Internal Revenue
bulletin

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HIGHLIGHTS OF THIS ISSUE

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

INCOME TAX

Rev. Rul. 2005–53, page 425.

Assets produced on a routine and repetitive basis. For purposes of the simplified service cost method and simplified production method provided in the regulations under section 263A of the Code, a taxpayer's self-constructed assets are produced on a routine and repetitive basis in the ordinary course of its trade or business if the assets are either mass-produced (numerous identical goods are manufactured using standardized designs and assembly line techniques) or have a high degree of turnover.

Rev. Rul. 2005–56, page 427.

LIFO; price indexes; department stores. The June 2005 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, June 30, 2005.

T.D. 9212, page 429.

Final regulations under section 861 of the Code describe the proper basis for determining the source of compensation for labor or personal services performed partly within and partly without the United States.

REG–149436–04, page 454.

Proposed regulations under section 6012 of the Code prescribe the form that cooperatives must use to file their income tax returns. The regulations affect all cooperatives that are currently required to file an income tax return on either Form 1120, *U.S. Corporation Income Tax Return*, or Form 990–C, *Farmers' Cooperative Association Income Tax Return*. Announcement 84–26 obsoleted.

Rev. Proc. 2005–60, page 449.

The purpose of this procedure is to inform authorized IRS e-file providers of their obligations to the Service and to consolidate existing guidance. The procedure combines the rules governing IRS e-file, including the rules regulating Electronic Return Originators (EROs) that electronically file (1) Form 1040 and 1040A, *U.S. Individual Income Tax Return*, and Form 1040EZ, *Income Tax Return for Single and Joint Filers With No Dependents*, contained in Publication 1345, *Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns*; (2) Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, contained in Rev. Proc. 2001–9; and (3) Form 941, *Employer's Quarterly Federal Tax Return*, contained in Rev. Proc. 99–39. Rev. Procs. 99–39, 2000–31, and 2001–9 superseded.

EMPLOYEE PLANS

Notice 2005–63, page 448.

Weighted average interest rate update; corporate bond indices; 30-year Treasury securities. The weighted average interest rate for August 2005 and the resulting permissible range of interest rates used to calculate current liability and to determine the required contribution are set forth.

EXEMPT ORGANIZATIONS

Announcement 2005–60, page 455.

A list is provided of organizations now classified as private foundations.

(Continued on the next page)

Actions Relating to Court Decisions is on the page following the Introduction.
Finding Lists begin on page ii.
Index for July through August begins on page iv.

Department of the Treasury
Internal Revenue Service

ESTATE TAX

T.D. 9214, page 435.

Final regulations under section 2651 of the Code provide an exception to the general rules for determining the generation assignment of a transferee of property for generation-skipping transfer (GST) purposes. The regulations also provide rules regarding a transferee assigned to more than one generation.

EMPLOYMENT TAX

Rev. Rul. 2005–52, page 423.

Tool allowance payments. This ruling holds that tool allowances paid to employees are not paid under an accountable plan because the substantiation and return of excess requirements are not met. All tool allowance payments under the arrangement must be included in the employees' gross income, reported on the employees' Forms W-2, and are subject to withholding and payment of federal employment taxes.

Notice 2005–59, page 443.

This notice provides information about additional criteria that will be applied in selecting proposals for the Internal Revenue Service's Industry Issue Resolution (IIR) program regarding application of accountable plan rules to specific industries.

EXCISE TAX

Notice 2005–62, page 443.

This notice modifies Notice 2005-4, 2005-2 I.R.B 289, by revising the guidance relating to the Certificate for Biodiesel, which is required as a condition for claiming a credit or payment under sections 6426(c), 6427(e), and 40A of the Code. This notice also provides guidance on issues related to the boidiesel credit or payment that are not addressed in Notice 2005-4. This notice further modifies Notice 2005-4 relating to the Certificate of Person Buying Aviation-Grade Kerosene for Commercial Aviation or Nontaxable Use, which is required to notify a position holder of certain transactions under sections 4081 and 4082. Notice 2005-4 modified.

ADMINISTRATIVE

T.D. 9213, page 440.

Section 6343(d) of the Code was added by the Taxpayer Bill of Rights 2 and authorizes the Service to return levied property in certain cases. Final regulations under section 6343 set forth the cases in which the Service may return levied property and the procedures for a taxpayer to request a return of property.

REG–149436–04, page 454.

Proposed regulations under section 6012 of the Code prescribe the form that cooperatives must use to file their income tax returns. The regulations affect all cooperatives that are currently required to file an income tax return on either Form 1120, *U.S. Corporation Income Tax Return*, or Form 990–C, *Farmers' Cooperative Association Income Tax Return*. Announcement 84–26 obsoleted.

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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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Actions Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce at an early date whether it will follow the holdings in certain cases. An Action on Decision is the document making such an announcement. An Action on Decision will be issued at the discretion of the Service only on unappealed issues decided adverse to the government. Generally, an Action on Decision is issued where its guidance would be helpful to Service personnel working with the same or similar issues. Unlike a Treasury Regulation or a Revenue Ruling, an Action on Decision is not an affirmative statement of Service position. It is not intended to serve as public guidance and may not be cited as precedent.

Actions on Decisions shall be relied upon within the Service only as conclusions applying the law to the facts in the particular case at the time the Action on Decision was issued. Caution should be exercised in extending the recommendation of the Action on Decision to similar cases where the facts are different. Moreover, the recommendation in the Action on Decision may be superseded by new legislation, regulations, rulings, cases, or Actions on Decisions.

Prior to 1991, the Service published acquiescence or nonacquiescence only in certain regular Tax Court opinions. The Service has expanded its acquiescence program to include other civil tax cases where guidance is determined to be helpful. Accordingly, the Service now may acquiesce or nonacquiesce in the holdings of memorandum Tax Court opinions, as well as those of the United States District Courts, Claims Court, and Circuit Courts of Appeal. Regardless of the court deciding the case, the recommendation of any Action on Decision will be published in the Internal Revenue Bulletin.

The recommendation in every Action on Decision will be summarized as acquiescence, acquiescence in result only, or nonacquiescence. Both "acquiescence" and "acquiescence in result only" mean that the Service accepts the holding of the court in a case and that the Service will follow it in disposing of cases with the same controlling facts. However, "acquiescence" indicates neither approval nor disapproval of the reasons assigned by the court for its conclusions; whereas, "acquiescence in result only" indicates disagreement or concern with some or all of those reasons. "Nonacquiescence" signifies that, although no further review was sought, the Service does not agree with the holding of the court and, generally, will not follow the decision in disposing of cases involving other taxpayers. In reference to an opinion of a circuit court of appeals, a "nonacquiescence" indicates that the Service will not follow the holding on a nationwide basis. However, the Service will recognize the precedential impact of the opinion on cases arising within the venue of the deciding circuit.

The Actions on Decisions published in the weekly Internal Revenue Bulletin are consolidated semiannually and appear in the first Bulletin for July and the Cumulative Bulletin for the first half of the year. A semiannual consolidation also appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner does NOT ACQUIESCE in the following Decision:

Sherman-Williams Co. Employee Health Plan Trust v. Commissioner,[1] 330 F.3rd 449 (6th Cir. 2003), rev'g 115 T.C. 440 (2000).

[1] Nonacquiescence relating to whether the Court of Appeals erred in concluding that investment income of a VEBA trust can be set aside and used separately before the end of a taxable year to pay the reasonable costs of administering health care benefits and thereby avoid the limits imposed by section 512(a)(3)(E) on exempt function income.

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

Section 62.—Adjusted Gross Income Defined

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

Tool allowance payments. This ruling holds that tool allowances paid to employees are not paid under an accountable plan because the substantiation and return of excess requirements are not met. All tool allowance payments under the arrangement must be included in the employees' gross income, reported on the employees' Forms W-2, and are subject to withholding and payment of federal employment taxes.

Rev. Rul. 2005–52

ISSUE

In the following situation, is the tool allowance paid by the employer to the employees paid under an accountable plan such that the payments are excluded from the employees' gross income and exempt from the withholding and payment of employment taxes?

FACTS

Employer operates an automobile repair and maintenance business. Employer hires service technicians to work in the business as employees. Employer requires these employees, as a condition of employment, to provide and maintain various tools needed for use in performing repair and maintenance services. Employer pays each employee an hourly wage. In addition, Employer pays each employee a set amount for each hour worked as a "tool allowance" to cover costs the employee incurs for acquiring and maintaining his tools.

Employer sets each employee's tool allowance annually by using a combination of data from a national survey of average tool expenses for automobile service technicians and specific information concerning tool-related expenses provided by the employee in response to an annual questionnaire completed by all service technicians who work for Employer. Employer does not reimburse expenses paid or incurred for listed property, as defined by § 280F(d) of the Internal Revenue Code (the Code), or depreciation expenses; thus, these expenses are not taken into account in calculating the amount of the annual tool allowance. Employer uses the data to project the employee's total annual tool expenses. Employer then uses a projection of the total number of hours the employee is expected to work during the year that will require the use of tools to convert the employee's estimated annual tool expenses into an hourly rate for the tool allowance. Thus, the hourly tool allowance is an estimate of the tool expense projected to be incurred per hour by the employee over the course of the coming year.

At the end of each pay period, each employee reports to Employer his hours worked requiring the use of tools. Employer multiplies the number of hours reported as worked requiring the use of tools by the employee's hourly rate for the tool allowance and pays the resulting amount to the employee in addition to compensation for services performed during the pay period. On a quarterly statement furnished to each employee, Employer reports: (1) the amount paid to the employee as a tool allowance during the quarter, and (2) the tool expenses estimated to be incurred in the quarter (*i.e.*, the hours reported worked requiring the use of tools times the tool allowance). Employees are not required to provide any substantiation of expenses actually incurred for tools either before or after the quarterly reports are issued. Employer does not require employees to return any portion of the tool allowances that exceeds the expenses they actually incur either before or after the quarterly reports are issued.

LAW

Section 61 of the Code provides that gross income means all income from whatever source derived, including compensation for services, fees, commissions, fringe benefits, and similar items.

Section 62(a)(2)(A) of the Code and § 1.62–2(b) of the Income Tax Regulations provide that, for purposes of determining adjusted gross income, an employee may deduct certain business expenses paid by the employee in connection with the performance of services as an employee under a reimbursement or other expense allowance arrangement with his employer.

Section 62(c) provides that, for purposes of § 62(a)(2)(A), an arrangement will not be treated as a reimbursement or other expense allowance arrangement if (1) the arrangement does not require the employee to substantiate the expenses covered by the arrangement to the payor, or (2) the arrangement provides the employee the right to retain any amount in excess of the substantiated expenses covered under the arrangement.

Section 1.62–2(c)(1) of the regulations provides that a reimbursement or other expense allowance arrangement satisfies the requirements of § 62(c) if it meets the requirements of business connection, substantiation, and returning amounts in excess of substantiated expenses. If an arrangement meets these requirements, all amounts paid under the arrangement are treated as paid under an accountable plan. § 1.62–2(c)(2)(i). Amounts treated as paid under an accountable plan are excluded from the employee's gross income, are not required to be reported on the employee's Form W–2, and are exempt from the withholding and payment of income and employment taxes. § 1.62–2(c)(4).

If an arrangement does not satisfy one or more of these requirements, all amounts paid under the arrangement are treated as paid under a "nonaccountable plan." § 1.62–2(c)(3). Amounts treated as paid under a nonaccountable plan are included in the employee's gross income, must be reported as wages or other compensation of the employee's on Form W–2, and are subject to withholding and payment of income and employment taxes. § 1.62–2(c)(5).

Section 1.62–2(d)(1) provides that an arrangement meets the business connection requirements if it provides advances, allowances, or reimbursements only for business expenses that are allowable as deductions and are paid or incurred by the employee in connection with the performance of services as an employee of the

employer. If, however, a payor arranges to pay an amount to an employee regardless of whether the employee incurs (or is reasonably expected to incur) *bona fide* employee business expenses, the arrangement does not satisfy the business connection requirements and all amounts paid under the arrangement are treated as paid under a nonaccountable plan. § 1.62–2(d)(3)(i).

Section 1.62–2(e)(1) provides that an arrangement meets the substantiation requirements if the arrangement requires each business expense to be substantiated to the payor in accordance with paragraph (e)(3), within a reasonable period of time. An arrangement for those expenses meets the substantiation requirements of § 1.62–2(e)(3) if information submitted to the payor is sufficient to enable the payor to identify the specific nature of each expense and to conclude that the expense is attributable to the payor's business activity. Generally the employee must submit an expense account or other written statement to the employer showing the business nature and amount of the employee's expenses. *See* § 1.162–17(b)(4).

Revenue Procedure 2002–41, 2002–1 C.B. 1098, provides an optional expense substantiation rule applicable only to certain employers in the pipeline construction industry. If an eligible employer's arrangement to pay employee business expenses otherwise satisfies the business connection and return of excess requirements, and amounts paid under the arrangement do not exceed $13.00 per hour, adjusted for inflation, an employee is deemed to have substantiated the expenses, and amounts paid under the arrangement are treated as paid under an accountable plan.

Section 1.62–2(f)(1) provides that an arrangement meets the return of excess requirements if the arrangement requires the employee to return to the payor within a reasonable period of time any amount paid under the arrangement in excess of substantiated expenses. Section 1.62–2(f)(2) provides authority for the Commissioner to issue rules, for *per diem* or mileage allowances only, under which an arrangement will be treated as satisfying the return of excess requirement even though the arrangement does not require the employee to return the portion of the allowance related to days or miles of travel substantiated but that exceeds the amount of the employee's expenses deemed substantiated pursuant to rules prescribed under § 274(d).

Section 1.62–2(g)(2)(ii) provides that if a payor provides employees with a periodic statement, no less frequently than quarterly, stating the amount, if any, paid under the arrangement that exceeds the expenses the employee has substantiated as required by the arrangement, and requesting the employee to substantiate any additional business expenses that have not yet been substantiated (whether or not such expenses relate to the expenses to which the original advance was paid) and/or to return any amounts remaining unsubstantiated within 120 days of the statement, an expense substantiated or an amount returned within that period will be treated as being substantiated or returned within a reasonable period of time.

Additionally, § 1.62–2(k) provides that if a payor's reimbursement or other expense allowance arrangement evidences a pattern of abuse of the rules of § 62(c) and the regulations thereunder, all payments made under the arrangement will be treated as made under a nonaccountable plan.

ANALYSIS

An amount paid by an employer to an employee to cover expenses incurred by the employee in the course of employment can be excluded from the employee's income and wages only if a particular Code section provides an exclusion for such amount or if the amount is paid under an accountable plan. No specific section of the Code excludes from wages amounts paid to employees for acquiring and maintaining tools used in the performance of services as employees. Thus, to be excluded from wages, amounts paid to employees to cover expenses incurred to acquire or maintain such tools must be paid under a reimbursement or other expense allowance arrangement that meets the requirements of § 62(c).

An arrangement qualifies as an accountable plan only if it satisfies all three requirements set forth in the statute and regulations. An arrangement that fails to meet one or more of the three requirements will be treated as a nonaccountable plan.

The arrangement described in this revenue ruling fails to meet both the substantiation and the return of excess requirements and thus does not qualify as an accountable plan.

Although reasonable expectations for expenses can be used to establish that a plan meets the business connection requirement, satisfaction of the substantiation and return of excess requirements must be based on expenses actually incurred. The arrangement in the facts of this ruling does not require employees to substantiate the actual expenses they are incurring; rather the employees report their time worked requiring the use of tools, and Employer converts the hours into an amount treated as expenses incurred based on statistical data. Reporting hours worked requiring the use of tools is not the equivalent of substantiating actual expenses incurred. Employers may not substitute a reasonable estimate of expenses to be incurred based on statistical data and hours worked for the substantiation of actual expenses that is required by § 1.62–2(e)(3) absent explicit guidance permitting the use of such deemed substantiation. *See*, *e.g.*, Rev. Proc. 2002–41.

Employer does not cure the absence of substantiation or return of excess by providing employees with the quarterly statement described in this revenue ruling. Employer does not require employees to provide substantiation of expenses actually incurred nor does Employer require employees to return any excess received within a reasonable period of time after receiving the quarterly statement. Thus, Employer is not providing a periodic statement within the meaning of § 1.62–2(g)(2)(ii).

Each of the accountable plan requirements must be independently satisfied. Thus, even if Employer required the employees to substantiate the actual amount of the expenses, and Employer treated any portion of the tool allowances they receive that exceeded substantiated expenses as additional wages, the arrangement would still not be an accountable plan. With the exception of circumstances where employee expenses are covered through a mileage or *per diem* allowance pursuant to § 1.62–2(f)(2), an arrangement is not an accountable plan if it includes amounts paid in excess of substantiated expenses in wages rather than requiring that they be returned. *See* § 1.62–2(f)(1); Rev. Proc. 2004–64, 2004–49 I.R.B. 898, (mileage allowances), or Rev. Proc. 2005–10,

2005–3 I.R.B. 341, (*per diem* allowances), or any successors.

HOLDING

The arrangement described in this revenue ruling is not an accountable plan. Therefore, the arrangement is a nonaccountable plan and all tool allowances paid under the arrangement must be included in the employees' gross income, reported as wages on the employees' Forms W–2, and are subject to withholding and payment of federal employment taxes.

DRAFTING INFORMATION

The principal author of this revenue ruling is Joe Spires of the Office of Associate Chief Counsel (Tax Exempt & Government Entities). For further information regarding this revenue ruling, contact Jeanne Royal Singley at (202) 622–0047 (not a toll-free call).

Section 263A.—Capitalization and Inclusion in Inventory Costs of Certain Expenses

26 CFR 1.263A–2: Rules relating to property produced by the taxpayer.

When are self-constructed assets produced on a routine and repetitive basis in the ordinary course of a taxpayer's trade or business for purposes of the simplified production method provided by section 1.263A–2(b)(2)(i)(D)? See Rev. Rul. 2005-53, page 425.

26 CFR 1.263A–1: Uniform capitalization of costs. (Also: § 1.263A–2.)

Assets produced on a routine and repetitive basis. For purposes of the simplified service cost method and simplified production method provided in the regulations under section 263A of the Code, a taxpayer's self-constructed assets are produced on a routine and repetitive basis in the ordinary course of its trade or business if the assets are either mass-produced (numerous identical goods are manufactured using standardized designs and assembly line techniques) or have a high degree of turnover.

Rev. Rul. 2005–53

BACKGROUND

In Notice 2003–36, 2003–1 C.B. 992, modified by Notice 2003–59, 2003–2 C.B. 429, the Treasury Department and the Internal Revenue Service indicate that they are aware that uncertainty exists as to what types of property constitute "eligible property" under §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D) of the Income Tax Regulations for which qualifying taxpayers may use the simplified service cost and simplified production methods. In particular, there is uncertainty about the proper interpretation and application of the term "routine and repetitive." The notice indicates that the Treasury Department and the Service plan to publish guidance that will clarify the types of property that qualify as eligible property under those sections and address the interpretation and application of the term "routine and repetitive." This revenue ruling clarifies the types of property that qualify as eligible property for purposes of §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D) and how the term "routine and repetitive" is interpreted for this purpose.

ISSUE

Under what circumstances are a taxpayer's self-constructed assets produced on a routine and repetitive basis in the ordinary course of its trade or business for purposes of the simplified service cost method and the simplified production method (the "simplified methods") under §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D) of the Income Tax Regulations?

FACTS

Situation 1. *U*, a manufacturer of office equipment, produces numerous identical copiers during the year using assembly line techniques. *U* leases the copiers and does not hold them for sale.

Situation 2. *V*, a manufacturer of automobiles, regularly produces molds that are specifically designed for the production of particular automobile parts. The molds cannot be adapted for a further or different use after changes or improvements are made to the particular part that is produced by the mold. The molds generally are used for one to three years. Accordingly, the molds have a high degree of turnover.

Situation 3. *W*, a telephone company, manufactures numerous identical poles using standardized designs and assembly line techniques for use in its business.

Situation 4. *X*, an electric utility, regularly purchases identical meters and installs them on its customers' properties. The meters measure the amount of electric current used by *X*'s customers. *X* does not manufacture meters. Meters are included in asset class 49.14 under Rev. Proc. 87–56, 1987–2 C.B. 674, as clarified and modified by Rev. Proc. 88–22, 1988–1 C.B. 785, and have a class life of 30 years.

Situation 5. *Y*, an electric utility, constructs from various components substations that it uses in transmitting and distributing electricity. Substations and their components are facilities built on land that house an assembly of equipment designed for switching, changing, or regulating the voltage of electricity. Each substation is intended to operate for an extended length of time, is specifically custom designed for a specific geographic site, and serves a particular function within *Y*'s electrical grid.

Situation 6. *Z*, a company that owns and operates a national chain of restaurants, continually constructs new restaurants each year. *Z* generally uses a standardized design when constructing new restaurants. However, local zoning laws and the physical characteristics of the specific construction site require *Z* to modify the design for each new restaurant.

LAW AND ANALYSIS

Section 263A of the Internal Revenue Code provides that producers of real or tangible personal property must capitalize the direct costs and a proper share of the indirect costs of such property.

Section 1.263A–1(e)(3) provides that indirect costs include service costs. For this purpose, § 1.263A–1(e)(4) states that service costs are a type of indirect costs that can be identified specifically with an administrative or support department or function. Service costs include capitalizable service costs, deductible service costs, and mixed service costs. Under § 1.263A–1(e)(4)(ii)(C), mixed service costs include service costs that are partially allocable to production activities

and partially allocable to non-production activities.

Section 1.263A–1(g)(3) provides that indirect costs are generally allocated to intermediate cost objectives such as departments or activities prior to the allocation of such costs to property produced. This section further provides that taxpayers are required to allocate indirect costs using either a specific identification method, a standard cost method, a burden rate method, or any other reasonable allocation method (as defined under the principles of § 1.263A–1(f)(4)).

Section 1.263A–2(b) allows producers to use the simplified production method to determine the additional § 263A costs properly allocable to ending inventories of property produced and other "eligible" property on hand at the end of the taxable year. Section 1.263A–2(b)(3)(i)(A) generally provides that the amount of additional § 263A costs that is allocable to eligible property remaining on hand at the close of the taxable year under the simplified production method is computed by multiplying the § 471 costs on hand at the end of the year by an absorption ratio. Section 1.263A–2(b)(3)(ii)(A) provides that the absorption ratio generally is equal to the additional § 263A costs incurred during the year divided by the § 471 costs incurred during the year.

Additional § 263A costs are the costs, other than interest, that were not capitalized under the taxpayer's method of accounting immediately prior to the effective date of § 263A, but that are required to be capitalized under § 263A. See § 1.263A–1(d)(3). Section 471 costs generally are the costs, other than interest, that the taxpayer capitalized under its method of accounting immediately prior to the effective date of § 263A. See § 1.263A–1(d)(2).

Section 1.263A–2(b)(2)(i) provides that a taxpayer electing to use the simplified production method generally must use the method for all production activities associated with the following categories of eligible property:

1. *Inventory property*. Stock in trade or other property properly includible in the inventory of the taxpayer. See § 1.263A–2(b)(2)(i)(A).

2. *Non-inventory property held for sale*. Non-inventory property held by a taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business. See § 1.263A–2(b)(2)(i)(B).

3. *Certain self-constructed assets*. Self-constructed assets substantially identical in nature to, and produced in the same manner as, inventory property produced by the taxpayer or other property produced by the taxpayer and held primarily for sale to customers in the ordinary course of the taxpayer's trade or business. See § 1.263A–2(b)(2)(i)(C).

4. *Self-constructed assets produced on a repetitive basis*. Self-constructed assets produced by the taxpayer on a routine and repetitive basis in the ordinary course of the taxpayer's trade or business. See § 1.263A–2(b)(2)(i)(D).

Section 1.263A–1(g)(4) generally requires taxpayers to allocate mixed service costs to property produced using reasonable factors or relationships under a direct reallocation method (as defined in § 1.263A–1(g)(4)(iii)(A)), a step-allocation method (as defined in § 1.263A–1(g)(4)(iii)(B)), or any other reasonable allocation method (as defined under the principles of § 1.263A–1(f)(4)).

Section 1.263A–1(h) permits taxpayers to use the simplified service cost method to determine the aggregate portion of mixed service costs incurred during the taxable year that are properly allocable to "eligible property." The categories of eligible property provided by the simplified service cost method are identical to the four categories of eligible property provided by the simplified production method. Compare § 1.263A–1(h)(2)(i) with § 1.263A–2(b)(2)(i).

Section 1.263A–1(h)(3)(i) provides that under the simplified service cost method, a taxpayer computes its capitalizable mixed service costs by multiplying its total mixed service costs by an allocation ratio. The allocation ratio can be either the labor-based or production-based ratio. See §§ 1.263A–1(h)(4) and (5).

The four categories of eligible property in §§ 1.263A–1(h)(2)(i) and 1.263A–2(b)(2)(i) all share common characteristics that make application of the simplified methods appropriate. Prior to the issuance of the final § 263A regulations, the temporary § 263A regulations, issued under T.D. 8131, 1987–1 C.B. 98, and published in the Federal Register on March 30, 1987, limited the availability of the simplified methods to two categories of property: inventory and non-inventory property held by a taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business. The preamble to the temporary § 263A regulations indicates that this limitation was prescribed because the simplified methods are not appropriate to account for the casual or occasional production of property. Instead, the simplified methods were "designed to alleviate the administrative burdens of complying with the new capitalization rules in situations where mass production of assets occurs on a repetitive and routine basis, with a typically high 'turnover' rate for the produced assets." See T.D. 8131, 1987–1 C.B. 98, 102. The final regulations retain these two categories of eligible property in §§ 1.263A–1(h)(2)(i)(A) and (B) and 1.263A–2(b)(2)(i)(A) and (B). See T.D. 8482, 1993–2 C.B. 77, published in the Federal Register on August 9, 1993.

Commentators to the temporary regulations suggested that the categories of property eligible for the simplified methods be expanded to other types of property that share the characteristics that are appropriate for application of the methods. In response, Notice 88–86, 1988–2 C.B. 401, published on August 5, 1988, expanded the availability of the simplified methods to:

1. property constructed by a taxpayer for use in its trade or business if the taxpayer is also producing, in the ordinary course of its business, inventory property (or any other property with respect to which the use of the simplified production method is permitted under the present regulations), and the property constructed by the taxpayer for use in its trade or business is substantially identical in nature to, and is produced in the same manner as, the inventory property (or such other property) produced by the taxpayer, and

2. property constructed by a taxpayer for use in its trade or business if, in the ordinary course of its production activities, the taxpayer produces such property on a routine and repetitive basis (*i.e.*, the taxpayer produces numerous items of such property within a taxable year.)

The final regulations follow Notice 88–86 and expand the categories of produced property eligible for the simplified methods by adding §§ 1.263A–1(h)(2)(i)(C) and (D) and 1.263A–2(b)(2)(i)(C) and (D).

The simplified methods are predicated on the assumption that it is appropriate to allocate production costs on a ratable basis when assets are either mass-produced (*i.e.*, numerous identical goods are manufactured using standardized designs and assembly line techniques) or have a high degree of turnover. In contrast, it is not appropriate to allocate production costs on a ratable basis when assets are neither mass-produced nor have a high degree of turnover.

The first three categories of eligible property provided in §§ 1.263A–1(h)(2)(i)(A)–(C) and 1.263A–2(b)(2)(i)(A)–(C) are either mass-produced and/or have a high degree of turnover or are identical to assets that are mass-produced and/or have a high degree of turnover. The fourth category of eligible property, self-constructed assets produced on a routine and repetitive basis, is similar to these first three categories. It was intended that the fourth category of eligible property provided by the simplified methods, §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D), possess the same characteristics shared by all of the preceding categories of eligible property. Therefore, to be eligible under the fourth category, the property also must be either mass-produced (numerous identical goods are manufactured using standardized designs and assembly line techniques) or have a high degree of turnover (in this case have a relatively short useful life). Mass production does not include all the terms provided by § 263A(g) and § 1.263A–2(a)(1) (for example, install, develop, and improve). Instead property is mass-produced only if it is *manufactured* numerous times during the year using standardized designs and assembly line techniques.

For example, the fourth category of eligible property provided by the simplified methods, §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D), includes property mass-produced by a vertically integrated business for use in its own business that would have been properly included in inventory of a third party if mass-produced for sale by the third party. Thus, if a telephone company mass-produces its own poles for use in its business, the poles would be eligible property for purposes of §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D).

In *Situation 1*, *U* is producing copiers on a routine and repetitive basis for purposes of the simplified methods because the copiers are mass-produced.

In *Situation 2*, *V* is producing molds on a routine and repetitive basis for purposes of the simplified methods because the molds have a high degree of turnover.

In *Situation 3*, *W* is producing poles on a routine and repetitive basis for purposes of the simplified methods because the poles are mass-produced.

In *Situation 4*, *X* is not producing meters on a routine and repetitive basis for purposes of the simplified methods because the meters are neither mass-produced by *X* nor have a high degree of turnover. Mass production does not include installation of meters and meters do not have a short useful life.

In *Situation 5*, *Y* is not producing substations on a routine and repetitive basis for purposes of the simplified methods because the substations are neither mass-produced nor have a high degree of turnover.

In *Situation 6*, *Z* is not producing restaurants on a routine and repetitive basis for purposes of the simplified methods because the restaurants are neither mass-produced nor have a high degree of turnover.

HOLDING

For purposes of the simplified methods under §§ 1.263A–1(h)(2)(i)(D) and 1.263A–2(b)(2)(i)(D), a taxpayer's self-constructed assets are produced on a routine and repetitive basis in the ordinary course of its trade or business if the assets are either mass-produced (numerous identical goods are manufactured using standardized designs and assembly line techniques) or have a high degree of turnover.

DRAFTING INFORMATION

The principal author of this revenue ruling is Scott H. Rabinowitz of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue ruling, contact Mr. Rabinowitz at (202) 622–4970 (not a toll-free call).

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

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

LIFO; price indexes; department stores. The June 2005 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, June 30, 2005.

Rev. Rul. 2005–56

The following Department Store Inventory Price Indexes for June 2005 were issued by the Bureau of Labor Statistics. The indexes are accepted by the Internal Revenue Service, under § 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 86–46, 1986–2 C.B. 739, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, June 30, 2005.

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

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

	Groups	June 2004	June 2005	Percent Change from June 2004 to June 2005[1]
1.	Piece Goods	490.9	504.8	2.8
2.	Domestics and Draperies	538.7	519.1	-3.6
3.	Women's and Children's Shoes	631.8	650.4	2.9
4.	Men's Shoes	854.5	878.2	2.8
5.	Infants' Wear	567.3	559.9	-1.3
6.	Women's Underwear	508.4	541.4	6.5
7.	Women's Hosiery	329.9	340.0	3.1
8.	Women's and Girls' Accessories	581.5	588.9	1.3
9.	Women's Outerwear and Girls' Wear	361.9	347.5	-4.0
10.	Men's Clothing	540.3	536.9	-0.6
11.	Men's Furnishings	578.3	562.8	-2.7
12.	Boys' Clothing and Furnishings	431.3	413.6	-4.1
13.	Jewelry	897.4	872.3	-2.8
14.	Notions	791.9	810.4	2.3
15.	Toilet Articles and Drugs	998.9	997.0	-0.2
16.	Furniture and Bedding	624.2	598.7	-4.1
17.	Floor Coverings	592.9	604.6	2.0
18.	Housewares	712.6	711.9	-0.1
19.	Major Appliances	200.4	204.3	1.9
20.	Radio and Television	41.9	39.0	-6.9
21.	Recreation and Education[2]	80.7	78.5	-2.7
22.	Home Improvements[2]	129.3	137.8	6.6
23.	Automotive Accessories[2]	112.4	114.6	2.0
	Groups 1–15: Soft Goods	559.3	552.0	-1.3
	Groups 16–20: Durable Goods	384.1	379.8	-1.1
	Groups 21–23: Misc. Goods[2]	93.4	93.4	0.0
	Store Total[3]	496.5	490.8	-1.1

[1]Absence of a minus sign before the percentage change in this column signifies a price increase.

[2]Indexes on a January 1986 = 100 base.

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

DRAFTING INFORMATION

The principal author of this revenue ruling is Michael Burkom of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue ruling, contact Mr. Burkom at (202) 622–7924 (not a toll-free call).

Section 861.—Income From Sources Within the United States

26 CFR 1.861–4: Compensation for labor or personal services.

T.D. 9212

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

Source of Compensation for Labor or Personal Services

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that describe the proper basis for determining the source of compensation for labor or personal services performed partly within and partly without the United States. These final regulations will affect individuals who earn compensation for labor or personal services performed partly within and partly without the United States and are needed to provide appropriate guidance regarding the determination of the proper source of that compensation.

DATES: *Effective Date*: These regulations are effective on July 14, 2005.

Applicability Date: For dates of applicability, see §1.861–4(d).

FOR FURTHER INFORMATION CONTACT: David Bergkuist, (202) 622–3850 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in these final regulations have been reviewed and approved by the **Office of Management and Budget** in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–1900.

The collections of information in these final regulations are in §1.861–4(b)(2)(ii)(C)(*1*)(*i*), (b)(2)(ii)(D), and (b)(2)(ii)(D)(*6*). The information required in §1.861–4(b)(2)(ii)(C)(*1*)(*i*) will enable an individual, where appropriate, to use an alternative basis other than that described in §1.861–4(b)(2)(ii)(A) or (B) to determine the source of his or her compensation as an employee for labor or personal services performed partly within and partly without the United States. The information required in §1.861–4(b)(2)(ii)(D) and (D)(*6*) will enable an employee to source certain fringe benefits on a geographical basis. The collections of information will, likewise, allow the IRS to verify these determinations.

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

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

Background

This document contains amendments to 26 CFR part 1. On August 6, 2004, proposed revisions to the regulations (REG–208254–90; REG–136481–04, 2004–37 I.R.B. 480) under section 861 of the Internal Revenue Code (Code) relating to the source of compensation for labor or personal services were published in the **Federal Register** (69 FR 47816). In the same document, a prior notice of proposed rulemaking (REG–208254–90, 2000–1 C.B. 577), published in the **Federal Register** on January 21, 2000 (65 FR 3401), was withdrawn. A public hearing was held on January 13, 2005. Two written comments were received. After consideration of these comments, the August 6, 2004, proposed regulations are adopted as amended by this Treasury decision.

Summary of Comments and Explanation of Revisions

These final regulations, as proposed in the notice of proposed rulemaking, retain the facts and circumstances basis as the general rule for determining the source of compensation for labor or personal services performed partly within and partly without the United States received by persons other than individuals and by individuals who are not employees. As proposed, the final regulations provide two general bases for determining the proper source of compensation that an individual receives as an employee for such labor or personal services. Under the first general basis of §1.861–4(b)(2)(ii)(A), an individual will source compensation, other than compensation in the form of certain fringe benefits, on a time basis, as defined in §1.861–4(b)(2)(ii)(E).

Under the second general basis of §1.861–4(b)(2)(ii)(B) and (D), an individual will source compensation in the form of fringe benefits, as described in §1.861–4(b)(2)(ii)(D)(*1*) through (*6*), on a geographical basis (*e.g.*, at the employee's principal place of work, as defined in section 217 and §1.217–2(c)(3)). The fringe benefits to which this general basis applies are housing, education, local transportation, tax reimbursement, hazardous or hardship duty pay, and moving expense reimbursement fringe benefits. This general basis will apply only if the amount of the fringe benefit is reasonable and is substantiated by adequate contemporaneous records or sufficient evidence under rules similar to those set forth in §1.274–5T(c) or (h) or §1.132–5.

Comments were received that proposed several changes with regard to the fringe benefits described in §1.861–4(b)(2)(ii)(D)(*1*) through (*6*). Under one suggestion, the specific definitions of the identified fringe benefits would be replaced with broad categories. The comment further suggested that the housing fringe benefit, education fringe benefit, and local transportation fringe benefit include employer-provided allowances that are based on estimated, rather than actual, expenses. The comment also requested that the definition of education fringe benefit be expanded to include payments for the education of the employee's spouse for studies that relate to the foreign location of the employment, such as language courses and job training at the foreign location, and to include pre-school and post-secondary education, home schooling costs, and language courses of the employee's dependents. With respect to the transportation fringe benefit, the comment requested

that automobile purchase assistance in the host country be included. The comment also requested that the amount of compensation qualifying for the hazardous or hardship duty pay fringe benefit not be limited to government-provided amounts. The comment suggested that the definition of moving expense reimbursement fringe benefit be expanded to include a list of specific expenses, such as moving allowances, home sale/purchase assistance, temporary living, car loss reimbursement, utility setup, appliance installation, auto registration, driver's license fees, power converters, and other related expenses. The comment also suggested three additional fringe benefits: home leave allowances, cost-of-living allowances, and exchange rate differential allowances.

The Treasury Department and the IRS considered the various comments regarding the approach, scope, and detail of the identified fringe benefits under the proposed regulations. In response to the comments, the final regulations modify the definition of education fringe benefit to include education expenses of the type described in section 530(b)(4)(A)(i) regardless of whether the education expenses are incurred in connection with enrollment or attendance at a school. The final regulations do not incorporate the suggestion for allowances based on estimated expenses because the Treasury Department and the IRS continue to believe that substantiation of relevant items is the more appropriate approach. Regarding the other proposed changes to the identified fringe benefits, the Treasury Department and the IRS believe that the regulations provide an appropriate scope of benefits, a reasonable manner of determining the appropriate amount of fringe benefit to be sourced geographically, and a reasonable limit to the amount of an individual's compensation that may be sourced under the exception to the general time basis rule of §1.861–4(b)(2)(ii)(E). As noted in the preamble to the proposed regulations, the Treasury Department and the IRS intend to keep the list and descriptions of identified fringe benefits current and continue to invite comments on whether the identified fringe benefits are appropriately defined and whether other fringe benefits should be identified and sourced on a specific geographic basis.

Furthermore, the final regulations retain the proposed provision that permits an employee to use an alternative basis, based upon the facts and circumstances, to source such compensation if he or she establishes to the satisfaction of the Commissioner that such an alternative basis more properly determines the source of the compensation. An individual seeking to use an alternative basis need not obtain the satisfaction of the Commissioner prior to filing his or her return. To obtain the satisfaction of the Commissioner, an individual who uses an alternative basis must retain in his or her records documentation setting forth why the alternative basis more properly determines the source of the compensation than the basis for determining source of compensation described in §1.861–4(b)(2)(ii)(A) or (B). One comment requested that substantiation by the individual's employer be accepted as substantiation by the employee, particularly where the alternative method is used by a group of employees. Whether an alternative basis more properly determines the source of an individual's compensation is based on the facts and circumstances of the individual's specific case. As a result, it is the individual employee, rather than the employer, who must demonstrate that the alternative basis more properly determines the source of the compensation than the basis for determining source of compensation described in §1.861–4(b)(2)(ii)(A) or (B). It is expected, however, that the individual employee would use, among other documentation, documentation provided by the employer for such substantiation.

Another comment requested relief from any penalties that might arise from inaccurate reporting or withholding if an alternative method is determined not to be acceptable or if the Commissioner determines that a method other than the two general methods determines the source of compensation in a more reasonable manner. The Treasury Department and the IRS believe that the existing standards of penalty administration, including applicable justifications, adequately address this matter.

Section 1.861–4(b)(2)(ii)(C)(*1*)(*i*) of the proposed regulations provided that to assert an alternative basis the individual must comply with the requirements set forth in any administrative pronouncement issued by the Commissioner. The final regulations require that to assert an alternative basis, the individual must provide the information related to the alternative basis required by applicable Federal tax forms and accompanying instructions. It is expected that the applicable Federal tax forms and accompanying instructions will require individuals with $250,000 or more in compensation for the tax year that use an alternative basis to respond to questions on the tax form and to attach to their income tax returns a written statement that sets forth: (1) the specific compensation income, or the specific fringe benefit, for which an alternative method is used; (2) for each such item, the alternative method of allocation of source used; (3) for each such item, a computation showing how the alternative allocation was computed; and (4) a comparison of the dollar amount of the compensation sourced within and without the United States under both the individual's alternative basis and the basis for determining source of compensation described in §1.861–4(b)(2)(ii)(A) or (B).

The proposed regulations at §1.861–4(b)(2)(ii)(C)(*3*) were reserved with respect to artists and athletes who are employees. Although requested, no comments were received on the definition of artists and athletes. The reservation is retained in these final regulations. As noted in the preamble to the proposed regulation, it is intended that the specific rules for artists and athletes who are employees, when issued, will require such individuals to determine the proper source of compensation for labor or personal services on the basis that most correctly reflects the proper source of that income under the facts and circumstances of the particular case, consistent with current law.

Proposed §1.861–4(b)(2)(ii)(F) provided that the source of multi-year compensation of an employee is generally determined on a time basis over the applicable period to which the compensation is attributable. Determination of the applicable period to which the compensation is attributable (including whether the compensation relates to more than one taxable year) is based upon the facts and circumstances of the particular case. Comments requested additional guidance in the area of equity based compensation, particularly with respect to stock options, that relate to services performed over a period of more than one year. These comments

requested guidance related to pre-grant sourcing, sourcing based upon exercise date, and non-conventional equity compensation awards. Because under the regulations the applicable period is determined based on the facts and circumstances of the particular case, and a taxpayer may assert an alternative method to source such compensation income pursuant to §1.861–4(b)(2)(ii)(C)(*1*)(*i*), the Treasury Department and the IRS concluded that §1.861–4(b)(2)(ii)(F), as proposed, was reasonable in its scope and the rules were not modified 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 is hereby certified that the collections of information contained in these regulations will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required. This certification is based upon that fact that the Treasury Department and the IRS believe that a time basis generally is the most appropriate method for determining the source of an individual employee's compensation for labor or personal services performed partly within and partly without the United States. The information necessary to apply the time basis should be readily available to employers and employees. For example, Form 2555, *"Foreign Earned Income"*, requires an individual who claims the foreign earned income exclusion to provide the IRS with information relating to the number of business days spent within the United States and any fringe benefits received. In addition, if an employee wishes to use an alternative method to source compensation, it is the employee that must document such alternative method. Pursuant to section 7805(f) of the 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 its impact on small business.

Drafting Information

The principal author of these final regulations is David Bergkuist 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 parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.861–4 is amended as follows:

1. The heading for paragraph (a) is revised.

2. A sentence is added at the beginning of paragraph (a)(1) introductory text.

3. Paragraph (b) is revised.

4. A sentence is added at the end of paragraph (d).

The revisions and addition read as follows:

§1.861–4 Compensation for labor or personal services.

(a) *Compensation for labor or personal services performed wholly within the United States*. (1) Generally, compensation for labor or personal services, including fees, commissions, fringe benefits, and similar items, performed wholly within the United States is gross income from sources within the United States. * * *

* * * * *

(b) *Compensation for labor or personal services performed partly within and partly without the United States*—(1) *Compensation for labor or personal services performed by persons other than individuals*—(i) *In general*. In the case of compensation for labor or personal services performed partly within and partly without the United States by a person other than an individual, the part of that compensation that is attributable to the labor or personal services performed within the United States, and that is therefore included in gross income as income from sources within the United States, is determined on the basis that most correctly reflects the proper source of the income under the facts and circumstances of the particular case. In many cases, the facts and circumstances will be such that an apportionment on the time basis, as defined in paragraph (b)(2)(ii)(E) of this section, will be acceptable.

(ii) *Example*. The application of paragraph (b)(1)(i) is illustrated by the following example.

Example. Corp X, a domestic corporation, receives compensation of $150,000 under a contract for services to be performed concurrently in the United States and in several foreign countries by numerous Corp X employees. Each Corp X employee performing services under this contract performs his or her services exclusively in one jurisdiction. Although the number of employees (and hours spent by employees) performing services under the contract within the United States equals the number of employees (and hours spent by employees) performing services under the contract without the United States, the compensation paid to employees performing services under the contract within the United States is higher because of the more sophisticated nature of the services performed by the employees within the United States. Accordingly, the payroll cost for employees performing services under the contract within the United States is $20,000 out of a total contract payroll cost of $30,000. Under these facts and circumstances, a determination based upon relative payroll costs would be the basis that most correctly reflects the proper source of the income received under the contract. Thus, of the $150,000 of compensation included in Corp X's gross income, $100,000 ($150,000 x $20,000/$30,000) is attributable to the labor or personal services performed within the United States and $50,000 ($150,000 x $10,000/$30,000) is attributable to the labor or personal services performed without the United States.

(2) *Compensation for labor or personal services performed by an individual*—(i) *In general*. Except as provided in paragraph (b)(2)(ii) of this section, in the case of compensation for labor or personal services performed partly within and partly without the United States by an individual, the part of such compensation that is attributable to the labor or personal services performed within the United States, and that is therefore included in gross income as income from sources within the United States, is determined on the basis that most correctly reflects the proper source of that income under the facts and circumstances of the particular case. In many cases, the facts and circumstances will be such that an apportionment on a time basis, as defined in paragraph (b)(2)(ii)(E) of this section, will be acceptable.

(ii) *Employee compensation*—(A) *In general*. Except as provided in paragraph (b)(2)(ii)(B) or (C) of this section, in the

case of compensation for labor or personal services performed partly within and partly without the United States by an individual as an employee, the part of such compensation that is attributable to the labor or personal services performed within the United States, and that is therefore included in gross income as income from sources within the United States, is determined on a time basis, as defined in paragraph (b)(2)(ii)(E) of this section.

(B) *Certain fringe benefits sourced on a geographical basis*. Except as provided in paragraph (b)(2)(ii)(C) of this section, items of compensation of an individual as an employee for labor or personal services performed partly within and partly without the United States that are described in paragraphs (b)(2)(ii)(D)(*1*) through (*6*) of this section are sourced on a geographical basis in accordance with those paragraphs.

(C) *Exceptions and special rules*—(*1*) *Alternative basis*—(*i*) *Individual as an employee generally*. An individual may determine the source of his or her compensation as an employee for labor or personal services performed partly within and partly without the United States under an alternative basis if the individual establishes to the satisfaction of the Commissioner that, under the facts and circumstances of the particular case, the alternative basis more properly determines the source of the compensation than a basis described in paragraph (b)(2)(ii)(A) or (B), whichever is applicable, of this section. An individual that uses an alternative basis must retain in his or her records documentation setting forth why the alternative basis more properly determines the source of the compensation. In addition, the individual must provide the information related to the alternative basis required by applicable Federal tax forms and accompanying instructions.

(*ii*) *Determination by Commissioner*. The Commissioner may, under the facts and circumstances of the particular case, determine the source of compensation that is received by an individual as an employee for labor or personal services performed partly within and partly without the United States under an alternative basis other than a basis described in paragraph (b)(2)(ii)(A) or (B) of this section if such compensation either is not for a specific time period or constitutes in substance a fringe benefit described in paragraph (b)(2)(ii)(D) of this section notwithstanding a failure to meet any requirement of paragraph (b)(2)(ii)(D) of this section. The Commissioner may make this determination only if such alternative basis determines the source of compensation in a more reasonable manner than the basis used by the individual pursuant to paragraph (b)(2)(ii)(A) or (B) of this section.

(*2*) *Ruling or other administrative pronouncement with respect to groups of taxpayers*. The Commissioner may, by ruling or other administrative pronouncement applying to similarly situated taxpayers generally, permit individuals to determine the source of their compensation as an employee for labor or personal services performed partly within and partly without the United States under an alternative basis. Any such individual shall be treated as having met the requirement to establish such alternative basis to the satisfaction of the Commissioner under the facts and circumstances of the particular case, provided that the individual meets the other requirements of paragraph (b)(2)(ii)(C)(*1*)(*i*) of this section. The Commissioner also may, by ruling or other administrative pronouncement, indicate the circumstances in which he will require individuals to determine the source of certain compensation as an employee for labor or personal services performed partly within and partly without the United States under an alternative basis pursuant to the authority under paragraph (b)(2)(ii)(C)(*1*)(*ii*) of this section.

(*3*) *Artists and athletes*. [Reserved.]

(D) *Fringe benefits sourced on a geographical basis*. Except as provided in paragraph (b)(2)(ii)(C) of this section, compensation of an individual as an employee for labor or personal services performed partly within and partly without the United States in the form of the following fringe benefits is sourced on a geographical basis as indicated in this paragraph (b)(2)(ii)(D). The amount of the compensation in the form of the fringe benefit must be reasonable, and the individual must substantiate such amounts by adequate records or by sufficient evidence under rules similar to those set forth in §1.274–5T(c) or (h) or §1.132–5. For purposes of this paragraph (b)(2)(ii)(D), the term *principal place of work* has the same meaning that it has for purposes of section 217 and §1.217–2(c)(3).

(*1*) *Housing fringe benefit*. The source of compensation in the form of a housing fringe benefit is determined based on the location of the individual's principal place of work. For purposes of this paragraph (b)(2)(ii)(D)(*1*), a housing fringe benefit includes payments to or on behalf of an individual (and the individual's family if the family resides with the individual) only for rent, utilities (other than telephone charges), real and personal property insurance, occupancy taxes not deductible under section 164 or 216(a), nonrefundable fees paid for securing a leasehold, rental of furniture and accessories, household repairs, residential parking, and the fair rental value of housing provided in kind by the individual's employer. A housing fringe benefit does not include payments for expenses or items set forth in §1.911–4(b)(2).

(*2*) *Education fringe benefit*. The source of compensation in the form of an education fringe benefit for the education expenses of the individual's dependents is determined based on the location of the individual's principal place of work. For purposes of this paragraph (b)(2)(ii)(D)(*2*), an education fringe benefit includes payments only for qualified tuition and expenses of the type described in section 530(b)(4)(A)(i) (regardless of whether incurred in connection with enrollment or attendance at a school) and expenditures for room and board and uniforms as described in section 530(b)(4)(A)(ii) with respect to education at an elementary or secondary educational institution.

(*3*) *Local transportation fringe benefit*. The source of compensation in the form of a local transportation fringe benefit is determined based on the location of the individual's principal place of work. For purposes of this paragraph (b)(2)(ii)(D)(*3*), an individual's local transportation fringe benefit is the amount that the individual receives as compensation for local transportation of the individual or the individual's spouse or dependents at the location of the individual's principal place of work. The amount treated as a local transportation fringe benefit is limited to the actual expenses incurred for local transportation and the fair rental value of any vehicle provided by the employer and used predominantly by the individual or the individual's spouse or dependents for local transportation. For this purpose, actual expenses in-

curred for local transportation do not include the cost (including interest) of the purchase by the individual, or on behalf of the individual, of an automobile or other vehicle.

(*4*) *Tax reimbursement fringe benefit*. The source of compensation in the form of a foreign tax reimbursement fringe benefit is determined based on the location of the jurisdiction that imposed the tax for which the individual is reimbursed.

(*5*) *Hazardous or hardship duty pay fringe benefit*. The source of compensation in the form of a hazardous or hardship duty pay fringe benefit is determined based on the location of the hazardous or hardship duty zone for which the hazardous or hardship duty pay fringe benefit is paid. For purposes of this paragraph (b)(2)(ii)(D)(*5*), a hazardous or hardship duty zone is any place in a foreign country which is either designated by the Secretary of State as a place where living conditions are extraordinarily difficult, notably unhealthy, or where excessive physical hardships exist, and for which a post differential of 15 percent or more would be provided under section 5925(b) of Title 5 of the U.S. Code to any officer or employee of the U.S. Government present at that place, or where a civil insurrection, civil war, terrorism, or wartime conditions threatens physical harm or imminent danger to the health and well-being of the individual. Compensation provided an employee during the period that the employee performs labor or personal services in a hazardous or hardship duty zone may be treated as a hazardous or hardship duty pay fringe benefit only if the employer provides the hazardous or hardship duty pay fringe benefit only to employees performing labor or personal services in a hazardous or hardship duty zone. The amount of compensation treated as a hazardous or hardship duty pay fringe benefit may not exceed the maximum amount that the U.S. government would allow its officers or employees present at that location.

(*6*) *Moving expense reimbursement fringe benefit*. Except as otherwise provided in this paragraph (b)(2)(ii)(D)(*6*), the source of compensation in the form of a moving expense reimbursement is determined based on the location of the employee's new principal place of work. The source of such compensation is determined based on the location of the employee's former principal place of work, however, if the individual provides sufficient evidence that such determination of source is more appropriate under the facts and circumstances of the particular case. For purposes of this paragraph (b)(2)(ii)(D)(*6*), sufficient evidence generally requires an agreement, between the employer and the employee, or a written statement of company policy, which is reduced to writing before the move and which is entered into or established to induce the employee or employees to move to another country. Such written statement or agreement must state that the employer will reimburse the employee for moving expenses that the employee incurs to return to the employee's former principal place of work regardless of whether he or she continues to work for the employer after returning to that location. The writing may contain certain conditions upon which the right to reimbursement is determined as long as those conditions set forth standards that are definitely ascertainable and can only be fulfilled prior to, or through completion of, the employee's return move to the employee's former principal place of work.

(E) *Time basis*. The amount of compensation for labor or personal services performed within the United States determined on a time basis is the amount that bears the same relation to the individual's total compensation as the number of days of performance of the labor or personal services by the individual within the United States bears to his or her total number of days of performance of labor or personal services. A unit of time less than a day may be appropriate for purposes of this calculation. The time period for which the compensation for labor or personal services is made is presumed to be the calendar year in which the labor or personal services are performed, unless the taxpayer establishes to the satisfaction of the Commissioner, or the Commissioner determines, that another distinct, separate, and continuous period of time is more appropriate. For example, a transfer during a year from a position in the United States to a foreign posting that lasted through the end of that year would generally establish two separate time periods within that taxable year. The first of these time periods would be the portion of the year preceding the start of the foreign posting, and the second of these time periods would be the portion of the year following the start of the foreign posting. However, in the case of a foreign posting that requires short-term returns to the United States to perform services for the employer, such short-term returns would not be sufficient to establish distinct, separate, and continuous time periods within the foreign posting time period but would be relevant to the allocation of compensation relating to the overall time period. In each case, the source of the compensation on a time basis is based upon the number of days (or unit of time less than a day, if appropriate) in that separate time period.

(F) *Multi-year compensation arrangements*. The source of multi-year compensation is determined generally on a time basis, as defined in paragraph (b)(2)(ii)(E) of this section, over the period to which such compensation is attributable. For purposes of this paragraph (b)(2)(ii)(F), *multi-year compensation* means compensation that is included in the income of an individual in one taxable year but that is attributable to a period that includes two or more taxable years. The determination of the period to which such compensation is attributable, for purposes of determining its source, is based upon the facts and circumstances of the particular case. For example, an amount of compensation that specifically relates to a period of time that includes several calendar years is attributable to the entirety of that multi-year period. The amount of such compensation that is treated as from sources within the United States is the amount that bears the same relationship to the total multi-year compensation as the number of days (or unit of time less than a day, if appropriate) that labor or personal services were performed within the United States in connection with the project bears to the total number of days (or unit of time less than a day, if appropriate) that labor or personal services were performed in connection with the project. In the case of stock options, the facts and circumstances generally will be such that the applicable period to which the compensation is attributable is the period between the grant of an option and the date on which all employment-related conditions for its exercise have been satisfied (the vesting of the option).

(G) *Examples*. The following examples illustrate the application of this paragraph (b)(2)(ii):

Example 1. B, a nonresident alien individual, was employed by Corp M, a domestic corporation, from March 1 to December 25 of the taxable year, a total of 300 days, for which B received compensation in the amount of $80,000. Under B's employment contract with Corp M, B was subject to call at all times by Corp M and was in a payment status on a 7-day week basis. Pursuant to that contract, B performed services (or was available to perform services) within the United States for 180 days and performed services (or was available to perform services) without the United States for 120 days. None of B's $80,000 compensation was for fringe benefits as identified in paragraph (b)(2)(ii)(D) of this section. B determined the amount of compensation that is attributable to his labor or personal services performed within the United States on a time basis under paragraph (b)(2)(ii)(A) and (E) of this section. B did not assert, pursuant to paragraph (b)(2)(ii)(C)(*1*)(*i*) of this section, that, under the particular facts and circumstances, an alternative basis more properly determines the source of that compensation than the time basis. Therefore, B must include in income from sources within the United States $48,000 ($80,000 x 180/300) of his compensation from Corporation M.

Example 2. (i) Same facts as in *Example 1* except that Corp M had a company-wide arrangement with its employees, including B, that they would receive an education fringe benefit, as described in paragraph (b)(2)(ii)(D)(*2*) of this section, while working in the United States. During the taxable year, B incurred education expenses for his dependent daughter that qualified for the education fringe benefit in the amount of $10,000, for which B received a reimbursement from Corp M. B did not maintain adequate records or sufficient evidence of this fringe benefit as required by paragraph (b)(2)(ii)(D) of this section. When B filed his Federal income tax return for the taxable year, B did not apply paragraphs (b)(2)(ii)(B) and (D)(*2*) of this section to treat the compensation in the form of the education fringe benefit as income from sources within the United States, the location of his principal place of work during the 300-day period. Rather, B combined the $10,000 reimbursement with his base compensation of $80,000 and applied the time basis of paragraph (b)(2)(ii)(A) of this section to determine the source of his gross income.

(ii) On audit, B argues that because he failed to substantiate the education fringe benefit in accordance with paragraph (b)(2)(ii)(D) of this section, his entire employment compensation from Corp M is sourced on a time basis pursuant to paragraph (b)(2)(ii)(A) of this section. The Commissioner, after reviewing Corp M's fringe benefit arrangement, determines, pursuant to paragraph (b)(2)(ii)(C)(*1*)(*ii*) of this section, that the $10,000 educational expense reimbursement constitutes in substance a fringe benefit described in paragraph (b)(2)(ii)(D)(*2*) of this section, notwithstanding a failure to meet all of the requirements of paragraph (b)(2)(ii)(D) of this section, and that an alternative geographic source basis, under the facts and circumstances of this particular case, is a more reasonable manner to determine the source of the compensation than the time basis used by B.

Example 3. (i) A, a United States citizen, is employed by Corp N, a domestic corporation. A's principal place of work is in the United States. A earns an annual salary of $100,000. During the first quarter of the calendar year (which is also A's taxable year), A performed services entirely within the United States. At the beginning of the second quarter of the calendar year, A was transferred to Country X for the remainder of the year and received, in addition to her annual salary, $30,000 in fringe benefits that are attributable to her new principal place of work in Country X. Corp N paid these fringe benefits separately from A's annual salary. Corp N supplied A with a statement detailing that $25,000 of the fringe benefit was paid for housing, as defined in paragraph (b)(2)(ii)(D)(*1*) of this section, and $5,000 of the fringe benefit was paid for local transportation, as defined in paragraph (b)(2)(ii)(D)(*3*) of this section. None of the local transportation fringe benefit is excluded from the employee's gross income as a qualified transportation fringe benefit under section 132(a)(5). Under A's employment contract, A was required to work on a 5-day week basis, Monday through Friday. During the last three quarters of the year, A performed services 30 days in the United States and 150 days in Country X and other foreign countries.

(ii) A determined the source of all of her compensation from Corp N pursuant to paragraphs (b)(2)(ii)(A), (B), and (D)(*1*) and (*3*) of this section. A did not assert, pursuant to paragraph (b)(2)(ii)(C)(*1*)(*i*) of this section, that, under the particular facts and circumstances, an alternative basis more properly determines the source of that compensation than the bases set forth in paragraphs (b)(2)(ii)(A), (B), and (D)(*1*) and (*3*) of this section. However, in applying the time basis set forth in paragraph (b)(2)(ii)(E) of this section, A establishes to the satisfaction of the Commissioner that the first quarter of the calendar year and the last three quarters of the calendar year are two separate, distinct, and continuous periods of time. Accordingly, $25,000 of A's annual salary is attributable to the first quarter of the year (25 percent of $100,000). This amount is entirely compensation that was attributable to the labor or personal services performed within the United States and is, therefore, included in gross income as income from sources within the United States. The balance of A's compensation as an employee of Corp N, $105,000 (which includes the $30,000 in fringe benefits that are attributable to the location of A's principal place of work in Country X), is compensation attributable to the final three quarters of her taxable year. During those three quarters, A's periodic performance of services in the United States does not result in distinct, separate, and continuous periods of time. Of the $75,000 paid for annual salary, $12,500 (30/180 x $75,000) is compensation that was attributable to the labor or personal services performed within the United States and $62,500 (150/180 x $75,000) is compensation that was attributable to the labor or personal services performed outside the United States. Pursuant to paragraphs (b)(2)(ii)(B) and (D)(*1*) and (*3*) of this section, A sourced the $25,000 received for the housing fringe benefit and the $5,000 received for the local transportation fringe benefit based on the location of her principal place of work, Country X. Accordingly, A included the $30,000 in fringe benefits in her gross income as income from sources without the United States.

Example 4. Same facts as in *Example 3*. Of the 150 days during which A performed services in Country X and in other foreign countries (during the final three quarters of A's taxable year), she performed 30 days of those services in Country Y. Country Y is a country designated by the Secretary of State as a place where living conditions are extremely difficult, notably unhealthy, or where excessive physical hardships exist and for which a post differential of 15 percent or more would be provided under section 5925(b) of Title 5 of the U.S. Code to any officer or employee of the U.S. government present at that place. Corp N has a policy of paying its employees a $65 premium per day for each day worked in countries so designated. The $65 premium per day does not exceed the maximum amount that the U.S. government would pay its officers or employees stationed in Country Y. Because A performed services in Country Y for 30 days, she earned additional compensation of $1,950. The $1,950 is considered a hazardous duty or hardship pay fringe benefit and is sourced under paragraphs (b)(2)(ii)(B) and (D)(*5*) of this section based on the location of the hazardous or hardship duty zone, Country Y. Accordingly, A included the amount of the hazardous duty or hardship pay fringe benefit ($1,950) in her gross income as income from sources without the United States.

Example 5. (i) During 2006 and 2007, Corp P, a domestic corporation, employed four United States citizens, E, F, G, and H to work in its manufacturing plant in Country V. As part of his or her compensation package, each employee arranged for local transportation unrelated to Corp P's business needs. None of the local transportation fringe benefit is excluded from the employee's gross income as a qualified transportation fringe benefit under section 132(a)(5) and (f).

(ii) Under the terms of the compensation package that E negotiated with Corp P, Corp P permitted E to use an automobile owned by Corp P. In addition, Corp P agreed to reimburse E for all expenses incurred by E in maintaining and operating the automobile, including gas and parking. Provided that the local transportation fringe benefit meets the requirements of paragraph (b)(2)(ii)(D)(*3*) of this section, E's compensation with respect to the fair rental value of the automobile and reimbursement for the expenses E incurred is sourced under paragraphs (b)(2)(ii)(B) and (D)(*3*) of this section based on E's principal place of work in Country V. Thus, the local transportation fringe benefit will be included in E's gross income as income from sources without the United States.

(iii) Under the terms of the compensation package that F negotiated with Corp P, Corp P let F use an automobile owned by Corp P. However, Corp P did not agree to reimburse F for any expenses incurred by F in maintaining and operating the automobile. Provided that the local transportation fringe benefit meets the requirements of paragraph (b)(2)(ii)(D)(*3*) of this section, F's compensation with respect to the fair rental value of the automobile is sourced under paragraphs (b)(2)(ii)(B) and (D)(*3*) of this section based on F's principal place of work in Country V. Thus, the local transportation fringe benefit will be included in F's gross income as income from sources without the United States.

(iv) Under the terms of the compensation package that G negotiated with Corp P, Corp P agreed to reimburse G for the purchase price of an automobile that G purchased in Country V. Corp P did not agree to reimburse G for any expenses incurred by

G in maintaining and operating the automobile. Because the cost to purchase an automobile is not a local transportation fringe benefit as defined in paragraph (b)(2)(ii)(D)(*3*) of this section, the source of the compensation to G will be determined pursuant to paragraph (b)(2)(ii)(A) or (C) of this section.

(v) Under the terms of the compensation package that H negotiated with Corp P, Corp P agreed to reimburse H for the expenses that H incurred in maintaining and operating an automobile, including gas and parking, which H purchased in Country V. Provided that the local transportation fringe benefit meets the requirements of paragraph (b)(2)(ii)(D)(*3*) of this section, H's compensation with respect to the reimbursement for the expenses H incurred is sourced under paragraphs (b)(2)(ii)(B) and (D)(*3*) of this section based on H's principal place of work in Country V. Thus, the local transportation fringe benefit will be included in H's gross income as income from sources without the United States.

Example 6. (i) On January 1, 2006, Company Q compensates employee J with a grant of options to which section 421 does not apply that do not have a readily ascertainable fair market value when granted. The stock options permit J to purchase 100 shares of Company Q stock for $5 per share. The stock options do not become exercisable unless and until J performs services for Company Q (or a related company) for 5 years. J works for Company Q for the 5 years required by the stock option grant. In years 2006–08, J performs all of his services for Company Q within the United States. In 2009, J performs 1/2 of his services for Company Q within the United States and 1/2 of his services for Company Q without the United States. In year 2010, J performs his services entirely without the United States. On December 31, 2012, J exercises the options when the stock is worth $10 per share. J recognizes $500 in taxable compensation (($10-$5) x 100) in 2012.

(ii) Under the facts and circumstances, the applicable period is the 5-year period between the date of grant (January 1, 2006) and the date the stock options become exercisable (December 31, 2010). On the date the stock options become exercisable, J performs all services necessary to obtain the compensation from Company Q. Accordingly, the services performed after the date the stock options become exercisable are not taken into account in sourcing the compensation from the stock options. Therefore, pursuant to paragraph (b)(2)(ii)(A), since J performs 3 1/2 years of services for Company Q within the United States and 1 1/2 years of services for Company Q without the United States during the 5-year period, 7/10 of the $500 of compensation (or $350) recognized in 2012 is income from sources within the United States and the remaining 3/10 of the compensation (or $150) is income from sources without the United States.

* * * * *

(d) *Effective date*. * * * Paragraph (b) and the first sentence of paragraph (a)(1) of this section apply to taxable years beginning on or after July 14, 2005.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (b) is amended by adding an entry for §1.861–4 in numerical order to the table to read as follows:

§602.101 OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
1.861–4	1545–1900
* * * * *	

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

Approved July 5, 2005.

Eric Solomon,
Acting Deputy Assistant Secretary for Tax Policy.

(Filed by the Office of the Federal Register on July 13, 2005, 8:45 a.m., and published in the issue of the Federal Register for July 14, 2005, 70 F.R. 40663)

Section 2651.—Generation Assignment

26 CFR 26.2651–1: Generation assignment.

T.D. 9214

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 26

Predeceased Parent Rule

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the predeceased parent rule, which provides an exception to the general rules of section 2651 of the Internal Revenue Code (Code) for determining the generation assignment of a transferee of property for generation-skipping transfer (GST) tax purposes. These regulations also provide rules regarding a transferee assigned to more than one generation. The regulations reflect changes to the law made by the Taxpayer Relief Act of 1997 and generally apply to individuals, trusts, and estates.

DATES: *Effective Date*: These regulations are effective July 18, 2005.

FOR FURTHER INFORMATION CONTACT: Lian A. Mito at (202) 622–7830 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

On September 3, 2004, a notice of proposed rulemaking (REG–145988–03, 2004–42 I.R.B. 693) relating to the predeceased parent rule was published in the **Federal Register** (69 FR 53862). The public hearing scheduled for December 14, 2004, was cancelled because no re-

quests to speak were received. Written comments responding to the notice of proposed rulemaking were received. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision. The revisions are discussed below.

Summary of Comments

The proposed regulations provided that, for purposes of determining whether the predeceased parent rule applies, an individual transferee's interest in property is established or derived at the time the transferor who transferred the property is subject to either the gift or estate tax on the property. If the transferor will be subject to a transfer tax imposed on the property transferred on more than one occasion, then the relevant time for determining whether the predeceased parent rule applies is the earliest time at which the transferor is subject to the gift or estate tax. In the case of a trust for which an election under section 2056(b)(7) (QTIP election) has been made, the proposed regulations provided that the interest of the remainder beneficiary is considered as established or derived when the QTIP trust was established. However, the proposed regulations also included an exception to this general rule by providing that, to the extent of the QTIP (but not a reverse QTIP) election, the remainder beneficiary's interest is deemed to have been established or derived on the death of the transferor's spouse (the income beneficiary), rather than on the transferor's earlier death.

One commentator indicated that this exception is unnecessary. The commentator believes that the proposed regulations misinterpreted the statute because a remainder beneficiary's interest in a trust that is subject to a QTIP (but not a reverse QTIP) election should always be deemed to have been established, not at the time of the trust's creation, but rather at the time when the income-beneficiary spouse is first subject to gift or estate tax on the trust property. This position applies the definition of "transferor" in section 2652 in the context of the reference to "established and derived" in section 2651(e), and is based on the conclusion that the tax in this situation is not imposed on the same transferor on more than one occasion. Thus, because the donee or surviving spouse becomes the transferor of a trust that is subject to a QTIP (but not reverse QTIP) election, the remainder beneficiary's interest in such a trust is established upon that spouse's gift of an interest in the trust or that spouse's death, in each case the time at which gift or estate tax on the trust is first imposed on that spouse. Viewed from this perspective, this provision of the proposed regulations is not an exception. The Treasury Department and the IRS agree, and the final regulations adopt the suggested change.

Under the proposed regulations, the predeceased parent rule does not apply to transfers to collateral heirs if, at the time of the transfer, "the transferor (or the transferor's spouse or former spouse) has any living lineal descendant." Thus, under the proposed regulations, if, at the time of the transfer, the transferor has no living lineal descendants but the transferor's spouse or former spouse does, the predeceased parent rule will not apply to any transfer by the transferor to a collateral heir. A number of commentators pointed out that the parenthetical language is inconsistent with the purpose and language of the statute, and will inappropriately narrow the application of the predeceased parent rule with respect to collateral heirs. The Treasury Department and the IRS agree, and the parenthetical language is removed in the final regulations. Accordingly, the final regulations require that, for the predeceased parent rule to apply to transfers to collateral heirs, only the transferor must have no living lineal descendants at the time of the transfer.

The proposed regulations provided an exception to the general rule that assigns an individual to the youngest of the generations to which that individual may be assigned. Under the exception, an adopted individual will be treated as a member of the generation that is one generation below the adoptive parent for purposes of determining whether a transfer to the adopted individual from the adoptive parent (or the spouse or former spouse of the adoptive parent, or a lineal descendant of a grandparent of the adoptive parent) is subject to the GST tax. The proposed regulations defined an "adopted individual" as an individual who is: (1) a descendant of a parent of the adoptive parent (or the spouse or former spouse of the adoptive parent); and (2) under the age of 18 at the time of the adoption.

Two commentators expressed concern that this objective test (specifically, the age at the time of the adoption) provides a strong inducement to engage in a tax-motivated adoption, particularly in the case of older minors, because of the amount of GST tax that thereby may be avoided. One commentator suggested lowering the limit on the age of the individual at the time of the adoption for purposes of the test. The other commentator recommended adding a third element to the definition of adopted individual, namely, that the individual was not adopted primarily for tax-avoidance purposes.

The Treasury Department and the IRS continue to believe that certain adopted minors should be treated as a member of the generation that is one generation below the adoptive parent, but only if the adoption is not primarily for the purpose of avoiding GST tax. Therefore, under the final regulations, the adopted individual will be treated as a member of the generation that is one generation below the adoptive parent for purposes of determining whether transfers from certain individuals to the adopted individual are subject to GST tax if the following requirements are satisfied: (1) the individual is legally adopted by the adoptive parent; (2) the individual is a descendant of a parent of the adoptive parent (or the adoptive parent's spouse or former spouse); (3) the individual is under the age of 18 at the time of the adoption; and (4) the individual is not adopted primarily for GST tax-avoidance purposes. The determination of whether an adoption is primarily for GST tax-avoidance purposes is to be made based upon all of the facts and circumstances. The Treasury Department and IRS believe that the most significant factor to be considered is whether there is a *bona fide* parent/child relationship between the adoptive parent and the adopted individual. Other factors that may be considered include (but are not limited to): the age of the adopted individual at the time of the adoption, and the relationship between the adopted individual and the individual's parents immediately before the adoption. Thus, the adoption of an infant will be less likely to be considered primarily for tax-avoidance purposes than the adoption of an individual who is age 17. Objective evidence that the parent was unwilling or unable to act as the individual's parent

(*e.g.*, the parent abandons the individual, or is adjudicated incompetent or incapacitated) may indicate that an adoption is not primarily for tax-avoidance purposes.

One commentator suggested clarifying the interaction between section 2651(b)(3), regarding the treatment of legal adoptions, and section 2651(f)(1), regarding individuals assigned to more than one generation. In order to provide that clarification, the Treasury Department and the IRS confirm that, for purposes of chapter 13, a legal adoption may create an additional generation assignment, but the adoption does not constitute a substitute for the blood relationship. Specifically, an individual who has been adopted will be treated as a blood relative of the adoptive parent under section 2651(b)(3) and generally is treated as a child of the adoptive parent under state law. In spite of the adoption, however, the adopted individual also continues to be a blood relative of the individual's birth parents. Thus, the generation assignment of the adopted individual with regard to a transfer from an ancestor of the birth parent, for example, will continue to be measured under section 2651(b), but, subject to the exception in §26.2651–2(b), the relationship between them may be subject to the special rule in section 2651(f)(1), which provides that an individual who would be assigned to more than one generation is assigned to the youngest of those generations.

The proposed regulations provided that any individual who dies no later than 90 days after a transfer is treated as having predeceased the transferor. One commentator recommended that the final regulations apply this 90-day rule to inter vivos, as well as testamentary, transfers. The 90-day rule is intended to replace a similar 90-day rule in §26.2612–1(a)(2), which is limited to testamentary transfers. Moreover, many state statutes contain similar rules that apply only to testamentary transfers. Accordingly, the final regulations do not adopt this recommendation, and revise the language of this provision to confirm that it addresses only transfers occurring by reason of the death of the transferor.

Two commentators requested confirmation that the reference to adoption in §26.2651–2(b) applies solely for purposes of the rule in section 2651(f)(1) and has no application to the rule in section 2651(b). Accordingly, the introductory language of §26.2651–2(b) has been revised.

Special Analyses

It has been determined that these proposed regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations and, because these regulations do not impose 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 preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small entities.

Drafting Information

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

* * * * *

Amendments to the Regulations

Accordingly, 26 CFR part 26 is amended as follows:

PART 26—GENERATION-SKIPPING TRANSFER TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1986

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

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

Par. 2. In §26.2600–1, the table is amended by:

1. Removing the entries for §26.2612–1, paragraphs (a)(1) and (a)(2).

2. Adding entries for §§26.2651–1, 26.2651–2, and 26.2651–3.

The additions read as follows:

§26.2600–1 Table of contents.

* * * * *

§26.2651–1 Generation assignment.

(a) Special rule for persons with a deceased parent.
(1) In general.
(2) Special rules.
(3) Established or derived.
(4) Special rule in the case of additional contributions to a trust.
(b) Limited application to collateral heirs.
(c) Examples.

§26.2651–2 Individual assigned to more than one generation.

(a) In general.
(b) Exception.
(c) Special rules.
(1) Corresponding generation adjustment.
(2) Continued application of generation assignment.
(d) Example.

§26.2651–3 Effective dates.

(a) In general.
(b) Transition rule.

Par. 3. Section 26.2612–1 is amended by:

1. Removing the paragraph designation and heading for (a)(1).

2. Removing paragraph (a)(2).

3. Removing the second sentence of paragraph (f) introductory text.

4. Removing *Examples 6* and *7* in paragraph (f).

5. Redesignating *Examples 8* through *15* as *Examples 6* through *13* in paragraph (f).

6. Revising the first sentence of newly designated Example 7 in paragraph (f).

7. Revising the first sentence of newly designated *Example 11* in paragraph (f).

The revisions read as follows:

§26.2612–1 Definitions.

* * * * *

(f) * * *

Example 7. Taxable termination resulting from distribution. The facts are the same as in *Example 6*, except twenty years after C's death the trustee exercises its discretionary power and distributes the entire principal to GGC. * * *

* * * * *

Example 11. Exercise of withdrawal right as taxable distribution. The facts are the same as in *Example 10*, except GC holds a continuing right to withdraw trust principal and after one year GC withdraws $10,000. * * *

* * * * *

Par. 4. Sections 26.2651–1, 26.2651–2 and 26.2651–3 are added to read as follows:

§26.2651–1 Generation assignment.

(a) *Special rule for persons with a deceased parent*—(1) *In general*. This paragraph (a) applies for purposes of determining whether a transfer to or for the benefit of an individual who is a descendant of a parent of the transferor (or the transferor's spouse or former spouse) is a generation-skipping transfer. If that individual's parent, who is a lineal descendant of the parent of the transferor (or the transferor's spouse or former spouse), is deceased at the time the transfer (from which an interest of such individual is established or derived) is subject to the tax imposed on the transferor by chapter 11 or 12 of the Internal Revenue Code, the individual is treated as if that individual were a member of the generation that is one generation below the lower of—

(i) The transferor's generation; or

(ii) The generation assignment of the individual's youngest living lineal ancestor who is also a descendant of the parent of the transferor (or the transferor's spouse or former spouse).

(2) *Special rules*—(i) *Corresponding generation adjustment*. If an individual's generation assignment is adjusted with respect to a transfer in accordance with paragraph (a)(1) of this section, a corresponding adjustment with respect to that transfer is made to the generation assignment of each—

(A) Spouse or former spouse of that individual;

(B) Descendant of that individual; and

(C) Spouse or former spouse of each descendant of that individual.

(ii) *Continued application of generation assignment*. If a transfer to a trust would be a generation-skipping transfer but for paragraph (a)(1) of this section, any generation assignment determined under this paragraph (a) continues to apply in determining whether any subsequent distribution from (or termination of an interest in) the portion of the trust attributable to that transfer is a generation-skipping transfer.

(iii) *Ninety-day rule*. For purposes of paragraph (a)(1) of this section, any individual who dies no later than 90 days after a transfer occurring by reason of the death of the transferor is treated as having predeceased the transferor.

(iv) *Local law*. A living person is not treated as having predeceased the transferor solely by reason of a provision of applicable local law; *e.g.*, an individual who disclaims is not treated as a predeceased parent solely because state law treats a disclaimant as having predeceased the transferor for purposes of determining the disposition of the disclaimed property.

(3) *Established or derived*. For purposes of section 2651(e) and paragraph (a)(1) of this section, an individual's interest is established or derived at the time the transferor is subject to transfer tax on the property. See §26.2652–1(a) for the definition of a transferor. If the same transferor, on more than one occasion, is subject to transfer tax imposed by either chapter 11 or 12 of the Internal Revenue Code on the property so transferred (whether the same property, reinvestments thereof, income thereon, or any or all of these), then the relevant time for determining whether paragraph (a)(1) of this section applies is the earliest time at which the transferor is subject to the tax imposed by either chapter 11 or 12 of the Internal Revenue Code. For purposes of section 2651(e) and paragraph (a)(1) of this section, the interest of a remainder beneficiary of a trust for which an election under section 2523(f) or section 2056(b)(7) (QTIP election) has been made will be deemed to have been established or derived, to the extent of the QTIP election, on the date as of which the value of the trust corpus is first subject to tax under section 2519 or section 2044. The preceding sentence does not apply to a trust, however, to the extent that an election under section 2652(a)(3) (reverse QTIP election) has been made for the trust because, to the extent of a reverse QTIP election, the spouse who established the trust will remain the transferor of the trust for generation-skipping transfer tax purposes.

(4) *Special rule in the case of additional contributions to a trust*. If a transferor referred to in paragraph (a)(1) of this section contributes additional property to a trust that existed before the application of paragraph (a)(1), then the additional property is treated as being held in a separate trust for purposes of chapter 13 of the Internal Revenue Code. The provisions of §26.2654–1(a)(2), regarding treatment as separate trusts, apply as if different transferors had contributed to the separate portions of the single trust. Additional subsequent contributions from that transferor will be added to the new share that is treated as a separate trust.

(b) *Limited application to collateral heirs*. Paragraph (a) of this section does not apply in the case of a transfer to any individual who is not a lineal descendant of the transferor (or the transferor's spouse or former spouse) if the transferor has any living lineal descendant at the time of the transfer.

(c) *Examples*. The following examples illustrate the provisions of this section:

Example 1. T establishes an irrevocable trust, Trust, providing that trust income is to be paid to T's grandchild, GC, for 5 years. At the end of the 5-year period or on GC's prior death, Trust is to terminate and the principal is to be distributed to GC if GC is living or to GC's children if GC has died. The transfer that occurred on the creation of the trust is subject to the tax imposed by chapter 12 of the Internal Revenue Code and, at the time of the transfer, T's child, C, who is a parent of GC, is deceased. GC is treated as a member of the generation that is one generation below T's generation. As a result, GC is not a skip person and Trust is not a skip person. Therefore, the transfer to Trust is not a direct skip. Similarly, distributions to GC during the term of Trust and at the termination of Trust will not be GSTs.

Example 2. On January 1, 2004, T transfers $100,000 to an irrevocable inter vivos trust that provides T with an annuity payable for four years or until T's prior death. The annuity satisfies the definition of a qualified interest under section 2702(b). When the trust terminates, the corpus is to be paid to T's grandchild, GC. The transfer is subject to the tax imposed by chapter 12 of the Internal Revenue Code and, at the time of the transfer, T's child, C, who is a parent of GC, is living. C dies in 2006. In this case, C was alive at the time the transfer by T was subject to the tax imposed by chapter 12 of the Internal Revenue Code. Therefore, section 2651(e) and paragraph (a)(1) of this section do not apply. When the trust subsequently terminates, the distribution to GC is a taxable termination that is subject to the GST tax to the extent the trust has an inclusion ratio greater than zero. See section 2642(a).

Example 3. T dies testate in 2002, survived by T's spouse, S, their children, C1 and C2, and C1's child, GC. Under the terms of T's will, a trust is established for the benefit of S and of T and S's descendants. Under the terms of the trust, all income is payable to S during S's lifetime and the trustee may distribute trust corpus for S's health, support and maintenance. At S's death, the corpus is to be distributed, outright, to C1 and C2. If either C1 or C2 has predeceased S, the deceased child's share of the corpus is to be distributed to that child's then-living descendants, per stirpes. The executor of T's estate makes the election under section 2056(b)(7) to treat the trust property as qualified terminable interest property (QTIP) but does not make the election under section 2652(a)(3)

(reverse QTIP election). In 2003, C1 dies survived by S and GC. In 2004, S dies, and the trust terminates. The full fair market value of the trust is includible in S's gross estate under section 2044 and S becomes the transferor of the trust under section 2652(a)(1)(A). GC's interest is considered established or derived at S's death, and because C1 is deceased at that time, GC is treated as a member of the generation that is one generation below the generation of the transferor, S. As a result, GC is not a skip person and the transfer to GC is not a direct skip.

Example 4. The facts are the same as in *Example 3*. However, the executor of T's estate makes the election under section 2652(a)(3) (reverse QTIP election) for the entire trust. Therefore, T remains the transferor because, for purposes of chapter 13 of the Internal Revenue Code, the election to be treated as qualified terminable interest property is treated as if it had not been made. In this case, GC's interest is established or derived on T's death in 2002. Because C1 was living at the time of T's death, the predeceased parent rule under section 2651(e) does not apply, even though C1 was deceased at the time the transfer from S to GC was subject to the tax under chapter 11 of the Internal Revenue Code. When the trust terminates, the distribution to GC is a taxable termination that is subject to the GST tax to the extent the trust has an inclusion ratio greater than zero. See section 2642(a).

Example 5. T establishes an irrevocable trust providing that trust income is to be paid to T's grandniece, GN, for 5 years or until GN's prior death. At the end of the 5-year period or on GN's prior death, the trust is to terminate and the principal is to be distributed to GN if living, or if GN has died, to GN's then-living descendants, per stirpes. S is a sibling of T and the parent of N. N is the parent of GN. At the time of the transfer, T has no living lineal descendant, S is living, N is deceased, and the transfer is subject to the gift tax imposed by chapter 12 of the Internal Revenue Code. GN is treated as a member of the generation that is one generation below T's generation because S, GN's youngest living lineal ancestor who is also a descendant of T's parent, is in T's generation. As a result, GN is not a skip person and the transfer to the trust is not a direct skip. In addition, distributions to GN during the term of the trust and at the termination of the trust will not be GSTs.

Example 6. On January 1, 2004, T transfers $50,000 to a great-grandniece, GGN, who is the great-grandchild of B, a brother of T. At the time of the transfer, T has no living lineal descendants and B's grandchild, GN, who is a parent of GGN and a child of B's living child, N, is deceased. GGN will be treated as a member of the generation that is one generation below the lower of T's generation or the generation assignment of GGN's youngest living lineal ancestor who is also a descendant of the parent of the transferor. In this case, N is GGN's youngest living lineal ancestor who is also a descendant of the parent of T. Because N's generation assignment is lower than T's generation, GGN will be treated as a member of the generation that is one generation below N's generation assignment (*i.e.*, GGN will be treated as a member of her parent's generation). As a result, GGN remains a skip person and the transfer to GGN is a direct skip.

Example 7. T has a child, C. C and C's spouse, S, have a 20-year-old child, GC. C dies and S subsequently marries S2. S2 legally adopts GC. T transfers $100,000 to GC. Under section 2651(b)(1), GC is assigned to the generation that is two generations below T. However, since GC's parent, C, is deceased at the time of the transfer, GC will be treated as a member of the generation that is one generation below T. As a result, GC is not a skip person and the transfer to GC is not a direct skip.

§26.2651–2 Individual assigned to more than 1 generation.

(a) *In general*. Except as provided in paragraph (b) or (c) of this section, an individual who would be assigned to more than 1 generation is assigned to the youngest of the generations to which that individual would be assigned.

(b) *Exception*. Notwithstanding paragraph (a) of this section, an adopted individual (as defined in this paragraph) will be treated as a member of the generation that is one generation below the adoptive parent for purposes of determining whether a transfer to the adopted individual from the adoptive parent (or the spouse or former spouse of the adoptive parent, or a lineal descendant of a grandparent of the adoptive parent) is subject to chapter 13 of the Internal Revenue Code. For purposes of this paragraph (b), an adopted individual is an individual who is—

(1) Legally adopted by the adoptive parent;

(2) A descendant of a parent of the adoptive parent (or the spouse or former spouse of the adoptive parent);

(3) Under the age of 18 at the time of the adoption; and

(4) Not adopted primarily for the purpose of avoiding GST tax. The determination of whether an adoption is primarily for GST tax-avoidance purposes is made based upon all of the facts and circumstances. The most significant factor is whether there is a *bona fide* parent/child relationship between the adoptive parent and the adopted individual, in which the adoptive parent has fully assumed all significant responsibilities for the care and raising of the adopted child. Other factors may include (but are not limited to), at the time of the adoption—

(i) The age of the adopted individual (for example, the younger the age of the adopted individual, or the age of the youngest of siblings who are all adopted together, the more likely the adoption will not be considered primarily for GST tax-avoidance purposes); and

(ii) The relationship between the adopted individual and the individual's parents (for example, objective evidence of the absence or incapacity of the parents may indicate that the adoption is not primarily for GST tax-avoidance purposes).

(c) *Special rules*—(1) *Corresponding generation adjustment*. If an individual's generation assignment is adjusted with respect to a transfer in accordance with paragraph (b) of this section, a corresponding adjustment with respect to that transfer is made to the generation assignment of each—

(i) Spouse or former spouse of that individual;

(ii) Descendant of that individual; and

(iii) Spouse or former spouse of each descendant of that individual.

(2) *Continued application of generation assignment*. If a transfer to a trust would be a generation-skipping transfer but for paragraph (b) of this section, any generation assignment determined under paragraph (b) or (c) of this section continues to apply in determining whether any subsequent distribution from (or termination of an interest in) the portion of the trust attributable to that transfer is a generation-skipping transfer.

(d) *Example*. The following example illustrates the provisions of this section:

Example. T has a child, C. C has a 20-year-old child, GC. T legally adopts GC and transfers $100,000 to GC. GC's generation assignment is determined by section 2651(b)(1) and GC is assigned to the generation that is two generations below T. In addition, because T has legally adopted GC, GC is generally treated as a child of T under state law. Under these circumstances, GC is an individual who is assigned to more than one generation and the exception in §26.2651–2(b) does not apply. Thus, the special rule under section 2651(f)(1) applies and GC is assigned to the generation that is two generations below T. GC remains a skip person with respect to T and the transfer to GC is a direct skip.

§26.2651–3 Effective dates.

(a) *In general*. The rules of §§ 26.2651–1 and 26.2651–2 are applicable for terminations, distributions, and transfers occurring on or after July 18, 2005.

(b) *Transition rule*. In the case of transfers occurring after December 31, 1997, and before July 18, 2005, taxpayers may

rely on any reasonable interpretation of section 2651(e).

For this purpose, these final regulations, as well as the proposed regulations issued on September 3, 2004, (69 FR 53862) are treated as a reasonable interpretation of the statute.

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

Approved June 30, 2005.

Eric Solomon,
Acting Deputy Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on July 15, 2005, 8:45 a.m., and published in the issue of the Federal Register for July 18, 2005, 70 F.R. 41140)

Section 6343.—Authority to Release Levy and Return Property

26 CFR 301.6343–3: Return of property in certain cases.

T.D. 9213

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 301

Return of Property in Certain Cases

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that amend regulations under section 6343 of the Internal Revenue Code (Code) relating to the return of property in certain cases. The regulations reflect changes made to section 6343 of the Code by the Taxpayer Bill of Rights 2. The regulations also reflect changes affecting levies enacted by the Internal Revenue Service Restructuring and Reform Act of 1998. The regulations affect taxpayers seeking the return of levied property from the Internal Revenue Service (IRS).

DATES: *Effective Date*: These regulations are effective on July 14, 2005.

Applicability Date: For dates of applicability, see §301.6343–3(k).

FOR FURTHER INFORMATION CONTACT: Kevin B. Connelly, (202) 622–3630 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Procedure and Administration Regulations (26 CFR part 301) relating to the return of property under section 6343 of the Code. Section 501(b) of the Taxpayer Bill of Rights 2 (TBOR2), Public Law 104–168 (110 Stat. 1452), amended section 6343 to authorize the IRS to return levied property in certain cases. The purpose of this provision is, to the extent possible, to return the taxpayer to the position the taxpayer would have been in had the levy not been issued. No interest shall be paid with respect to property returned to the taxpayer under this provision. These final regulations reflect the amendments made by section 501(b) of TBOR2.

These regulations also reflect amendments made by the Internal Revenue Service Restructuring and Reform Act (RRA 1998), Public Law 105–206 (112 Stat. 685), which added new sections 6331(i) and (j) to the Code to provide that no levy may be made during the pendency of proceedings for refund of divisible taxes or prior to completion of an investigation of the status of property that is to be sold under section 6335. RRA 1998 also added section 6331(k) to the Code, which provides that no levy may be made during the period an offer-in-compromise or an installment agreement is pending or in effect. In addition, RRA 1998 added section 6330, which provides in certain circumstances for notice and an opportunity for a hearing before a levy can be made.

Explanation of Provisions

On February 14, 2001, a notice of proposed rulemaking (REG–101520–97, 2001–1 C.B. 1057) reflecting these changes was published in the **Federal Register** (66 FR 10249). No written comments were received in response to the notice of proposed rulemaking and no public hearing was requested, scheduled or held. These final regulations adopt the provisions of the notice of proposed rulemaking without change.

Comments on the Proposed Regulation

None

Modifications of Proposed Regulation

None

Special Analyses

It has been determined that this final regulation 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) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Code, the preceding notice of proposed rulemaking was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Kevin B. Connelly, Office of Associate Chief Counsel (Procedure and Administration), Collection Bankruptcy & Summons Division, CC:PA:CBS, IRS.

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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 301.6343–3 is added to read as follows:

§301.6343–3 Return of property in certain cases.

(a) *In general*. If money has been levied upon and applied toward the taxpayer's liability, or property has been levied upon

and sold, and the receipts have been applied toward the taxpayer's liability, or property has been levied upon and purchased by the United States and the United States still possesses the property, and the Commissioner determines that any of the conditions in paragraph (c) of this section exist, the Commissioner may return—

(1) An amount of money equal to the amount of money levied upon;

(2) An amount of money equal to the amount of money received by the United States from a sale of the property; or

(3) The specific property levied upon and purchased by the United States.

(b) *Return of levied upon property in possession of the Internal Revenue Service (IRS) pending sale under section 6335*. Other than as provided in §301.6343–1(b) or in paragraph (d) of this section, the Commissioner, in his or her discretion, may return levied upon property that is in the possession of the United States pending sale under section 6335.

(c) *Conditions authorizing the return of property*. The Commissioner may return property upon determining that one of the following conditions exist:

(1) *Premature or not in accordance with administrative procedures*. The levy was premature or otherwise not in accordance with the administrative procedures of the Secretary.

(2) *Installment agreement*. Subsequent to the levy, the taxpayer enters into an agreement under section 6159 to satisfy the liability for which the levy was made by means of installment payments. If, however, the agreement specifically provides that already levied upon property will not be returned under section 6343(d), the Commissioner may not grant a request for return of property under this paragraph (c)(2).

(3) *Facilitate collection*. The return of property will facilitate the collection of the tax liability for which the levy was made.

(4) *Best interests of the United States and the taxpayer*—(i) *In general*. The taxpayer or the National Taxpayer Advocate (or his or her delegate) has consented to the return of property, and the return of property would be in the best interest of the taxpayer, as determined by the National Taxpayer Advocate (or his or her delegate), and in the best interest of the United States, as determined by the Commissioner.

(ii) *Best interest of the taxpayer*. The National Taxpayer Advocate (or his or her delegate) generally will determine whether the return of property is in the best interest of the taxpayer. If, however, a taxpayer requests the Commissioner to return property and has not specifically requested the National Taxpayer Advocate (or his or her delegate) to determine the taxpayer's best interest, a finding by the Commissioner that the return of property is in the best interest of the taxpayer will be sufficient to support the return of property. Only the National Taxpayer Advocate (or his or her delegate) may determine that a return of property is not in the best interest of the taxpayer.

(5) *Examples*. The following examples illustrate the provisions of this paragraph (c):

Example 1. A owes $1,000 in Federal income taxes. The IRS levies on a broker with respect to a money market account belonging to the taxpayer and receives payment from the broker which it applies to the taxpayer's outstanding liability. However, the IRS failed to follow procedure provided by the Internal Revenue Manual (but not required by statute) with regard to managerial approval prior to the making of the levy. The Commissioner may return an amount of money equal to the amount of money the IRS levied upon and applied toward the taxpayer's tax liability.

Example 2. B owes $1,000 in Federal income taxes. The IRS levies on a bank with respect to a savings account belonging to the taxpayer and receives funds from the bank, which it applies to the taxpayer's liability. Subsequent to the levy, B enters into an installment agreement, under which B will pay timely installments to satisfy the entire liability. The installment agreement does not by its terms preclude the return of levied upon property. The revenue officer verifies that B is financially capable of paying the entire liability, including accruals, in the agreed-upon installment payments. The Commissioner may return an amount of money equal to the amount of money levied upon and applied toward the taxpayer's liability.

Example 3. C owns a house that is deteriorating and in unsalable condition. C is in the process of renovating the house for sale when the IRS levies upon C's bank account for the payment of a $20,000 outstanding Federal tax liability and receives funds in the amount of $3,000, which it applies toward C's liability. A notice of federal tax lien is the only lien encumbrancing the house. C requests that an amount of money equal to the amount seized from the bank account be returned so that C can complete the renovations on the house. Without the funds, C will be unable to complete the renovations and sell the house. Upon examination, the Commissioner determines that the IRS will be able to collect the entire tax liability if C's house is restored to salable condition. If the National Taxpayer Advocate, or the Commissioner in lieu of the National Taxpayer Advocate, determines that the return of the seized money is in the taxpayer's best interest, the Commissioner may return an amount of money equal to the amount seized from the bank account, in the best interest of the taxpayer and the United States.

(d) *Best Interests of the United States and the taxpayer to release levy and return of property where levy made in violation of law*—(1) *In general*. If the IRS makes a levy in violation of the law, it is in the best interests of the United States and the taxpayer to release the levy and the IRS will return to the taxpayer any property obtained pursuant to the levy. For example, the IRS will release the levy and return the taxpayer's property if the levy was made—

(i) Without giving the requisite thirty-day notice of the right to a hearing under section 6330;

(ii) During the pendency of a proceeding for refund of divisible tax in violation of section 6331(i);

(iii) Before investigation of the status of levied upon property in violation of section 6331(j);

(iv) During the pendency of an offer-in-compromise in violation of section 6331(k)(1); or

(v) During the period an offer to enter into an installment agreement is pending (or for 30 days following the rejection of an offer, or, if the rejection is timely appealed, during the period that the appeal is pending) or during the period an installment agreement is in effect (or during the 30 days following a termination or, if a timely appeal of termination is filed, during the period the appeal is pending) in violation of section 6331(k)(2).

(2) *Property may not be credited to outstanding liability without the taxpayer's permission*. When the release of a levy and the return of property are required under this paragraph (d), the property or the proceeds from the sale of the property received by the IRS pursuant to the levy must be returned to the taxpayer unless the taxpayer requests otherwise. The property or proceeds of sale may not be credited to any outstanding tax liability of the taxpayer, including the one with respect to which the IRS made the levy, without the written permission of the taxpayer.

(e) *Time of return*. Levied upon property in possession of the IRS (other than money) may be returned under paragraphs (c) and (d) of this section at any time. An amount of money equal to the amount of money levied upon or received from a sale of property may be returned at any time be-

fore the expiration of 9 months from the date of the levy. When a request for the return of money filed in accordance with paragraph (h) of this section is filed before the expiration of the 9-month period, or a determination to return an amount of money is made before the expiration of the 9-month period, the money may be returned within a reasonable period of time after the expiration of the 9-month period if additional time is necessary for investigation or processing.

(f) *Purchase by the United States*. For purposes of paragraph (a)(2) of this section, if property is declared purchased by the United States at a sale pursuant to section 6335(e)(1)(C), the United States will be treated as having received an amount of money equal to the minimum price determined by the Commissioner before the sale.

(g) *Determinations by the Commissioner*. The Commissioner must determine whether any of the conditions authorizing the return of property exists if a taxpayer submits a request for the return of property in accordance with paragraph (h) of this section. The Commissioner also may make this determination independently. If the Commissioner determines that conditions authorizing the return of property are not present, the Commissioner may not authorize the return of property. If the Commissioner determines that conditions authorizing the return of property are present, the Commissioner may (but is not required to, unless the reason for the return of property is that the levy was made in violation of law and is governed by paragraph (d) of this section) authorize the return of property. If the Commissioner decides independently to return property under paragraph (c)(4) of this section based on the best interests of the taxpayer and the United States, the taxpayer or the National Taxpayer Advocate (or his or her delegate) must consent to the return of property.

(h) *Procedures for request for the return of property*—(1) *Manner*. A request for the return of property must be made in writing to the address on the levy form.

(2) *Form*. The written request must include the following information—

(i) The name, current address, and taxpayer identification number of the person requesting the return of money (or property purchased by the United States);

(ii) A description of the property levied upon;

(iii) The date of the levy; and

(iv) A statement of the grounds upon which the return of money is being requested (or property purchased by the United States).

(i) *No interest*. No interest will be paid on any money returned under this section.

(j) *Administrative collection upon default*. If the Commissioner returns property under this section, and the taxpayer fails to pay the previously assessed liability for which the levy was made on the returned property, the Commissioner may administratively collect the liability. Collection may include levying again on the returned property as long as statutory and administrative requirements are followed.

(k) *Effective date*. This section is applicable on July 14, 2005.

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

Approved June 30, 2005.

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

(Filed by the Office of the Federal Register on July 13, 2005, 8:45 a.m., and published in the issue of the Federal Register for July 14, 2005, 70 F.R. 40669)

Part III. Administrative, Procedural, and Miscellaneous

Information About Additional Criteria That Will be Applied in Selecting Proposals for the Internal Revenue Service's Industry Issue Resolution (IIR) Program

Notice 2005–59

This notice provides information about additional criteria that will be applied in considering proposals regarding accountable plans for the Internal Revenue Service's Industry Issue Resolution (IIR) program. The objective of the IIR Program is to identify frequently disputed or burdensome tax issues that are common to a significant number of business taxpayers that may be resolved through published or other administrative guidance. *See* Rev. Proc. 2003–36, 2003–1 C.B. 859.

During the IIR Pilot Program, the Service initiated a project involving the tax treatment of employer reimbursements of various equipment-related expenses to employees in a segment of the pipeline construction industry. Whether or not such expenses are included in the employee's income and wages is governed generally by whether or not the employer makes payments to the employee under an accountable plan in accordance with the requirements of § 62(c) of the Internal Revenue Code.[1] The industry representatives maintained that their industry practice made compliance with the accountable plan requirements unworkable. As a result of the project, the Service published two pieces of guidance: Rev. Rul. 2002–35, 2002–1 C.B. 1067, making clear that expense reimbursement in the industry is excluded from income and wages only if made in accordance with the accountable plan requirements, and Rev. Proc. 2002–41, 2002–1 C.B. 1098, providing for deemed substantiation of expenses at a specified rate to make it possible for employers in the industry to comply with the accountable plan requirements.

Since the completion of the IIR pilot program, several submissions to the IIR program have asserted that compliance with various aspects of the accountable plan rules set forth under § 62(c) are unduly burdensome for businesses in certain other industries and have asked for published guidance providing administrative relief similar to that provided in Rev. Proc. 2002–41.

The Service provided guidance as part of the IIR pilot project for a segment of the pipeline construction industry because the industry had successfully demonstrated that employers could not comply with the existing accountable plan rules given certain fundamental aspects of their industry practice that could not readily be changed, if changed at all. For purposes of evaluating future IIR submissions raising similar concerns about application of the accountable plan rules in specific industries, the Service will make a comparable assessment as to whether the accountable plan rules are unworkable given aspects of industry practice that cannot be changed at all or cannot be changed without great difficulty. In addition to the requirements of Rev. Proc. 2003–36, factors to be considered in determining whether there is need for relief as to this issue would include, but not be limited to the following:

(a) an established industry history showing that high turnover in the labor force or short-term employment with multiple employers is typical;

(b) large expenses for maintenance, although infrequent, are predictable relative to the compensation paid to the employees for their services;

(c) individual employers are unwilling to reimburse in full for sporadic expenses for equipment maintenance because a significant portion of the reimbursement will accrue to the benefit of a later employer/competitor;

(d) there is a uniformity of expenses across the workforce or the existence of a uniform objective predictive proxy for measuring the expense, and

(e) existing methods of substantiating expenses, such as Rev. Proc. 2004–64, 2004–49 I.R.B. 898 (mileage allowances), do not accurately reflect the expenses incurred by the employees on behalf of the employer.

The mere cost of collecting records, substantiating expenses and reconciling the amount of expenses with the amount of reimbursements paid does not support a claim of burden meriting relief from the requirements of the accountable plan rules.

DRAFTING INFORMATION

The principal author of this notice is Joe Spires of the Office of Associate Chief Counsel (Tax Exempt & Government Entities). For further information regarding this notice, contact Jeanne Royal Singley at (202) 622–0047 (not a toll-free call).

Modification of Notice 2005–4; Biodiesel and Aviation-Grade Kerosene

Notice 2005–62

Section 1. PURPOSE

This notice modifies Notice 2005–4, 2005–2 I.R.B. 289, as modified by Notice 2005–24, 2005–12 I.R.B. 757, by revising the guidance relating to the Certificate for Biodiesel, which is required as a condition for claiming a credit or payment under §§ 6426(c), 6427(e), and 40A of the Internal Revenue Code. This notice also provides guidance on issues related to the biodiesel credit or payment that are not addressed in Notice 2005–4. This notice further modifies Notice 2005–4 relating to the Certificate of Person Buying Aviation-Grade Kerosene for Commercial Aviation or Nontaxable Use, which is required to notify a position holder of certain transactions under §§ 4081 and 4082.

Notice 2005–4 provides guidance on certain excise tax provisions in the Code that were added or affected by the American Jobs Creation Act of 2004 (Pub. L. 108–357) (the Act).

[1] Whether a payment of this type is a rental payment rather than the reimbursement of an employee expense may involve the question whether the worker is serving as an independent contractor or employee. Although these payments in almost every case would not qualify as actual rental payments, it is a highly factual question. *See*, *e.g.*, *Eliseo v. Commissioner*, T.C. Memo. 2000–176. Further, in this context, the Service is restricted from addressing classification of workers by section 530(b) of the Revenue Act of 1978.

Section 2. BIODIESEL CERTIFICATE

(a) Section 2 of Notice 2005–4 provides guidance on credits and payments allowed for biodiesel fuel. Section 2(h) of that notice describes the Certificate for Biodiesel that, under the Code, the claimant must obtain "from" the producer of the biodiesel. This notice revises the certificate to clarify that the claimant may obtain the certificate either directly from the producer of the biodiesel or indirectly from a biodiesel reseller.

(b) Section 2(h) of Notice 2005–4 also requires that each claim contain a statement that the claimant has in its possession an unexpired biodiesel certificate. This notice revises that rule so that the claimant generally must submit a copy of the certificate with its claim.

(c) This notice also provides guidance on accounting for commingled biodiesel.

(d) Finally, this notice provides a transitional rule for claims that were made before August 29, 2005.

(e) Accordingly, section 2(h) of Notice 2005–4 is revised to read as follows:

Section 2. ALCOHOL AND BIODIESEL CLAIMS

* * * * *

(h) *Content of claim; commingled biodiesel*—(1) *In general*. Section 6426(c)(4) of the Code provides that the biodiesel mixture credit of § 6426 is not allowed unless the producer of the mixture obtains a certificate, in such form and manner as may be prescribed by the Secretary, from the producer of the biodiesel that identifies the product produced and the percentage of biodiesel and agri-biodiesel in the product. Section 40A(b)(4) provides a similar rule for the biodiesel mixture credit and biodiesel credit allowed by § 40A. Under this notice, these rules will also apply to the credit or payment allowed for biodiesel mixtures by § 6427(e). Accordingly, each claim for a credit or payment under § 6426, 6427(e), or 40A must contain the following information with respect to biodiesel or a biodiesel mixture covered by the claim:

(i) The amount of agri-biodiesel and the amount of biodiesel other than agri-biodiesel in the biodiesel or biodiesel mixture.

(ii) A copy of the Certificate for Biodiesel described in paragraph (h)(2) of this section and, if applicable, the Statement(s) of Biodiesel Reseller described in paragraph (h)(3) of this section. However, in the case of a certificate and statement that supports a claim made on more than one claim form, the certificate and statement are to be included with the first claim and the claimant is to provide information related to the certificate on any subsequent claim in accordance with the instructions applicable to the claim form.

(iii) A statement by the claimant that the claimant has no reason to believe that any information in the certificate (described in paragraph (h)(2) of this section) or statement (described in paragraph (h)(3) of this section) is false.

(2) *Certificate for Biodiesel*—(i) *In general*. The certificate to be obtained by the claimant claiming a credit or payment under § 6426, 6427(e), or 40A consists of a statement that is signed under penalties of perjury by a person with authority to bind the biodiesel producer, is substantially in the same form as the model certificate in paragraph (h)(2)(ii) of this section, and contains all the information necessary to complete such model certificate. In the case of a claimant that is the producer of the biodiesel, the information required on lines 2–7 of the model certificate is not applicable and those lines do not need to be completed. The certificate identification number is determined by the producer and must be unique to each certificate. A biodiesel producer may, with respect to a particular sale of biodiesel, provide multiple separate certificates, each applicable to a portion of the total volume of biodiesel sold. Thus, for example, a biodiesel producer that sells 5,000 gallons of biodiesel may provide its buyer with five certificates for 1,000 gallons each. The multiple certificates may be provided either to the buyer at or after the time of sale or to a reseller in the circumstances described in paragraph (h)(3)(i) of this section.

(ii) *Model certificate*.

CERTIFICATE FOR BIODIESEL

Certificate Identification Number: _____

(To support a claim related to biodiesel or a biodiesel mixture under the Internal Revenue Code)

The undersigned biodiesel producer ("Producer") hereby certifies the following under penalties of perjury:

1. _____

_____

_____

Producer's name, address, and employer identification number

2. _____

_____

_____

Name, address, and employer identification number of person buying the biodiesel from Producer

3. _____

Date and location of sale to buyer

4. This certificate applies to _____ gallons of biodiesel.

5. Producer certifies that the biodiesel to which this certificate relates is:

_____% Agri-biodiesel (derived solely from virgin oils)

_____% Biodiesel other than agri-biodiesel

This certificate applies to the following sale:

_____ Invoice or delivery ticket number

_____ Total number of gallons of biodiesel sold under that invoice or delivery ticket number (including biodiesel not covered by this certificate)

_____ Total number of certificates issued for that invoice or delivery ticket number

6. _____

_____

_____

Name, address, and employer identification number of reseller to whom certificate is issued (only in the case of certificates reissued to a reseller after the return of the original certificate)

7. _____ Original Certificate Identification Number (only in the case of certificates reissued to a reseller after return of the original certificate)

Producer is registered as a biodiesel producer with registration number _____. Producer's registration has not been suspended or revoked by the Internal Revenue Service.

Producer certifies that the biodiesel to which this certificate relates is monoalkyl esters of long chain fatty acids derived from plant or animal matter that meets the requirements of the American Society of Testing and Materials D6751 and the registration requirements for fuels and fuel additives established by EPA under section 211 of the Clean Air Act (42 U.S.C. 7545).

Producer understands that the fraudulent use of this certificate may subject Producer and all parties making any fraudulent use of this certificate to a fine or imprisonment, or both, together with the costs of prosecution.

_____

Printed or typed name of person signing this certificate

_____

Title of person signing

_____

Signature and date signed

(3) *Statement of Biodiesel Reseller*—(i) *In general*. A person that receives a Certificate for Biodiesel, and subsequently sells the biodiesel without producing a biodiesel mixture or claiming the biodiesel credit, is to give the certificate and a statement that satisfies the requirements of this paragraph (h)(3) to its buyer. The statement must contain all of the information necessary to complete the model certificate in paragraph (h)(3)(iii) of this section and be attached to the Certificate for Biodiesel. A reseller cannot make multiple copies of a Certificate for Biodiesel to divide the certificate between multiple buyers. If a single Certificate for Biodiesel applies to biodiesel that a reseller expects to sell to multiple buyers, the reseller should return the certificate (together with any statements provided by intervening resellers) to the producer who may reissue to the reseller multiple Certificates for Biodiesel in the appropriate volumes. The reissued certificates must include the Certificate Identification Number from the certificate that has been returned.

(ii) *Withdrawal of the right to provide a certificate*. The Internal Revenue Service may withdraw the right of a buyer of biodiesel to provide the certificate and a statement under this section if the Internal Revenue Service cannot verify the accuracy of the buyer's statements. The Internal Revenue Service may notify any person to whom the buyer has provided a statement that the buyer's right to provide the certificate and a statement has been withdrawn.

(iii) *Model statement of biodiesel reseller.*

STATEMENT OF BIODIESEL RESELLER

(To support a claim related to biodiesel or a biodiesel mixture under the Internal Revenue Code)

The undersigned biodiesel producer ("Reseller") hereby certifies the following under penalties of perjury:

1. _____

_____

_____

Resellers's name, address, and employer identification number

2. _____

_____

_____

Name, address, and employer identification number of Reseller's buyer

3. _____

Date and location of sale to buyer

4. _____

Volume of biodiesel sold

5. _____

Certificate Identification Number on the Certificate for Biodiesel

Reseller has bought the biodiesel described in the accompanying Certificate for Biodiesel and Reseller has no reason to believe that any information in the certificate is false.

Reseller has not been notified by the Internal Revenue Service that its right to provide a certificate and a statement has been withdrawn.

Reseller understands that the fraudulent use of this statement may subject Reseller and all parties making any fraudulent use of this statement to a fine or imprisonment, or both, together with the costs of prosecution.

_____

Printed or typed name of person signing this certificate

_____

Title of person signing

_____

Signature and date signed

(4) *Commingled biodiesel*—(i) *In general*. For purposes of this paragraph (h)(4), *commingled biodiesel* means—

(A) Biodiesel held by its producer in a storage tank that is used to store both agri-biodiesel and biodiesel other than agri-biodiesel; and

(B) Biodiesel held by a person other than its producer in a storage tank unless a single Certificate for Biodiesel applies to the tank.

(ii) *Reasonable methods may be used to identify commingled biodiesel*. A person that holds commingled biodiesel may identify the biodiesel it sells or uses by any reasonable method, including a first-in, first-out method applied either on a tank-by-tank basis or on an aggregate basis to all commingled biodiesel the person holds. Thus, for example, a reseller may treat the biodiesel it first purchases as the first biodiesel it resells, and a biodiesel mixture producer may treat the biodiesel it first purchases as the first biodiesel it uses to produce a biodiesel mixture.

(5) *Effective date*. This paragraph (h) of this section applies with respect to biodiesel sold or used by its producer after August 29, 2005, but taxpayers may rely on it as if it were applicable with respect to biodiesel sold or used by its producer on or before that date. In addition, the Internal Revenue Service may accept claims relating to biodiesel sold or used by its producer on or before August 29, 2005 if the claim evidences a good faith effort to comply with the applicable Code provision or the rules of Notice 2005–4 as in effect before August 29, 2005 and the Service can reasonably verify the amount of biodiesel and agri-biodiesel covered by the claim.

* * * * *

Section 3. DEFINITION OF A BIODIESEL MIXTURE

(a) *Definition in the Code*. Section 6426(c)(3) provides that *biodiesel mixture* means a mixture of biodiesel and diesel fuel (as defined in § 4083(a)(3)), determined without regard to any use of kerosene, that (1) is sold by the taxpayer producing the mixture to any person for

use as a fuel, or (2) is used as a fuel by the taxpayer producing the mixture.

(b) *Explanation of terms*—(1) The diesel fuel in a biodiesel mixture may be either dyed or undyed. However, taxpayers are reminded of the penalty in § 6715 for the willful alteration of the strength or composition of any dye in dyed fuel. Also see § 48.6715–1 of the Manufacturers and Retailers Excise Tax Regulations.

(2) A biodiesel mixture generally is used as a fuel when it is consumed to produce energy. Thus, for example, a biodiesel mixture that is consumed in a furnace to produce heat is used as a fuel. However, the destruction of a biodiesel mixture in a fire or other casualty loss is not treated as use as a fuel.

(3) A biodiesel mixture is a mixture of biodiesel and diesel fuel containing at least 0.1 percent (by volume) of diesel fuel. Thus, for example, a mixture of 999 gallons of biodiesel and 1 gallon of diesel fuel is a biodiesel mixture.

(4) Kerosene in a mixture of biodiesel and diesel fuel is not included in the volume for purposes of determining whether the biodiesel mixture satisfies the volume requirements set forth in paragraph (b)(3) of this section. Further, the gallons of kerosene in the mixture of biodiesel and diesel fuel are not included in the gallons of biodiesel for which a credit or payment is allowed.

(c) *Effective date*—(1) *In general*. Paragraphs (b)(1), (2), and (4) of this section are applicable January 1, 2005, the effective date of Notice 2005–4. Paragraph (b)(3) of this section applies with respect to mixtures produced after August 29, 2005 and, except as provided in paragraph (c)(2) of this section, is not taken into account in determining the tax treatment of any mixture produced on or before that date.

(2) *Reliance permitted in certain cases*. A taxpayer may rely on paragraph (b)(3) of this section to claim a biodiesel mixture credit for a mixture produced on or before August 29, 2005 if the taxpayer has not taken any action inconsistent with the claim requirements under this notice such as providing a Certificate for Biodiesel or a Statement of Biodiesel Reseller with respect to the biodiesel in the mixture.

Section 4. DEFINITION OF AGRI-BIODIESEL

(a) *In general*. Section 40A(d)(2) defines *agri-biodiesel* as meaning biodiesel derived solely from virgin oils, "including" esters derived from virgin vegetable oils from corn, soybeans, sunflower seeds, cottonseeds, canola, crambe, rapeseeds, safflowers, flaxseeds, rice bran, and mustard seeds, and from animal fats. The language "including" indicates that this list is not exclusive. Thus, for example, biodiesel derived solely from virgin oils includes esters derived from palm oil and fish oil.

(b) *Commingled feedstock*. If virgin oils and recycled oils are commingled for use as a feedstock in the production of biodiesel, the biodiesel is not derived solely from virgin oils as required by § 40A(d)(2).

(c) *Effective date*. Paragraph (a) of this section is applicable January 1, 2005, the effective date of Notice 2005–4. Paragraph (b) of this section applies with respect to biodiesel produced after August 29, 2005.

Section 5. CLAIMS FOR PAYMENTS THAT EXCEED THE ALLOWABLE CREDIT

(a) *Background*. Section 6426 generally allows a biodiesel mixture credit against any tax imposed by § 4081, including those taxes unrelated to biodiesel mixtures or alcohol mixtures. The § 6426 credit is claimed on a Form 720, *Quarterly Federal Excise Tax Return*, which is filed at the end of each quarter. Section 6427(e)(1) generally allows a payment relating to a person's production of a biodiesel mixture. The § 6427(e)(1) payment may be claimed before Form 720 is due and as often as once a week if certain conditions are met. However, § 6427(e)(2) provides that no amount is payable under § 6427(e)(1) for any mixture with respect to which an amount is allowed as a credit under § 6426. If a claim is made under § 6427(e) for an amount that is allowable as a credit under § 6426, section 2(d)(2) of Notice 2005–4 provides that payment under § 6427(e) is treated as an excessive amount under § 6206. Unless this excessive amount is repaid with interest before the due date of the Form 720 on which the credit under § 6426 is allowable, it may be assessed as if it were a tax imposed by § 4081 and a penalty under § 6675 may be imposed.

(b) *Computation of payment limitation*. A person producing biodiesel mixtures outside the bulk transfer/terminal system and liable for tax imposed by § 4081 solely because of the removal or sale of the mixtures can avoid making excessive claims for payment under § 6427(e) by limiting claims filed on a form other than Form 720 to—

(1) 75.6 percent of the total credits and payments allowable with respect to agri-biodiesel used to produce the mixtures (24.4 percent of the allowable credits and payments must be claimed on Form 720); and

(2) 51.2 percent of the total credits and payments allowable with respect to biodiesel other than agri-biodiesel used to produce the mixtures (48.8 percent of the allowable credits and payment must be claimed on Form 720).

(c) *Example*. The following example illustrates the application of this section:

(1) *P* is a biodiesel mixture producer. *P* produces blended taxable fuel outside of the bulk transfer/terminal system by adding biodiesel to taxed diesel fuel. See §§ 48.4081–1(c)(1) and 48.4081–3(g). *P* has no § 4081 liability other than its liability as a blender on its sale of the biodiesel mixture. During the period August 1 through August 10, 2005, *P* uses 5,000 gallons of agri-biodiesel to produce a biodiesel mixture. The total of the credits and payments allowable with respect to the biodiesel used to produce the mixture is $5,000 (5,000 x $1.00).

(2) On August 11, *P* files Form 8849, *Claim for Refund of Excise Taxes*, for the period August 1 – August 10. To avoid an excessive claim, *P* limits the claim on Form 8849 to $3,780 (75.6 percent of $5,000) reporting 3,780 gallons of agri-biodiesel.

(3) On Form 720, *Quarterly Federal Excise Tax Return*, *P* reports liability for IRS No. 60(c) of $1,220 (5,000 gallons x $.244) and claims a credit on Schedule C for $1,220 (24.4 percent of $5,000) for the period August 1 – August 10, reporting on Schedule C 1,220 gallons of agri-biodiesel.

(d) *Effective date*. This section is applicable January 1, 2005, the effective date of Notice 2005–4.

Section 6. AVIATION-GRADE KEROSENE

(a) *In general*—(1) Section 4 of Notice 2005–4 provides guidance on the taxation of aviation-grade kerosene under the Act. Under sections 4(d) and 4(e), a position holder is not liable for tax if, among other conditions, it obtains a certificate from the

operator of the aircraft into which the aviation-grade kerosene is delivered. This certificate, described in section 4(g), is signed by the aircraft operator and includes the name of the position holder.

(2) In a so-called "flash title transaction," the position holder sells (as defined in § 48.0–2(a)(5)) the aviation-grade kerosene to a wholesale distributor (reseller) that in turn sells the kerosene to the aircraft operator as the kerosene is being removed from a terminal into the fuel tank of an aircraft.

(3) For purposes of determining whether the conditions of sections 4(d)(1)(ii) and 4(e)(2) of Notice 2005–4 are met in a case described in paragraph (a)(2) of this section, the position holder will be treated as having a certificate (in the form described in section 4(g)) from the operator of the aircraft if: (i) the aircraft operator puts the reseller's name, address, and employer identification number on the certificate in place of the position holder's name, address, and employer identification number; and (ii) the reseller provides the position holder with a statement of aviation-grade kerosene reseller. The reseller statement is a statement that is signed under penalties of perjury by a person with authority to bind the reseller; is provided at the bottom or on the back of the certificate (or in an attached document); and contains the reseller's name, address, and employer identification number, the position holder's name, address, and employer identification number, and a statement that the reseller has no reason to believe that any information in the accompanying aircraft operator's certificate is false.

(b) *Effective date*. This section is applicable August 29, 2005.

Section 7. CORRECTION TO NOTICE 2005–4

The last sentence of section 2(a) of Notice 2005–4 is revised to read as follows: Under the Code's coordination rules, the sum of all credits and payments per gallon of alcohol or biodiesel may not exceed the credit rate per gallon prescribed in § 40 or 40A, whichever is applicable.

Section 8. PAPERWORK REDUCTION ACT

The collection of information contained in this notice has been reviewed and approved by the office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545–1915.

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

The collections of information in this notice are in the following sections.

Section 2 of the notice describes the statement that the biodiesel reseller must give to its buyer with respect to the biodiesel mixture credit or biodiesel credit.

Section 6 of the notice describes the statement that an aviation-grade kerosene reseller must give to the position holder of aviation grade kerosene.

The collections of information are required to obtain a tax benefit. This information will be used to substantiate claims for the tax benefits. The likely respondents are businesses, not-for-profit institutions, and state, local, or tribal governments.

The estimated total annual reporting and or recordkeeping burden is 5,100 hours.

The estimated average annual burden per respondent and/or recordkeeper is approximately is .25 hours.

The estimated number of respondents and recordkeepers is 240.

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

Section 9. EFFECT ON OTHER DOCUMENTS

Notice 2005–4 is modified as described in sections 2, 6, and 7 of this notice.

Section 10. DRAFTING INFORMATION

The principal authors of this notice are Susan Athy and Deborah Karet of the Office of the Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, please contact Ms. Athy (regarding biodiesel) or Ms. Karet (regarding aviation-grade kerosene) at (202) 622–3130 (not a toll-free call).

Weighted Average Interest Rates Update

Notice 2005–63

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

CORPORATE BOND WEIGHTED AVERAGE INTEREST RATE

Sections 412(b)(5)(B)(ii) and 412(l)(7)(C)(i), as amended by the Pension Funding Equity Act of 2004, provide that the interest rates used to calculate current liability and to determine the required contribution under § 412(l) for plan years beginning in 2004 or 2005 must be within a permissible range based on the weighted average of the rates of interest on amounts invested conservatively in long term investment grade corporate bonds during the 4-year period ending on the last day before the beginning of the plan year.

Notice 2004–34, 2004–1 C.B. 848, provides guidelines for determining the corporate bond weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability. That notice establishes that the corporate bond weighted average is based on the monthly composite corporate bond rate derived from designated corporate bond indices.

The composite corporate bond rate for July 2005 is 5.37 percent. Pursuant to Notice 2004–34, the Service has determined this rate as the average of the monthly yields for the included corporate bond indices for that month.

The following corporate bond weighted average interest rate was determined for

plan years beginning in the month shown below.

For Plan Years Beginning in: Month	Year	Corporate Bond Weighted Average	90% to 100% Permissible Range
August	2005	5.87	5.28 to 5.87

30-YEAR TREASURY SECURITIES WEIGHTED AVERAGE INTEREST RATE

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

Section 404(a)(1) of the Code, as amended by the Pension Funding Equity Act of 2004, permits an employer to elect to disregard subclause (II) of § 412(b)(5)(B)(ii) to determine the maximum amount of the deduction allowed under § 404(a)(1).

The rate of interest on 30-year Treasury securities for July 2005 is 4.41 percent. Pursuant to Notice 2002–26, 2002–1 C.B. 743, the Service has determined this rate as the monthly average of the daily determination of yield on the 30-year Treasury bond maturing in February 2031.

The following 30-year Treasury rates were determined for the plan years beginning in the month shown below.

For Plan Years Beginning in: Month	Year	30-Year Treasury Weighted Average	90% to 105% Permissible Range	90% to 110% Permissible Range
August	2005	4.94	4.44 to 5.18	4.44 to 5.43

Drafting Information

The principal authors of this notice are Paul Stern and Tony Montanaro of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 (a toll-free number), between the hours of 8:00 a.m. and 6:30 p.m. Eastern time, Monday through Friday. Mr. Stern may be reached at 1–202–283–9703. Mr. Montanaro may be reached at 1–202–283–9714. The telephone numbers in the preceding sentences are not toll-free.

26 CFR 601.602: Tax forms and instructions.
(Also Part 1, §§ 6012, 6061, 6033, 1.6011–1(a), 1.6012–5, 301.6061–1(b).)

Rev. Proc. 2005–60

TABLE OF CONTENTS

SECTION 1. PURPOSE

.01 This revenue procedure informs Authorized IRS *e-file* Providers of their obligations to the Internal Revenue Service (the Service), taxpayers, and other participants in the IRS *e-file* Program. This revenue procedure combines the rules governing IRS *e-file*, including the rules regulating Authorized IRS *e-file* Providers that facilitate the electronic filing of:

(1) Form 1040 and 1040A, *U.S. Individual Income Tax Return*, and Form 1040EZ, *Income Tax Return for Single and Joint Filers With No Dependents*, previously contained in Publication 1345, *Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns*, and Rev. Proc. 2000–31, 2000–2 C.B. 146;

(2) Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, previously contained in Rev. Proc. 2001–9, 2001–1 C.B. 328; and

(3) the rules governing electronic filing for the Form 941, *Employer's Quarterly Federal Tax Return*, previously contained in Rev. Proc. 99–39, 1999–2 C.B. 532.

.02 This revenue procedure also regulates Authorized IRS *e-file* Providers that facilitate the electronic filing of:

(1) Form 1120, *U.S. Corporation Income Tax Return*;

(2) Forms 1120S, *U.S. Income Tax Return for an S Corporation*;

(3) Form 990, *Return of Organization Exempt From Income Tax*; and

(4) Form 990–PF, *Return of Private Foundation or Section 4947(a)(1) Trust Treated as a Private Foundation*.

.03 IRS *e-file* allows return filers to file their returns through an ERO, or by using a personal computer, modem or the Internet, and commercial tax preparation software. The returns that can be filed under IRS *e-file* include:

(1) Form 56, *Notice Concerning Fiduciary Relationship*;

(2) Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*;

(3) Form 941, *Employer's Quarterly Federal Tax Return*;

(4) Form 990, *Return of Organization Exempt From Income Tax*;

(5) Form 990–EZ, *Short Form Return of Organization Exempt From Income Tax*;

(6) Form 990–PF, *Return of Private Foundation or Section 4947(a)(1) Trust Treated as a Private Foundation*;

(7) Forms 1040 and 1040A, *U.S. Individual Income Tax Return*;

(8) Form 1040EZ, *Income Tax Return for Single and Joint Filers With No Dependents*;

(9) Form 1065, *U.S. Return of Partnership Income*;

(10) Form 1120, *U.S. Corporation Income Tax Return*;

(11) Form 1120–POL, *U.S. Income Tax Return for Certain Political Organizations*;

(12) Form 1120S, *U.S. Income Tax Return for an S Corporation*;

(13) Form 1041, *U.S. Income Tax Return for Estates and Trusts*;

(14) Form 1065, *U.S. Return of Partnership Income*;

(15) Form 2350, *Application for Extension of Time to File U.S. Income Tax Return* (or any successor form);

(16) Form 2688, *Application for Additional Extension of Time To File U.S. Individual Income Tax Return* (or any successor form);

(17) Form 4868, *Application for Automatic Extension of Time to File U.S. Individual Income Tax Return* (or any successor form);

(18) Form 7004, *Application for Automatic Extension of Time to File Corporation Income Tax Return* (or any successor form);

(19) Form 8868, *Application for Extension of Time To File an Exempt Organization Return* (or any successor form); and

(20) Form 9465, *Installment Agreement Request.*

.04 This revenue procedure does not cover procedures governing electronic filing of Form 1040NR, *U.S. Nonresident Alien Income Tax Return*. For procedures governing the electronic filing of Form 1040NR, see Rev. Proc. 2000–24, 2000–1 C.B. 1133.

.05 This revenue procedure also does not cover providers of information returns that are filed under the FIRE (Filing Information Returns Electronically) Program. The information returns not covered by this revenue procedure include:

(1) Form 1042–S, *Foreign Person's U.S. Source Income Subject to Withholding*;

(2) Form 1098, *Mortgage Interest Statement*;

(3) Form 5498, *Individual Retirement Arrangement Contribution Information*;

(4) Form 8027, *Employer's Annual Information Return of Tip Income and Allocated Tips*;

(5) Form W–2G, *Certain Gambling Winnings*; and

(6) Questionable Forms W–4, *Employee's Withholding Allowance Certificate*. See Publication 1220, *Specifications for Filing Forms 1098, 1099, 5498 and W2–G Magnetically or Electronically*.

SECTION 2. BACKGROUND AND CHANGES

.01 Section 1.6011–1(a) of the Income Tax Regulations provides that every person subject to income tax must make a return or statement as required by the regulations. The return or statement must include the information required by the applicable regulations or forms.

.02 Section 301.6061–1(b) of the Regulations on Procedure and Administration authorizes the Secretary to prescribe in forms, instructions, or other appropriate guidance the method of signing any return, statement, or other document required to be made under any provision of the internal revenue laws or regulations.

.03 Section 1.6012–5 provides that the Commissioner may authorize the use, at

the option of a person required to make a return, of a composite return in lieu of any form specified in 26 CFR Part 1 (Income Tax), subject to such conditions, limitations, and special rules governing the preparation, execution, filing, and correction thereof as the Commissioner may deem appropriate.

.04 Section 6011(e)(1) of the Internal Revenue Code (the Code) gives specific authority for the Service and the Treasury Department to "prescribe regulations providing standards for determining which returns must be filed on magnetic media or in other machine-readable form." On January 12, 2005, the Service and the Treasury Department published in the Federal Register (T.D. 9175, 2005–10 I.R.B. 665 [70 FR 2012–01]) temporary regulations mandating the electronic filing of certain Forms 1120, 1120S, 990 and 990–PF under sections 301.6011–5T, 301.6037–2T, and 301.6033–4T. On November 12, 1999, the Service and the Treasury Department also published in the Federal Register (T.D. 8843, 1999–2 C.B. 590 [64 FR 61502]) final regulations mandating the electronic filing of certain Forms 1065 under section 301.6011–3.

.05 This revenue procedure combines the rules governing IRS *e-file* including the rules governing electronic filing of:

(1) Form 1040 and 1040A, *U.S. Individual Income Tax Return*, and Form 1040EZ, *Income Tax Return for Single and Joint Filers With No Dependents*, contained in Publication 1345, *Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns*, and Rev. Proc. 2000–31, 2000–2 C.B. 146;

(2) Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, contained in Rev. Proc. 2001–9; and

(3) Form 941, *Employer's Quarterly Federal Tax Return*, contained in Rev. Proc. 99–39.

.06 This revenue procedure also includes the rules governing electronic filing of:

(1) Form 990, *Return of Organization Exempt From Income Tax*;

(2) Form 990–EZ, *Short Form Return of Organization Exempt From Income Tax*;

(3) Form 990–PF, *Return of Private Foundation or Section 4947(a)(1) Trust Treated as a Private Foundation*;

(4) Form 1041, *U.S. Income Tax Return for Estates and Trusts*;

(5) Form 1065, *U.S. Return of Partnership Income*;

(6) Form 1120, *U.S. Corporation Income Tax Return*;

(7) Form 1120–POL, *U.S. Income Tax Return for Certain Political Organizations*; and

(8) Form 1120S, *U.S. Income Tax Return for an S Corporation*.

.07 Many of the rules governing participation in IRS *e-file* are now set forth in IRS Publications. See section 5.01 of this revenue procedure.

SECTION 3. DEFINITIONS

.01 Authorized IRS *e-file* Provider. A participant in IRS *e-file* is referred to as an "Authorized IRS *e-file* Provider." The five categories of Authorized IRS *e-file* Providers are:

(1) ELECTRONIC RETURN ORIGINATOR. An Electronic Return Originator (ERO) originates the electronic submission of returns.

(2) INTERMEDIATE SERVICE PROVIDER. An Intermediate Service Provider receives tax return information from an ERO (or from a taxpayer or tax exempt organization that files electronically using a personal computer, modem or the Internet, and commercial tax preparation software), processes the return information, and either forwards the information to a Transmitter, or sends the information back to the ERO (or taxpayer or exempt organization).

(3) SOFTWARE DEVELOPER. A Software Developer develops software for the purposes of (a) formatting electronic return information according to publications issued by the Service that set forth electronic return file specifications and record layouts for tax returns; and/or (b) transmitting electronic tax return information directly to the Service.

(4) TRANSMITTER. A Transmitter transmits electronic return information directly to the Service.

(5) REPORTING AGENT. A Reporting Agent is an accounting service, franchiser, bank, service bureau, or other entity that complies with Rev. Proc. 2003–69, 2003–2 C.B. 403, and is authorized to perform one or more of the acts listed in Rev. Proc. 2003–69 on behalf of a taxpayer.

The five categories of Authorized IRS *e-file* Providers are not mutually exclusive. For example, an ERO can, at the same time, be a Transmitter, Software Developer, or Intermediate Service Provider depending on the function(s) performed.

.02 Responsible Official. A Responsible Official is an individual with authority over the IRS *e-file* operation of the office(s) of the Authorized IRS *e-file* Provider, is the first point of contact with the Service, and has authority to sign revised IRS *e-file* applications. A Responsible Official is responsible for ensuring that the Authorized IRS *e-file* Provider adheres to the provisions of this revenue procedure and the publications and notices governing the IRS *e-file* Program.

SECTION 4. ACCEPTANCE TO PARTICIPATE IN THE IRS *e-file* PROGRAM

.01 Sole proprietors, businesses, and organizations that wish to become an Authorized IRS *e-file* Provider must apply for participation and must be accepted by the Service.

.02 The procedures governing application to the IRS *e-file* Program are included in Publication 3112, *IRS e-file Application and Participation*.

.03 The circumstances under which the Service may deny participation in the IRS *e-file* Program are also included in Publication 3112. An applicant who is denied participation may seek administrative review of the denial. See section 8 of this revenue procedure.

.04 To continue participation in the IRS *e-file* Program, an Authorized IRS *e-file* Provider must adhere to all requirements of this revenue procedure and the publications and notices governing IRS *e-file*.

SECTION 5. RESPONSIBILITIES OF AN AUTHORIZED IRS *e-file* PROVIDER

.01 To ensure that returns are accurately and efficiently filed, an Authorized IRS *e-file* Provider must comply with the provisions of this revenue procedure and all publications and notices governing IRS *e-file*. The Service will from time to time update such publications and notices to reflect changes to the program. It is the responsibility of the Authorized IRS *e-file* Provider to ensure that it complies with the latest version of all publications and

notices. The publications and notices governing the IRS *e-file* Program include:

(1) Publication 1345, *Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns*;

(2) Publication 1345A, *Filing Season Supplement for Authorized IRS e-file Providers of Individual Income Tax Returns*;

(3) Publication 1346, *Electronic Return File Specifications and Record Layouts for Individual Income Tax Returns*;

(4) Publication 1436, *Test Package for Electronic Filers of Individual Income Tax Returns*;

(5) Publication 1437, *Procedures for the 1041 e-file Program, U.S. Income Tax Return for Estates and Trusts*;

(6) Publication 1438, *File Specifications, Validation Criteria and Record Layouts for the 1041 e-file Program, U.S. Income Tax Return for Estates and Trusts*;

(7) Publication 1438–A, *(Supplement) 1041 e-file Program, U.S. Income Tax Return for Estates and Trusts*;

(8) Publication 1474, *Technical Specifications Guide For Reporting Agent Authorization For Magnetic Tape/Electronic Filers and Federal Tax Depositors*;

(9) Publication 1524, *Procedures for 1065 e-file Program, U.S. Return of Partnership Income*;

(10) Publication 1525, *File Specifications, Validation Criteria and Record Layouts for the 1065 e-file Program, U.S. Return of Partnership Income*;

(11) Publication 1855, *Technical Specifications Guide for the Electronic Filing of Form 941, Employer's Quarterly Federal Tax Return*;

(12) Publication 3112, *IRS e-file Application and Participation*;

(13) Publication 3416, *1065 e-file Program, U.S. Return of Partnership Income (Publication 1525 Supplement)*;

(14) Publication 3715, *Technical Specifications Guide for the Electronic Filing of Form 940, Employer's Federal Unemployment (FUTA) Tax Return*;

(15) Publication 3823, *Employment Tax e-file System Implementation and User Guide*;

(16) Publication 4162, *Modernized e-File Test Package for Forms 1120/1120S*;

(17) Publication 4163, *Modernized e-File Information for Authorized IRS e-file Providers of Forms 1120/1120S*;

(18) Publication 4164, *Modernized e-File Guide for Software Developers and Transmitters*;

(19) Publication 4205, *Modernized e-File Test Package for Exempt Organization Filings*;

(20) Publication 4206, *Modernized e-File Information for Authorized IRS e-file Providers of Exempt Organization Filings*; and

(21) Postings to the IRS web site at: *http://www.irs.gov* on the Internet, and published guidance in the Internal Revenue Bulletin and the Federal Register.

.02 The publications and notices listed in section 5.01 supplement this revenue procedure. A violation of any provision of these publications and notices is considered a violation of this revenue procedure and may subject an Authorized IRS *e-file* Provider to the sanctions provided in section 7 of this revenue procedure.

.03 The security of taxpayer accounts and personal information is a top priority for the IRS. It is the responsibility of each Authorized IRS *e-file* Provider to have security systems in place to prevent unauthorized access to taxpayer accounts and personal information by third parties. The Gramm-Leach-Bliley Act, codified at 15 U.S.C. §§ 6801–6827, includes rules applicable to Authorized IRS *e-file* Providers that are designed to ensure the security and privacy of taxpayer information. Violation of the provisions of the Gramm-Leach-Bliley Act and the implementing rules and regulations promulgated by the Federal Trade Commission, or violations of the non-disclosure rules contained in sections 6713 or 7216 or the regulations promulgated thereunder, are considered violations of this revenue procedure and may subject an Authorized IRS *e-file* Provider to the sanctions provided in section 7 of this revenue procedure. See section 6.01 of this revenue procedure.

.04 In addition to the responsibilities defined in 5.01, 5.02, and 5.03 above, additional Authorized IRS *e-file* Providers responsibilities may be defined in statutes and regulations.

SECTION 6. PENALTIES

.01 Penalties for Disclosure or Use of Information.

(1) An Authorized IRS *e-file* Provider, except a Software Developer that does not have access to taxpayer information, is a tax return preparer under the definition of section 301.7216–1(b)(2). Tax return preparers are subject to criminal penalties for unauthorized disclosure or use of tax return information. See section 7216 of the Internal Revenue Code and section 301.7216–1(a). In addition, section 6713 establishes civil penalties for unauthorized disclosure or use of income tax return information by tax return preparers.

(2) Under section 301.7216–2(h), disclosure of tax return information among Authorized IRS *e-file* Providers for the purpose of electronically filing a return is permissible. For example, an ERO may pass on tax return information to an Intermediate Service Provider and/or a Transmitter for the purpose of having an electronic return formatted and transmitted to the Service.

.02 Other Preparer Penalties.

(1) Preparer penalties may be asserted against an individual or firm meeting the definition of an income tax return preparer under section 7701(a)(36) and section 301.7701–15. Preparer penalties that may be asserted under appropriate circumstances include, but are not limited to, those set forth in sections 6694, 6695, and 6713.

(2) Under section 301.7701–15(d)(1), Authorized IRS *e-file* Providers are not income tax return preparers for the purpose of assessing most preparer penalties as long as their services are limited to "typing, reproduction, or other mechanical assistance in the preparation of a return or claim for refund."

(3) If an ERO, Intermediate Service Provider, Transmitter, or the product of a Software Developer alters the income tax return information in a nonsubstantive way, this alteration will be considered to come under the "mechanical assistance" exception described in section 301.7701–15(d)(1), and will not cause an Authorized IRS *e-file* Provider to become an income tax preparer. A nonsubstantive change is a correction or change limited to a transposition error, misplaced entry, spelling error, or arithmetic correction.

(4) If an ERO, Intermediate Service Provider, Transmitter, or the product of a Software Developer alters income tax return information in a way that does not come under the "mechanical assistance" exception, such Authorized IRS *e-file*

Provider may be held liable for income tax return preparer penalties. See section 301.7701–15; Rev. Rul. 85–189, 1985–2 C.B. 341 (describing a situation where a Software Developer was determined to be an income tax return preparer and subject to certain preparer penalties).

.03 Other Penalties. In addition to the above specified provisions, the Service may assert all appropriate preparer, nonpreparer, and disclosure penalties against an Authorized IRS *e-file* Provider as warranted under the circumstances.

SECTION 7. MONITORING AND SANCTIONING AN AUTHORIZED IRS *e-file* PROVIDER

.01 The Service will monitor Authorized IRS *e-file* Providers for compliance with the rules governing IRS *e-file*. The Service may sanction an Authorized IRS *e-file* Provider for violating any provision of this revenue procedure or the publications and notices governing IRS *e-file*.

.02 Sanctions that the Service may impose upon an Authorized IRS *e-file* Provider for violations described in section 7.01 of this revenue procedure include a written reprimand, suspension or expulsion from the program, and other sanctions, depending on the severity of the infraction. Publication 3112 describes the infraction categories and the rules governing the imposition of sanctions.

SECTION 8. ADMINISTRATIVE REVIEW PROCESS

.01 An applicant that has been denied participation in IRS *e-file* (see section 4.03 of this revenue procedure) has the right to an administrative review. During the administrative review process, the denial of participation remains in effect.

.02 An Authorized IRS *e-file* Provider may seek administrative review for any sanction the Service may impose under section 7 of this revenue procedure.

.03 Publication 3112 describes the procedures regarding administrative review of a denial of participation in IRS *e-file* and any sanction imposed by the Service.

SECTION 9. PILOT PROGRAMS

.01 The Service regularly conducts pilot programs to introduce new technology into the IRS *e-file* Program. These pilot programs are usually conducted within a limited geographic area or within a limited taxpayer or practitioner community. The Service establishes rules for participating in these pilot programs and embodies these rules in an implementing document typically referred to as a "Memorandum of Understanding" or "Memorandum of Agreement." Pilot participants must agree to the provisions of the implementing document in order to participate in the pilot program.

.02 An implementing document supplements this revenue procedure, but does not supersede it.

.03 A violation of a provision of an implementing document is considered a violation of this revenue procedure and may subject the participant to sanctions (see section 7 of this revenue procedure).

SECTION 10. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 99–39, 1999–2 C.B. 532; Rev. Proc. 2000–31, 2000–2 C.B. 146; and Rev. Proc. 2001–9, 2001–1 C.B. 328 are superseded.

SECTION 11. EFFECTIVE DATE

This revenue procedure is effective August 29, 2005.

SECTION 12. INTERNAL REVENUE SERVICE OFFICE CONTACT

All questions regarding this revenue procedure should be directed to the Internal Revenue Service. The telephone number for this purpose is (202) 283–0261 (not a toll-free number).

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Return Required by Subchapter T Cooperatives Under Section 6012

REG–149436–04

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that prescribe the form that cooperatives must use to file their income tax returns. The regulations affect all cooperatives that are currently required to file an income tax return on either Form 1120, "*U.S. Corporation Income Tax Return*," or Form 990–C, "*Farmers' Cooperative Association Income Tax Return*."

DATES: Written or electronic comments and requests for a public hearing must be received by October 27, 2005.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–149436–04), 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–149436–04), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the IRS Internet site at *www.irs.gov/regs*, or via the Federal eRulemaking Portal at *www.regulations.gov* (IRS-REG–149436–04). A public hearing may be scheduled if requested by any person who timely submits comments.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Donnell M. Rini-Swyers, (202) 622–4910; concerning submissions of comments, or to request a hearing, Richard Hurst, (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

Under existing regulations, all cooperatives to which subchapter T applies (Subchapter T cooperatives) are required to make income tax returns. Except in the case of farmers' cooperatives, the regulations require that the return be made on Form 1120. In the case of farmers' cooperatives, the regulations require that the return be made on Form 990-C.

Most taxpayers required to make an income tax return on Form 1120 must file their return on or before the 15th day of the third month following the close of the taxpayer's taxable year (2½ month deadline). Some Subchapter T cooperatives that make their returns on Form 1120 are required to file by the 2½ month deadline, but others are not required to file their returns until the 15th day of the ninth month following the close of the taxpayer's taxable year (8½ month deadline). Because the Form 1120 does not distinguish between Subchapter T cooperatives that must file by the 2½ month deadline and those that must file by the 8½ month deadline, the IRS has difficulty determining which filing deadline applies and deciding whether to assert delinquency and failure to pay penalties in the case of returns filed after the 2½ month deadline.

Explanation of Provisions

The proposed regulations provide that all Subchapter T cooperatives must make their income tax returns on Form 1120-C, "*U.S. Income Tax Return for Cooperative Associations*," or such other form as may be designated by the Commissioner. The information that Subchapter T cooperatives will be required to provide on new Form 1120–C will assist taxpayers and the IRS in determining the appropriate filing deadline. Having that information will reduce the burden on taxpayers and will help the IRS avoid asserting penalties in inappropriate cases. Having all Subchapter T cooperatives make their income tax returns on Form 1120–C will also eliminate confusion over which form to file and will promote efficiency in addressing income tax issues common to Subchapter T cooperatives.

Effect on Other Documents

The following publication is obsolete as of the date this regulation is published as a final rule in the **Federal Register**.

Announcement 84–26, 1984–11 I.R.B. 42.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its 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 clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these regulations is Donnell M. Rini-Swyers, Office of Assistant Chief Counsel (Procedure & Administration).

* * * * *

Proposed Amendments to the Regulations

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

PART 1—INCOME TAXES, REPORTING AND RECORDKEEPING REQUIREMENTS

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

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

Par. 2. Section 1.6012–2 is amended by revising paragraph (f) to read as follows:

§1.6012–2 Corporations required to make returns of income.

* * * * *

(f) *Subchapter T cooperatives*—(1) *In general*. For taxable years ending on or after December 31, 2006, a cooperative organization described in section 1381 (including a farmers' cooperative exempt from tax under section 521) is required to make a return, whether or not it has taxable income and regardless of the amount of its gross income, on Form 1120–C, "*U.S. Income Tax Return for Cooperative Associations*," or such other form as may be designated by the Commissioner.

(2) *Farmers' cooperatives*. For taxable years ending before December 31, 2006, a farmers' cooperative organization described in section 521(b)(1) (including a farmers' cooperative that is not exempt from tax under section 521) is required to make a return on Form 990–C, "*Farmers' Cooperative Association Income Tax Return*."

* * * * *

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

(Filed by the Office of the Federal Register on July 28, 2005, 8:45 a.m., and published in the issue of the Federal Register for July 29, 2005, 70 F.R. 43811)

Foundations Status of Certain Organizations

Announcement 2005–60

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

360 Sports Organization, Inc., Homewood, IL
8300 Sheridan Dr., Inc., Clarence, NY
Abram Kessel Goldberg Fish Foundation, Cedarhurst, NY
Abundant Life Encyclopedia, Inc., Horsham, PA
ACFE Foundation, Inc., Springfield, MO
Accord Foundation, Bellevue, WA
Acova, Inc., Avoca, IA
Advocacy Resource System, Wyoming, MI
Africa-Expo, Las Vegas, NV
Africa Health Strategies, Washington, DC
African American Family Liaison Organization, Inc., Wimauma, FL
Air Intelligence, Inc., Fly Creek, NY
Alabama Sports Hall of Fame Foundation, Birmingham, AL
Allen Kiwanis Club Foundation, Allen, TX
Alliance for Strong Communities, Inc., New Haven, CT
Alpha Foundation, Washington, DC
Alvarado Project, San Francisco, CA
Amana Christian Training Center, Inc., Santa Clara, CA
American Abstinence Institute, Chicago, IL
American Friends for Jewish Institutions & Orphanage in Odessa, Flushing, NY
American Friends of Leshivat Ahrchot Torah, Inc., New York, NY
American Friends of Mosdos Eli Bezri, Inc., New York, NY
American Friends of Yeshiva Etz Joseph, Inc., North Miami Beach, FL
Amigos of University De Fresnillo, Mission, TX
Amir Community Development, Inc., Atlanta, GA
An Artists Life, Inc., Boston, MA
Angel Wings Cat Rescue & Sanctuary, Kingston, TN
Animalsave, Fort Lee, NJ
Apaga, Inc., Great Neck, NY
Apostolic Joy and Miracles Child Development Center, Inc., Riviera Beach, FL
Appalachian Institute for the Advancement of Women, Girls & Children, Inc., Morgantown, WV
Applied Ballet Arts Foundation, Oakland, CA
Arachnoiditis Foundation, Inc., Santa Rosa Beach, FL
Aries Foundation, Inc., Midlothian, VA
Arizona Athletic Association, Glendale, AZ
Arizona High School Allstar Games, Inc., Casa Grande, AZ
Arkansas American Indian Cultural and Heritage Society, Inc., Seneca, MO
Armenian Orthodox Theological Research Institute, Inc., Greenville, RI
Asociacian De Maestros Apoyando Ninos, Las Cruces, NM
Association for the Promotion of the Individuals Laws of Life, Inc., New York, NY
Atchafalaya Basin Foundation, Morgan City, LA
Atlanta Youth Arts Foundation, Inc., Cumming, GA
Avante-Garde, Inc., Silver Spring, MD
Baltimores Ark, Inc., Baltimore, MD
Bartow Community, Inc., Cartersville, GA
Bay Area Pedestrian Education Group, Oakland, CA
Bear Foods, Inc., Boston, MA
Beloved Community Public Charter School, Washington, DC
Benefits Aids Babies & Youths, Havertown, PA
Berkeley Striders Track Club, Moncks Corner, SC
Bioss USA Leadership Association, Seattle, WA

Birmingham Youth Service Corps, N. Birmingham, AL
Blackwater Little League, Waverly, VA
BLC Foundation, Castle Rock, CO
Book Station Library, Grand Junction, MI
Bosnian & Herzegovinian Association Northern California, Campbell, CA
Boston Counseling & Legal Services, Inc., Boston, MA
Boston Historical Society, Inc., Boston, NY
Bourn Dance Competition Team, Uniontown, OH
Boys and Girls Club of Bay City and Matagorda County, Bay City, TX
Brentwood Youth Soccer Club, Inc., Brentwood, NY
Bridge Ministries, Lincoln, NE
Bristol Tree Society, Bristol, RI
Broncos Swimming and Diving Booster Club, International Falls, MN
Burton Sharpe Ministries, Seattle, WA
Butler County-Georgiana Family Life Services Center, Georgiana, AL
Cactus Cowboy Corral, Inc., Vail, AZ
Cajacet Project, Inc., Newport, RI
Cal Ripkin Baseball League of Great Kills, Inc., Staten Island, NY
Calling the Shots, St. Paul, MN
Cambridge-Salem 481 Charities, Inc., Cambridge, NY
Camp Tamarack Summer Program, Menominee, MI
Capable Allies Relying on Each Other akas CARE, Selma, OR
Career Forum for the Under-Employed, Stanford, CA
Carnaval Independencia Centro America Y Mexico, Inc., Miami, FL
Castleberry Community Drugfree Committee, River Oaks, TX
Catherine Cole Taylor Center for the Arts, Inc., Santa Rose Beach, FL
Central Connecticut Arts Science and Technology Initiative, Meriden, CT
Central Soccer League, Inc., Oceanside, CA
Chance House, Inc., Roxbury, MA
Chagrin River Valley Association, Solon, OH
Changehaven, Inc., Reno, NV
Cherab Foundation, Inc., Union, NJ
Chicago Block Club Association, Chicago, IL
Children of Sosnovaya Street, Seattle, WA
Childrens World of Fun Family Learning Center, Inkster, MI
Christian Mission to Gaza, Corona, CA
Christian Team Resources, Scottsdale, AZ
Chukchansi Indian Housing Authority, Coarsegold, CA
Circle of Growth Foundation, Inc., Flushing, NY
Citizens for Hayden-Tomahawk Island, Inc., Portland, OR
Citizens for Homeless Relief, Inc., Tullahoma, TN
Citizens Redevelopment Corp., Asbury Park, NJ
Classy Cats Chariot, Inc., Jacksonville, FL
Clinton Friends of the Parks, Clinton, MO
Clovis Heat Softball Association, Inc., Clovis, NM
Club of Budapest, San Francisco, CA
Coalition for African-American Health and Wellness, Tucson, AZ
Coalition of Concerned Communities, Inc., Culver City, CA
Coastal Brain Injury Support Group, New Bern, NC
Collegiate Strength & Conditioning Coaches Association, Inc., Provo, UT
Come to Christ, Richardson, TX
Commemorative Historical Society World War Two Living, San Jose, CA
Committee for the Human Rights of Children, Inc., Miami, FL
Community Care and Counseling of Hartsville, Inc., Hartsville, SC
Community Connection of Northwest Indiana, Merrillville, IN
Compassionate Hearts-Serving Hands, Inc., Sunrise, FL
Computer Literacy Association, Valdez, AK
Constituency for the Caribbean, Inc., New York, NY
Consumer Advancement, Flint, MI
Cornwells Home & School, Bensalem, PA
Corona Lions Universal Foundation, Inc., Corona, NY
Country Place of Pierz, Pierz, MN
Coyote Productions, Inc., Park Hill, OK
Crandon Water Ski Club, Inc., Crandon, WI
Creatures for Culture, Inc., New York, NY
Crossroads Christian Ministry, Medford, OR
Crusade for Life International, Denver, CO
Cultured Community Service Center, Queens Village, NY
Dallas Area All-Stars Track Club Incorporation, Hutchins, TX
D A N C — Dance Alive in Northern Colorado, Loveland, CO
Darren C. Stevens Foundation, New York, NY
Daskalos Foundation, Inc., Cambridge, MA
Delaware Small Business Foundation, Georgetown, DE
Delta Chi Educational Foundation, Inc., Indianapolis, IN
Derech Emet, Brooklyn, NY
Desert Labrador Retriever Rescue, Inc., Phoenix, AZ
Desire Area Resident Community Development, Lansing, MI
Detroit Deacons Baptist Council, Inc., Detroit, MI
Diabetes World Advocacy Foundation, Seattle, WA
Diamond Force Girls Fast Pitch Association, Chambersburg, PA
Disability Resource Center, Everett, WA
Discover Foundation, Pleasant Grove, UT
DMZ Forum, Inc., East Meadow, NY
Donate Life, Inc., Brookline, MA
Doobys Clown Brotherhood for the Uplift of Gods People, Inc., Atlanta, GA
Doors and Passageways of Return Foundation, Washington, DC
Dora Moore Children Center, Inc., Houston, TX
Dorchester County Communities in Schools, Ridgeville, SC
Dreamshapers, Mooresville, NC
Drive-In Theatre Museum, Inc., Mason City, IA
Dunamei Christian Leadership Network, Inc., Irvine, CA
Eagle Court Apartments, Randall, MN
East Chapel Hill High School Foundation, Chapel Hill, NC
East Idaho Juniors, Inc., Blackfoot, ID
East Timor Disaster Response Organization, Inc., Washington, DC
Eastern Legal Immigration Advocate Networks, Atlantic City, NJ
Eden Foundation, San Antonio, TX
Educational Global Associates, Washington, DC
Educore Foundation, Inc., Encinitas, CA
Elizabeths Park, Bradford, VT
Ellison Watson Ellison and Associates, Inc., Texas City, TX
Emerald Coast Comets, Inc., Ft. Walton Beach, FL
Environmental Quality Initiative, Inc., Bethel, PA
Esteemed Woman Foundation, Inc., Norwalk, CT

Etowah County Law Enforcement Memorial, Gadsen, AL
Eyesight International USA, Seattle, WA
Fairfield Industrial High School Alumni Association, Gardena, CA
Fairfield Main St., Inc., Fairfield, TX
Faith Not Sight, Inc., Fair Lawn, NJ
Families First, Inc., Ferndale, MI
Family Medicine Educational Foundation, Inc., Glendale, CA
Fanya Corporation, Los Angeles, CA
Far Southeast Family Strengthening Collaborative, Washington, DC
Farkas Foundation, Inc., Scottsdale, AZ
Farmington Motor City Madness, Farmington, MI
Federal Hill South Neighborhood Association, Baltimore, MD
Ferrell Family Services, Capitol Heights, MD
Finance Institute for Global Sustainability, Chapel Hill, NC
First Family Pledge Foundation, Inc., Vero Beach, FL
Firststep Networking Solutions, San Diego, CA
Fit 5 Fitness Council, Portage, MI
Flatiron Foundation, Inc., Brooklyn, NY
Florida Fire and Police Honor Guard Competition, Orlando, FL
Florida Tissue Services, Inc., Pensacola, FL
Floyd Bennett Cricket Club, Inc., Far Rockaway, NY
Food Mission of Christ of Kentucky, Inc., Stanford, KY
For Your Life Foundation, Inc., Houston, TX
Fort Myers Historical Museum Foundation, Inc., Fort Myers, FL
Foundation for Community-Based Initiatives, Dallas, TX
Foundation for Independence and Growth, Inc., N. Lauderdale, FL
Freedom Round-Up, Philadelphia, PA
Freightliner Toys for Tots, Gastonia, NC
Fresh Start, Inc., Columbus, GA
Friends in Family Unity, Inc., Sacramento, CA
Friends of Charlotte Harbor Estuary, Inc., Port Charlotte, FL
Friends of Londonderry Hockey, Londonderry, NH
Friends of New Mexico Tribal Libraries, Santa Fe, NM
Friends of Redbird Airport, Dallas, TX
Friends of the Family, Inc., Taos, NM
Friends of the Pontiac Public Library, Pontiac, MI
Friends of Weaver, Los Alamitos, CA
Friendship Community Development Corporation, Mobile, AL
From Bondage to Freedom, Los Angeles, CA
Fund for Our Children, Old Tappan, NJ
Galaxy 2000 Entertainment, Mesa, AZ
Gemach Mordechai Aron Chaiam, Inc., Brooklyn, NY
Genesee Coalition on Adolescent Pregnancy Parenting & Prevention, Flint, MI
Genesis Troupe, Livonia, MI
Geneva Avenue Elderly Housing, Inc., Boston, MA
Georgia Community Resources Exchange, Inc., Atlanta, GA
Giveback Foundation, Chicago, IL
G M B C Community Development Corporation, Houston, TX
Go CAIA, Tucson, AZ
God is Good, Incorporated, El Reno, OK
Golden Gate Chapter Lupus Foundation of America, Inc., San Francisco, CA
Good Samaritan Ministry, Inc., New York, NY
Good Shepherd Outreach Center, Newport News, VA
Grace Project, Inc., Shreveport, LA
Grand Central Parkway, Forest Hills, NY
Great Dane Rescue Alliance, Inc., Plymouth, MI
Great Lakes Opera, Southfield, MI
Greater Ann Arbor Omega Foundation, Ann Arbor, MI
Greater New York Chinatown Social Services Agency, Inc., New York, NY
Greenville Dream Center, Pelzer, SC
Harambee African Female Rites of Passage Collective Program Process, Baltimore, MD
Harbor Foundation, Wilmington, NC
Harby Hawks Booster Club, Alvin, TX
Harlem Music Lab, Inc., New York, NY
Haus of Marcellus, Dallas, TX
Haven International Ministries, Los Angeles, CA
Healing Hearts Ministries, Inc., Miami, FL
Health Information of America, Inc., Cedar Grove, NJ
Health Research Group, Rocksburg Bath, VA
Hearts of Gold Foundation, Rochester, MN
Heat Halsell Education and Training Center, Philadelphia, PA
Help Me, Augusta, ME
Helping People Grow Academy, Charlotte, NC
Helping Young Haitians Succeed, Riverdale, MD
Herb Millro Classic, Seattle, WA
Heroes of the Flame, Inc., Houston, TX
Higher Dimensions, Inc., Byron, GA
Hilltop Speed Track Club, Vallejo, CA
His Servants of Fire Christian International Ministries, La Habra, CA
Hollyberry Foundation, Abingdon, VA
Hollyview RHF Housing, Inc., Long Beach, CA
Holocaust Awareness Ark, Yonkers, NY
Home Ownership Preparation & Experience, Big Lake, MN
Hope for Honduras, Inc., Overland Park, KS
Hope House, Inc., New Haven, CT
Hope of Glory Mission, Inc., Mobile, AL
Hopkins County Community Resource Coordination Group, Sulphur Springs, TX
Horizon Circle of Friends, Allegan, MI
Humanity United Globally, Honolulu, HI
I Support Charity, New York, NY
IBIC Institute, Inc., Greenwich, CT
Illinois Committee of Blind Vendors, Chenoa, IL
Indiana Angels, Greenwood, IN
Indiana Hooved Animal Humane Society, Salem, IN
Insight Ministries International, Las Vegas, NV
Institute for Species Specific Milk, Temecula, CA
International Shrine for Boxing & Wrestling, Los Angeles, CA
International Soap Box Derby, Inc., Akron, OH
Internet Ministries Fish Net, Tucson, AZ
Into the Harvest, Milpitas, CA
Invisible Theatre Company, Inc., Baltimore, MD
Irish Center of Washington, DC, Vienna, VA
Israel Metropolitan Social Action & Education Foundation, Greenville, SC
Jack Barnett Scholarship Fund, Uncasville, CT
JCM Spirit Club, Jackson, TN
Jefferson City Early Childhood Parent Teacher Organization, Jefferson City, MO
Jesus Run, Incorporated, Highland Ranch, CO

Jewish Continuity Foundation, Monsey, NY
Joe Cali Ministries, Phoenix, AZ
John Braun Foundation, Elkhart Lake, WI
Johnson City Rotary Foundation, Johnson City, NY
Joshua Rescue Foundation, Walnut Creek, CA
JS-Lyn Child Care, Inc., Lithonia, GA
Kaamilah Foundation, Inglewood, CA
Kafuku Farm Institute, Inc., Davis, CA
Kassiwi Sanctuary & Coalition for Preservation of Indigenous Culture, Beecher Falls, VT
K C Force, Blue Springs, MO
KCFC — Kansas City Fencing Center, Shawnee Mission, KS
Kentucky Family Development Institute, Inc., Frankfort, KY
Kick, Inc., Charlestown, MA
Kids Helping Kids in Crisis, Inc., Wayne, NJ
Kids in a Drug-Free Society, New York, NY
Kids World Daycare, Inc., Holly Springs, MS
Kiwanis Club of Capital City Foundation, Inc., Boise, ID
Kiwanis Club of Midtown St. Petersburg Youth Foundation, Inc., St. Petersburg, FL
Kiwanis Club of Saugerties Foundation, Saugerties, NY
Korean American Society of Hawaii, Honolulu, HI
Korean Senior Center of Central Florida, Inc., Orlando, FL
Lafayette Crossing Foundation, Inc., Keswick, VA
Lafayette High School Athletic Educational Foundation, Williamsburg, VA
Land Assembly for Neighborhood Development, Detroit, MI
Lang Ranch Elementary School Booster Club, Thousand Oaks, CA
Lavender and Green Alliance, Inc., Mineola, NY
Leap of Faith Community Outreach, Evansville, IN
Leap of Faith Ministries, Inc., Canon City, CO
Liberation Independence Freedom Empowerment Foundation, Inc., Redding, CA
Liberian American Community Organization, Los Angeles, CA
Liberty International Family and Educational Services, Inc., Hartford, CT
Life Improvement, Inc., West Palm Beach, FL
Life With Lupus Guild, Chicago, IL
LIRR Commuters Campaign, Inc., Bayport, NY
Little Traverse Bay Band of Odawa Indians Elders Association, Harbor Springs, MI
Living Room Opera, St. Paul, MN
LJC Ministries, Lemon Grove, CA
Logan Community Foundation, Logan, IA
M-Powerhouse, Washington, DC
Macon Better Housing Foundation, Macon, GA
Malakoff Area Garden Club, Malakoff, TX
Mammoth Lakes Celtic Festival, Inc., Mammoth Lakes, CA
Manitowish Waters Skiing Skeeters, Inc., Manitowish Waters, WI
Marion Jones Ministry, Nashville, TN
Markey Road Neighborhood Association, Dayton, OH
Marshfield Sister Cities, Inc., Marshfield, WI
Mart Emergency Medical Services, Inc., Mart, TX
Martinsburg Blue Sox, Martinsburg, WV
Mary Vincent Foundation, West Covina, CA
Marysville Independent Traveling Teams, Marysville, OH
Massachusetts Low-Income Taxpayers Clinic, Inc., Norwell, MA
Matthews Christian Youth Group, Oswego, IL
Meadowlark Foundation, Inc., Great Falls, MT
Mega Complex Outreach, Inc., Missouri City, TX
Melanoma Assistance Program, Inc., Pensacola, FL
Mentor Link, Inc., Bronx, NY
Mercy Mountain Transportation, Inc., Williamsburg, KY
Michigan State University Investment Club, East Lansing, MI
Milledgeville Resident Council, Inc., Milledgeville, GA
Mills Remediation & Tutoring Center, Inc., Southside, AL
Minnesota Shakespeare Project, Minneapolis, MN
Miracle Farm, Inc., Gladwyne, PA
Miss Ohio Scholarship Pageant, Mansfield, OH
Mission Teens, Detroit, MI
MMBC Ministries, Temple, TX
Mothers Care Support Services, Inc., Madison, AL
Mount Moriah Baptist Church of Spartanburg Foundation, Inc., Spartanburg, SC
Moving Forward Towards Independence, Napa, CA
Mueenabad Fund, Inc., New Park, PA
Music Ministries, Inc., Union, NJ
Nashville Chamber Singers, Nashville, TN
National African-American Archives and Museum, Mobile, AL
National Assistance Dog Advocate Coalition, Brooklyn, NY
National Association of Yemeni Americans, Inc., Dearborn, MI
National School Fitness Foundation, Salt Lake City, UT
National Youth Athletic Association, Lynnwood, WA
Nationwide Masonic Brotherhood, Inc., Linden, NJ
New Covenant Promise Foundation, Caledonia, NY
New England Seacoast Institute, Nahant, MA
New Mercies, Inc., Newport News, VA
New Mexico Association of Community Action Agencies, Albuquerque, NM
New River Valley Feline Rescue & Care Center, Christianburg, VA
New York Raptors Special Hockey Club, Inc., Larchmont, NY
Newtown Colonial Girls Softball League, Inc., Newtown, PA
Nipmuc Indian Development Corp., Webster, MA
No Limit Youth Ministries-Programs of Louisville, Inc., Louisville, KY
Noon Optimist Foundation of Elkhart Indiana, Elkhart, IN
North Carolina County Youth Foundation, Inc., Asheville, NC
North Carolina State Indian Housing Authority, Fayetteville, NC
North Dakota Native American Foster Parent Association, Bismarck, ND
Northeast Community Counsel of Austin Texas, Austin, TX
Northeast Kiwanis Club of Lincoln Nebraska Foundation, Lincoln, NE
Northside Affordable Housing Opportunities, Inc., Jacksonville, FL
Ohio Rural Partners, Reynoldsburg, OH

Oklahoma Association & Leadership of Student Assistance Program, Yukon, OK
One Faith Ministries, Fairdealing, MO
One Song Many Voices Foundation, Bethesda, MD
Operation Rebound, Flint, MI
Optimal Community Support Services, Inc., Houston, TX
Or Yechiel, Brooklyn, NY
Orange Business Incubator, Inc., Orange, VA
Organization of Black Airline Pilots, Silver Spring, MD
Oromo Community of Denver, Denver, CO
Owensboro Ice Foundation, Inc., Owensboro, KY
Panther Childrens Foundation, Camarillo, CA
Parents and Friends of Boy Scout Troop 212 of Santa Clara County, San Jose, CA
Partners in Torah, Inc., New York, NY
Path of Hope Foundation, Fountain Valley, CA
Patriots Praise Corps, Phelan, CA
Patterson Scrip Program, Fremont, CA
Perry Fund for Others, Charlottesville, VA
Perry-Yokley Family Development Center, Merced, CA
Pfc Dan Bullock Foundation, Mount Laurel, NJ
Phoebes Work, Minneapolis, MN
Pilgrim House, Inc., Sheffield, AL
Pine Creek Headwaters Protection Group, Wellsboro, PA
Pinellas County African American History Museum, Inc., Clearwater, FL
Plainfield Minority Golf Association, Plainfield, NJ
Port Arthur Municipal Non-Profit Corporation, Port Arthur, TX
Pound Band Boosters, Pound, VA
Powerhouse Foundation, Inc., League City, TX
PPRC Nursing Home, Inc., High Point, NC
PRN Care Nonprofit Corporation, Upland, CA
Project Open Arms, San Francisco, CA
Project Still I Rise, Inc., Dallas, TX
Promise Academy Charter School, Long Beach, CA
Promised Assurance, Madera, CA
Providing Every American Child Education and Well Being Organization, Austin, TX
Radicand Foundation, Birmingham, AL
Rainbow House for Women and Children, Inc., San Antonio, TX
Rainbow Unity Foundation, Des Moines, IA
Rapendeh, Bedford, TX
Raym-Co Scholarship Foundation, Inc., Bristol, CT
R E A C H the Youth, Inc., Madison, AL
Reed City Firefighters Auxiliary, Reed City, MI
Refreshing Florida Community Development Corporation, Haines City, FL
Refugee Women United for Progress, Phoenix, AZ
Renaissance Townhomes, Inc., Denton, TX
Resource Center for Westside Communities, Chicago, IL
Rites of Passage for Girls, Denver, CO
Roanoke Stars Basketball, Inc., Penhook, VA
Rockland Street Baseball, Inc., Portsmouth, NH
Rocky Boy Health Board, Box Elder, MT
Ron-Sher, Inc., Downey, CA
Sandlewood Senior Apartments, San Bernardino, CA
Sanibel-Captiva Kiwanis Charitable Foundation, Inc., Sanibel, FL
Sanibel-Captiva Review, Inc., Sanibel Island, FL
Santa Barbara Christian Homesteaders, Inc., Buellton, CA
Santa Clara Palomino World Series, Inc., Saratoga, CA
Saving the Impotent Christian, Inc., Citrus Heights, CA
Second Amendment Legal Studies Association, Montclair, VA
Second Humanitarian Fund, Waterford, MI
Self-Esteem Tennis Foundation, Scottsdale, AZ
Senior Volunteer Service Organization, Oakdale, CA
Shaarei Halacha, Inc., Brooklyn, NY
Shock Wave Athletic Association, Colonial Heights, VA
Show Us the Way, Papillion, NE
Shull Technology Booster Club, San Dimas, CA
Siddique Foundation of America, Auburn, AL
Signature Band & Choir Camp, Inc., Syracuse, NY
Silver City Development Corporation, Meriden, CT
Sirkulo Pilipino, Canoga Park, CA
Skills for Living Foundation, Inc., Monticello, MN
SLV PNY-Colt Baseball, Inc., Ben Lomond, CA
Social High — Scope Educators, Torrance, CA
Society for Outdoor Sculpture, Inc., South Windsor, CT
Solo Academic Boosters Club, Solon, OH
South Haven Drop in Center, South Haven, MI
South Lake High School Theatre Arts Boosters, Oakton, VA
Southlake Aquatics, Inc., Southlake, TX
Southside Hornets Athletic Association, Fort Worth, TX
Southwest Alabama EMS Educational Conference, Inc., Mobile, AL
Sparta Resident Council, Inc., Milledgeville, GA
Spice Dogs, Sacramento, CA
Spiritual Gifts, Louisville, KY
Sponsor a Voice, Atlanta, GA
Sprott Christian Youth Center, Inc., Moncure, NC
Spruce Housing Non-Profit Corporation, Teaneck, NJ
St. Andrews Community Services for All Ages SACS, Sacramento, CA
Standing Together Assisting Youth, Jacksonville, FL
Stars on Call, Inc., Owings Mills, MD
Starshine & Company Productions, Cave Creek, AZ
Step by Step Ministries, Saint Charles, IL
Stratford Community Theatre, Stratford, SD
Summit Missions, Incorporated, Pensacola, FL
Sunnyvale Kiwanis Club Foundation, Sunnyvale, CA
Sweet Life Program, Las Vegas, NV
Swim Tucson Foundation, Tucson, AZ
Sylvestors Freedom House, Inc., Bridgman, MI
Synetic Foundation, Inc., Macon, GA
T-Bird Foundation & Alumni Association, Inc., Cheyenne, WY
T L P Development Corporation, Philadelphia, PA
Talent Motivation Center, Inc., Hollywood, FL
Tarrant County Family and Childrens Fund, Bedford, TX
Team One Productions, Inc., Cordova, TN
Teens With a Vision, Inc., Winston Salem, NC

Texas Organic Research Center, Inc., Dallas, TX
Texas USA Wrestling, Fort Worth, TX
The Zone, Howard, SD
Theatre Medina, Denver, CO
Thoreau School Parent Teacher Group, Concord, MA
Three Trees Charitable Trust, Lafayette, OR
Touch of Kindness, Inc., Pocasset, MA
Treasure Valley Interpreter Association, Inc., Boise, ID
Tri-County Independent Living Center of Utah, Ogden, UT
Trust for Jewish Philanthropy, Inc., New York, NY
Tucson Synchro, Inc., Tucson, AZ
Tutor Company Foundation, Danville, CA
University Retirement Community at Davis Foundation, Inc., Davis, CA
V T & D Community Development Corporation, Inc., Laud Lakes, FL
Valencia High School Choir Booster Club, Placentia, CA
Valliant Band Booster Club, Valliant, OK
Vidor Junior Football League Pirates, Vidor, TX
Village Resource, Chicago, IL
Vision Quest Sports and Fitness, Auburn, WA
Visionary Foundation, Columbus, OH
Vocational Outreach of Maryland, Ltd., Red Lion, PA
Wakanyeja Pawicayapi, Inc., Porcupine, SD
Wall Street Lions Cultural Foundation, Inc., Flushing, NY
Wayne Bull Adams Foundation, Inc., Waco, TX
Wentzville Football Booster Club, Wentzville, MO
West Corporation, Washington, DC
White House Commission on the National Moment of Remembrance, Washington, DC
Willow Manor, Inc., Lake Charles, LA
Windsong Swim Team, Inc., Houston, TX
WMMQ Coat for Kids Program, Inc., Lansing, MI
Women in Transition Counseling and Education Center, Tacoma, WA
Women of Avaya Valuing Excellence, Inc., Westminster, CO
Womens Serenity Retreat, Dalton, GA
WordSoundAction, Inc., Bethesda, MD
Worlds Recovery, Tonasket, WA
Wrights Community Center, Sacramento, CA
Y.com, Mahtomedi, MN
Yes There is Hope of Midway GA, Midway, GA
Youth Activities Foundation, Inc., Louisville, KY
Youth Investment Coalition Corp. of Northampton County, Woodland, NC
Youth Media Productions, Inc., Debary, FL
Yulee Career Institute, Inc., Jacksonville, FL

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Definition of Terms

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

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

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

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

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

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

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

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

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

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

Abbreviations

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

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

Numerical Finding List[1]

Bulletins 2005–27 through 2005–35

Announcements:

Notices:

Proposed Regulations:

Revenue Procedures:

Revenue Procedures— Continued:

Revenue Rulings:

Tax Conventions:

Treasury Decisions:

[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2005–1 through 2005–26 is in Internal Revenue Bulletin 2005–26, dated June 27, 2005.

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

Bulletins 2005–27 through 2005–35

Announcements:

84-26
Obsoleted by
REG-149436-04, 2005-35 I.R.B. *454*

Notices:

2005-4
Modified by
Notice 2005-62, 2005-35 I.R.B. *443*

2005-51
Modified and superseded by
Notice 2005-57, 2005-32 I.R.B. *267*

Proposed Regulations:

REG-142686-01
Withdrawn by
Ann. 2005-55, 2005-33 I.R.B. *317*

REG-100420-03
Corrected by
Ann. 2005-57, 2005-33 I.R.B. *318*

REG-102144-04
Corrected by
Ann. 2005-56, 2005-33 I.R.B. *318*

Revenue Procedures:

64-54
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

66-33
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

69-13
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

70-8
Modified by
Rev. Proc. 2005-46, 2005-30 I.R.B. *142*

71-1
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

72-22
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

87-8
Obsoleted by
Rev. Proc. 2005-44, 2005-29 I.R.B. *110*

87-9
Obsoleted by
Rev. Proc. 2005-44, 2005-29 I.R.B. *110*

Revenue Procedures— Continued:

89-20
Superseded by
Rev. Proc. 2005-52, 2005-34 I.R.B. *326*

90–11
Modified by
Rev. Proc. 2005-40, 2005-28 I.R.B. *83*

90-30
Section 4 superseded by
Rev. Proc. 2005-54, 2005-34 I.R.B. *353*
Section 5 superseded by
Rev. Proc. 2005-55, 2005-34 I.R.B. *367*
Section 6 superseded by
Rev. Proc. 2005-56, 2005-34 I.R.B. *383*
Section 7 superseded by
Rev. Proc. 2005-58, 2005-34 I.R.B. *402*
Section 8 superseded by
Rev. Proc. 2005-59, 2005-34 I.R.B. *412*

90-31
Section 4 superseded by
Rev. Proc. 2005-52, 2005-34 I.R.B. *326*
Section 5 superseded by
Rev. Proc. 2005-54, 2005-34 I.R.B. *353*
Section 6 superseded by
Rev. Proc. 2005-55, 2005-34 I.R.B. *367*
Section 7 superseded by
Rev. Proc. 2005-56, 2005-34 I.R.B. *383*
Section 8 superseded by
Rev. Proc. 2005-58, 2005-34 I.R.B. *402*
Section 9 superseded by
Rev. Proc. 2005-59, 2005-34 I.R.B. *412*

93-22
Obsoleted by
Rev. Proc. 2005-44, 2005-29 I.R.B. *110*

98-18
Obsoleted by
Rev. Proc. 2005-45, 2005-30 I.R.B. *141*

99-39
Superseded by
Rev. Proc. 2005-60, 2005-35 I.R.B. *449*

2000-31
Superseded by
Rev. Proc. 2005-60, 2005-35 I.R.B. *449*

2000-49
Superseded by
Rev. Proc. 2005-41, 2005-29 I.R.B. *90*

2001-9
Superseded by
Rev. Proc. 2005-60, 2005-35 I.R.B. *449*

2001-16
Superseded by
Rev. Proc. 2005-42, 2005-30 I.R.B. *128*

Revenue Procedures— Continued:

2002-9
Modified and amplified by
Rev. Rul. 2005-42, 2005-28 I.R.B. *67*
Rev. Proc. 2005-35, 2005-28 I.R.B. *76*
Rev. Proc. 2005-43, 2005-29 I.R.B. *107*
Rev. Proc. 2005-47, 2005-32 I.R.B. *269*

2004-50
Superseded by
Rev. Proc. 2005-49, 2005-31 I.R.B. *165*

Revenue Rulings:

65-109
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

68-549
Obsoleted by
Rev. Rul. 2005-43, 2005-29 I.R.B. *88*

82-29
Modified and clarified by
Rev. Proc. 2005-39, 2005-28 I.R.B. *82*

2005-41
Corrected by
Ann. 2005-50, 2005-30 I.R.B. *152*

Treasury Decisions:

9186
Corrected by
Ann. 2005-53, 2005-31 I.R.B. *258*

9206
Corrected by
Ann. 2005-49, 2005-29 I.R.B. *119*

9207
Corrected by
Ann. 2005-52, 2005-31 I.R.B. *257*

[1] A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2005–1 through 2005–26 is in Internal Revenue Bulletin 2005–26, dated June 27, 2005.

INDEX

Internal Revenue Bulletins 2005–27 through 2005–35

The abbreviation and number in parenthesis following the index entry refer to the specific item; numbers in roman and italic type following the parentheses refer to the Internal Revenue Bulletin in which the item may be found and the page number on which it appears.

Key to Abbreviations:

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

EMPLOYEE PLANS

EMPLOYMENT TAX

EMPLOYMENT TAX—Cont.

ESTATE TAX

EXCISE TAX

EXCISE TAX—Cont.

EXEMPT ORGANIZATIONS

GIFT TAX

INCOME TAX

INCOME TAX—Cont.

INCOME TAX—Cont.