31.6011(a)-4(a)(4) were revised to remove the details regarding the procedures to use for opting out of the Form 944

program and provide that the IRS will issue guidance published in the Internal Revenue Bulletin containing these procedures. The IRS will issue procedures in other forms of guidance published in the IRB regarding how to opt out of Form 944 for taxable year 2009 and how to elect to file Form 944 for taxable year 2010 and beyond. This will allow the IRS to administer the program more effectively, by having the flexibility to adjust the procedures as necessary due to changes in the program and taxpayer response.

Form 944 — Regulations Concerning Deposit Requirements Under Section 6302

These temporary regulations revise the 2006 temporary regulation concerning requirements for employers to make deposits of employment taxes under section 6302 and §31.6302-1 to make a few clarifying changes to §31.6302-1 related to Form 944. These temporary regulations continue to permit employers who file Form 944 to deposit or pay their accumulated employment taxes annually when they file their Form 944 if they satisfy the provisions of the *de minimis* deposit rule, as modified in §31.6302-1T(f)(4)(iii), rather than make monthly or semi-weekly deposits. These temporary regulations continue to contain the exception in §31.6302-1T(c)(6) for employers who filed Form 944 in the preceding year but who no longer qualify because their annual employment tax liability exceeds the eligibility threshold.

Also, these temporary regulations continue to provide a different lookback period for Form 944 filers to use to determine an employer's status as a monthly or semi-weekly depositor. The lookback period was changed in the 2006 temporary and proposed regulations because once an employer begins to file annual Form 944 returns, it may not be possible for the IRS to determine the employer's aggregate amount of employment tax liability during the lookback period set forth in the existing regulations (12-month period ending the preceding June 30) because the employer may not have filed any quarterly returns during that period. Under the 2006 temporary regulation, §31.6302-1T(b)(4)(i) provided that the lookback period for employers who filed Form 944 during the

current, or preceding, calendar year is the second calendar year preceding the current calendar year. For example, the lookback period for calendar year 2009 is calendar year 2007.

In these temporary regulations, §31.6302-1T(b)(4)(i) is clarified to reflect that the lookback period is the second preceding calendar year for employers who filed Form 944 for either of the two previous calendar years, not just the one previous calendar year. This clarification was needed because an employer would not have filed the requisite quarterly returns to use the other lookback period (12-month period ending June 30) if they filed Form 944 in either of the prior years. For example, if an employer filed Form 944 in 2006 but not in 2007, the lookback period for 2008 would be 2006, because they would not have filed quarterly returns for July through December 2006 and, thus, it would be impossible to use July 2006 — June 2007 as the lookback period.

Section 31.6302-1T(b)(4)(i) also is revised to clarify that the amount of tax reported during the lookback period is determined without regard to the employer's filing requirement. In other words, in the preceding example, if an employer is required to file Forms 941 for 2008 but filed Form 944 for the lookback period (2006), the amount of employment tax liability reported for the lookback period would be the amount of employment tax the employer reported on its Form 944 for 2006 even though the employer will file Forms 941 to report its 2008 liability. The reverse also is true. The employment tax liability reported for the lookback period (2006) of an employer required to file Form 944 for 2008 would be the sum of the liabilities it reported on its four Forms 941 for 2006.

In addition, §31.6302-1T(b)(4)(ii) is revised by changing the term "supplemental" to "adjusted" and deleting the reference to Form 941c, "*Supporting Statement To Correct Information*," due to the revisions to the process of adjusting employment tax liability. Final regulations (T.D. 9405, 2008-32 I.R.B. 293) relating to employment tax adjustments were published in the **Federal Register** (73 FR 37371) on July 1, 2008. For periods ending on or before December 31, 2008, the employment tax liability reported on the original return includes any prior period adjustments reported on that

return (for example, prior period adjustments supported by a Form 941c attached to the return for a subsequent period). For periods beginning on or after January 1, 2009, employers can no longer make prior period adjustments on a return. Instead, employers will use an adjusted return or claim for refund to make corrections to the amounts reported on their original returns. Lastly, §31.6302-1T is revised by adding references to Form 944 in paragraphs (e)(2) and (g)(1).

Form 941 — New Deposit Rule Safe Harbor Under Section 6302

In addition to revising the 2006 temporary regulation regarding Form 944, these temporary regulations incorporate the safe harbor for employers who file Forms 941 that was included in the 2006 proposed regulation. The safe harbor helps small employers who file Form 941 and have an unexpected increase in their deposit liability for a quarterly return period. These temporary regulations provide an alternate method for determining whether the employer's employment tax obligations are *de minimis*, which is based on the employment taxes due for the prior return period. This special rule applies only to employers filing quarterly tax returns and, therefore, does not apply to employers who file Form 944.

Generally, deposits of taxes reported on Form 941, "*Employer's QUARTERLY Federal Tax Return*," are due monthly or semi-weekly. If an employer failed to make timely deposits of employment taxes, the employer, absent reasonable cause, is subject to the penalty for failure to deposit under section 6656. Prior to these temporary regulations, §31.6302-1(f)(4) (the *de minimis* deposit rule) provided that, for quarterly and annual return periods, if the aggregate amount of employment taxes for the return period is less than \$2,500 and that amount was deposited or paid with a timely filed return for that return period, the amount was deemed to have been timely deposited and the employer was not subject to the penalty for failure to deposit. Accordingly, employers who paid their employment taxes when they timely filed their quarterly returns were deemed to have timely deposited their taxes if the amount of taxes due was less than \$2,500 for that quarter. Similarly, employers

who paid their employment taxes when they timely filed their annual returns were deemed to have timely deposited if the amount of taxes due was less than \$2,500 for the entire year.

Under these temporary regulations, pursuant to §31.6302-1T(f)(4)(i) and (ii), employers may pay their employment taxes when they timely file their quarterly returns and be deemed to have timely deposited if the amount of the taxes due for the current quarter or for the prior quarter is less than \$2,500.

This special rule can be illustrated by the following example: an employer has less than \$50,000 in employment taxes reported during the lookback period and is therefore a monthly depositor under §31.6302-1(b)(2). The employer's employment tax liabilities for the first and second quarters of 2010 are \$2,450 and \$2,400, respectively. In the third quarter of 2010, however, the employer's employment tax liability is \$2,550. Under the *de minimis* deposit rule in effect prior to these temporary regulations, if the employer pays the \$2,550 with its return for the third quarter of 2010, the amount would not be considered timely deposited for that quarter and, therefore, the employer would be assessed the section 6656 penalty for failure to deposit.

Modifying the *de minimis* deposit rule to allow employers to base the determination on the employment taxes due for the immediately preceding quarter provides a safe harbor for employers regarding their deposit obligations. Thus, in this example, when the employer had an increase in its employment tax liability for the third quarter of 2010, its remittance still would be deemed to have been timely deposited because the taxes for the immediately preceding return period were *de minimis*. These regulations have no application to the One-Day rule in §31.6302-1(c)(2), which requires employers to make a deposit on the next banking day if they accumulate \$100,000 or more of employment taxes on any day during a deposit period. Therefore, if an employer accumulates \$100,000 or more of employment taxes during a deposit period, the employer must make a deposit on the next banking day even if the employer's employment tax liability for the prior quarter was *de minimis*. Due to the programming changes necessary to implement this safe

harbor, the safe harbor will be available for deposit periods beginning on or after January 1, 2010.

Special Analyses

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

Drafting Information

The principal authors of these final regulations are Raymond Bailey and Audra M. Dineen of the Office of the Associate Chief Counsel (Procedure and Administration).

* * * * *

Amendments to the Regulations

Accordingly, 26 CFR part 31 is amended as follows:

PART 31—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE

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

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

Par. 2. Section 31.6011(a)-1 is amended by revising paragraph (a)(1) and adding paragraph (g) to read as follows:

§31.6011(a)-1 Returns under Federal Insurance Contributions Act.

(a) * * * (1) [Reserved]. For further guidance, see §31.6011(a)-1T(a)(1).

* * * * *

(g) [Reserved]. For further guidance, see §31.6011(a)-1T(g).

Par. 3. Section 31.6011(a)-1T is revised to read as follows:

§31.6011(a)-1T Returns under Federal Insurance Contributions Act (temporary).

(a) *Requirement*—(1) *In general.* Except as otherwise provided in §31.6011(a)-5, every employer required to make a return under the Federal Insurance Contributions Act, as in effect prior to 1955, for the calendar quarter ended December 31, 1954, in respect of wages other than wages for agricultural labor, shall make a return for each subsequent calendar quarter (whether or not wages are paid in such quarter) until he has filed a final return in accordance with §31.6011(a)-6. Except as otherwise provided in §31.6011(a)-5, every employer not required to make a return for the calendar quarter ended December 31, 1954, shall make a return for the first calendar quarter thereafter in which he pays wages, other than wages for agricultural labor, subject to the tax imposed by the Federal Insurance Contributions Act as in effect after 1954, and shall make a return for each subsequent calendar quarter (whether or not wages are paid therein) until he has filed a final return in accordance with §31.6011(a)-6. Except as otherwise provided in §31.6011(a)-8 and in §31.6011(a)-1(a)(3), (a)(4), and (a)(5), Form 941, “*Employer’s QUARTERLY Federal Tax Return*,” is the form prescribed for making the return required by this subparagraph. Such return shall not include wages for agricultural labor required to be reported on any return prescribed by §31.6011(a)-1(a)(2). The return shall include wages received by an employee in the form of tips only to the extent of the tips reported by the employee to the employer in a written statement furnished to the employer pursuant to section 6053(a).

(a)(2) through (a)(4) [Reserved]. For further guidance, see §31.6011(a)-1(a)(2) through (a)(4).

(5) *Employers in the Employers’ Annual Federal Tax Program (Form 944)*—(i) *In general.* Employers notified of their qualification for the Employers’ Annual Federal Tax Program (Form 944) are required to file Form 944, “*Employer’s ANNUAL Federal Tax Return*,” instead of Form 941 to make a return as required

by paragraph (a)(1) of this section. Upon proper request by the employer, the Internal Revenue Service (IRS) will notify employers in writing of their qualification for the Employers’ Annual Federal Tax Program (Form 944). Qualified employers are those with an estimated annual employment tax liability (that is, social security, Medicare, and withheld Federal income taxes) of \$1,000 or less for the entire calendar year, except employers required under §31.6011(a)-1(a)(2) to make a return on Form 943, “*Employer’s Annual Federal Tax Return for Agricultural Employees*,” or §31.6011(a)-1(a)(3) to make a return on Schedule H (Form 1040), “*Household Employment Taxes*.” The IRS may increase the amount of the estimated annual employment tax liability that qualifies employers to file Form 944 through a revenue procedure, notice, or other IRS guidance published in the Internal Revenue Bulletin. The IRS will notify employers when they no longer qualify for the Employers’ Annual Federal Tax Program (Form 944) and must file Forms 941 instead.

(ii) *Requests to participate and eligibility to opt out of the Employers’ Annual Federal Tax Program (Form 944).* The IRS will establish procedures in a revenue procedure, notice, or other guidance published in the Internal Revenue Bulletin for employers to follow to request to receive notification to participate in the Employers’ Annual Federal Tax Program (Form 944) and to be removed from the Employers’ Annual Federal Tax Program (Form 944) after becoming a participant in order to file Forms 941 instead.

(b) through (f) [Reserved]. For further guidance, see §31.6011(a)-1(b) through (f).

(g) *Effective/applicability dates*—(1) *In general.* Paragraphs (a)(1) and (a)(5) of this section apply to taxable years beginning on or after December 30, 2008. The rules of paragraph (a)(1) of this section that apply to taxable years beginning before December 30, 2008, are contained in §31.6011(a)-1. The rules of paragraph (a)(5) of this section that apply to taxable years beginning before December 30, 2008, are contained in §31.6011(a)-1T in effect prior to December 30, 2008.

(2) *Expiration date.* The applicability of this section will expire on or before December 23, 2011.

Par. 4. Section 31.6011(a)–4 is amended by revising paragraph (a)(1) and adding paragraph (d) to read as follows:

§31.6011(a)–4 Returns of income tax withheld.

(a) * * * (1) [Reserved]. For further guidance, see §31.6011(a)–4T(a)(1).

* * * * *

(d) [Reserved]. For further guidance, see §31.6011(a)–4T(d).

Par. 5. Section 31.6011(a)–4T is revised to read as follows:

§31.6011(a)–4T Returns of income tax withheld (temporary).

(a) *Withheld from wages*—(1) *In general.* Except as otherwise provided in §31.6011(a)–4(a)(2), (a)(3), (a)(4), and (b), and in §31.6011(a)–5, every person required to make a return of income tax withheld from wages pursuant to section 3402 shall make a return for the first calendar quarter in which the person is required to deduct and withhold such tax and for each subsequent calendar quarter, whether or not wages are paid therein, until the person has filed a final return in accordance with §31.6011(a)–6. Except as otherwise provided in §31.6011(a)–4(a)(2), (a)(3), (a)(4) and (b), and in §31.6011(a)–8, Form 941, “Employer’s *QUARTERLY Federal Tax Return*,” is the form prescribed for making the return required under this paragraph (a)(1).

(a)(2) through (a)(3) [Reserved]. For further guidance, see §31.6011(a)–4(a)(2) through (a)(3).

(4) *Employers in the Employers’ Annual Federal Tax Program (Form 944)*—(i) *In general.* Employers notified of their qualification for the Employers’ Annual Federal Tax Program (Form 944) are required to file Form 944, “Employer’s *ANNUAL Federal Tax Return*,” instead of Form 941 to make a return of income tax withheld from wages pursuant to section 3402. Upon proper request by the employer, the Internal Revenue Service (IRS) will notify employers in writing of their qualification for the Employers’ Annual Federal Tax Program (Form 944). Qualified employers are those with an estimated annual employment tax liability (that is, social security, Medicare, and withheld

federal income taxes) of \$1,000 or less for the entire calendar year, except employers required under §31.6011(a)–4(a)(2) to make a return on Schedule H (Form 1040), “Household Employment Taxes,” or §31.6011(a)–4(a)(3) to make a return on Form 943, “Employer’s Annual Federal Tax Return for Agricultural Employees.” The IRS may increase the amount of the estimated annual employment tax liability that qualifies employers to file Form 944 through a revenue procedure, notice or other IRS guidance published in the Internal Revenue Bulletin. The IRS will notify employers when they no longer qualify for the Employers’ Annual Federal Tax Program (Form 944) and must file Forms 941 instead.

(ii) *Request to participate and eligibility to opt out of the Employers’ Annual Federal Tax Program (Form 944).* The IRS will establish procedures in a revenue procedure, notice, or other IRS guidance published in the Internal Revenue Bulletin for employers to follow to request to receive notification to participate in the Employers’ Annual Federal Tax Program (Form 944) and to be removed from the Employers’ Annual Federal Tax Program (Form 944) after becoming a participant in order to file Forms 941 instead.

(b) through (c) [Reserved]. For further guidance, see §31.6011(a)–4(b) through (c).

(d) *Effective/applicability dates*—(1) *In general.* Paragraphs (a)(1) and (a)(4) of this section apply to taxable years beginning on or after December 30, 2008. The rules of paragraph (a)(1) of this section that apply to taxable years beginning before December 30, 2008, are contained in §31.6011(a)–4. The rules of paragraph (a)(4) of this section that apply to taxable years beginning before December 30, 2008, are contained in §31.6011(a)–4T in effect prior to December 30, 2008.

(2) *Expiration date.* The applicability of this section will expire on or before December 23, 2011.

Par. 6. Section 31.6302–0 is amended by revising the entries for §31.6302–1(f)(4)(i), (g)(1) and (n) to read as follows:

§31.6302–0 Table of contents.

* * * * *

§31.6302–1 Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act (FICA) attributable to payments made after December 31, 1992.

* * * * *

(f) * * *

(4) * * *

(i) [Reserved]. For further guidance, see §31.6302–0T, the entry for §31.6302–1T(f)(4)(i).

* * * * *

(g) * * *

(1) [Reserved]. For further guidance, see §31.6302–0T, the entry for §31.6302–1T(g)(1).

* * * * *

(n) [Reserved]. For further guidance, see §31.6302–0T, the entry for §31.6302–1T(n).

Par. 7. Section 31.6302–0T is added to read as follows:

§31.6302–0T Table of contents (temporary).

This section lists the captions that appear in §31.6302–1T.

Section 31.6302–1T Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act (FICA) attributable to payments made after December 31, 1992 (temporary).

(a) through (b)(3) [Reserved]. For further guidance, see §31.6302–0, the entries for §31.6302–1(a) through (b)(3).

(4) Lookback period.

(i) In general.

(ii) Adjustments and claims for refund.

(c)(1) through (c)(4) [Reserved]. For further guidance, see §31.6302–0, the entries for §31.6302–1(c)(1) through (c)(4).

(c)(5) Exception to the monthly and semi-weekly deposit rules for employers in the Employers’ Annual Federal Tax Program (Form 944).

(c)(6) Extension of time to deposit for employers in the Employers’ Annual Federal Tax Program (Form 944) during the preceding year.

(d) *Examples 1 through 5* [Reserved]. For further guidance, see §31.6302–0,

the entries for §31.6302-1(d) *Examples 1* through 5.

Example 6. Extension of time to deposit for employers who filed Form 944 for the preceding year satisfied.

(e) through (f)(3) [Reserved]. For further guidance, see §31.6302-0, the entries for §31.6302-1(e) through (f)(3).

(4) *De minimis* rule.

(i) *De minimis* deposit rules for quarterly and annual return periods beginning on or after January 1, 2001.

(ii) *De minimis* deposit rule for quarterly return periods beginning on or after January 1, 2010

(iii) *De minimis* deposit rule for employers who file Form 944.

(f)(5) *Examples 1* and 2 [Reserved]. For further guidance, see §31.6302-0, the entries for §31.6302-1(f)(5) *Examples 1* and 2.

Example 3. *De minimis* deposit rule for employers who file Form 944 satisfied.

(g) [Reserved]. For further guidance, see §31.6302-0, the entry for §31.6302-1(g).

(1) In general.

(g)(2) through (m) [Reserved]. For further guidance, see §31.6302-0, the entries for §31.6302-1(g)(2) through (m).

(n) Effective/applicability dates.

Par. 8. Section 31.6302-1 is amended by revising paragraphs (e)(2), (f)(4)(i), (g)(1) and (n) and adding paragraph (f)(4)(ii) to read as follows:

* * * * *

(e) * * *

(2) [Reserved]. For further guidance, see §31.6302-1T(e)(2).

(f) * * *

(4) * * * (i) and (ii) [Reserved]. For further guidance, see §31.6302-1T(f)(4)(i) and (ii).

* * * * *

(g) * * *(1) [Reserved]. For further guidance, see §31.6302-1T(g)(1).

* * * * *

(n) [Reserved]. For further guidance, see §31.6302-1T(n).

Par. 9. Section 31.6302-1T is revised to read as follows:

§31.6302-1T Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act

(FICA) attributable to payments made after December 31, 1992 (temporary).

(a) through (b)(3) [Reserved]. For further guidance, see §31.6302-1(a) through (b)(3).

(4) *Lookback period*—(i) *In general.* For employers who file Form 941, “Employer’s *QUARTERLY Federal Tax Return*,” the lookback period for each calendar year is the twelve month period ended the preceding June 30. For example, the lookback period for calendar year 2006 is the period July 1, 2004, to June 30, 2005. The lookback period for employers who file Form 944, “Employer’s *ANNUAL Federal Tax Return*,” or filed Form 944 either of the two previous calendar years, is the second calendar year preceding the current calendar year. For example, the lookback period for calendar year 2006 is calendar year 2004. In determining status as either a monthly or semi-weekly depositor, an employer should determine the aggregate amount of employment tax liabilities reported on its return(s) (Form 941 or Form 944) for the lookback period. The amount of employment tax liabilities reported for the lookback period is the amount the employer reported on either Forms 941 or Form 944 even if the employer is required to file the other form(s) for the current calendar year. New employers shall be treated as having employment tax liabilities of zero for any part of the lookback period before the date the employer started or acquired its business.

(ii) *Adjustments and claims for refund.* The employment tax liability reported on the original return for the return period is the amount taken into account in determining whether the aggregate amount of employment taxes reported for the lookback period exceeds \$50,000. Any amounts reported on adjusted returns or claims for refund pursuant to sections 6205, 6402, 6413 and 6414 filed after the due date of the original return are not taken into account when determining the aggregate amount of employment taxes reported for the lookback period. However, prior period adjustments reported on Forms 941 or 944 for 2008 and earlier years are taken into account in determining the employment tax liability for the return period in which the adjustments are reported.

(c)(1) through (c)(4) [Reserved]. For further guidance, see §31.6302-1(c)(1) through (c)(4).

(5) *Exception to the monthly and semi-weekly deposit rules for employers in the Employers’ Annual Federal Tax Program (Form 944).* Generally, an employer who files Form 944 for a taxable year may remit its accumulated employment taxes with its timely filed return for that taxable year and is not required to deposit under either the monthly or semi-weekly rules set forth in §31.6302-1(c)(1) and (2) during that taxable year. An employer who files Form 944 whose actual employment tax liability exceeds the eligibility threshold, as set forth in §§31.6011(a)-1T(a)(5) and 31.6011(a)-4T(a)(4), will not qualify for this exception and should follow the deposit rules set forth in this section.

(6) *Extension of time to deposit for employers in the Employers’ Annual Federal Tax Program (Form 944) during the preceding year.* An employer who filed Form 944 for the preceding year but will file Forms 941 instead for the current year will be deemed to have timely deposited its current year’s January deposit obligation(s) under §31.6302-1(c)(1) through (4) if the employer deposits the amount of such deposit obligation(s) by March 15 of that year.

(d) *Examples 1* through 5 [Reserved]. For further guidance, see §31.6302-1(d) *Examples 1* through 5.

Example 6. *Extension of time to deposit for employers who filed Form 944 for the preceding year satisfied.* F (a monthly depositor) was notified to file Form 944 to report its employment tax liabilities for the 2006 calendar year. F filed Form 944 on January 31, 2007, reporting a total employment tax liability for 2006 of \$3,000. Because F’s annual employment tax liability for the 2006 taxable year exceeded \$1,000 (the applicable eligibility threshold for that taxable year), the Internal Revenue Service (IRS) notified F to file Forms 941 for calendar year 2007 and thereafter. Based on F’s liability during the lookback period (calendar year 2005, pursuant to paragraph (b)(4)(i) of this section), F is a monthly depositor for 2007. F accumulates \$1,000 in employment taxes during January 2007. Because F is a monthly depositor, F’s January deposit obligation is due February 15, 2007. F does not deposit these accumulated employment taxes on February 15, 2007. F accumulates \$1,500 in employment taxes during February 2007. F’s February deposit is due March 15, 2007. F deposits the \$2,500 of employment taxes accumulated during January and February on March 15, 2007. Pursuant to §31.6302-1T(c)(6), F will be deemed to have timely deposited the employment taxes due for January 2007, and, thus, the IRS will

not impose a failure-to-deposit penalty under section 6656 for that month.

(e)(1) [Reserved]. For further guidance, see §31.6302-1(e)(1).

(2) The term *employment taxes* does not include taxes with respect to wages for domestic service in a private home of the employer, unless the employer is otherwise required to file a Form 941 or Form 944 under §31.6011(a)-4, §31.6011(a)-4T, or §31.6011(a)-5. In the case of employers paying advance earned income credit amounts, the amount of taxes required to be deposited shall be reduced by advance amounts paid to employees. Also, see §31.6302-3 concerning a taxpayer's option with respect to payments made before January 1, 1994, to treat backup withholding amounts under section 3406 separately.

(f)(1) through (f)(3) [Reserved]. For further guidance, see §31.6302-1(f)(1) through (f)(3).

(4) *De minimis rule*—(i) *De minimis deposit rules for quarterly and annual return periods beginning on or after January 1, 2001*. If the total amount of accumulated employment taxes for the return period is *de minimis* and the amount is fully deposited or remitted with a timely filed return for the return period, the amount deposited or remitted will be deemed to have been timely deposited. The total amount of accumulated employment taxes is *de minimis* if it is less than \$2,500 for the return period or if it is *de minimis* pursuant to paragraph (f)(4)(ii) of this section.

(ii) *De minimis deposit rule for quarterly return periods beginning on or after January 1, 2010*. For purposes of paragraph (f)(4)(i) of this section, if the total amount of accumulated employment taxes for the immediately preceding quarter was less than \$2,500, unless §31.6302-1(c)(3) applies to require a deposit at the close of the next banking day, then the employer will be deemed to have timely deposited the employer's employment taxes for the current quarter if the employer complies with the time and method payment requirements contained in paragraph (f)(4)(i) of this section.

(iii) *De minimis deposit rule for employers who file Form 944*. An employer who files Form 944 whose employment tax liability for the year equals or exceeds \$2,500 but whose employment tax liability for a quarter of the year is *de minimis* pursuant to paragraph (f)(4)(i) of this section

will be deemed to have timely deposited the employment taxes due for that quarter if the employer fully deposits the employment taxes accumulated during the quarter by the last day of the month following the close of that quarter. Employment taxes accumulated during the fourth quarter can be either deposited by January 31 or remitted with a timely filed return for the return period.

(5) *Examples 1 and 2* [Reserved]. For further guidance, see §31.6302-1(f)(5) *Examples 1 and 2*.

Example 3. De minimis deposit rule for employers who file Form 944 satisfied. K (a monthly depositor) was notified to file Form 944 to report its employment tax liabilities for the 2006 calendar year. In the first quarter of 2006, K accumulates employment taxes in the amount of \$1,000. On April 28, 2006, K deposits the \$1,000 of employment taxes accumulated in the 1st quarter. K accumulates another \$1,000 of employment taxes during the second quarter of 2006. On July 31, 2006, K deposits the \$1,000 of employment taxes accumulated in the 2nd quarter. K's business grows and accumulates \$1,500 in employment taxes during the third quarter of 2006. On October 31, 2006, K deposits the \$1,500 of employment taxes accumulated in the 3rd quarter. K accumulates another \$2,000 in employment taxes during the fourth quarter. K files Form 944 on January 31, 2007, reporting a total employment tax liability for 2006 of \$5,500 and submits a check for the remaining \$2,000 of employment taxes with the return. K will be deemed to have timely deposited the employment taxes due for all of 2006, because K complied with the *de minimis* deposit rule provided in paragraph (f)(4)(iii) of this section. Therefore, the IRS will not impose a failure-to-deposit penalty under section 6656 for any month of the year. Under this *de minimis* deposit rule, as K was required to file Form 944 for calendar year 2006, if K's employment tax liability for a quarter is *de minimis*, then K may deposit that quarter's liability by the last day of the month following the close of the quarter. This *de minimis* rule allows K to have the benefit of the same quarterly *de minimis* amount K would have received if K filed Form 941 each quarter instead of Form 944 annually. Thus, as K's employment tax liability for each quarter was *de minimis*, K could deposit quarterly.

(g) *Agricultural employers—special rules*—(1) *In general*. An agricultural employer reports wages paid to farm workers annually on Form 943 (*Employer's Annual Tax Return for Agricultural Employees*) and reports wages paid to nonfarm workers quarterly on Form 941 or annually on Form 944. Accordingly, an agricultural employer must treat employment taxes reportable on Form 943 ("Form 943 taxes") separately from employment taxes reportable on Form 941 or Form 944 ("Form 941 or Form 944 taxes"). Form 943 taxes and Form 941 or Form 944 taxes are not combined for purposes of determining

whether a deposit of either is due, whether the One-Day rule of §31.6302-1(c)(3) applies, or whether any safe harbor is applicable. In addition, separate Federal tax deposit coupons must be used to deposit Form 943 taxes and Form 941 or Form 944 taxes. (See §31.6302-1(b) for rules for determining an agricultural employer's deposit status for Form 941 taxes.) The determination of whether an agricultural employer is a monthly or semi-weekly depositor of Form 943 taxes is made according to the rules of this paragraph (g).

(g)(2) through (m) [Reserved]. For further guidance, see §31.6302-1(g)(2) through (m).

(n) *Effective/applicability dates*—(1) *In general*. Sections 31.6302-1 through 31.6302-3 apply with respect to the deposit of employment taxes attributable to payments made after December 31, 1992. To the extent that the provisions of §§31.6302-1 through 31.6302-3 are inconsistent with the provisions of §§31.6302(c)-1 and 31.6302(c)-2, a taxpayer will be considered to be in compliance with §§31.6301-1 through 31.6302-3 if the taxpayer makes timely deposits during 1993 in accordance with §§31.6302(c)-1 and 31.6302(c)-2. Paragraphs (b)(4), (c)(5), (c)(6), (d) *Example 6*, (e)(2), (f)(4)(i), (f)(4)(iii), (f)(5) *Example 3*, and (g)(1) of this section apply to taxable years beginning on or after December 30, 2008. Paragraph (f)(4)(ii) of this section applies to taxable years beginning on or after January 1, 2010. The rules of paragraphs (e)(2) and (g)(1) of this section that apply to taxable years beginning before December 30, 2008, are contained in §31.6302-1 in effect prior to December 30, 2008. The rules of paragraphs (b)(4), (c)(5), (c)(6), (d) *Example 6*, (f)(4)(i), (f)(4)(iii), and (f)(5) *Example 3* of this section that apply to taxable years beginning on or after January 1, 2006 and before December 30, 2008, are contained in §31.6302-1T in effect prior to December 30, 2008. The rules of paragraphs (b)(4) and (f)(4) of this section that apply to taxable years beginning before January 1, 2006, are contained in §31.6302-1 in effect prior to January 1, 2006.

(2) *Expiration date*. The applicability of this section will expire on or before December 23, 2011.

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

Approved December 18, 2008.

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

(Filed by the Office of the Federal Register on December 24, 2008, 8:45 a.m., and published in the issue of the Federal Register for December 29, 2008, 73 F.R. 79354)

Section 6103.—Confidentiality and Disclosure of Returns and Return Information

26 CFR 301.6103(j)(1)–1: Disclosures of return information to officers and employees of the Department of Commerce for certain statistical purposes and related activities.

T.D. 9439

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 301

Disclosure of Return Information to the Bureau of Economic Analysis

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation and removal of temporary regulations.

SUMMARY: This document contains final regulations relating to disclosures of corporate tax return information to the Bureau of Economic Analysis (Bureau). The final regulations authorize the IRS to disclose certain items of corporate tax return information to the Secretary of Commerce for purposes of structuring United States national economic accounts and conducting related statistical activities authorized by law. The final regulations facilitate the assistance of the IRS to the Bureau in its statistics programs, require no action by taxpayers, and have no effect on their tax liabilities.

DATES: *Effective Date:* These regulations are effective on December 29, 2008.

Applicability Date: These regulations apply to disclosures made to the Bureau of Economic Analysis on or after December 29, 2008.

FOR FURTHER INFORMATION CONTACT: Charles B. Christopher, (202) 622–4570 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains final regulations amending the Procedure and Administration Regulations (26 CFR Part 301) under section 6103(j)(1)(B) of the Internal Revenue Code (Code). The final regulations contain rules relating to the disclosure of corporate tax return information to the Bureau of Economic Analysis (Bureau) of the Department of Commerce for the purpose of, but only to the extent necessary in, structuring national economic accounts and conducting related statistical activities authorized by law.

Section 6103(j)(1)(B) provides that, upon written request from the Secretary of Commerce, the Secretary of the Treasury shall furnish to BEA return information that is prescribed by Treasury regulations for the purpose of, but only to the extent necessary in, structuring of national economic accounts and conducting related statistical activities authorized by law. Prior regulations under section 6103(j)(1)(B) permitted the disclosure to BEA of return information from corporate returns processed by the IRS's Statistics of Income Division for its corporate sample file.

By letter dated December 18, 2003, the Department of Commerce requested disclosure of certain items of return information obtained from all corporate returns, not just those processed by the IRS's Statistics of Income Division for its corporate sample file. Proposed regulations (REG–148864–03, 2006–2 C.B. 320 [71 FR 38323]) and temporary regulations (T.D. 9267, 2006–2 C.B. 313 [71 FR 38262]) were published in the **Federal Register** on July 6, 2006. The Department of Commerce thereafter submitted comments requesting certain technical corrections to the items of corporate return information authorized to be disclosed. No other

comments were received, and no public hearing was requested or held. After consideration of the comments received from the Department of Commerce, the proposed regulations, as amended by this Treasury decision, are adopted as final regulations, and the corresponding temporary regulations are removed. See §601.601(d)(2)(ii)(b). These final regulations generally retain the provisions of the proposed regulations with the inclusion of the additional requested items as explained in more detail in this preamble.

Explanation and Summary of Comments

Proposed §301.6103(j)(1)–1(c)(3) provided an itemized description of the corporate tax return information authorized to be disclosed to the Bureau for the purpose of structuring national economic accounts and conducting related statistical activities required by law. In its comments, the Department of Commerce requested that certain additional items of corporate tax return information that are essential to the Bureau's ability to measure accurately U.S. economic activity be included in the itemized list in the final regulations. Most of the additional items of corporate tax return information to which the Department of Commerce requests access are slightly different variants of the same items authorized in the proposed regulations. The inclusion of these items will enable the Bureau to measure accurately corporate profits, gross domestic product, and other measures of activity in the economy. After consideration of these comments, the Treasury Department and IRS have included the additional requested items in the final regulations.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. Because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6)

does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small businesses.

Drafting Information

The principal author of these regulations is Robin M. Tuczak, Office of the Associate Chief Counsel (Procedure & Administration).

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

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

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

Par. 2. Section 301.6103(j)(1)–1 is amended by revising paragraphs (c) introductory text, (c)(1) and (e) and removing and reserving paragraph (c)(2), and adding paragraph (c)(3) to read as follows:

§301.6103(j)(1)–1 Disclosures of return information to officers and employees of the Department of Commerce for certain statistical purposes and related activities.

* * * * *

(c) Disclosure of return information reflected on returns of corporations to officers and employees of the Bureau of Economic Analysis.

(1) As authorized by law for purposes of, but only to the extent necessary in, conducting and preparing statistical analyses, the Internal Revenue Service will disclose to officers and employees of the Bureau of Economic Analysis all return information, regardless of format or medium and including edited information from the Statistics of Income sample, of designated classes or categories of corporations with respect to the tax imposed by chapter 1 of the Internal Revenue Code.

(2) [Reserved].

(3) The Internal Revenue Service will disclose the following return information reflected on returns filed by corporations to officers and employees of the Bureau of Economic Analysis:

(i) From the business master files of the Internal Revenue Service—

(A) Taxpayer identity information (as defined in section 6103(b)(6)) with respect to corporate taxpayers;

(B) Business or industry activity codes;

(C) Filing requirement code; and

(D) Physical location.

(ii) From Form SS–4, “*Application for Employer Identification Number*,” filed by an entity identifying itself on the form as a corporation or a private services corporation—

(A) Taxpayer identity information (as defined in section 6103(b)(6), including legal, trade, and business name);

(B) Physical location;

(C) State or country of incorporation;

(D) Entity type (corporate only);

(E) Estimated highest number of employees expected in the next 12 months;

(F) Principal activity of the business;

(G) Principal line of merchandise;

(H) Posting cycle date relative to filing; and

(I) Document code.

(iii) From an employment tax return filed by a corporation—

(A) Taxpayer identity information (as defined in section 6103(b)(6));

(B) Total compensation reported;

(C) Taxable wages paid for purposes of Chapter 21 to each employee;

(D) Master file tax account code (MFT);

(E) Total number of individuals employed in the taxable period covered by the return;

(F) Posting cycle date relative to filing;

(G) Accounting period covered; and

(H) Document code.

(iv) From returns of corporate taxpayers, including Form 1120, “*U.S. Corporation Income Tax Return*,” Form 851, “*Affiliations Schedule*,” and other business returns, schedules and forms that the Internal Revenue Service may issue—

(A) Taxpayer identity information (as defined in section 6103(b)(6)), including that of a parent corporation, affiliate, or subsidiary; a shareholder; a foreign corpo-

ration of which one or more U.S. shareholders (as defined in section 951(b)) own at least 10% of the voting stock; a foreign trust; and a U.S. agent of a foreign trust;

(B) Gross sales and receipts;

(C) Gross income, including life insurance company gross income;

(D) Gross income from sources outside the U.S.;

(E) Gross rents from real property;

(F) Other Gross Rents;

(G) Total Gross Rents;

(H) Returns and allowances;

(I) Percentage of foreign ownership of corporations and trusts;

(J) Fact of ownership of foreign partnerships;

(K) Fact of ownership of foreign entity disregarded as a foreign entity;

(L) Country of the foreign owner;

(M) Gross value of the portion of the foreign trust owned by filer;

(N) Country of incorporation;

(O) Cost of labor, salaries, and wages;

(P) Total assets;

(Q) The quantity of certain forms attached that are returns of U.S. persons with respect to foreign disregarded entities, partnerships, and corporations.

(R) Posting cycle date relative to filing;

(S) Accounting period covered;

(T) Master file tax account code (MFT);

(U) Document code; and

(V) Principal industrial activity code.

* * * * *

(e) *Effective/applicability date.* This section applies to disclosures to the Bureau of Economic Analysis on or after December 29, 2008.

§301.6103(j)(1)–1T [Removed]

Par. 3. Section 301.6103(j)(1)–1T is removed.

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

Approved December 17, 2008.

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

(Filed by the Office of the Federal Register on December 24, 2008, 8:45 a.m., and published in the issue of the Federal Register for December 25, 2008, 73 F.R. 79361)

Section 6302.—Mode or Time of Collection

26 CFR 31.6302-1: Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act (FICA) attributable to payments made after December 31, 1992.

Temporary regulations relate to the annual filing of Federal employment tax returns and requirements

for employment tax deposits. These temporary regulations relate to sections 6011 and 6302 of the Internal Revenue Code (Code) concerning reporting and paying income taxes withheld from wages and reporting and paying taxes under the Federal Insurance Contributions Act (FICA) (collectively, “employment taxes”). See T.D. 9440, page 409.

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations.

A revenue ruling holds that Dubai Merchantile Exchange, which is a United Arab Emirates Authorized Market Institution, is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code. See Rev. Rul. 2009-4, page 408.

Part III. Administrative, Procedural, and Miscellaneous

Required Minimum Distributions for 2009

Notice 2009-9

PURPOSE

This notice provides guidance to financial institutions on reporting required minimum distributions for 2009 after enactment of the Worker, Retiree, and Employer Recovery Act of 2008, P. L. 110-458.

BACKGROUND

On December 23, 2008, the President signed the Worker, Retiree, and Employer Recovery Act of 2008 (the Act) into law. Section 201 of the Act waives any required minimum distributions (RMDs) for 2009 from retirement plans that hold each participant's benefit in an individual account, such as § 401(k) plans and § 403(b) plans, and certain § 457(b) plans. The Act also waives any RMD for 2009 from an Individual Retirement Arrangement (IRA). This means that most participants and beneficiaries otherwise required to take minimum distributions from these types of accounts are not required to withdraw any amount in 2009. If they do make a withdrawal in 2009 (that is not an RMD for 2008), they might be able to roll over the withdrawn amount into other eligible retirement plans. Of course, they must still include any previously untaxed portion of the withdrawal that they do not roll over in their gross income. See *Individual Retirement Arrangements (IRAs)*, Publication 590, and *Pension and Annuity Income*, Publication 575, for additional information on rollovers and on calculating the taxable portion of a distribution.

The Act does not waive any 2008 RMDs, even for individuals who were eligible and chose to delay taking their 2008 RMD until April 1, 2009 (e.g., retired employees and IRA owners who turned 70½ in 2008). These individuals must still take their full 2008 RMD by April 1, 2009. The 2009 RMD waiver under the Act does apply to individuals who may be eligible to postpone taking their 2009 RMD until

April 1, 2010 (generally, retired employees and IRA owners who attain age 70½ in 2009). However, the Act does not waive any RMDs for 2010.

If a beneficiary is receiving distributions over a 5-year period, he or she can now waive the distribution for 2009, effectively taking distributions over a 6-year rather than a 5-year period.

IRA REPORTING

Issuers of the 2008 Form 5498, *IRA Contribution Information*, should **not** put a check in Box 11. However, in recognition of the short amount of time to make programming changes, if a financial institution issues a 2008 Form 5498 with a check in Box 11, the IRS will not consider such form issued incorrectly solely because of the check in Box 11, provided the IRA owner is notified by the financial institution no later than March 31, 2009, that no RMD is required for 2009.

In addition, the RMD information required under Notice 2002-27, 2002-1 C.B. 814, need not be sent to IRA owners for 2009. If a financial institution sends a separate RMD statement to an IRA owner, either initially or in response to the owner's request for the financial institution to calculate the RMD for 2009, the financial institution must show the RMD for 2009 as zero (0). Alternatively, the financial institution may send the IRA owner a statement showing the RMD that would have been required but for the waiver of RMDs for 2009, along with an explanation of the waiver for 2009.

The IRS encourages all financial institutions to inform IRA owners who delayed taking their 2008 RMD until April 1, 2009, that they are still required to take that distribution.

EFFECT ON OTHER DOCUMENTS

Notice 2002-27 is modified.

DRAFTING INFORMATION

The principal author of this notice is Anita Bower of the Employee Plans, Tax Exempt and Government

Entities Division. Questions regarding this notice may be sent via e-mail to RetirementPlanQuestions@irs.gov.

Treatment of Certain Obligations Under Section 956(c)

Notice 2009-10

1. On October 27, 2008, the Treasury Department and the Internal Revenue Service (Service) published Notice 2008-91. See Notice 2008-91, 2008-43 I.R.B. 1001. This notice provides that the regulations described in Notice 2008-91 will apply (in addition to the period described in Notice 2008-91) to the third consecutive taxable year of a foreign corporation, if any, (including any short taxable year) that ends after October 3, 2008, and that ends on or before December 31, 2009.

2. On May 27, 2008, the Treasury Department and the Service published Rev. Proc. 2008-26, 2008-21 I.R.B. 1014, which applies to determine whether securities are "readily marketable" for purposes of section 956(c)(2)(J) for any day during calendar years 2007 or 2008, for which it is relevant whether securities are readily marketable for purposes of that section. This notice extends the application of Rev. Proc. 2008-26 to any day during calendar year 2009, for which it is relevant whether securities are readily marketable for purposes of section 956(c)(2)(J) (in addition to any day during calendar years 2007 or 2008).

DRAFTING INFORMATION

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

Brokers May Furnish Certain Composite Annual Tax Reporting Statements by February 17, 2009, Without Penalty

Notice 2009-11

PURPOSE

This notice provides additional time for furnishing certain composite annual tax reporting statements.

BACKGROUND

Section 403 of the Energy Improvement and Extension Act of 2008, Div. B of Pub. L. No. 110-343, 122 Stat. 3765 (the Act), enacted on October 3, 2008, amended section 6045(b) of the Internal Revenue Code to change from January 31 to February 15 the deadline for furnishing to customers the information statements required by section 6045, including Form 1099-B (*Proceeds From Broker and Barter Exchange Transactions*), effective for statements required to be furnished after December 31, 2008. Because February 15, 2009, is a Sunday, and because February 16, 2009, is a legal holiday, the deadline under section 6045(b) with respect to reportable items from calendar year 2008 is February 17, 2009, pursuant to section 7503. The Act also added language to section 6045(b) to permit reporting entities to furnish other

items that they must report to customers in January by the extended deadline when these other items are furnished with a “consolidated reporting statement (as defined in regulations).” There is not yet a regulatory definition of the term “consolidated reporting statement.” Section 6722 imposes a penalty on any reporting entity that fails to furnish any required payee statement by its deadline.

DEADLINE FOR REPORTING ITEMS FROM 2008

This notice applies to reporting entities that furnish Form 1099-B and that customarily report the items furnished on Form 1099-B to customers on an annual composite form recipient statement (as described in Section 4.2 of Rev. Proc. 2008-36, 2008-33 I.R.B. 340). This notice provides that such reporting entities have until February 17, 2009, to report all items that they customarily report on these annual composite form recipient statements to all customers whether or not each customer’s transactional history for 2008 triggered an obligation to furnish Form 1099-B to that particular customer. This notice modifies the 2008 General Instructions for Forms 1099, 1098, 5498, and W-2G and applies only to the reporting of items from calendar year 2008.

EXAMPLE

This notice is illustrated by the following example:

Broker, a brokerage firm, customarily issues an annual composite form recipient statement to each of its customers that reports dividends as required by section 6042(c), interest as required by section 6049(c), and the gross proceeds of the sale of securities and other items as required by section 6045(b). Broker issued correct annual composite form recipient statements to all of its customers on February 12, 2009. Because only 80 percent of Broker’s customers sold securities or other items in 2008, only 80 percent of the annual composite form recipient statements contained information required to be reported under section 6045(b) on Form 1099-B. Because the composite form recipient statements customarily included dividends and interest with items reportable on Form 1099-B, and because Broker provided correct statements to each of its customers by February 17, 2009, the IRS will treat Broker as having met its reporting deadline requirements under sections 6042(c) and 6049(c) for items from calendar year 2008 reported on the annual composite form recipient statements and will not assess any penalties under section 6722 for these items.

DRAFTING INFORMATION

The principal author of this notice is Stephen Schaeffer of the Office of Associate Chief Counsel (Procedure & Administration). For further information regarding this notice, please contact Stephen Schaeffer at (202) 622-4910 (not a toll-free call).

Part IV. Items of General Interest

Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations

Employer's Annual Federal Tax Return and Modifications to the Deposit Rules

REG-148568-04

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: This document revises the notice of proposed rulemaking published in the **Federal Register** on January 3, 2006. In this issue of the Bulletin, the IRS is issuing temporary regulations (T.D. 9440) relating to the annual filing of Federal employment tax returns and requirements for employment tax deposits under sections 6011 and 6302 of the Internal Revenue Code (Code). Those temporary regulations generally allow certain employers to file a Form 944, "Employer's ANNUAL Federal Tax Return," rather than Form 941, "Employer's QUARTERLY Federal Tax Return." In addition to rules related to Form 944, those temporary regulations provide an additional method for employers who file Form 941 to determine whether the amount of accumulated employment taxes is considered *de minimis*. The temporary and proposed regulations affect taxpayers that file Form 941, "Employer's QUARTERLY Federal Tax Return," Form 944, "Employer's ANNUAL Federal Tax Return," and any related Spanish-language returns or returns for U.S. possessions. The text of those regulations also serves as the text of these proposed regulations.

DATES: Written or electronic comments and requests for a public hearing must be received by March 30, 2009.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-148568-04), room

5203, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-148568-04), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-148568-04).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Audra M. Dineen at (202) 622-4910; concerning submissions of comments and requests for a public hearing, Oluwafunmilayo Taylor of the Publications and Regulations Branch at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

Temporary regulations in this issue of the Bulletin amend the Regulations on Employment Taxes and Collection of Income Tax at Source (26 CFR part 31) under section 6011 relating to the federal employment tax return filing requirements and section 6302 relating to the employment tax deposit requirements. The regulations concern the reporting and paying of income taxes withheld from wages and taxes under the Federal Insurance Contributions Act (FICA). The text of those temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations. The temporary and proposed regulations are part of the IRS's effort to reduce taxpayer burden by permitting certain employers to file one return annually to report their employment tax liabilities instead of four quarterly returns.

Proposed Effective/Applicability Date

The regulations, as proposed, will apply to taxable years ending on or after the date of publication of the Treasury decision adopting these rules as final regulations in the **Federal Register**.

Special Analyses

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

It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities pursuant to the Regulatory Flexibility Act (5 U.S.C. Chapter 6). The regulations under sections 6011 and 6302 affect only a small number of taxpayers that file employment tax returns. Therefore, the Treasury Department and the IRS have determined that these regulations will not affect a substantial number of small entities. In addition, the Treasury Department and the IRS have determined that any impact on entities affected by the regulations will not be significant. The regulations merely allow certain employers to file their employment tax return annually rather than quarterly. Therefore, these regulations will reduce the burden on these employers, by reducing the number of returns they must file each year. Based on these facts, the IRS has determined that these regulations will not have a significant economic impact on a substantial number of small entities. Pursuant to section 7805(f) of the Internal Revenue Code, this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Comments and Requests for a Public Hearing

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

uled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these final regulations are Raymond Bailey and Audra M. Dineen of the Office of the Associate Chief Counsel (Procedure and Administration).

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 31 is proposed to be amended as follows:

PART 31—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE

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

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

Par. 2. Section 31.6011(a)–1, which was proposed to be amended at 71 FR 46 on January 3, 2006, is further amended by revising paragraph (a)(1) and paragraph (a)(5) and adding paragraph (g) to read as follows:

§31.6011(a)–1 Returns under Federal Insurance Contributions Act.

(a) * * *(1) [The text of proposed §31.6011(a)–1(a)(1) is the same as the text of §31.6011(a)–1T(a)(1) published elsewhere in this issue of the Bulletin].

* * * * *

(5) [The text of proposed §31.6011(a)–1(a)(5) is the same as the text of §31.6011(a)–1T(a)(5) published elsewhere in this issue of the Bulletin].

* * * * *

(g) [The text of proposed §31.6011(a)–1(g) is the same as the text of §31.6011(a)–1T(g) published elsewhere in this issue of the Bulletin].

Par. 3. Section 31.6011(a)–4, which was proposed to be amended at 71 FR 46 (January 3, 2006), is further amended by revising paragraphs (a)(1) and (a)(4) and adding paragraph (d) to read as follows:

§31.6011(a)–4 Returns of income tax withheld.

(a) * * *(1) [The text of proposed §31.6011(a)–4(a)(1) is the same as the text of §31.6011(a)–4T(a)(1) published elsewhere in this issue of the Bulletin].

* * * * *

(4) [The text of proposed §31.6011(a)–4(a)(4) is the same as the text of §31.6011(a)–4T(a)(4) published elsewhere in this issue of the Bulletin].

* * * * *

(d) [The text of proposed §31.6011(a)–4(d) is the same as the text of §31.6011(a)–4T(d) published elsewhere in this issue of the Bulletin].

Par. 4. Section 31.6302–0 is amended by revising the entries for §31.6302–1(f)(4)(i), (g)(1) and (n) to read as follows:

§31.6302–0 Table of contents.

* * * * *

§31.6302–1 Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act (FICA) attributable to payments made after December 31, 1992.

* * * * *

(f) * * *
(4) * * *

(i) [The text of the proposed entry for §31.6302–1(f)(4)(i) is the same as the text of the entry for §31.6302–1T(f)(4)(i) published elsewhere in this issue of the Bulletin].

* * * * *

(g) * * *

(1) [The text of the proposed entry for §31.6302–1(g)(1) is the same as the text of the entry for §31.6302–1T(g)(1) published elsewhere in this issue of the Bulletin].

* * * * *

(n) [The text of the proposed entry for §31.6302–1(n) is the same as the text of the entry for §31.6302–1T(n) published elsewhere in this issue of the Bulletin].

Par. 5. Section 31.6302–1, which was proposed to be amended at 71 FR 46 on January 3, 2006, is further amended by revising paragraphs (b)(4), (c)(5), (c)(6), (d)

Example 6, (e)(2), (f)(4), (f)(5) Example 3, (g)(1) and (n) to read as follows:

§31.6302–1 Federal tax deposit rules for withheld income taxes and taxes under the Federal Insurance Contributions Act (FICA) attributable to payments made after December 31, 1992.

* * * * *

(b) * * *

* * * * *

(4) [The text of proposed §31.6302–1(b)(4) is the same as the text of §31.6302–1T(b)(4) published elsewhere in this issue of the Bulletin].

(c) * * *

(5) [The text of proposed §31.6302–1(c)(5) is the same as the text of §31.6302–1T(c)(5) published elsewhere in this issue of the Bulletin].

(6) [The text of proposed §31.6302–1(c)(6) is the same as the text of §31.6302–1T(c)(6) published elsewhere in this issue of the Bulletin].

(d) * * *

Example 6. [The text of proposed §31.6302–1(d) Example 6 is the same as the text of §31.6302–1T(d) Example 6 published elsewhere in this issue of the Bulletin].

(e) * * *

(2) [The text of proposed §31.6302–1(e)(2) is the same as the text of §31.6302–1T(e)(2) published elsewhere in this issue of the Bulletin].

(f) * * *

(4) [The text of proposed §31.6302–1(f)(4) is the same as the text of §31.6302–1T(f)(4) published elsewhere in this issue of the Bulletin].

(5) * * *

Example 3. [The text of proposed §31.6302–1(f)(5) Example 3 is the same as the text of §31.6302–1T(f)(5) Example 3 published elsewhere in this issue of the Bulletin].

(g) * * * (1) [The text of proposed §31.6302–1(g)(1) is the same as the text of §31.6302–1T(g)(1) published elsewhere in this issue of the Bulletin].

* * * * *

(n) [The text of proposed §31.6302–1(n) is the same as the text of §31.6302–1T(n)(1) published elsewhere in this issue of the Bulletin].

* * * * *

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

(Filed by the Office of the Federal Register on December 24, 2008, 8:45 a.m., and published in the issue of the Federal Register for December 29, 2008, 73 F.R. 79423)

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

Guidance Regarding Foreign Base Company Sales Income

REG-150066-08

AGENCY: Internal Revenue Service (IRS), Treasury.

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

SUMMARY: In this issue of the Bulletin, the IRS and Treasury Department are issuing temporary regulations (T.D. 9438) relating to foreign base company sales income, in cases in which personal property sold by a controlled foreign corporation (CFC) is manufactured, produced, or constructed pursuant to a contract manufacturing arrangement or by one or more branches of the CFC. The temporary regulations modify the foreign base company sales income regulations to adequately address current business structures and practices, particularly the growing importance of contract manufacturing and other manufacturing arrangements. The temporary regulations, in general, will affect CFCs and their United States shareholders. The text of the temporary regulations also serves as the text of the proposed regulations. This document also provides notice of a public hearing.

DATES: Written or electronic comments must be received by March 30, 2009. Outlines of the topics to be discussed at the public hearing scheduled for April 20, 2009, at 10 a.m. must be received by April 2, 2009.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-150066-08), room 5203 Internal Revenue Service, PO Box 7604 Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-150066-08), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC 20224. Alternatively, taxpayers may submit electronic comments via the Federal eRulemaking Portal at www.regulations.gov (IRS-REG-150066-08).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Ethan Atticks, (202) 622-3840; concerning submissions of comments, hearing, and/or to be placed on the building access list to attend the hearing, Richard A. Hurst at Richard.A.Hurst@irscounsel.treas.gov or (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provision

The temporary regulations in this issue of the Bulletin amend the Income Tax Regulations (26 CFR part 1) relating to foreign base company sales income, in cases in which personal property sold by a controlled foreign corporation (CFC) is manufactured, produced, or constructed pursuant to a contract manufacturing arrangement or by one or more branches of the CFC. These regulations, in general, will affect CFCs and their United States shareholders. The text of those temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains these proposed regulations.

Special Analyses

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

of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Comments and Public Hearing

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

A public hearing has been scheduled for April 20, 2009, beginning at 10 a.m. in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the Constitution Avenue entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written comments or electronic comments by March 30, 2009, and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by April 2, 2009. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Ethan Atticks of the Office of

Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

* * * * *

Proposed Amendments to the Regulations

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

PART 1—INCOME TAXES

Paragraph 1. The authority citation for 26 CFR part 1 continues to read in part as follows:

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

Par. 2. Section 1.954-3 is amended by revising paragraphs (b)(1)(i)(c), (b)(1)(ii)(a), (b)(1)(ii)(c), (b)(2)(i)(b), (b)(2)(i)(d), (b)(2)(ii)(a), (b)(2)(ii)(b), (b)(2)(ii)(e), (b)(4) *Example 3*, (c) and (d), and adding *Examples 8* and *9* to paragraph (b)(4), and adding paragraphs (e), (f) and (g) to read as follows:

§1.954-3 Foreign base company sales income.

* * * * *

(b) * * * (1) * * * (i) * * *

(c) [The text of the proposed amendments to §1.954-3(b)(1)(i)(c) is the same as the text of §1.954-3T(b)(1)(i)(c) published elsewhere in this issue of the Bulletin].

(ii) * * * (a) [The text of the proposed amendments to §1.954-3(b)(1)(ii)(a) is the same as the text of §1.954-3T(b)(1)(ii)(a)

published elsewhere in this issue of the Bulletin].

* * * * *

(c) [The text of the proposed amendments to §1.954-3(b)(1)(ii)(c) is the same as the text of §1.954-3T(b)(1)(ii)(c) published elsewhere in this issue of the Bulletin].

(2) * * * (i) * * *

(b) [The text of the proposed amendments to §1.954-3(b)(2)(i)(b) is the same as the text of §1.954-3T(b)(2)(i)(b) published elsewhere in this issue of the Bulletin].

* * * * *

(d) [The text of the proposed amendments to §1.954-3(b)(2)(i)(d) is the same as the text of §1.954-3T(b)(2)(i)(d) published elsewhere in this issue of the Bulletin].

* * * * *

(ii) * * *

(a) [The text of the proposed amendments to §1.954-3(b)(2)(ii)(a) is the same as the text of §1.954-3T(b)(2)(ii)(a) published elsewhere in this issue of the Bulletin].

(b) [The text of the proposed amendments to §1.954-3(b)(2)(ii)(b) is the same as the text of §1.954-3T(b)(2)(ii)(b) published elsewhere in this issue of the Bulletin].

* * * * *

(e) [The text of the proposed amendments to §1.954-3(b)(2)(ii)(e) is the same as the text of §1.954-3T(b)(2)(ii)(e) published elsewhere in this issue of the Bulletin].

* * * * *

(4) * * *

Example 3. [The text of the proposed amendments to §1.954-3(b)(4) *Example 3* is the same as the text of §1.954-3T(b)(4) *Example 3* published elsewhere in this issue of the Bulletin].

* * * * *

Example 8. [The text of the proposed amendments to §1.954-3(b)(4) *Example 8* is the same as the text of §1.954-3T *Example 8* published elsewhere in this issue of the Bulletin].

Example 9. [The text of the proposed amendments to §1.954-3(b)(4) *Example 9* is the same as the text of §1.954-3T *Example 9* published elsewhere in this issue of the Bulletin].

(e) [The text of the proposed amendments to §1.954-3(e) is the same as the text of §1.954-3T(e) published elsewhere in this issue of the Bulletin].

(f) [The text of the proposed amendments to §1.954-3(f) is the same as the text of §1.954-3T(f) published elsewhere in this issue of the Bulletin].

(g) [The text of the proposed amendments to §1.954-3(g) is the same as the text of §1.954-3T(g) published elsewhere in this issue of the Bulletin].

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

(Filed by the Office of the Federal Register on December 24, 2008, 8:45 a.m., and published in the issue of the Federal Register for December 29, 2008, 73 F.R. 79421)

Announcement of Disciplinary Sanctions From the Office of Professional Responsibility

Announcement 2009-2

The Office of Professional Responsibility (OPR) announces recent disciplinary sanctions involving attorneys, certified public accountants, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and appraisers. These individuals are subject to the regulations governing practice before the Internal Revenue Service (IRS), which are set out in Title 31, Code of Federal Regulations, Part 10, and which are published in pamphlet form as

Treasury Department Circular No. 230. The regulations prescribe the duties and restrictions relating to such practice and prescribe the disciplinary sanctions for violating the regulations.

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

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

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

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

representations to conditions designed to promote high standards of conduct.

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

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

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

Disciplinary sanctions are described in these terms:

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

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

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

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

plan agent may also offer to resign in order to avoid a disciplinary proceeding.

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

OPR has authority to disclose the grounds for disciplinary sanctions in these situations: (1) an ALJ or the Secretary’s delegate on appeal has issued a decision on or after September 26, 2007, which was the effective date of amendments to the regulations that permit making such decisions publicly available; (2) the individual has settled a disciplinary case by signing OPR’s “consent to sanction” form, which requires consenting individuals to admit to one or more violations of the regulations and to consent to the disclosure of the individual’s own return information related to the admitted violations (for example, failure to file Federal income tax returns); or (3) OPR has issued a decision in an expedited proceeding for suspension.

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

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Alabama				
Florence	Bowlin, Donald W.	CPA	Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license)	Indefinite from December 1, 2008

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Arizona				
Scottsdale	Cifelli, Thomas A.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 3, 2008
Phoenix	Groh, Gregory G.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 1, 2008
Chandler	Huynh, Hoang V.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from November 5, 2008
Payson	Johnson, Richard B.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 5, 2008
Mesa	Matheny, Ronald S.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 1, 2008
Phoenix	Olson, Carl R.	CPA	Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license in Kansas)	Indefinite from December 15, 2008
Dewey	Wirth, Andrew T.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 3, 2008
California				
Ventura	Hartnett, John G.	Attorney	Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license in Massachusetts)	Indefinite from December 11, 2008
Colorado				
Englewood	Simon, Harry L.	Attorney	Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from November 5, 2008

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Illinois				
Northbrook	Kipnis, Mark S.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (conviction under 18 U.S.C. §§ 1341 and 1346, frauds and swindles)	Indefinite from December 4, 2008
Waukegan	Meuth, Patterson C.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 4, 2008
Kansas				
Emporia	Markowitz, Daniel J.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment in Missouri)	Indefinite from December 17, 2008
Overland Park	Olson, Carl R., See Arizona Stewart, Kimberly	CPA	Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license)	Indefinite from December 15, 2008
Kentucky				
Louisville	Brooks, Troy L.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment in Tennessee)	Indefinite from December 9, 2008
Louisiana				
Lafayette	Peddy, Jr., Millard C.	CPA	Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license)	Indefinite from December 17, 2008
Massachusetts				
East Walpole	Brauer, David P. Hartnett, John G., See California	Attorney	Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 11, 2008

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Minnesota				
	Varriano, Richard D., See North Dakota			
Mississippi				
Jackson	McIntyre, James G.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 17, 2008
Oxford	Scruggs, Richard F.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 17, 2008
Missouri				
Kirkwood	Belz, Mark	Attorney	Suspended by decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 12, 2008
	Markowitz, Daniel J., See Kansas			
New York				
New York	Lefrak, Joseph S.	Attorney	Suspended by decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from November 12, 2008
Dix Hills	Napolitano, James P.	CPA	Suspended by ALJ default decision for violation of § 10.51 (failure to exercise due diligence in representations to client)	Indefinite from September 23, 2008
North Carolina				
Raleigh	McLamb, Jr., James O.	CPA	Suspended by default decision in expedited proceeding under § 10.82 (revocation of CPA license)	Indefinite from December 17, 2008
North Dakota				
Fargo	Varriano, Richard D.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney suspension in Minnesota)	Indefinite from December 9, 2008

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Oklahoma				
Bethany	Farrow, Katherine L.	CPA	Suspended by consent for violation of § 10.51 (failure to timely file Federal income tax returns)	Indefinite from November 1, 2008
Oregon				
Sandy	Ryan, Jane D.	CPA	Suspended by default decision in expedited proceeding under § 10.82 (conviction under State of Oregon law 164.055, theft in the first degree)	Indefinite from December 9, 2008
Tennessee				
	Brooks, Troy L., See Kentucky			
Martin	Speight, Harry M.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 15, 2008
Greenville	Welch, Lawrence A.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney disbarment)	Indefinite from December 9, 2008
Virginia				
Ashburn	Askintowicz, John W.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (attorney license annulled in West Virginia)	Indefinite from December 15, 2008
West Virginia				
	Askintowicz, John W., See Virginia			

City & State	Name	Professional Designation	Disciplinary Sanction	Effective Date(s)
Wisconsin				
Ripon	Goluba, David A.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (suspension of attorney license)	Indefinite from December 9, 2008
Racine	Shumate, Thomas M.	Attorney	Suspended by default decision in expedited proceeding under § 10.82 (conviction under 26 U.S.C. § 7212, corruptly impeding the administration of the IRS laws)	Indefinite from December 1, 2008

Definition of Terms

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

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

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

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

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

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

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

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

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

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

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

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

Abbreviations

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

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

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

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

Numerical Finding List¹

Bulletins 2009–1 through 2009–5

Announcements:

2009-1, 2009-1 I.R.B. 242
2009-2, 2009-5 I.R.B. 424

Notices:

2009-1, 2009-2 I.R.B. 250
2009-2, 2009-4 I.R.B. 344
2009-3, 2009-2 I.R.B. 250
2009-4, 2009-2 I.R.B. 251
2009-5, 2009-3 I.R.B. 309
2009-6, 2009-3 I.R.B. 311
2009-7, 2009-3 I.R.B. 312
2009-8, 2009-4 I.R.B. 347
2009-9, 2009-5 I.R.B. 419
2009-10, 2009-5 I.R.B. 419
2009-11, 2009-5 I.R.B. 420

Proposed Regulations:

REG-148568-04, 2009-5 I.R.B. 421
REG-160872-04, 2009-4 I.R.B. 358
REG-158747-06, 2009-4 I.R.B. 362
REG-150670-07, 2009-4 I.R.B. 378
REG-113462-08, 2009-4 I.R.B. 379
REG-150066-08, 2009-5 I.R.B. 423

Revenue Procedures:

2009-1, 2009-1 I.R.B. 1
2009-2, 2009-1 I.R.B. 87
2009-3, 2009-1 I.R.B. 107
2009-4, 2009-1 I.R.B. 118
2009-5, 2009-1 I.R.B. 161
2009-6, 2009-1 I.R.B. 189
2009-7, 2009-1 I.R.B. 226
2009-8, 2009-1 I.R.B. 229
2009-9, 2009-2 I.R.B. 256
2009-10, 2009-2 I.R.B. 267
2009-11, 2009-3 I.R.B. 313
2009-12, 2009-3 I.R.B. 321
2009-13, 2009-3 I.R.B. 323
2009-14, 2009-3 I.R.B. 324
2009-15, 2009-4 I.R.B. 356

Revenue Rulings:

2009-1, 2009-2 I.R.B. 248
2009-2, 2009-2 I.R.B. 245
2009-3, 2009-5 I.R.B. 382
2009-4, 2009-5 I.R.B. 408

Treasury Decisions:

9434, 2009-4 I.R.B. 339
9435, 2009-4 I.R.B. 333
9436, 2009-3 I.R.B. 268

Treasury Decisions— Continued:

9437, 2009-4 I.R.B. 341
9438, 2009-5 I.R.B. 387
9439, 2009-5 I.R.B. 416
9440, 2009-5 I.R.B. 409

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

Finding List of Current Actions on Previously Published Items¹

Bulletins 2009–1 through 2009–5

Notices:

2001-55

Modified by

Notice 2009-1, 2009-2 I.R.B. 250

2002-27

Modified by

Notice 2009-9, 2009-5 I.R.B. 419

2007-54

Obsoleted by

T.D. 9436, 2009-3 I.R.B. 268

2008-11

Obsoleted by

T.D. 9436, 2009-3 I.R.B. 268

2008-12

Obsoleted by

T.D. 9436, 2009-3 I.R.B. 268

Rev. Proc. 2009-11, 2009-3 I.R.B. 313

2008-13

Obsoleted by

T.D. 9436, 2009-3 I.R.B. 268

List of forms modified and superseded by

Rev. Proc. 2009-11, 2009-3 I.R.B. 313

Modified and clarified by

Notice 2009-5, 2009-3 I.R.B. 309

2008-46

Obsoleted by

T.D. 9436, 2009-3 I.R.B. 268

Rev. Proc. 2009-11, 2009-3 I.R.B. 313

Revenue Procedures:

2007-17

Superseded by

Rev. Proc. 2009-14, 2009-3 I.R.B. 324

2007-71

Modified by

Notice 2009-3, 2009-2 I.R.B. 250

2008-1

Superseded by

Rev. Proc. 2009-1, 2009-1 I.R.B. 1

2008-2

Superseded by

Rev. Proc. 2009-2, 2009-1 I.R.B. 87

2008-3

Superseded by

Rev. Proc. 2009-3, 2009-1 I.R.B. 107

2008-4

Superseded by

Rev. Proc. 2009-4, 2009-1 I.R.B. 118

Revenue Procedures— Continued:

2008-5

Superseded by

Rev. Proc. 2009-5, 2009-1 I.R.B. 161

2008-6

Superseded by

Rev. Proc. 2009-6, 2009-1 I.R.B. 189

2008-7

Superseded by

Rev. Proc. 2009-7, 2009-1 I.R.B. 226

2008-8

Superseded by

Rev. Proc. 2009-8, 2009-1 I.R.B. 229

2008-9

Superseded by

Rev. Proc. 2009-9, 2009-2 I.R.B. 256

2008-61

Superseded by

Rev. Proc. 2009-3, 2009-1 I.R.B. 107

2008-68

Amplified and superseded by

Rev. Proc. 2009-15, 2009-4 I.R.B. 356

Revenue Rulings:

65-286

Obsoleted by

T.D. 9435, 2009-4 I.R.B. 333

76-54

Obsoleted by

T.D. 9435, 2009-4 I.R.B. 333

92-19

Supplemented by

Rev. Rul. 2009-3, 2009-5 I.R.B. 382

2008-19

Modified by

Rev. Rul. 2009-3, 2009-5 I.R.B. 382

¹ A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2008–27 through 2008–52 is in Internal Revenue Bulletin 2008–52, dated December 29, 2008.

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