Internal Revenue
bulletin

Bulletin No. 2000–43
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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

Notice 2000–56, page 393.

This notice provides guidance under section 1032 of the Code on which entity is treated as the grantor and owner of a grantor trust when a parent corporation contributes its stock to a rabbi trust for the benefit of the employees of a subsidiary.

Rev. Proc. 2000–42, page 394.

This procedure informs taxpayers of the information they must submit to request a closing agreement under section 1.1503–2(g)(2)(iv)(B) of the regulations to prevent the recapture of dual consolidated losses (DCLs) upon the occurrence of certain triggering events.

Rev. Proc. 2000–44, page 409.

Insurance companies; loss reserves; discounting unpaid losses. The loss payment patterns and discount factors are set forth for the 2000 accident year. These factors will be used for computing discounted unpaid losses under section 846 of the Code.

Rev. Proc. 2000–45, page 417.

Insurance companies; discounted estimated salvage recoverable. The salvage discount factors are set forth for the 2000 accident year. These factors will be used for computing estimated salvage recoverable under section 832 of the Code.

Announcement 2000–78, page 428.

The Service is requesting comments on the proposed regulations regarding the monthly limit for transit passes and transportation, in a commuter highway vehicle, provided by an employer to employees under section 132(f) of the Code.

EMPLOYEE PLANS

REG–114697–00, page 421.

Nondiscrimination requirements for certain defined contribution retirement plans. Proposed regulations would prescribe conditions under which certain defined contribution retirement plans (sometimes referred to as “new comparability” plans) are permitted to demonstrate compliance with applicable nondiscrimination requirements based on plan benefits rather than plan contributions. A public hearing is scheduled for January 25, 2001.

Notice 2000–55, page 393.

Weighted average interest rate update. The weighted average interest rate for October 2000 and the resulting permissible range of interest rates used to calculate current liability for purposes of the full funding limitation of section 412(c)(7) of the Code are set forth.

TAX CONVENTIONS

Notice 2000–57, page 389.

The agreement between the United States and Netherlands identifying U.S. and Dutch pension plans for tax treaty benefits is set forth.

ADMINISTRATIVE

Rev. Proc. 2000–43, page 404.

***Ex parte* communication prohibition.** Guidance is provided to taxpayers and IRS employees about *ex parte* communications during the appeals process.

(Continued on the next page)

Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

Announcement 2000–85, page 429.
This document contains corrections to a notice of proposed rulemaking (REG–108522–00, 2000–34 I.R.B 187) relating to the recognition of gain on certain transfers to certain foreign trusts and estates.

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 consolidated 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 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 first 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 first Bulletin of the succeeding semiannual period, respectively.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

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

Section 832.—Insurance Company Taxable Income

26 CFR 1.832–4: Gross income.

The salvage discount factors are set forth for the 2000 accident year. These factors will be used for computing estimated salvage recoverable for purposes of section 832 of the Code. See Rev. Proc. 2000–45, page 417.

Section 846.—Discounted Unpaid Losses Defined

26 CFR 1.846–1: Application of discount factors.

The loss payment patterns and discount factors are set forth for the 2000 accident year. These factors will be used for computing discounted unpaid losses under section 846 of the Code. See Rev. Proc. 2000–44, page 409.

26 CFR 1.846–1: Application of discount factors.

The salvage discount factors are set forth for the 2000 accident year. These factors will be used for computing estimated salvage recoverable for purposes of section 832 of the Code. See Rev. Proc. 2000–45, page 417.

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions

Following is a Copy of the News Release Issued by International (U.S. Competent Authority) on April 20, 2000 (IR–INT–2000–9)

Notice 2000–57

AGREEMENT IDENTIFIES U.S. AND DUTCH PENSION PLANS FOR TAX TREATY BENEFITS

Washington – The Competent Authorities of the The Netherlands and the United States reached a mutual agreement on the qualification of certain Dutch and U.S. pensions for treaty benefits under Article 35 of the US-Netherlands Income Tax Treaty. The agreement specifies the procedures for claiming treaty benefits in each country and the methods each country will use to grant treaty benefits.

The agreement constitutes a Mutual Agreement in accordance with the Convention between the Kingdom of the Netherlands and the United States of America for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, signed on December 18, 1992, and amended by Protocol signed on October 13, 1993.

The agreement is as follows:

Chapter I

Qualification for treaty benefits under article 35 of the 1992 Netherlands-US income tax treaty

Questions have been raised regarding the types of US and Netherlands resident tax exempt trusts, companies or other organisations providing pension or retirement benefits that qualify for treaty benefits under article 35 of the Convention between the Kingdom of the Netherlands and the United States of America for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, signed on 18 December 1992, and amended by Protocol signed on 13 October 1993 (in the following: the Treaty). In practise there are many different types of funds or plans established to provide pension or retirement benefits and it is not always clear which of these funds or plans fulfill the requirements of article 35 of the Treaty. This issue is being discussed between the Netherlands and the US competent authorities under the mutual agreement procedure of article 29 of the Treaty, with the following initial conclusions.

In view of the present uncertainty it has been decided to identify all the different types of US and Netherlands resident tax exempt trusts, companies or other organisations providing pension or retirement benefits that are considered to fall within the scope of article 35 of the Treaty and also to indicate the appropriate procedures for filing a request for an application of treaty benefits under said treaty provision.

In the course of the mutual agreement discussions it became apparent that, whereas with respect to certain types of US and Netherlands resident tax exempt trusts, companies or other organisations providing pension or retirement benefits it is beyond doubt that they fall within the scope of article 35 of the Treaty, with respect to other types of US and Netherlands resident tax exempt trusts, companies or other organisations providing pension or retirement benefits this is less clear. The Netherlands and US authorities concluded that all the different types of Netherlands and US resident tax exempt trusts, companies or other organisations providing pension or retirement benefits mentioned in chapter II and IV of this agreement would be considered to fall within the scope of article 35 of the Treaty.

However, in order to ensure that treaty protection is restricted to qualifying US resident tax exempt trusts providing pension or retirement benefits, the Netherlands competent authority would -at least for the time being- prefer a closer monitoring of all requests filed for an application of treaty benefits under article 35 of the Treaty.

It is understood that for the purpose of this publication the term "Code section" refers to sections of the US Internal Revenue Code and that the term "trust" includes a custodial account treated as a trust for US federal income tax purposes.

Chapter II

US resident tax exempt trusts providing pension or retirement benefits

Subject to the conditions of article 26, article 35, paragraph 2, and article 34, paragraph 4, of the Treaty:

1. a US resident tax exempt trust providing pension or retirement benefits under a Code section 401 (a) qualified pension plan, profit sharing plan or stock bonus plan (including Code section 401 (k) arrangements); or
2. a US resident tax exempt trust providing pension or retirement benefits under a Code section 457(b) pension plan or under a Code section 403(b) plan; or
3. a US resident tax exempt trust which is an Individual retirement account (Code section 408), a Roth Individual retirement account (Code section 408A), or a Simple retirement account, or a US resident tax exempt trust which is providing pension or retirement benefits under a Simplified employee pension plan; or
4. a US resident common trust fund or group trust which is tax exempt under Code section 501 (a) with respect to funds that equitably belong to its participating trusts, all of which are entities mentioned under point 1) above; or
5. a US resident common trust fund or group trust which is tax exempt under the Internal Revenue Code with respect to funds that equitably belong to its participating trusts, some of which are trusts other than those mentioned under point 1) above, but all of which are trusts mentioned under point 1), 2), or 3) above, is considered to qualify for treaty benefits under article 35 of the Treaty and may claim application of treaty benefits with respect to income derived from the Netherlands referred to in article 10 (dividends) of the Treaty. The Netherlands does not apply a withholding tax on outgoing interest payments as meant in article 12 of the Treaty.

However, a US resident tax exempt trust mentioned under point 2) or 3) above will not be considered to qualify for treaty benefits under article 35 of the Treaty in any taxable year if less than 70% of the total amount of the withdrawals from such US trust during that year is used to provide pension, retirement or other employee benefits as meant in article 35 of the Treaty.

Any type of US resident tax exempt trust not mentioned above, which consid-

ers itself to qualify for treaty benefits under article 35 of the Treaty, may present its case to the Netherlands tax unit BPO buitenland, Heerlen (address: P.O. Box 2865, 6401 DJ HEERLEN, The Netherlands), or to the US competent authorities requesting for a competent authority consideration under article 29 of the Treaty.

Chapter III

Appropriate procedures for filing a request for an application of treaty benefits in the Netherlands

The Netherlands has two methods for granting treaty benefits for income referred to in article 10 (dividends) of the Treaty, these methods being: the so-called exemption method (in which case the treaty rate is applied at source) and the so-called refund method.

As a general rule, the Netherlands applies the exemption method when granting treaty benefits in the case of Dutch source dividend income received by a resident of the US, which means that treaty benefits will be granted by means of an exemption from Netherlands withholding tax at source. In view of the Netherlands competent authority's preference for a closer monitoring of all requests filed for an application of treaty benefits under article 35 of the Treaty, a US resident tax exempt trust (including a US common trust fund or group trust) mentioned in point 1) through 5) of chapter II of this publication shall - as a general rule - be required to use the refund method when filing its request for an application of treaty benefits under article 35 of the Treaty. Only if certain conditions are fulfilled, such US resident tax exempt trust may use the exemption method when filing its request for an application of treaty benefits under article 35 of the Treaty.

The Netherlands regulations for the implementation of the Treaty, published in the "Staatscourant" 5 January 1994, nr. 3 and lastly amended on December 1996 ("Staatscourant" 30 December 1996, nr. 250), give a detailed description of the procedures to be applied in the case of respectively the exemption method and the refund method.

The exemption method may be used if the US resident tax exempt trust requesting treaty benefits under article 35 of the Treaty:

* has been issued a certification letter (Form 6166) by the US Internal Revenue Service for the taxable year(s) in question, stating that the trust in question is a trust forming part of a pension, profit sharing, or stock bonus plan qualified under Code section 401 (a) of the Internal Revenue Code (an example of a certification letter (Form 6166) is attached); or

* has been issued a so-called "qualification" certification by the competent Netherlands tax authorities, stating that the trust in question is a US resident tax exempt trust as described in article 35, paragraph 1, of the Treaty.

Requests for a "qualification" certification may be filed with the tax unit BPO buitenland, Heerlen (address: P.O. Box 2865, 6401 DJ HEERLEN, The Netherlands).

A "qualification" certification, issued by the competent Netherlands authorities, is in principle valid indefinitely. However, a "qualification" certification will no longer be valid in the event:

*there is a material change in facts or circumstances; or

*It is determined that the "qualification" certification was issued erroneously; or

*the US resident tax exempt trust in question has not claimed an application of treaty benefits under article 35 of the Treaty for five consecutive calendar years. Since a certification letter (Form 6166) issued by the US Internal Revenue Service is not valid indefinitely, a US resident tax exempt trust which has been issued a certification letter (Form 6166) by the US Internal Revenue Service may also file a request for a "qualification" certificate with the competent Netherlands tax authorities.

Irrespective of the above, use of the refund method is mandatory in any taxable year for a US resident tax exempt trust mentioned under point 2) or 3) of chapter II, if less than 70% of the total amount of the withdrawals from such US trust during that year is used to provide pension or retirement benefits.

Where assets of the pension fund(s) or pension plan(s) are held in custodial accounts, the amended form IB 92 USA will require a certification that the claim for a refund of Dutch dividend tax is filed for the benefit of the custodial accounts in question.

The status of all US resident tax exempt trusts providing pension or retirement benefits and claiming treaty benefits under article 35 of the Treaty may at any time be subject to verification by the competent Netherlands tax authority. If considered necessary, use will be made of the exchange of information procedure (article 30 of the Treaty).

The Netherlands regulations for the implementation of the Treaty (including the "special arrangements" issued by the Netherlands competent authority in the relation to the US) and Form IB 92 USA will - where necessary - be amended in accordance with the above. A model of the "special arrangements" is published in the Infobulletin of 12 January 1999.

The new procedures will become applicable beginning with dividends made payable after 30 June 2000. The presently existing procedures will remain applicable for dividends made payable before or on 30 June 2000.

Chapter IV

Netherlands resident tax exempt companies providing pension or retirement benefits

Subject to the conditions of article 26, article 35, paragraph 2, and article 34, paragraph 4, of the Treaty, a Netherlands resident tax exempt company constituted and operated exclusively to administer or provide benefits as meant in article 5, paragraph b), of the Netherlands corporation tax act (including a Netherlands resident tax exempt company constituted and operated exclusively to administer or provide benefits under a pension plan as meant in article 8, paragraph 1, under f), of the Netherlands income tax act) is considered to qualify for treaty benefits under article 35 of the Treaty and may claim application of treaty benefits with respect to income derived from the United States of America referred to in article 10 (dividends) and in article 12 (interest) of the Treaty.

Any type of Netherlands resident tax exempt company not mentioned above, which considers itself to qualify for treaty benefits under article 35 of the Treaty, may present its case to the United States competent authority, or to the Netherlands competent authority requesting for a competent authority consideration under article 29 of the Treaty.

Chapter V

Appropriate procedures for filing a request for an application of treaty benefits in the United States of America

Under US tax law a Netherlands resident taxpayer (including a Netherlands resident tax exempt company referred to in article 35 of the Treaty) may file for an application of treaty benefits at source, or may claim a refund of US income tax withheld according to regulations set forth under the Internal Revenue Code. The following procedures apply to a Netherlands resident tax exempt company.

A Netherlands resident tax exempt company described in this agreement should claim exemption from US income tax withholding under Article 35 of the 1992 Netherlands-US income tax treaty on dividends or interest income referred to in articles 10 and 12, respectively, of that treaty by providing a properly completed IRS Form W-8BEN to the withholding agent or payer of such income before the income is paid or credited to the company. A company filing Form W-8BEN should cite Article 35 of the treaty on line 10 thereof, and state that it is a Netherlands resident tax exempt company described in this agreement.

Notwithstanding the foregoing, until December 31, 2000, and to the extent provided in transition rules set forth in regulations under Internal Revenue Code section 1441 and Notice 99–25, 1999–20 I.R.B. 75, a Netherlands resident tax exempt company may provide, and a withholding agent may rely upon, other appropriate documentation of the company's exempt status, including, for example, a Form 1001, supplemented by a statement, or a valid Netherlands Form IB 93 USA (certified by the tax inspector competent in the case of the Netherlands tax exempt company in question) stating that the company is a Netherlands resident tax exempt company described in this agreement.

Alternatively, the company may seek a refund of taxes withheld on such dividend or interest income by timely filing a United States income tax return and claiming a refund of such taxes.

The status of all Netherlands resident tax exempt companies providing pension or retirement benefits and claiming treaty benefits under article 35 of the Treaty may be subject to verification by the Internal Revenue Service. If considered necessary, use will be made of the exchange of information procedure (article 30 of the Treaty).

A Netherlands resident tax exempt company as meant in article 5, paragraph b), of the Netherlands corporation tax act (including a Netherlands resident tax exempt company providing pension or retirement benefits as meant in article 8, paragraph 1, under f), of the Netherlands income tax act) may have the Netherlands tax authority concur in its claim of tax exempt status by means of a so-called article 26 declaration (Form IB 93 USA), certified by the tax inspector competent in the case of the Netherlands tax exempt company in question. This will not, however, preclude an audit and determination of the company's substantive liability.

As noted in Article 6 of the Protocol, Article 35(2) of the Treaty provides that dividends from a Real Estate Investment Trust are not eligible for Article 35 benefits. Article 35(2) also provides that income of an exempt pension trust is not exempt under Article 35 if it is received from a related person that is not itself an exempt pension trust. Paragraph VIII of the Agreed Minutes to the Protocol provides the understanding of the negotiators that for purposes of Article 35(2), a person will be considered to be a "related person" if more than 80 percent of the vote or value of any class of shares is owned by the person deriving the income.

Chapter VI

Tax exempt trusts, companies or other organisations providing other employee benefits

In order to determine whether a clarification of the qualification under article 35 of the Treaty for the various types of tax exempt trusts, companies or other organisations providing other employee benefits is also considered necessary, comments or questions regarding this issue are invited and may be sent to to one of the following addresses:

Ministry of Finance of the Netherlands
Directorate for International Tax Policy and Legislation
P.O. Box 20201
2500 EE Den Haag
The Netherlands

Assistant Commissioner
(International)
attn. Tax Treaty Division
Internal Revenue Service
P.O. Box 23598
Washington, D.C. 20024
United States of America

Attachment:
Form 6166 (Rev. 6–96)

Part III. Administrative, Procedural, and Miscellanous

Weighted Average Interest Rate Update

Notice 2000–55

Notice 88–73 provides guidelines for determining the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of § 412(c)(7) of the Internal Revenue Code as amended by the Omnibus Budget Reconciliation Act of 1987 and as further amended by the Uruguay Round Agreements Act, Pub. L. 103–465 (GATT).

The average yield on the 30-year Treasury Constant Maturities for October 2000 is 5.83 percent.

The following rates were determined for the plan years beginning in the month shown below.

Month	Year	Weighted Average	90% to 105% Permissible Range	90% to 110% Permissible Range
October	2000	5.95	5.35 to 6.24	5.35 to 6.54

Drafting Information

The principal author of this notice is Todd Newman of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, call the Employee Plans Actuarial hotline, (202) 622-6076 between 2:30 and 3:30 p.m. Eastern time (not a toll-free number). Mr. Newman's number is (202) 622-8458 (also not a toll-free number).

Rabbi Trusts

Notice 2000–56

I. PURPOSE

This notice provides guidance on which entity is treated as the grantor and owner of a grantor trust when a parent corporation contributes its stock to a rabbi trust for the benefit of the employees of a subsidiary.

II. BACKGROUND

(i) Rabbi Trust Model

Rev. Proc. 92–64, 1992–2 C.B. 422, contains a model grantor trust for use in nonqualified executive compensation arrangements that are popularly referred to as "rabbi trust" arrangements. Under that revenue procedure, the Service will not rule on unfunded deferred compensation arrangements that use a trust other than the model trust, except in rare and unusual circumstances. Section 1(d) of the model trust document states that "Any assets held by the Trust will be subject to the claims of the Company's general creditors under federal and state law in the event of Insolvency, as defined in Section 3(a) herein." In the case of a trust that provides benefits to employees of a subsidiary, it is the Service's position that Section 1(d) will not be satisfied unless the assets held by the trust are subject to the claims of the subsidiary's creditors (whether or not those assets are also subject to the claims of the parent's creditors). In this case, it has been the Service's position that the subsidiary is treated as the grantor and owner of the rabbi trust.

(ii) Final Regulations under Section 1032 of the Internal Revenue Code

Section 1032 states that no gain or loss is recognized to a corporation on the receipt of money or other property in exchange for stock of the corporation. Regulations were recently issued under section 1032 of the Internal Revenue Code (*see* 65 F.R. 31073 (May 16, 2000)). Section 1.1032–3(b)(1) of these regulations provides that no gain or loss is recognized on the disposition of the issuing corporation's stock by an acquiring entity if the requirements set forth in Reg. § 1.1032–3(c) are met. Section 1.1032–3(c)(2) requires, among other things, that the acquiring entity transfer the stock of the issuing corporation to another person immediately after acquiring the stock from the issuing corporation (the "immediacy requirement"). Under the regulations, if the requirements of Reg. § 1.1032–3(c), including the immediacy requirement, are met, the transaction is treated as if, immediately before the acquiring entity transfers the stock of the issuing corporation, the acquiring entity purchased the issuing corporation's stock from the issuing corporation for fair market value with cash contributed to the acquiring entity by the issuing corporation (or, if necessary, through intermediate corporations or partnerships). This series of transactions is commonly referred to as the "cash purchase model."

Rabbi trust arrangements typically do not involve an immediate transfer of stock to employees. In the case of a rabbi trust arrangement in which Parent Stock is treated for federal tax purposes as owned by a subsidiary for a period of time before the Parent Stock is transferred to the employees of the subsidiary, the immediacy requirement of Reg. §1.1032–3(c)(2) will not be satisfied when the Parent Stock is transferred from the rabbi trust to employees of the subsidiary. Because the cash purchase model of those Regulations will as a result not apply, the nonrecognition treatment of section 1032 will be inapplicable in such a case, and, thus, the subsidiary typically will recognize gain on the transfer of the Parent Stock from the rabbi trust to employees of the subsidiary.

III. TREATMENT OF PARENT CORPORATION AS GRANTOR OF A RABBI TRUST

The Service and Treasury have determined that when a parent corporation contributes Parent Stock to a rabbi trust to assist a subsidiary in meeting the subsidiary's deferred compensation obligations to its employees or service providers, and the Parent Stock is both subject to the claims of the creditors of the parent corporation and subject to the requirement that any Parent Stock not

transferred to the subsidiary's employees will revert to the parent on termination of the trust, then the parent corporation will be considered the grantor and the owner of the Parent Stock held in the trust, even though the Parent Stock is also subject to the claims of the creditors of the subsidiary. If these conditions are satisfied, the Parent Stock (or other assets) will not be considered transferred to the subsidiary until such time as they are used to satisfy the subsidiary's deferred compensation obligation to its employees or service providers, or when a claim is made against the trust by a creditor of the subsidiary in the case of the subsidiary's insolvency. Thus, the immediacy requirement of Reg. § 1.1032–3(c)(2) would be satisfied with respect to the Parent Stock.

This concept is illustrated in Example 10 of Reg. § 1.1032–3(e). In the example, in Year 1, the issuing corporation, X, forms a trust which it will use to satisfy deferred compensation obligations owed by Y, X's wholly owned subsidiary, to Y's employees. X funds the trust with X stock which would revert to X upon termination of the trust, subject to the employees' rights to be paid the deferred compensation. The creditors of X can reach all trust assets upon the insolvency of X. Similarly, the creditors of Y can reach all trust assets upon the insolvency of Y. In Year 5, the trust transfers X stock to the employees of Y in satisfaction of the deferred compensation obligation. The example states that X is considered to be the grantor of the trust, and, under section 677 of the Code, X is also the owner of the trust. Y is not considered a grantor or owner of the trust corpus at the time X transfers X stock to the trust. Any income earned by the trust would be reflected on X's income tax return. In Year 5, when employees of Y receive X stock in satisfaction of the deferred compensation obligation, no gain or loss is recognized by X or Y on the deemed disposition of the X stock by Y. Immediately before Y's deemed disposition of the X stock, Y is treated as purchasing the X stock from X for fair market value using cash contributed to Y by X. Under section 358, X's basis in its Y stock increases by the amount of cash deemed contributed. Accordingly, when employees or service providers of Y receive X stock in satisfaction of the deferred compensation obligation, the requirements of § 1.1032–3(c) are satisfied, and no gain or loss is recognized by X or Y on the deemed disposition of the X stock by Y.

Similarly, the parent corporation will be treated as the grantor and owner of assets other than Parent Stock that are contributed by the parent corporation to a rabbi trust if the assets are both subject to the claims of the creditors of the parent corporation and subject to the requirement that any such assets not transferred to the subsidiary's employees or service providers will revert to the parent on termination of the trust, even though such assets are also subject to the claims of the creditors of the subsidiary. The cash purchase model applies only to transfers of stock by the parent corporation to the trust. Therefore, when assets other than Parent Stock are transferred from the trust to the employees of the subsidiary, the subsidiary is treated as receiving the other assets from the parent corporation with the parent's carryover basis and the subsidiary will recognize gain or loss (if any) on the transfer of the assets to the subsidiary's employees or service providers.

IV. MODIFICATION TO MODEL TRUST UNDER REV. PROC. 92–64

The Service will rule on a request submitted under Rev. Proc. 92–64 where the model language has been modified to provide that Parent Stock (or other assets) contributed by a parent corporation to a rabbi trust for the benefit of employees or service providers of a subsidiary is subject to the claims of the creditors of both the parent corporation and the subsidiary, and the remaining Parent Stock (or other assets) contributed by the parent corporation reverts to the parent corporation upon termination of the trust.

V. TRANSITION PROVISIONS FOR EXISTING TRUSTS

The Service will not challenge a taxpayer's position that no gain or loss is recognized by a subsidiary upon the rabbi trust's disposition of Parent Stock contributed to the rabbi trust by the parent corporation on or before May 16, 2001, with respect to trusts in existence on or before June 15, 2000.

If the terms of the rabbi trust are amended to provide that assets (including Parent Stock) contributed by the parent corporation to the rabbi trust are subject to claims of the parent corporation's creditors (in addition to being subject to the claims of the subsidiary's creditors) and those assets not transferred to the subsidiary's employees or service providers will revert to the parent corporation upon termination of the rabbi trust, the Service will not treat such amendment as a constructive dividend to the parent corporation, provided the amendment is adopted by May 16, 2001.

VI. EFFECT ON OTHER GUIDANCE

Rev. Proc. 92–64 will not fail to be satisfied if Parent Stock (or other assets) contributed by a parent corporation to a rabbi trust for the benefit of employees or service providers of a subsidiary is subject to the claims of the creditors of the parent corporation and the subsidiary, and the remaining Parent Stock (or other assets) contributed by the parent corporation reverts to the parent corporation upon termination of the trust.

DRAFTING INFORMATION

The principal author of this notice is Susan Lennon of the Office of the Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the Service and the Treasury Department participated in its development. For further information regarding this notice, contact Ms. Lennon at (202) 622-6030 (not a toll-free telephone number).

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26 CFR 1.1503–2 Dual consolidated loss.
26 CFR 301.7121–1 Closing agreements.

Rev. Proc. 2000–42

SECTION 1. PURPOSE

This revenue procedure informs taxpayers of the information they must submit to request a closing agreement under §1.1503–2(g)(2)(iv)(B)(2)(i) to prevent the recapture of dual consolidated losses (DCLs) upon the occurrence of certain triggering events.

Before this revenue procedure, the Internal Revenue Service and the Department of the Treasury had not specified in detail how taxpayers should request these

closing agreements. The Service and Treasury are issuing this revenue procedure to provide taxpayers with guidance on the information and representations they should include in a §1503(d) closing agreement request and to facilitate the process and reduce the time necessary for the Service to process requests.

Appendix A to this revenue procedure is a model closing agreement. The Service intends the model closing agreement to serve as an example of the format and contents of a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement and to aid taxpayers in understanding how the information required by this revenue procedure will be used in the closing agreement. Taxpayers should note, however, that the model agreement is only an example. A taxpayer's actual agreement could differ from the model. Finally, Appendix B is a flow chart of the entities included in the model closing agreement, along with notes explaining the model agreement.

SECTION 2. BACKGROUND

The United States taxes the worldwide income of domestic corporations. The United States allows certain domestic corporations to file consolidated returns with other affiliated domestic corporations. When two or more domestic corporations file a consolidated return, losses that one corporation incurs generally may reduce or eliminate tax on income that another corporation earns.

Because other countries may apply different standards for determining the residence and taxability of a corporation (e.g., based on the management and control of the corporation), some domestic corporations are dual resident corporations and, as such, are also subject to the income tax of a foreign country on their income on a residence basis (and not on a source basis). Foreign countries often have provisions that permit commonly owned entities to combine their income and losses through consolidation or some other form of combined reporting for income tax purposes.

Prior to the Tax Reform Act of 1986, if a dual resident corporation were a resident of a foreign country with tax laws that permitted the losses of the corporation to be used to offset the income of another person (e.g., under a consolidated return provision), then the dual resident corporation could use any losses it generated twice: once to offset the income of affiliates resident in the United States (but not abroad), and again to offset the income of its affiliates resident only in the other country. Thus, such a dual resident corporation could use a single economic loss to offset two separate items of income in two jurisdictions. Congress expressed concerns that this dual use of a loss could result in an undue tax advantage to certain foreign investors that made investments in domestic corporations, and could create an undue incentive for certain foreign corporations to acquire domestic corporations and for domestic corporations to acquire foreign rather than domestic assets. Staff of Joint Committee on Taxation, 99th Cong., 2nd Sess., General Explanation of the Tax Reform Act of 1986, at 1064 – 1065 (1987). As part of the Tax Reform Act of 1986, Congress responded by enacting §1503(d) to prevent the use of DCLs that resulted from consolidation in multiple jurisdictions.

The Treasury and Service issued temporary regulations under §1503(d) in 1989 (T.D. 8261, 1989–2 C.B. 220), and final regulations in 1992 (T.D. 8434, 1992–2 C.B. 240). The final regulations in §1.1503–2 are generally effective for taxable years beginning on or after October 1, 1992; the temporary regulations in §1.1503–2A are effective for taxable years beginning after December 31, 1986, and before October 1, 1992. The temporary regulations were initially designated as §1.1503–2T, but were redesignated as §1.1503–2A by the final regulations.

Section 1503(d) provides that a DCL of a dual resident corporation shall not be allowed to reduce the taxable income of any other member of the corporation's affiliated group for any taxable year. The term dual resident corporation includes a domestic corporation that is subject to the income tax of a foreign country on its worldwide income or on a residence basis and a separate unit of a domestic corporation (e.g., a foreign branch, an interest in a partnership, an interest in a trust, or a disregarded entity that a foreign country taxes at the entity level). *See* Treas. Reg. §1.1503–2(c)(2) – (4). This revenue procedure will collectively refer to dual resident corporations and separate units as "DRCs."

The final §1503(d) regulations permit a taxpayer to elect to use a DCL of a DRC by entering into an agreement under §1.1503–2(g)(2)(i) in which the taxpayer certifies that the DCL has not been, and will not be, used to offset the income of another person under the laws of a foreign country. Certain subsequent events, known as "triggering events" require the taxpayer to recapture the losses as income, including an interest charge. Treas. Reg. §§1.1503–2(g)(2)(iii) and (vii). If a taxpayer fails to comply with the §1503(d) recapture provisions upon the occurrence of a triggering event, then the DRC (or a successor-in-interest) that incurred the DCL generally will not be eligible for relief to use any DCLs incurred in the five (5) taxable years beginning with the year in which recapture is required. Treas. Reg. §1.1503–2(g)(2)(vii)(F)(1).

Triggering events occur when: (1) any portion of the loss taken into account in computing the DCL is used by any means to offset the income of any other person for foreign tax purposes within fifteen (15) years; (2) a DRC or domestic owner of a separate unit ceases to be a member of the consolidated group that filed the agreement at a time when there is a continuing ability to use the DCL to offset income of another person for foreign tax purposes; (3) an unaffiliated DRC or unaffiliated domestic owner of a separate unit becomes a member of a consolidated group, unless there is no continuing ability to use the DCL to offset income of another person for foreign tax purposes; (4) a DRC transfers its assets to a transferee in a transaction that results, under the laws of a foreign country, in a carryover of the losses, expenses, or deductions that make up the DCL; (5) a domestic owner of a separate unit disposes of fifty (50) percent or more of the assets of, or its interest in, the separate unit at a time when there is a continuing ability to use the DCL to offset income of another person for foreign tax purposes; (6) an unaffiliated DRC or unaffiliated domestic owner of a separate unit becomes a foreign corporation in a transaction that, for foreign tax purposes, is not treated as involving a transfer of assets to a new entity, unless there is no continuing ability to use the DCL to offset income of another person for foreign tax purposes; or (7) the taxpayer fails to file an annual certification required under §1.1503–2(g)(2)(vi)(B). Treas. Reg. §1.1503–2(g)(2)(iii)(A).

The final regulations provide two exceptions to events described as triggering events, making the events not triggering events requiring recapture of losses and an interest charge. The first exception, under §1.1503–2(g)(2)(iv)(A), applies when a DRC, or its assets, is acquired by another member of the DRC's consolidated group. The second exception, under §1.1503–2(g)(2)(iv)(B), applies, provided the taxpayer enters into a closing agreement, when a DRC or a domestic owner of a separate unit becomes disaffiliated from its consolidated group, or when an unaffiliated domestic corporation or new consolidated group acquires the DRC or its assets.

The Service is aware that as a result of taxpayers' ability to elect entity classification under the §7701 elective Federal tax classification regulations that became effective as of January 1, 1997 (i.e., the check-the-box regulations), the number of DRCs may increase, and taxpayers may become subject to the §1503(d) DCL provisions, including the recapture provisions. For instance, the conversion of a foreign branch to a foreign corporation may be treated as a triggering event under the final §1503(d) regulations. *See* Treas. Reg. §§1.1503–2(g)(2)(iii)(A)(4) – (7) and Treas. Reg. §301.7701–3(g)(1). Therefore, this procedure is also intended to publicize the Service's procedures and requirements that will prevent certain reorganization and disposition transactions involving DRCs from resulting in §1503(d) recapture consequences.

SECTION 3. SCOPE

.01 General.

This section provides the conditions that must be satisfied for the Service to consider requests from taxpayers for a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement.

.02 Taxpayers Must Be In Compliance And Must First Request Any Treas. Reg. §301.9100 Relief Needed.

Before requesting a closing agreement under §1.1503–2(g)(2)(iv)(B)(2)(i), the taxpayer should ensure that it has complied with the regulations issued under §1503(d), including having filed the requisite agreements, elections, and certifications under §1.1503–2(g)(2) (or §1.1503–2A(c)(3) or (d)(3) if the taxpayer is asking for relief under §1.1503–2A). *See infra*, section 3.07 (which provides when the Service will consider including in a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement, DCLs covered by the temporary §1503(d) regulations). In practical terms, this means that the taxpayer should first request and secure (or at least simultaneously request) any necessary relief under §301.9100 for an extension of time to make any required election or application under the §1503(d) regulations. For example, a taxpayer that has not filed the requisite agreements and elections under §1.1503–2(g)(2)(i) must first request (or simultaneously request) §301.9100 relief to file the elections and agreements.

Under §§1.1503–2(g)(2)(iii)(A) and (iv)(B), a taxpayer must enter into a closing agreement with the Service before the taxpayer files its tax return for the taxable year of a triggering event to prevent the recapture of losses and the accompanying interest charge. Under this revenue procedure, however, a taxpayer can prevent the recapture of losses and the interest charge if the taxpayer submits its request for a closing agreement by the due date of its tax return (including extensions) for the triggering event year and specifies on its tax return that it is requesting a §1503(d) closing agreement.

.03 Statutes Of Limitations.

The Service may request a taxpayer to execute a consent to extend the period of limitations for assessment of tax for the taxable periods related to the DCLs for which the taxpayer has requested a closing agreement.

.04 When And By Whom A Closing Agreements May Be Executed.

Treas. Reg. §1.1503–2(g)(2)(iv)(B)(1) provides that if the requirements of §1.1503–2(g)(2)(iv)(B)(2) are met, the following events will not constitute triggering events requiring the recapture of DCLs: (1) an affiliated DRC or an affiliated domestic owner becomes an unaffiliated domestic corporation or a member of a new consolidated group; (2) an unaffiliated DRC or an unaffiliated domestic owner becomes a member of a consolidated group; (3) assets of a DRC are acquired by an unaffiliated domestic corporation or a member of a new consolidated group; or (4) a domestic owner of a separate unit transfers its interest in the separate unit to an unaffiliated domestic corporation or to a member of a new consolidated group. Treas. Reg. §1.1503–2(g)(2)(iv)(B)(2) requires (among other requirements) that the taxpayers enter into a closing agreement with the Service which provides that the taxpayers will be jointly and severally liable for the total amount of the recapture of the DCLs and an interest charge upon any subsequent triggering event.

The Service may execute a closing agreement under §1.1503–2(g)(2)(iv)(B)(2)(i) and §7121 with the following taxpayers: (1) the consolidated group (i.e., the parent on behalf of the consolidated group), the unaffiliated DRC, or the unaffiliated domestic owner that filed the §1.1503–2(g)(2)(i) agreement for the relevant DCLs, and (2) the unaffiliated domestic corporation or the new consolidated group, provided the requirements of §1.1503–2(g)(2)(iv)(B) are satisfied. This revenue procedure will refer to these taxpayers as the "Taxpayer Parties." Authorized officers of the Taxpayer Parties must sign the closing agreement (generally two originals per party to the agreement).

.05 Taxpayers That Cannot Execute A Closing Agreement.

The Service will not execute a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement with foreign entities/transferees, individuals, or partnerships. Section 1.1503–2 does not provide for closing agreements with such taxpayers.

.06 Losses Must Be DCLs.

The Service will not execute a closing agreement with taxpayers for net operating losses (NOLs) that are not DCLs. Therefore, taxpayers must represent that the losses at issue are DCLs.

.07 Closing Agreements For Losses Under The Temporary Regulations.

The final regulations provide for taxpayers to enter into a §1.1503–2(g)(2)-

(iv)(B)(2)(i) closing agreement with the Service to prevent certain events from resulting in recapture and an interest charge; the temporary regulations do not contain such a provision. In appropriate circumstances, taxpayers may elect to apply the final regulations to DCLs which are otherwise subject to §1.1503–2A. Treas. Reg. §1.1503–2(h). If a taxpayer files a request to enter into a closing agreement for losses covered by the final regulations, under this revenue procedure, the Service will consider a request to include in the closing agreement DCLs otherwise covered by §1.1503–2A for which the taxpayer has not made a §1.1503–2(h) election to apply the final regulations. This revenue procedure's reference to "representations and citations as appropriate under §1.1503–2A," means representations and citations related to a DCL covered by §1.1503–2A.

SECTION 4. PROCEDURE TO ENTER INTO A CLOSING AGREEMENT

.01 General.

The first revenue procedure published each year (the Annual Revenue Procedure) outlines the general procedures of the Service for the issuance of letter rulings and determination letters, including closing agreements entered into under the authority of §7121, by the National Office. *See, e.g.*, Rev. Proc. 2000–1, 2000–1 I.R.B. 4. Taxpayers should note that the Service also publishes an annual revenue procedure, generally in the first Internal Revenue Bulletin of the year, which provides a list of those areas of the Code under the jurisdiction of the Associate Chief Counsel (International), for which the Service will not issue advance letter rulings, (e.g., certain §1503(d) determinations, such as whether the conditions for excepting losses of a DRC from the definition of a DCL are satisfied). *See, e.g.*, Rev. Proc. 2000–7, 2000–1 I.R.B. 227.

The consolidated group (i.e., the parent on behalf of the consolidated group), the unaffiliated DRC, or the unaffiliated domestic owner that filed the agreements under §1.1503–2(g)(2)(i) for the DCLs for which the closing agreement would relate may file a request to enter into a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement by following the procedures of the most recent Annual Revenue Procedure and this revenue procedure. Taxpayers must include the user fee required by the most recent Annual Revenue Procedure.

.02 Additional Information.

Because the information, representations, and documentation necessary to enter into a closing agreement depend on all the facts and circumstances, the Service may require information, representations, and documentation in addition to that set forth in this revenue procedure and the most recent Annual Revenue Procedure. Taxpayers should submit such additional information in accordance with the Annual Revenue Procedure and within the time allowed by the Annual Revenue Procedure. If a taxpayer does not submit the information requested within the time provided, the request will be closed and the taxpayer will be notified in writing. *See, e.g.*, section 10.06(3), Rev. Proc. 2000–1. If while processing a taxpayer's request for a §1503(d) closing agreement, the Service determines that the taxpayer is not in compliance with the §1503(d) regulations and needs relief under §301.9100 to obtain an extension of time to make a required election or application under the §1503(d) regulations, then the taxpayer has thirty (30) days from the date the Service notifies the taxpayer to file a request for relief under §301.9100. If a taxpayer does not submit the §301.9100 request within the thirty-day period, the §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement request will be closed and the taxpayer will be notified in writing.

Taxpayers are responsible for keeping the Service informed of all material changes to the information, representations, and documentation submitted as part of the closing agreement request.

SECTION 5. INFORMATION TAXPAYERS MUST INCLUDE IN REQUEST

.01 General.

This section describes the information, representations, and documentation that taxpayers are expected to provide with a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement request. Taxpayers should organize information and representations following the format of this procedure and should use appropriate descriptive headings. To facilitate the processing of the closing agreement request, taxpayers must also provide a full statement of all relevant facts related to the taxpayers and the DCLs.

Taxpayers must address each item in this section, providing all relevant facts. If an item is not applicable, taxpayers should so state and briefly explain why.

.02 Information Related To Taxpayer Parties, Relevant Members Of The Consolidated Group, And DRCs.

Taxpayers must provide a full statement of the facts, including the following general information, as appropriate, about each Taxpayer Party, relevant member of the consolidated group, and DRC with losses that will be covered by the closing agreement.

1. Name, address, and employer identification number.
2. Type of entity, and date and place of incorporation or other formation.
3. Information about the formation and treatment of disregarded entities directly or indirectly owned by a Taxpayer Party (including the date the entity became or elected to become a disregarded entity under §301.7701–3).
4. Classifications of the entity under §1.1503–2(c)(2) – (4) (e.g., dual resident corporation, foreign branch separate unit, hybrid entity separate unit) before and after any triggering event. If the taxpayer is requesting that the closing agreement include losses covered by the temporary regulations, the taxpayer should classify the entity under §1.1503–2A(b) (e.g., dual resident corporation, foreign branch separate unit, partnership interest separate unit).
5. Detailed explanation of the chain of ownership between the parent of the consolidated group (or in the case where there is no U.S. consolidated group, the unaffiliated domestic owner of the DRC) and the DRC before and after any triggering event (as described in §1.1503–2(g)(2)(iii) or §1.1503–2A(c)(3)(iii), as appropriate).

6. The taxable year of a Taxpayer Party to the closing agreement (both before and after any triggering event). If as a result of a triggering event there is a requirement for filing a short-period return under §1.1502–76(b) or other relevant provision, taxpayer should provide related information and an explanation.
7. The office that has jurisdiction over the Federal income tax returns of a Taxpayer Party to the closing agreement.

.03 Additional Information Related To DRCs.

Taxpayers must provide the following additional information for each DRC with losses that will be covered by the closing agreement:

1. The country or countries that tax the DRC on its worldwide income or on a residence basis. If the DRC is a separate unit, identify the separate unit and name under which it conducts business, and the country in which its principal place of business is located.
2. Description of the principal business activity.
3. Amounts and taxable years of DRC's NOLs.
4. Date the period of limitations on assessment of tax expires related to each DCL.

.04 List And Description Of All Triggering Events.

For all losses to be included in the §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement, taxpayers must provide a list and description of all triggering events described in §1.1503–2(g)(2)(iii) and §1.1503–2A(c)(3)(iii) as appropriate (including specific citations). In particular, taxpayers should explain how the triggering events are treated under the Code, including information about any taxable transfers or any nonrecognition provisions that apply, and should provide information about all parties, stock, and assets involved. Taxpayers should indicate whether any triggering event listed includes a transaction within the meaning of §1.1502–75(d)(2) or (3) whereby the common parent of the consolidated group that filed the §1.1503–2(g)(2)(i) agreements is no longer in existence or whereby the common parent was a party to a reverse acquisition, through which the consolidated group continues.

Taxpayers should state whether an exception to a triggering event applies and should explain the exception in detail and include a citation to the relevant provision (e.g., §1.1503–2(g)(2)(iv)(A), §1.1503–2(g)(2)(iv)(B), or §1.1503–2A(c)(3)(vi)). If a taxpayer has exercised rebuttal rights provided in §§1.1503–2(g)(2)(iii)(A)(2) – (7), taxpayer must provide information related to those rebuttals.

.05 Specific Representations And Agreements Required For Closing Agreement.

Taxpayers must provide the following representations and agreements, when applicable, to secure a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement:

1. That a corporation is a DRC as described in §1.1503–2(c)(2). Taxpayers must provide a representation for each relevant entity, and provide a §1.1503–2A representation as appropriate.
2. That a foreign branch, interest in a partnership, or interest in a trust is a separate unit as described in the appropriate subsection of §1.1503–2(c)(3) and a DRC as described in §1.1503–2(c)(2). Taxpayers must provide a representation for each relevant entity, and provide a §1.1503–2A representation as appropriate.
3. That a hybrid entity separate unit is a hybrid entity separate unit as described in §1.1503–2(c)(4) and a DRC as described in §1.1503–2(c)(2). Taxpayers must provide a representation for each relevant entity, and provide a §1.1503–2A representation as appropriate.
4. That the NOLs described are DCLs under §1.1503–2(c)(5) (or under §1.1503–2A(b)(2) as appropriate).
5. That the requisite elections, agreements, and certifications were timely made under §1.1503–2(g)(2)(i) (or §1.1503–2A(c)(3) or (d)(3) as appropriate).
6. That the DCLs were computed as required under §1.1503–2(d)(1) (or §1.1503–2A(f)(1) as appropriate).
7. That the necessary reporting and certifications were made under §1.1503–2(g)(2)(vi) (or §1.1503–2A(c)(3)(v) as appropriate).
8. That the consolidated group, unaffiliated DRC, or unaffiliated domestic owner will or has filed an election and agreement described in §1.1503–2(g)(2)(i) with its timely filed Federal income tax return for the year(s) of the triggering event(s) described in §1.1503–2(g)(2)(iii). Taxpayers should provide a §1.1503–2A representation as appropriate.
9. That apart from the triggering events listed, no triggering event described in §1.1503–2(g)(2)(iii) (or §1.1503–2A(c)(3)(iii) as appropriate) has occurred applicable to the DCLs.
10. That upon any subsequent triggering event described in §1.1503–2(g)(2)(iii), the Taxpayer Parties will be jointly and severally liable for the total amount of the recapture of the DCLs to which the closing agreement relates and the related interest charge under §1.1503–2 (g)(2)(vii), to the extent the triggering event does not fall under one of the exceptions provided in §1.1503–2(g)(2)(iv)(A) or (B).
11. That the new consolidated group or unaffiliated domestic corporation will treat any potential recapture of the DCLs under §1.1503–2(g)(2)(vii) as unrealized built–in gain for purposes of §384(a), subject to any applicable exceptions thereunder, and will treat the total recapture amount of the described DCLs as recognized built-in gain for purposes of §384(a), subject to any applicable exceptions thereunder.
12. That the new consolidated group or unaffiliated domestic corporation will comply with the reporting requirements described in §1.1503–2(g)(2)(vi) for each DCL for the taxable years covered by the closing agreement.
13. That an election was made (or was not made) under §1.1503–2(h)(2) or (3) for any DCLs incurred in taxable years beginning before October 1, 1992. Taxpayers should provide an explanation for the election provision used.
14. That an event described in

§§1.1503–2(g)(2)(iii)(A)(2) – (7) is not a triggering event under such provision because the transfer did not result in a carryover under foreign law of such losses, or because such losses cannot be used to offset the income of another person under foreign law. Taxpayers should represent the specific requirements under the provision cited. *See, e.g.*, section 3.01(4) and section 4.01(22), Rev. Proc. 2000–7 (the National Office of the Service generally will not make a determination related to the rebuttals).

.06 Documents Required.

As part of the initial submission requesting a §1.1503–2(g)(2)(iv)(B)(2)(i) closing agreement, taxpayers must provide the following documents when applicable:

1. Copies of all elections, agreements and certifications required by §1.1503–2(g)(2) (or §1.1503–2A (c)(3) or (d)(3)).
2. Copies of all ruling letters issued by the Service under §301.9100 providing for an extension of time to make a required election or application under the §1503(d) regulations.
3. Copy of all consents to an extension of the statute of limitations on assessment and collection.
4. Documents supporting the rebuttal of a presumption of a triggering event described in §§1.1503–2(g)(2)(iii) (A)(2) – (7).
5. Other documents as requested by the Service.

SECTION 6. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1706.

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 collection of information is contained in sections 4 and 5 of this revenue procedure. This information will enable the Service to determine whether to execute a closing agreement under §§1503(d) and 7121 of the Code. The likely respondents are domestic corporations.

The estimated average annual reporting and/or recordkeeping burden is two-thousand (2,000) hours.

The estimated average annual burden per applicant is one-hundred (100) hours. The estimated number of applicants is twenty (20). The estimated frequency of responses is on occasion.

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

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Camille B. Evans of the Office of the Associate Chief Counsel (International). For further information regarding this revenue procedure contact Camille B. Evans or Kenneth D. Allison of the Office of the Associate Chief Counsel (International) at (202) 622-3860 (not a toll free call).

Appendix A

DEPARTMENT OF THE TREASURY
INTERNAL REVNUE SERVICE

MODEL CLOSING AGREEMENT ON
FINAL DETERMINATION
COVERING SPECIFIC MATTERS

Under section 7121 of the Internal Revenue Code of 1986, as amended (the Code), Corporation A, 123 Main Street, Wilmington, DE 20000, EIN 11-1234567, a domestic corporation, as common parent on behalf of all the members of a consolidated group (the Corporation A Group); Corporation B, 124 Main Street, Wilmington, DE 20000, EIN 22-1234567, a domestic corporation, as common parent on behalf of all the members of a consolidated group as of January 1, Year 3 (the Corporation B Group); and the Commissioner of Internal Revenue hereby make the following closing agreement (Closing Agreement) based on the representations made by Corporation A and Corporation B, in paragraphs one (1) through fourteen (14) below:

WHEREAS:

(1) Corporation A, a Delaware corporation and party to this Closing Agreement, owned through December 31, Year 2, all of the stock of Corporation B, a Delaware corporation and party to this Closing Agreement. Until December 31, Year 2, Corporation A had outstanding Class X common stock and Class Y common stock. Corporation A is the common parent of an affiliated group of corporations that files a consolidated federal income tax return on a calendar year basis (the Corporation A Group). Corporation B was a member of the Corporation A Group through December 31, Year 2. On January 1, Year 3, Corporation B became the common parent of an affiliated group of corporations that files a consolidated federal income tax return on a calendar year basis (the Corporation B Group).

(2) Corporation B owns all of the stock of Corporation D, a Delaware corporation (EIN 33-1234567) and a member of the Corporation A Group through December 31, Year 2, and of Corporation E, a Delaware corporation (EIN 44-1234567) and a member of the Corporation A Group through December 31, Year 2. Corporation D and Corporation E became members of the Corporation B Group on January 1, Year 3.

(3) Since 1970, Corporation D has maintained assets and operated a widgets business in Country 1 through a branch in Country 1 (Branch 1). Branch 1 is a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a dual resident corporation (DRC) as defined in Treas. Reg. §1.1503–2(c)(2).

(4) Since 1970, Corporation E has maintained assets and operated a widgets business in Country 2 through a branch in Country 2 (Branch 2). Branch 2 is a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a DRC as defined in Treas. Reg. §1.1503–2(c)(2).

(5) Since 1975, Corporation E has maintained assets and operated a widgets business in Country 3 through a branch in

Country 3 (Branch 3). Branch 3 is a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a DRC as defined in Treas. Reg. §1.1503–2(c)(2).

(6) Since 1972, Corporation E has maintained assets and operated a widgets business in Country 4 through a branch in Country 4 (Branch 4). Branch 4 is a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a DRC as defined in Treas. Reg. §1.1503–2(c)(2).

Branch 1, Branch 2, Branch 3, and Branch 4 will hereinafter collectively be referred to as the "Corporation B Branches."

(7) The income and losses of Branch 4 were included in the Corporation A Group through Date A, Year 2. The income and losses of Branch 1, Branch 2, and Branch 3 were included in the Corporation A Group through December 31, Year 2.

(8) On Date A, Year 2, Corporation E, sold all of the assets of Branch 4 to an unrelated Country 4 company, Corporation 4. Corporation E's sale of Branch 4's assets is not a triggering event under Treas. Reg. §1.1503–2(g)(2)(iii)(A)(5) because the sale did not result in a carryover under Country 4 law of Branch 4's losses, expenses, or deductions to Corporation 4. As a result of this Date A, Year 2 sale, Branch 4 ceased to be a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a DRC as defined in Treas. Reg. §1.1503–2(c)(2). *See Appendix B, Note 1.*

(9) On December 31, Year 2, Corporation A distributed all of the stock of Corporation B to its Corporation A Class X common stockholders in exchange for all of the Corporation A Class X common stock in a split-off transaction described in Code §355. As a result of this split-off transaction: (a) Corporation B, Corporation D, and Corporation E, and the income and losses of Branch 1, Branch 2, and Branch 3 ceased to be included in the Corporation A Group; (b) Corporation B became the common parent of the Corporation B Group; and (c) the income and losses of Branch 1, Branch 2, and Branch 3 became included with the Corporation B Group. *See Appendix B, Note 2.*

(10) On Date C, Year 3, Corporation E sold the Branch 3 assets to an unrelated Country 3 company, Corporation 3. Corporation E's sale of Branch 3's assets is not a triggering event under Treas. Reg. §1.1503–2(g)(2)(iii)(A)(5) because the sale did not result in a carryover under the laws of Country 3 of Branch 3's losses, expenses, or deductions to Corporation 3. As a result of this Date C, Year 3 sale, Branch 3 ceased to be a separate unit as described in Treas. Reg. §1.1503–2(c)(3)(i)(A) and a DRC as defined in Treas. Reg. §1.1503–2(c)(2). *See Appendix B, Note 3.*

(11) The Corporation B Branches incurred net operating losses (NOLs) for the Year 1 taxable year and the Year 2 taxable year. Such losses were computed in accordance with Treas. Reg. §1.1503–2 (d)(1) and are as follows:

BRANCH	*Year 1 Tax Year*	*Year 2 Tax Year*
Branch 1	$	$
Branch 2	$	$
Branch 3	$	$
Branch 4	$	$ N.A. *
TOTAL	$	$

**See Appendix B, Note 4.*

The Corporation B Branches' NOLs for the Year 1 taxable year and the Year 2 taxable year will hereinafter collectively be referred to as the Corporation B Branches NOLs.

(12) The Corporation A Group used all of the Corporation B Branches NOLs within the meaning of Treas. Reg. §1.1503–2(c)(15).

(13) Corporation A, as common parent of the Corporation A Group, filed the elections and agreements described in Treas. Reg. §1.1503–2(g)(2)(i) for the Corporation B Branches NOLs incurred for the Year 1 taxable year and the Year 2 taxable year.

(14) Excluding the distribution of Corporation B stock to the Corporation A Class X common stockholders in a Code §355 split-off transaction, on December 31, Year 2, (as described in paragraph 9 above), causing Corporation B and its affiliates to cease being members of the Corporation A Group, no triggering event described in Treas. Reg. §1.1503–2 (g)(2)(iii) has occurred that is applicable to the Corporation B Branches NOLs.

THEREFORE, based on the above information and material submitted by Corporation A and Corporation B in connection with this Closing Agreement, and in the absence of other material factual or legal circumstances concerning the events described above, it is determined for federal income tax purposes that with respect to the Corporation B Branches NOLs:

(1) This Closing Agreement is a closing agreement described in Treas. Reg. §1.1503–2(g)(2)(iv)(B)(2)(i).

(2) The Corporation B Branches are separate units as described in Treas. Reg.

§1.1503–2(c)(3)(i)(A) and are dual resident corporations as defined in Treas. Reg. §1.1503–2(c)(2).

(3) The Corporation B Branch NOLs are dual consolidated losses under Treas. Reg. §1.1503–2(c)(5).

(4) But for Treas. Reg. §1.1503–2 (g)(2)(iv)(B)(2), the distribution of Corporation B stock to the Corporation A Class X common stockholders in a Code §355 split-off transaction, causing Corporation B, Corporation D, and Corporation E to cease being members of the Corporation A Group and the income and losses of the Corporation B Branches to cease being included in the Corporation A Group, was a triggering event under Treas. Reg. §1.1503–2(g)(2)(iii)(A)(2) requiring the recapture of Corporation B Branch NOLs as required by Treas. Reg. §1.1503–2(g)(2)(vii).

(5) Under Treas. Reg. §1.1503–2 (g)(2)(iv)(B)(2), the distribution of Corporation B stock to Corporation A Class X common stockholders in a Code §355 split-off transaction, whereby Corporation B, Corporation D, and Corporation E ceased to be members of the Corporation A Group and the income and losses of the Corporation B Branches ceased to be included in the Corporation A Group, is not considered to be a triggering event requiring the recapture of the Corporation B Branch NOLs and an interest charge.

(6) Upon any subsequent triggering event described in Treas. Reg. §1.1503–2(g)(2)(iii), the Corporation A Group and the Corporation B Group will be jointly and severally liable for the total amount of recapture of the dual consolidated losses of the Corporation B Branches and the related interest charge under Treas. Reg. §1.1503–2(g)(2)(vii), to the extent the triggering event does not fall under one of the exceptions provided in Treas. Reg. §1.1503–2(g)(2)(iv)(A) or (B). The character and source of the recapture amount shall be determined pursuant to Treas. Reg. §1.1503-2(g)(2)(vii)(D). An event otherwise constituting a triggering event applicable to the Corporation B Branch NOLs under Treas. Reg. §1.1503–2(g)(2)(iii)(A) shall not constitute a triggering event if it occurs in any taxable year after the fifteenth (15th) taxable year following the year in which the Corporation B Branch NOLs were incurred.

(7) The Corporation B Group will treat any potential recapture amount under Treas. Reg. §1.1503–2(g)(2)(vii) as unrealized built-in gain for purposes of Code §384(a), subject to any applicable exceptions thereunder, and such total recapture amount shall constitute recognized built-in gain of the Corporation B Group for purposes of Code §384(a), subject to any applicable exceptions thereunder.

(8) The Corporation B Group will comply with the reporting requirements described in Treas. Reg. §1.1503–2 (g)(2)(vi) with respect to each Corporation B Branch NOL for the Year 1 taxable year and the Year 2 taxable year.

(9) If the amount of the Corporation B Branch NOLs is adjusted by the Internal Revenue Service, judicial authority, or otherwise in a final determination of taxes for taxable years ending December 31, Year 1, and December 31, Year 2, the provisions of this Closing Agreement will apply *mutatis mutandis* to such final adjusted loss amounts.

NOW THIS CLOSING AGREEMENT WITNESSETH, that Corporation A, Corporation B, and the Commissioner of Internal Revenue hereby mutually agree to the determinations set forth above and further mutually agree that those determinations shall be final and conclusive, subject, however, to reopening in the event of fraud, malfeasance, or misrepresentation of material fact, and provided that any change or modification of applicable statutes or tax conventions shall render this Closing Agreement ineffective to the extent that it is dependent upon such statutes or tax conventions.

IN WITNESS WHEREOF, by signing the foregoing, the above parties signify that they have read and agreed to the terms of this document.

CORPORATION A

By:________________________________ Date:____________________

Title: ________________________________

CORPORATION B

By:________________________________ Date:____________________

Title: ________________________________

COMMISSIONER OF INTERNAL REVENUE

By:________________________________ Date:____________________

Title: Associate Chief Counsel (International)

By:________________________________ Date:____________________

Title: Director, International

Prohibition of *Ex Parte* Communications Between Appeals Officers And Other Internal Revenue Service Employees

Rev. Proc. 2000–43

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SECTION 1. PURPOSE AND SCOPE

Section 1001(a) of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105–206, 112 Stat. 685 (RRA 98), states that "The Commissioner of Internal Revenue shall develop and implement a plan to reorganize the Internal Revenue Service. The plan shall ...

(4) ensure an independent appeals function within the Internal Revenue Service, including the prohibition in the plan of ex parte communications between appeals officers and other Internal Revenue Service employees to the extent that such communications appear to compromise the independence of the appeals officers."

Notice 99–50, 1999–40 I.R.B. 444 (October 4, 1999), set forth a proposed revenue procedure concerning the ex parte communication prohibition. The proposed revenue procedure provided guidance in the form of a series of questions and answers that address situations frequently encountered by the Service during the course of an administrative appeal and invited public comment. The Department of the Treasury and the Internal Revenue Service have considered all comments received, and the proposed revenue procedure has been modified to take into account the concerns raised. Specifically, the scope of permissible communications has been clarified, limitations have been placed on communications between Appeals and certain employees in the Office of Chief Counsel, concerns about communications that take place in the context of multi-functional meetings have been addressed, and other questions and answers have been modified. In addition, new questions and answers have been included to define key terms and clarify responsibilities of the parties, permit taxpayers/representatives to waive the prohibition, and to address certain management issues.

SECTION 2. BACKGROUND

In 1927, the Internal Revenue Service established an administrative appeal process to resolve tax disputes without litigation. The Appeals mission is to resolve tax controversies, without litigation, on a basis that is fair and impartial to both the Government and the taxpayer. Local Appeals Officers have traditionally reported to different managers than the Service officials who proposed the adjustment. Appeals has historically been able to settle the vast majority of the cases that come within its jurisdiction.

The inventory of cases handled by Appeals falls into two major categories — nondocketed and docketed B determined by whether the case is pending in the United States Tax Court. Nondocketed cases typically involve an administrative protest by the taxpayer of the findings and conclusions of the Examination, Collection, or other IRS function that initially considers a taxpayer's case. The taxpayer's protest is typically followed by a conference, or series of conferences, with the taxpayer or the taxpayer's representative, during which Appeals and the taxpayer attempt to reach resolution of the issues in dispute. Docketed cases involve disputes where the taxpayer has filed a petition in the U.S. Tax Court, contesting a determination made by the Service in a statutory notice of deficiency. Following the filing of the petition, taxpayers who have not previously availed themselves of the opportunity for an Appeals conference generally are afforded an opportunity to resolve their case with Appeals before the case proceeds further in the litigation process. *See generally* Rev. Proc. 87–24, 1987–1 C.B. 720. In both types of disputes, Appeals has broad authority to negotiate settlements by applying a "hazards of litigation" standard.

Proceedings before Appeals have traditionally followed a much less formal course than court proceedings. While proceedings before Appeals are designed to be fair and impartial, they are not subject to judicial rules of evidence or procedure. Some early legislative proposals during 1998 would have required Appeals to adopt more formal and less flexible processes. S. Rep. No. 1669, 105th Cong., 2nd Sess., § 304(a) (Feb. 24, 1998), would have established an independent Office of Appeals in the Internal Revenue Service, the head of which was to be appointed by and report directly to the Oversight Board. Further, this proposal would have barred Appeals from considering issues not "raised" by the originating function and prohibited "any communication" with the originating function unless the taxpayer or taxpayer's representative had an opportunity to be present.

As ultimately enacted, § 1001(a)(4) of RRA 98 did not impose a comprehensive overhaul of Appeals' processes. Instead, that section requires the IRS, as part of its reorganization plan, to establish an independent Office of Appeals "within the Internal Revenue Service." The plan must prohibit ex parte communications "to the extent such communications appear to compromise the independence" of Appeals. When the evolution of § 1001(a)(4) of RRA 98 during the1998 legislative process is considered in light of Appeals longstanding methods of operation, it can be fairly concluded that Appeals must be accorded a significant degree of independence from other IRS components, and should be mindful to avoid ex parte communications with other IRS functions that might appear to compromise that independence. The statutory provision cannot, however, be interpreted as mandating a major redesign of the fundamental processes Appeals has traditionally followed to carry out its dispute resolution mission.

The procedures set forth in this Revenue Procedure are designed to accommodate the overall interests of tax admin-

istration, while preserving operational features that are vital to Appeals' case resolution processes within the structure of the IRS and ensuring more open lines of communication between Appeals and the taxpayer/representative. Thus, in order to preserve the informal give-and-take and flexibilities that have been conducive to achieving settlements in Appeals, the guidance provided in this revenue procedure does not adopt the formal ex parte procedures that would apply in a judicial proceeding. The guidance is designed to ensure the independence of the Appeals organization, while preserving the role of Appeals as a flexible administrative settlement authority, operating within the Internal Revenue Service's overall framework of tax administration responsibilities. For example, as more fully explained in Section 3 below:

- Appeals will retain procedures for (a) returning cases that are not ready for Appeals consideration, (b) raising certain new issues, and (c) seeking review and comments from the originating IRS function with respect to new information or evidence furnished by the taxpayer or representative.
- Appeals will continue to be able to obtain legal advice from the Office of Chief Counsel, subject to limitations designed to ensure that the advice to Appeals is not provided by the same field attorneys who previously gave advice on the same issue to the IRS officials who made the determination Appeals is reviewing. These limitations adopt some of the suggestions received in response to Notice 99–50 and reflect a balance between meeting Appeals' needs for legal assistance and avoiding ex parte communications that might appear to compromise Appeals' independence.
- Finally, the Revenue Procedure makes clear that the Commissioner and others responsible for overall IRS operations (including Appeals) may continue to communicate ex parte with Appeals in order to fulfill their responsibilities.

SECTION 3. GUIDANCE CONCERNING THE *EX PARTE* COMMUNICATIONS PROHIBITION DESCRIBED IN SECTION 1001(a)(4) OF THE INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1998

Q-1 What is "ex parte communication" and when is it prohibited?

A-1 For the purposes of this revenue procedure, ex parte communications are communications that take place between Appeals and another Service function without the participation of the taxpayer or the taxpayer's representative (taxpayer/representative). While the legislation refers to "appeals officers," the overall intent of the ex parte provision is to ensure the independence of the entire Appeals organization. Ex parte communications between any Appeals employee, *e.g.*, Appeals Officers, Appeals Team Case Leaders, Appeals Tax Computation Specialists, and employees of other Internal Revenue Service offices are prohibited to the extent that such communications appear to compromise the independence of Appeals.

Q-2 Is the prohibition on ex parte communications limited to oral communications?

A-2 No. The prohibition is not limited to oral communications. It applies to any form of communication, oral or written (manually or computer generated).

Q-3 Are communications between Appeals Officers and other Appeals employees subject to the prohibition on ex parte communications?

A-3 No. As indicated in A-1 above, the ex parte communication prohibition was intended to preserve the independence of the Appeals organization as a whole. Intra-Appeals communications during the deliberation process do not compromise or appear to compromise that independence. Appeals employees may communicate freely with other Appeals employees without inviting the taxpayer/representative to participate.

Q-4 Is the administrative file transmitted to Appeals by the office that made the determination which is subject to the Appeals process (the originating function) considered to be an ex parte communication within the context of this revenue procedure?

A-4 No. The administrative file is not considered to be an ex parte communication within the context of this revenue procedure. The administrative file, containing the proposed determination and the taxpayer's protest or other approved means of communicating disagreement with the proposed determination, sets forth the boundaries of the dispute between the taxpayer and the Service and forms the basis for Appeals to assume jurisdiction.

Q-5 Does the prohibition on ex parte communications extend to discussions between Appeals employees and the originating function during the course of preliminary review of a newly assigned case?

A-5 It depends on the nature of the communication. During the preliminary review of a newly assigned case, officials in Appeals may ask questions that involve ministerial, administrative, or procedural matters and do not address the substance of the issues or positions taken in the case. For example, Appeals employees may make the following types of inquiries without involving the taxpayer/representative:

- Questions about whether certain information was requested and whether it was received.
- Questions about whether a document referred to in the workpapers that the Appeals Officer cannot locate in the file is available.
- Questions to clarify the content of illegible documents or writings.
- Questions about case controls on the IRS's management information systems.
- Questions relating to tax calculations that are solely mathematical in nature. Communications with the originating function which extend beyond matters of the type described above and address the substance of the issues in the case are prohibited unless the taxpayer is given the opportunity to participate. Examples of prohibited communications include:
- Discussions about the accuracy of the facts presented by the taxpayer and the relative importance of the facts to the determination.
- Discussions of the relative merits or

alternative legal interpretations of authorities cited in a protest or in a report prepared by the originating function.

- Discussions of the originating function's perception of the demeanor or credibility of the taxpayer or taxpayer's representative.

Q-6 Does the ex parte communications prohibition apply to Appeals consideration of cases which originated in the Collection function, e.g., collection due process (CDP) appeals, collection appeals program (CAP) cases, offers in compromise, trust fund recovery penalty cases, etc.?

A-6 Yes. The principles applicable to discussions between Appeals employees and officials in other originating functions also apply to discussions between Appeals and Collection employees. Appeals may not engage in discussions of the strengths and weaknesses of the issues and positions in the case, which would appear to compromise Appeals' independence. The taxpayer/representative should be given an opportunity to participate in any discussion that involves matters other than ministerial, administrative or procedural matters.

Section 3401 of RRA 98 (§§ 6320 and 6330 of the Internal Revenue Code), regarding due process in IRS collection actions, states that at a hearing, the Appeals Officer must obtain verification that the requirements of any applicable law or administrative procedure have been met. Communications seeking to verify compliance with legal and administrative requirements are similar to the ministerial, administrative or procedural inquiries discussed in A-5 above. Therefore, such communications are not subject to the prohibition on ex parte communications.

Q-7 Does the prohibition on ex parte communications change the criteria for premature referrals?

A-7 As a general rule, there is no change to current criteria or procedures. In essence, RRA 98 reinforces the instructions in Section 8.2.1.2 of the Internal Revenue Manual (IRM) and reaffirms Appeals' role as the settlement arm of the Service. If a case is not ready for Appeals consideration, Appeals may return it for further development or for other reasons described in IRM 8.2.1.2. Appeals may communicate with the originating function regarding the anticipated return of the case, but may not engage in a discussion of matters beyond the types of ministerial, administrative or procedural matters set forth in A-5 as part of a discussion of whether the premature referral guidelines require further activity by the originating function.

Q-8 Is there any change to the Appeals new issue policy?

A-8 No. The prohibition against ex parte communications does not affect Appeals' existing policy about raising new issues in Appeals. However, any new issue must first satisfy Appeals' new issue policy. New issues must continue to meet the "material" and "substantial" tests of IRM 8.6.1.4 and succeeding sections. If discussions with the originating function are needed in order to evaluate the strengths and weaknesses of the possible new issue, the taxpayer/representative must be given an opportunity to participate in such discussions. Appeals will continue to follow the principles of Policy Statement P-8-49 and the "General Guidelines" outlined in IRM 8.6.1.4.2 in deciding whether or not to raise a new issue.

Q-9 May Appeals continue to have ongoing communication with the originating function during the course of an appeal?

A-9 Yes. However, the prohibition on ex parte communications will affect the manner in which Appeals has traditionally operated during the course of the appeal. Appeals must give the taxpayer/representative the opportunity to participate in any discussions with the originating function which concern matters beyond the ministerial, administrative or procedural matters described in A-5 above.

Q-10 What should Appeals do if new information or evidence is submitted? Can Appeals still return the new material to the originating function for review and comment?

A-10 There is no change to existing procedures. The principles in IRM 8.2.1.2.2 remain in effect. The originating function should be given the opportunity to timely review and comment on significant new information presented by the taxpayer. "Significant new information" is information of a non-routine nature which, in the judgment of Appeals, may have had an impact on the originating function's findings or which may impact on the Appeals' independent evaluation of the litigating hazards. Generally, the review can be accomplished by sending the material to the originating function while Appeals retains jurisdiction of the case and proceeds with resolution of other issues. However, if it appears that important new information or evidence was purposely withheld from the originating function, the entire case should be returned to the originating function and jurisdiction relinquished pursuant to IRM 8.2.1.2.2(3). The taxpayer/representative must be notified when a case is returned to the originating function or new material not available during initial consideration has been sent to the originating function. The results of the originating function's review of the new information will be communicated to the taxpayer/representative.

Q-11 ***Does the prohibition on ex parte communications have any impact on the relationship between Appeals and Counsel?***

A-11 Chief Counsel is the legal adviser to the Commissioner of Internal Revenue and his or her officers and employees (including employees of Appeals) on all matters pertaining to the interpretation, administration and enforcement of the internal revenue laws and related statutes. Attorneys in the Office of Chief Counsel are expected to provide legal advice based on a determination of ". . . the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them," without bias in favor of either the Government or the taxpayer. Rev. Proc. 64–22, 1964–1 C.B. 689. To balance Appeals employees' need to obtain legal advice with the requirement that they avoid ex parte communications that would appear to compromise Appeals' independence, the following limitations will apply to communications between Appeals employees and attorneys in the Office of Chief Counsel in cases not docketed in the United States Tax Court:

Appeals employees should not communicate ex parte regarding an issue in a case pending before them with Counsel

field attorneys who have previously provided advice on that issue in the case to the IRS employees who made the determination Appeals is reviewing. Counsel will assign a different attorney to provide assistance to Appeals. If an Appeals employee believes it is necessary to seek advice from any Counsel field attorney who previously provided advice to the originating function regarding that issue in the case, the taxpayer/representative will be provided an opportunity to participate in any such communications.

Appeals' requests for legal advice that raise questions that cannot be answered with a high degree of certainty by application of established principles of law to particular facts will be referred to the Chief Counsel National Office and will be handled as requests for field service advice or technical advice, as appropriate, in accordance with applicable procedures. The response of the National Office to Appeals will be disclosed to the taxpayer in accordance with § 6110.

Appeals employees are cautioned that, while they may obtain legal advice from the Office of Chief Counsel, they remain responsible for independently evaluating the strengths and weaknesses of the specific issues presented by the cases assigned to them, and for making independent judgments concerning the overall strengths and weaknesses of the cases and the hazards of litigation. Consistent with this assignment of responsibility, Counsel attorneys will not provide advice that includes recommendations of settlement ranges for an issue in a case pending before Appeals or for the case as a whole.

The foregoing limitations on ex parte communications do not apply to cases docketed in the United States Tax Court. Docketed cases will be handled in accordance with Rev. Proc. 87–24, 1987–1 C.B. 720, and the Tax Court Rules of Practice and Procedure.

Q-12 Appeals is required to submit certain cases to the Joint Committee on Taxation for review. On occasion, the Joint Committee (or its staff) will question a settlement or raise a new issue. Are communications with the Joint Committee (or its staff) covered by the ex parte communications prohibition?

A-12 No. The prohibition applies only to communications between Appeals and other Internal Revenue Service employees.

Q-13 Does the prohibition on ex parte communications have any impact on the requirement that Industry Specialization Program (ISP) issues in cases in Appeals jurisdiction be reviewed and approved by the Appeals ISP Coordinator?

A-13 No. Existing procedures for review and approval remain in place. The Appeals ISP Coordinator serves as a resource person for the Appeals organization. The purpose of the review is to ensure consistency of settlements and adherence to approved settlement guidelines. Communications between Appeals employees and the Appeals ISP Coordinator are entirely internal within Appeals, and consequently, the ex parte communications prohibition does not apply.

Q-14 Delegation Order 247, 1996-1 C.B. 356, gives Examination case managers limited settlement authority to resolve ISP coordinated issues which have Appeals Settlement Guidelines, provided that they secure the review and approval of both the Examination and Appeals ISP Coordinators. Would such communications constitute a violation of the ex-parte communications prohibition?

A-14 No. The purpose of the review is to ensure that the resolution by Examination fits within the guidelines developed by Appeals and that the application of the guidelines is consistent. The role of the Appeals ISP coordinator is directive in nature and has no impact on the independence of Appeals.

Q-15 Does the prohibition on ex parte communications apply in the context of meetings which include representatives from Appeals, Counsel, Collection and Examination (ACCE meetings), industry wide ISP coordination meetings, or meetings of Compliance Councils or the Large Case Policy Board?

A-15 Generally, no. Meetings of this type usually involve general discussions of how to handle technical issues or procedural matters. As long as the discussions do not identify specific taxpayers, the prohibition on ex parte communications would not apply. Participants in cross-functional meetings need to remain cognizant of the prohibition on ex parte communications and ensure that discussions do not appear to compromise the independence of Appeals.

Q-16 Does the prohibition on ex parte communications apply to communications between Appeals and the Commissioner or other Service officials who have overall supervisory responsibility for IRS operations?

A-16 No. In accordance with § 7803, the Commissioner is responsible for managing and directing the administration of the internal revenue laws and tax conventions to which the United States is a party. In the course of exercising that statutory responsibility, the Commissioner and those officials, such as the Deputy Commissioner Operations, who have overall supervisory responsibility for IRS operations may communicate with Appeals about specific cases or issues and may direct that other IRS officials participate in meetings or discussions about such cases or issues without providing the taxpayer or representative an opportunity to participate.

Q-17 Does the prohibition on ex parte communications apply to discussions Appeals employees have with personnel in the IRS competent authority office regarding a taxpayer's request for relief under a tax treaty?

A-17 No. Communications between Appeals employees and IRS officials considering relief under competent authority procedures are not subject to the ex parte prohibitions because the Appeals Officer may assume that the competent authority is acting at the request, and with the consent, of the taxpayer.

Q-18 Does the prohibition on ex parte communications have any impact on Appeals communications with the Taxpayer Advocate Service (TAS) on an open case?

A-18 No. Communications by Appeals with the TAS that are initiated by the TAS are not subject to the prohibition because the Appeals Officer may assume that the

TAS is acting at the request, and with the consent, of the taxpayer.

Q-19 Are communications between Appeals and outside consultants or experts under contract to the IRS subject to the ex parte communication prohibition?

A-19 Yes. Under the ex parte rules adopted here, outside consultants or experts under contract to the IRS (other than those employed directly by Appeals) will be treated as "other IRS employees." Therefore, the principles set forth in A-5 will apply. Appeals must give the taxpayer/representative the opportunity to participate in case-specific discussions that concern matters beyond the non-substantive ministerial, administrative or procedural matters described in A-5 above.

Q-20 A number of questions and answers have referred to communications with the "originating function." How is that term defined?

A-20 An "originating function" is an organization within the IRS that makes determinations which are subject to the Appeals process. For purposes of this revenue procedure, the term includes the Examination, Collection, Service Center, International, and Tax Exempt/Government Entities functions, or their successor organizations.

Q-21 Several responses in this document refer to the taxpayer/representative being given an "opportunity to participate." What does this phrase mean?

A-21 It means that the taxpayer/representative will be given a reasonable opportunity to attend a meeting or be a participant in a conference call between Appeals and the originating function when the strengths and weaknesses of issues or positions in the taxpayer's case are discussed. The taxpayer/representative will be notified of a scheduled meeting or conference call and invited to participate. If the taxpayer/representative is unable to participate at the scheduled time, reasonable accommodations will be made to reschedule. This does not mean that the Service will delay scheduling a meeting for a protracted period of time to accommodate the taxpayer/representative. Facts and circumstances will govern what constitutes a reasonable delay.

Q-22 May the taxpayer/representative waive the prohibition on ex parte communications?

A-22 Yes. If the taxpayer/representative is given an opportunity to participate in a discussion, but decides that such participation is unnecessary, the prohibition can be waived. Generally, a waiver will be granted on a communication-by-communication basis. However, if the taxpayer/representative so desires, the waiver could encompass all communications that might occur during the course of Appeals' consideration of a specified case. The Appeals Officer should document the waiver in the Case Activity Record.

Q-23 What if the taxpayer/representative declines to participate or seeks to delay the meeting/conference call beyond a reasonable time?

A-23 Appeals should proceed with the meeting or discussion and document the taxpayer/representative's declination or the reason for proceeding in the absence of the taxpayer/representative. This could be accomplished by an entry in the Case Activity Record and a letter to the taxpayer/representative documenting the reason for proceeding.

Q-24 The IRM provides for computational review within 120 days of a team case being assigned. If this review reveals computational errors affecting the proposed tax liability, can Appeals discuss these errors with the originating function without violating the prohibition on ex parte communications?

A-24 It depends on the nature of the error. If the discrepancy is purely mathematical, any discussion would likely be informational only, and no violation of the prohibition is likely. Both the taxpayer/representative and the originating function would be advised before a mathematical correction is made.

However, if the error involves the interpretation of a legal principle or application of the law to a particular set of facts, the taxpayer/representative should be afforded the opportunity to participate in any scheduled meetings with the originating function to discuss the discrepancy. In such cases, there may be instances where the best approach is for Appeals to return the case for further development and correction.

Q-25 Does the prohibition on ex parte communications apply to pre-conference meetings between Appeals and Examination?

A-25 Yes. This is clearly a situation where the intended communications could appear to compromise the independence of Appeals. Pre-conference meetings should not be held unless the taxpayer/representative is given the opportunity to participate.

Q-26 Does the prohibition on ex parte communications apply to post-settlement conferences between Appeals and Examination?

A-26 No. The post-settlement conference with Examination is intended to inform Examination about the settlement of issues and to supply information that may be helpful in the examination of subsequent cycles. Appeals' objective is to ensure that Examination fully understands the settlement and the rationale for the resolution. In addition, the conference provides an opportunity for Appeals to discuss with Examination the application of Delegation Orders 236 and 247 (*i.e.*, settlement by Examination consistent with prior Appeals settlement or ISP settlement guidelines) to issues settled by Appeals.

The tax periods that are the subject of the post-settlement conference have been finalized, and the participants are cautioned to limit discussion to the results in the closed cycle. Discussion of the resolution of issues present in the closed periods does not jeopardize the independence of Appeals. Any discussion that addresses open cycles of the same taxpayer should be postponed, and the guidance provided in this revenue procedure relating to ongoing disputes should be followed.

Q-27 Does the prohibition on ex parte communications alter existing procedures for handling claims filed late in the Appeals process?

A-27 No. There is no change to existing procedure. The claim should be referred to the originating function with a request for expedited examination. Because such a referral is in the nature of a ministerial act and involves no discussion about the strengths and weaknesses of the issue, the referral is not subject to the prohibition.

Q-28 How will the Service monitor compliance with the prohibition on ex parte communications?

A-28 Employees will receive training on the contents of this revenue procedure and will be encouraged to seek managerial guidance whenever they have questions about the propriety of an ex parte communication. Managers will consider feedback from other functions and will be responsible for monitoring compliance during their day-to-day interaction with employees, as well as during workload reviews and closed case reviews. Violations will be addressed in accordance with existing administrative and personnel processes.

Q-29 Are IRS employees assigned to functions other than Appeals responsible for complying with the prohibition on ex parte communication?

A-29 Yes. It is recognized that Appeals cannot always fully control communications from other IRS personnel. Appeals will make every effort to promptly terminate any discussion that verges into matters not permitted by these rules. However, all IRS and Counsel employees share the responsibility to ensure that communications do not appear to compromise the independence of Appeals. Violations will be addressed in accordance with existing administrative and personnel processes.

SECTION 4. EFFECTIVE DATE

This revenue procedure is effective for communications between Appeals Officers and other Internal Revenue Service employees which take place after October 23, 2000, the date this revenue procedure is published in the Internal Revenue Bulletin.

DRAFTING INFORMATION

The principal author of this revenue procedure is David M. Geber, Appeals LMSB Operations, Headquarters Appeals. For further information regarding this revenue procedure, contact Mr. Geber at (202) 694-1827 (not a toll-free number).

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26 CFR 601.201: Rulings and determination letters (Also Part I, Sections 846; 1.846–1.)

Rev. Proc. 2000–44

SECTION 1. PURPOSE

This revenue procedure prescribes the loss payment patterns and discount factors for the 2000 accident year. These factors will be used for computing discounted unpaid losses under § 846 of the Internal Revenue Code. *See* Rev. Proc. 98–11, 1998–1 C.B. 358, for background concerning the loss payment patterns and application of the discount factors.

SEC. 2. SCOPE

This revenue procedure applies to any taxpayer that is required to discount its unpaid losses under § 846 for a line of business using discount factors published by the Secretary.

SEC. 3. TABLES OF DISCOUNT FACTORS

.01 The following tables present separately for each line of business the discount factors under § 846 for accident year 2000. All the discount factors presented in this section were determined using the applicable interest rate under § 846(c) for 2000, which is 6.09 percent, and by assuming all loss payments occur in the middle of the calendar year.

.02 If the groupings of individual lines of business on the annual statement change, taxpayers must discount the unpaid losses on the affected lines of business in accordance with the discounting patterns that would have applied to those unpaid losses based on their classification on the 1995 annual statement. *See* Rev. Proc. 98–11, 1998–1 C. B. 358, section 2, for additional background on discounting under section 846 and the use of the Secretary's tables.

.03 Section V of Notice 88–100, 1988–2 C.B. 439, provides a composite discount factor to be used in determining the discounted unpaid losses for accident years that are not separately reported on the annual statement. Taxpayers that do not use the methodology set forth in section V of Notice 88–100 should instead use the discount factor for the appropriate year in the Secretary's table for that line of business. If such taxpayers have unpaid losses relating to an accident year that is older than the last accident year for which a discount factor is presented in the Secretary's table, those unpaid losses should be discounted using the discount factor for the last accident year in the Secretary's table. *See* section 2.03(3) of Rev. Proc. 98–11.

.04 Tables

Accident and Health
(Other Than Disability Income or Credit Disability Insurance)

Discount factor for all years equals 97.0874 percent.

Auto Physical Damage

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	89.9430	89.9430	10.0570	9.7134	96.5830
AY+ 1	99.3814	9.4384	0.6186	0.5834	94.3008
AY+ 2	N/A	0.3093	0.3093	0.3003	97.0874

Commercial Auto/Truck Liability/Medical

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	25.8075	25.8075	74.1925	65.1995	87.8788
AY+ 1	49.8793	24.0718	50.1207	44.3762	88.5386
AY+ 2	67.6592	17.7799	32.3408	28.7654	88.9446
AY+ 3	79.7711	12.1119	20.2289	18.0419	89.1890
AY+ 4	88.2132	8.4421	11.7868	10.4453	88.6190
AY+ 5	93.1778	4.9646	6.8222	5.9679	87.4779
AY+ 6	95.9623	2.7845	4.0377	3.4633	85.7748
AY+ 7	97.0091	1.0468	2.9909	2.5960	86.7980
AY+ 8	97.5719	0.5628	2.4281	2.1744	89.5538
AY+ 9	98.2191	0.6471	1.7809	1.6403	92.1035
AY+10	N/A	0.6471	1.1338	1.0737	94.6950
AY+11	N/A	0.6471	0.4867	0.4725	97.0874

.Composite Discount Factors

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	35.4611	35.4611	64.5389	55.4546	85.9243
AY+ 1	59.1449	23.6838	40.8551	34.4374	84.2916
AY+ 2	70.8220	11.6771	29.1780	24.5073	83.9923
AY+ 3	81.9019	11.0799	18.0981	14.5875	80.6022
AY+ 4	86.3688	4.4669	13.6312	10.8749	79.7797
AY+ 5	90.0497	3.6809	9.9503	7.7459	77.8458
AY+ 6	92.7488	2.6991	7.2512	5.4375	74.9880
AY+ 7	93.8259	1.0771	6.1741	4.6593	75.4648
AY+ 8	94.2415	0.4156	5.7585	4.5150	78.4051
AY+ 9	94.8568	0.6153	5.1432	4.1561	80.8087
AY+10	N/A	0.6153	4.5279	3.7755	83.3830
AY+11	N/A	0.6153	3.9125	3.3716	86.1744
AY+12	N/A	0.6153	3.2972	2.9431	89.2617
AY+13	N/A	0.6153	2.6819	2.4886	92.7929
AY+14	N/A	0.6153	2.0665	2.0063	97.0874

Fidelity/Surety

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	24.1540	24.1540	75.8460	70.2828	92.6652
AY+ 1	59.0961	34.9421	40.9039	38.5727	94.3008
AY+ 2	N/A	20.4520	20.4520	19.8563	97.0874

Financial Guaranty/Mortgage Guaranty

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	9.2513	9.2513	90.7487	84.0520	92.6206
AY+ 1	50.5659	41.3146	49.4341	46.6168	94.3008
AY+ 2	N/A	24.7171	24.7171	23.9971	97.0874

International (Composite)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	35.4611	35.4611	64.5389	55.4546	85.9243
AY+ 1	59.1449	23.6838	40.8551	34.4374	84.2916
AY+ 2	70.8220	11.6771	29.1780	24.5073	83.9923
AY+ 3	81.9019	11.0799	18.0981	14.5875	80.6022
AY+ 4	86.3688	4.4669	13.6312	10.8749	79.7797
AY+ 5	90.0497	3.6809	9.9503	7.7459	77.8458
AY+ 6	92.7488	2.6991	7.2512	5.4375	74.9880
AY+ 7	93.8259	1.0771	6.1741	4.6593	75.4648
AY+ 8	94.2415	0.4156	5.7585	4.5150	78.4051
AY+ 9	94.8568	0.6153	5.1432	4.1561	80.8087
AY+10	N/A	0.6153	4.5279	3.7755	83.3830
AY+11	N/A	0.6153	3.9125	3.3716	86.1744
AY+12	N/A	0.6153	3.2972	2.9431	89.2617
AY+13	N/A	0.6153	2.6819	2.4886	92.7929
AY+14	N/A	0.6153	2.0665	2.0063	97.0874

Medical Malpractice — Claims-Made

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	6.3899	6.3899	93.6101	77.2316	82.5035
AY+ 1	24.0011	17.6112	75.9989	63.7954	83.9426
AY+ 2	42.6970	18.6959	57.3030	48.4238	84.5048
AY+ 3	58.0610	15.3640	41.9390	35.5479	84.7609
AY+ 4	69.6653	11.6043	30.3347	25.7603	84.9203
AY+ 5	75.6033	5.9380	24.3967	21.2130	86.9502
AY+ 6	81.8786	6.2753	18.1214	16.0413	88.5212
AY+ 7	87.8539	5.9753	12.1461	10.8637	89.4415
AY+ 8	89.5207	1.6668	10.4793	9.8084	93.5982
AY+ 9	94.3025	4.7818	5.6975	5.4805	96.1916
AY+10	N/A	4.7818	0.9157	0.8890	97.0874

Medical Malpractice — Occurrence

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	2.1239	2.1239	97.8761	72.1344	73.6997
AY+ 1	6.4831	4.3592	93.5169	72.0374	77.0314
AY+ 2	15.5987	9.1156	84.4013	67.0354	79.4246
AY+ 3	31.9062	16.3075	68.0938	54.3211	79.7739
AY+ 4	45.0931	13.1868	54.9069	44.0468	80.2208
AY+ 5	50.0751	4.9821	49.9249	41.5977	83.3206
AY+ 6	60.9728	10.8976	39.0272	32.9064	84.3166
AY+ 7	69.2138	8.2411	30.7862	26.4221	85.8247
AY+ 8	72.8658	3.6519	27.1342	24.2698	89.4433
AY+ 9	80.0005	7.1347	19.9995	18.3990	91.9973
AY+10	N/A	7.1347	12.8648	12.1707	94.6050
AY+11	N/A	7.1347	5.7300	5.5631	97.0874

Miscellaneous Casualty

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	77.6669	77.6669	22.3331	21.1962	94.9091
AY+ 1	94.0673	16.4004	5.9327	5.5946	94.3008
AY+ 2	N/A	2.9664	2.9664	2.8800	97.0874

Other Liability — Claims-Made

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	10.2440	10.2440	89.7560	74.2142	82.6844
AY+ 1	29.3763	19.1323	70.6237	59.0277	83.5805
AY+ 2	44.4111	15.0349	55.5889	47.1365	84.7949
AY+ 3	67.8197	23.4086	32.1803	25.8963	80.4726
AY+ 4	73.4753	5.6555	26.5247	21.6482	81.6150
AY+ 5	78.8604	5.3852	21.1396	17.4198	82.4039
AY+ 6	83.5027	4.6422	16.4973	13.6992	83.0388
AY+ 7	84.0676	0.5649	15.9324	13.9516	87.5674
AY+ 8	85.2129	1.1453	14.7871	13.6216	92.1180
AY+ 9	90.5992	5.3863	9.4008	8.9033	94.7074
AY+10	N/A	5.3863	4.0145	3.8976	97.0874

Other Liability — Occurrence

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	13.5751	13.5751	86.4249	68.2254	78.9418
AY+ 1	26.3964	12.8213	73.6036	59.1744	80.3960
AY+ 2	40.2725	13.8761	59.7275	48.4857	81.1782
AY+ 3	55.4566	15.1841	44.5434	35.7988	80.3685
AY+ 4	65.3309	9.8742	34.6691	27.8085	80.2112
AY+ 5	74.0647	8.7339	25.9353	20.5062	79.0668
AY+ 6	80.9090	6.8442	19.0910	14.7055	77.0281
AY+ 7	84.3622	3.4532	15.6378	12.0442	77.0197
AY+ 8	84.6163	0.2542	15.3837	12.5159	81.3585
AY+ 9	86.7311	2.1147	13.2689	11.1000	83.6538
AY+10	N/A	2.1147	11.1542	9.5978	86.0463
AY+11	N/A	2.1147	9.0395	8.0041	88.5462
AY+12	N/A	2.1147	6.9247	6.3134	91.1715
AY+13	N/A	2.1147	4.8100	4.5197	93.9645
AY+14	N/A	2.1147	2.6953	2.6168	97.0874

Multiple Peril Lines
(Homeowners/Farmowners Multiple Peril, Commercial Multiple Peril, and Special Liability (Ocean Marine, Aircraft (All Perils), Boiler and Machinery))

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	55.9587	55.9587	44.0413	39.1921	88.9894
AY+ 1	77.8939	21.9352	22.1061	18.9856	85.8842
AY+ 2	84.0083	6.1144	15.9917	13.8440	86.5701
AY+ 3	91.3188	7.3105	8.6812	7.1573	82.4462
AY+ 4	92.1670	0.8482	7.8330	6.7195	85.7851
AY+ 5	94.3838	2.2168	5.6162	4.8455	86.2767
AY+ 6	96.4959	2.1121	3.5041	2.9651	84.6181
AY+ 7	97.3670	0.8712	2.6330	2.2484	85.3944
AY+ 8	98.0034	0.6364	1.9966	1.7299	86.6410
AY+ 9	98.4059	0.4025	1.5941	1.4207	89.1194
AY+10	N/A	0.4025	1.1916	1.0926	91.6918
AY+11	N/A	0.4025	0.7892	0.7446	94.3565
AY+12	N/A	0.4025	0.3867	0.3754	97.0874

Other
(Including Credit)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	66.7418	66.7418	33.2582	31.4101	94.4432
AY+ 1	89.2755	22.5337	10.7245	10.1133	94.3008
AY+ 2	N/A	5.3622	5.3622	5.2061	97.0874

Private Passenger Auto Liability/Medical

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	37.9339	37.9339	62.0661	56.4356	90.9282
AY+ 1	67.7044	29.7705	32.2956	29.2089	90.4424
AY+ 2	81.5316	13.8272	18.4684	16.7457	90.6722
AY+ 3	89.8898	8.3583	10.1102	9.1565	90.5677
AY+ 4	94.6531	4.7633	5.3469	4.8080	89.9215
AY+ 5	97.1265	2.4734	2.8735	2.5532	88.8539
AY+ 6	98.4587	1.3322	1.5413	1.3366	86.7155
AY+ 7	98.9811	0.5224	1.0189	0.8799	86.3544
AY+ 8	99.2330	0.2519	0.7670	0.6740	87.8739
AY+ 9	99.4067	0.1737	0.5933	0.5362	90.3643
AY+10	N/A	0.1737	0.4196	0.3899	92.9156
AY+11	N/A	0.1737	0.2460	0.2348	95.4492
AY+12	N/A	0.1737	0.0723	0.0702	97.0874

Products Liability — Claims-Made

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	4.9750	4.9750	95.0250	75.9026	79.8765
AY+ 1	15.1072	10.1322	84.8928	70.0889	82.5617
AY+ 2	30.9560	15.8488	69.0440	58.0331	84.0523
AY+ 3	38.2420	7.2860	61.7580	54.0627	87.5396
AY+ 4	68.6101	30.3681	31.3899	26.0760	83.0712
AY+ 5	78.5966	9.9865	21.4034	17.3779	81.1923
AY+ 6	88.3971	9.8005	11.6029	8.3417	71.8934
AY+ 7	93.2957	4.8986	6.7043	3.8042	56.7423
AY+ 8	88.3815	-4.9142	11.6185	9.0975	78.3015
AY+ 9	89.6105	1.2290	10.3895	8.3856	80.7125
AY+10	N/A	1.2290	9.1604	7.6304	83.2971
AY+11	N/A	1.2290	7.9314	6.8291	86.1028
AY+12	N/A	1.2290	6.7024	5.9791	89.2095
AY+13	N/A	1.2290	5.4733	5.0774	92.7656
AY+14	N/A	1.2290	4.2443	4.1207	97.0874

Products Liability – Occurrence

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	9.0653	9.0653	90.9347	69.1525	76.0464
AY+ 1	14.9035	5.8382	85.0965	67.3506	79.1462
AY+ 2	29.2591	14.3555	70.7409	56.6660	80.1036
AY+ 3	45.6462	16.3871	54.3538	43.2383	79.5496
AY+ 4	57.5945	11.9483	42.4055	33.5647	79.1518
AY+ 5	63.8634	6.2689	36.1366	29.1518	80.6712
AY+ 6	75.2266	11.3632	24.7734	19.2231	77.5957
AY+ 7	78.2679	3.0413	21.7321	17.2613	79.4274
AY+ 8	78.1898	-0.0781	21.8102	18.3929	84.3316
AY+ 9	81.8722	3.6825	18.1278	15.7201	86.7184
AY+10	N/A	3.6825	14.4453	12.8845	89.1953
AY+11	N/A	3.6825	10.7628	9.8762	91.7625
AY+12	N/A	3.6825	7.0803	6.6847	94.4128
AY+13	N/A	3.6825	3.3979	3.2989	97.0874

Reinsurance A
(Nonproportional Property)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	27.1668	27.1668	72.8332	64.8422	89.0284
AY+ 1	68.7008	41.5340	31.2992	26.0111	83.1046
AY+ 2	70.0362	1.3354	29.9638	26.2197	87.5046
AY+ 3	87.5338	17.4976	12.4662	9.7940	78.5641
AY+ 4	90.2132	2.6794	9.7868	7.6307	77.9687
AY+ 5	91.3751	1.1619	8.6249	6.8986	79.9846
AY+ 6	94.3845	3.0095	5.6155	4.2190	75.1316
AY+ 7	93.3293	-1.0552	6.6707	5.5628	83.3917
AY+ 8	N/A	1.0387	5.6320	4.8317	85.7905
AY+ 9	N/A	1.0387	4.5932	4.0560	88.3049
AY+10	N/A	1.0387	3.5545	3.2332	90.9598
AY+11	N/A	1.0387	2.5158	2.3602	93.8153
AY+12	N/A	1.0387	1.4771	1.4340	97.0874

Reinsurance B
(Nonproportional Liability)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	6.6962	6.6962	93.3038	69.1335	74.0951
AY+ 1	22.3944	15.6982	77.6056	57.1746	73.6733
AY+ 2	32.6486	10.2542	67.3514	50.0947	74.3781
AY+ 3	50.2234	17.5748	49.7766	35.0434	70.4014
AY+ 4	53.5839	3.3605	46.4161	33.7162	72.6391
AY+ 5	55.6838	2.0999	44.3162	33.6066	75.8338
AY+ 6	63.6144	7.9306	36.3856	27.4848	75.5376
AY+ 7	66.4211	2.8066	33.5789	26.2678	78.2269
AY+ 8	N/A	2.8066	30.7723	24.9766	81.1660
AY+ 9	N/A	2.8066	27.9656	23.6069	84.4138
AY+10	N/A	2.8066	25.1590	22.1537	88.0547
AY+11	N/A	2.8066	22.3524	20.6120	92.2140
AY+12	N/A	2.8066	19.5457	18.9764	97.0874

Reinsurance C
(Financial Lines)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	11.4622	11.4622	88.5378	77.2190	87.2158
AY+ 1	44.5791	33.1169	55.4209	47.8112	86.2692
AY+ 2	63.9134	19.3343	36.0866	30.8085	85.3739
AY+ 3	65.6185	1.7051	34.3815	30.9285	89.9569
AY+ 4	79.9778	14.3593	20.0222	18.0220	90.0101
AY+ 5	88.9152	8.9374	11.0848	9.9140	89.4380
AY+ 6	91.2490	2.3338	8.7510	8.1140	92.7206
AY+ 7	94.7645	3.5155	5.2355	4.9872	95.2564
AY+ 8	N/A	3.5155	1.7200	1.6699	97.0874

Special Property
(Fire, Allied Lines, Inland Marine, Earthquake, Glass, Burglary and Theft)

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	57.4895	57.4895	42.5105	40.4949	95.2586
AY+ 1	90.5193	33.0297	9.4807	8.9404	94.3008
AY+ 2	N/A	4.7404	4.7404	4.6023	97.0874

Workers' Compensation

Tax Year	Cumulative Losses Paid (%)	Estimated Losses Paid Each Year (%)	Unpaid Losses at Year End (%)	Discounted Unpaid Losses at Year End (%)	Discount Factors (%)
AY+ 0	23.6461	23.6461	76.3539	62.5642	81.9398
AY+ 1	44.8166	21.1705	55.1834	44.5688	80.7648
AY+ 2	57.9652	13.1486	42.0348	33.7399	80.2667
AY+ 3	72.0542	14.0889	27.9458	21.2831	76.1583
AY+ 4	80.5542	8.5000	19.4458	13.8242	71.0909
AY+ 5	84.8876	4.3334	15.1124	10.2026	67.5118
AY+ 6	87.1173	2.2297	12.8827	8.5274	66.1927
AY+ 7	88.2647	1.1473	11.7353	7.8649	67.0194
AY+ 8	88.5404	0.2757	11.4596	8.0599	70.3333
AY+ 9	88.8062	0.2658	11.1938	8.2770	73.9426
AY+10	N/A	0.2658	10.9279	8.5072	77.8484
AY+11	N/A	0.2658	10.6621	8.7515	82.0804
AY+12	N/A	0.2658	10.3963	9.0107	86.6720
AY+13	N/A	0.2658	10.1304	9.2856	91.6604
AY+14	N/A	0.2658	9.8646	9.5773	97.0874

DRAFTING INFORMATION

The principal author of this revenue procedure is Katherine A. Hossofsky of the Office of the Associate Chief Counsel (Financial Institutions and Products). For further information regarding this revenue procedure, contact Ms. Hossofsky at (202) 622-3477 (not a toll-free number).

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26 CFR 601.201: Rulings and determination letters (Also Part I, Sections 832, 846; 1.832–4, 1.846–1.)

Rev. Proc. 2000–45

SECTION 1. PURPOSE

This revenue procedure prescribes the salvage discount factors for the 2000 accident year. These factors will be used for computing discounted estimated salvage recoverable under § 832 of the Internal Revenue Code.

SEC. 2. BACKGROUND

Section 832(b)(5)(A) requires that all estimated salvage recoverable (including that which cannot be treated as an asset for state accounting purposes) be taken into account in computing the deduction for losses incurred. Under § 832 (b)(5)(A), paid losses are to be reduced by salvage and reinsurance recovered during the taxable year. This amount is adjusted to reflect changes in discounted unpaid losses on nonlife insurance contracts and in unpaid losses on life insurance contracts. An adjustment is then made to reflect any changes in discounted estimated salvage recoverable and in reinsurance recoverable.

Pursuant to § 832(b), the amount of estimated salvage is determined on a discounted basis in accordance with procedures established by the Secretary.

SEC. 3. SCOPE

This revenue procedure applies to any taxpayer that is required to discount estimated salvage recoverable under § 832.

SEC. 4. APPLICATION

.01 The following tables present separately for each line of business the discount factors under § 832 for the 2000 accident year. All the discount factors presented in this section were determined using the applicable interest rate under § 846(c) for 2000, which is 6.09 percent, and by assuming all estimated salvage is recovered in the middle of each calendar year. *See* Rev. Proc. 98–12, 1998–1 C.B. 367, for background regarding the tables.

.02 These tables must be used by taxpayers irrespective of whether they elected to discount unpaid losses using their own historical experience under § 846.

.03 Section V of Notice 88–100, 1988–2 C. B. 439, provides guidance concerning the determination of discount factors for unpaid losses for accident years not separately reported on the annual statement. Taxpayers that do not use the methodology set forth in section V of Notice 88–100 should instead use the discount factors for the appropriate year in the Secretary's table for that line of business. If such taxpayers have unpaid losses relating to an accident year that is older than the last accident year for which a discount factor is presented in the Secretary's table, those unpaid losses should be discounted using the discount factor for the last accident year in the Secretary's table. *See* section 2.03(3) of Rev. Proc. 98–11, 1998–1 C.B. 358.

.04 Tables.

Accident and Health (Other Than Disability Income or Credit Disability Insurance)

Discount factor for all years equals 97.0874 percent.

Auto Physical Damage

Tax Year	Discount Factors (%)
AY+ 0	95.7079
AY+ 1	94.3008
AY+ 2	97.0874

Commercial Auto/Truck Liability/Medical

Tax Year	Discount Factors (%)
AY+ 0	88.4462
AY+ 1	87.6196
AY+ 2	89.3091
AY+ 3	88.6027
AY+ 4	88.4348
AY+ 5	90.7689
AY+ 6	86.1529
AY+ 7	91.6750
AY+ 8	90.1421
AY+ 9	92.6871
AY+10	95.2242
AY+11	97.0874

Composite Discount Factors

Tax Year	Discount Factors (%)
AY+ 0	86.0068
AY+ 1	84.4299
AY+ 2	84.0175
AY+ 3	83.9135
AY+ 4	84.6433
AY+ 5	85.2133
AY+ 6	85.2701
AY+ 7	85.3660
AY+ 8	88.1610
AY+ 9	90.6657
AY+10	93.2331
AY+11	95.7807
AY+12	97.0874

Fidelity/Surety

Tax Year	Discount Factors (%)
AY+ 0	93.0043
AY+ 1	94.3008
AY+ 2	97.0874

Financial Guaranty/Mortgage Guaranty

Tax Year	Discount Factors (%)
AY+ 0	94.8017
AY+ 1	94.3008
AY+ 2	97.0874

International (Composite)

Tax Year	Discount Factors (%)
AY+ 0	86.0068
AY+ 1	84.4299
AY+ 2	84.0175
AY+ 3	83.9135
AY+ 4	84.6433
AY+ 5	85.2133
AY+ 6	85.2701
AY+ 7	85.3660
AY+ 8	88.1610
AY+ 9	90.6657
AY+10	93.2331
AY+11	95.7807
AY+12	97.0874

Medical Malpractice — Claims-Made

Tax Year	Discount Factors (%)
AY+ 0	70.6135
AY+ 1	73.2471
AY+ 2	71.8267
AY+ 3	71.2085
AY+ 4	74.7120
AY+ 5	73.1233
AY+ 6	82.6622
AY+ 7	91.6505
AY+ 8	96.4072
AY+ 9	97.0874

Medical Malpractice — Occurrence

Tax Year	Discount Factors (%)
AY+ 0	64.5191
AY+ 1	67.8389
AY+ 2	72.3139
AY+ 3	76.0455
AY+ 4	72.9166
AY+ 5	78.8620
AY+ 6	83.7311
AY+ 7	86.8009
AY+ 8	91.1931
AY+ 9	93.8108
AY+10	96.4471
AY+11	97.0874

Miscellaneous Casualty

Tax Year	Discount Factors (%)
AY+ 0	95.1290
AY+ 1	94.3008
AY+ 2	97.0874

Multiple Peril Lines (Homeowners/Farmowners Multiple Peril, Commercial Multiple Peril, and Special Liability (Ocean Marine, Aircraft (All Perils), Boiler and Machinery))

Tax Year	Discount Factors (%)
AY+ 0	88.5313
AY+ 1	87.5052
AY+ 2	88.2611
AY+ 3	87.9246
AY+ 4	89.0327
AY+ 5	90.4578
AY+ 6	90.4533
AY+ 7	89.4276
AY+ 8	91.7961
AY+ 9	94.4397
AY+10	97.0874

Other (Including Credit)

Tax Year	Discount Factors (%)
AY+ 0	96.1583
AY+ 1	94.3008
AY+ 2	97.0874

Other Liability — Claims-Made

Tax Year	Discount Factors (%)
AY+ 0	77.8928
AY+ 1	83.2885
AY+ 2	82.3182
AY+ 3	80.0331
AY+ 4	82.9792
AY+ 5	87.5716
AY+ 6	86.1171
AY+ 7	91.6842
AY+ 8	93.7737
AY+ 9	96.4015
AY+10	97.0874

Other Liability — Occurrence

Tax Year	Discount Factors (%)
AY+ 0	78.8476
AY+ 1	79.5688
AY+ 2	81.9224
AY+ 3	83.8683
AY+ 4	85.1067
AY+ 5	82.7221
AY+ 6	86.7561
AY+ 7	88.6932
AY+ 8	92.7419
AY+ 9	95.2771
AY+10	97.0874

Private Passenger Auto Liability/Medical

Tax Year	Discount Factors (%)
AY+ 0	91.7145
AY+ 1	91.1741
AY+ 2	90.2569
AY+ 3	89.8777
AY+ 4	89.4206
AY+ 5	89.8689
AY+ 6	88.6823
AY+ 7	89.3993
AY+ 8	90.0819
AY+ 9	92.6259
AY+10	95.1657
AY+11	97.0874

Products Liability — Claims-Made

Tax Year	Discount Factors (%)
AY+ 0	79.2866
AY+ 1	81.3032
AY+ 2	85.7298
AY+ 3	85.6427
AY+ 4	81.3092
AY+ 5	88.2121
AY+ 6	81.0185
AY+ 7	88.3819
AY+ 8	96.8185
AY+ 9	97.0874

Products Liability — Occurrence

Tax Year	Discount Factors (%)
AY+ 0	75.8372
AY+ 1	78.4119
AY+ 2	76.8096
AY+ 3	78.0983
AY+ 4	79.8362
AY+ 5	79.1928
AY+ 6	80.5510
AY+ 7	72.7819
AY+ 8	78.1849
AY+ 9	80.6043
AY+10	83.2009
AY+11	86.0229
AY+12	89.1515
AY+13	92.7357
AY+14	97.0874

Reinsurance A (Nonproportional Property)

Tax Year	Discount Factors (%)
AY+ 0	86.7196
AY+ 1	89.8651
AY+ 2	92.5548
AY+ 3	91.9205
AY+ 4	79.2342
AY+ 5	94.8666
AY+ 6	93.5010
AY+ 7	96.0788
AY+ 8	97.0874

Reinsurance B (Nonproportional Liability)

Tax Year	Discount Factors (%)
AY+ 0	74.9392
AY+ 1	77.1865
AY+ 2	77.9061
AY+ 3	77.3172
AY+ 4	79.7911
AY+ 5	74.9223
AY+ 6	76.6707
AY+ 7	84.0847
AY+ 8	86.4718
AY+ 9	88.9546
AY+10	91.5395
AY+11	94.2379
AY+12	97.0874

Reinsurance C (Financial Lines)

Tax Year	Discount Factors (%)
AY+ 0	81.2986
AY+ 1	83.6608
AY+ 2	86.8994
AY+ 3	92.7099
AY+ 4	91.3004
AY+ 5	93.1619
AY+ 6	89.7226
AY+ 7	96.9751
AY+ 8	97.0874

Special Property (Fire, Allied Lines, Inland Marine, Earthquake, Glass, Burglary and Theft)

Tax Year	Discount Factors (%)
AY+ 0	92.3377
AY+ 1	94.3008
AY+ 2	97.0874

Workers' Compensation

Tax Year	Discount Factors (%)
AY+ 0	78.6954
AY+ 1	81.0988
AY+ 2	82.9848
AY+ 3	84.5349
AY+ 4	84.6485
AY+ 5	84.8143
AY+ 6	85.9824
AY+ 7	86.7267
AY+ 8	89.1111
AY+ 9	91.6840
AY+10	94.3504
AY+11	97.0874

DRAFTING INFORMATION

The principal author of this revenue procedure is Katherine A. Hossofsky of the Office of the Associate Chief Counsel (Financial Institutions and Products). For further information regarding this revenue procedure, contact Ms. Hossofsky at (202) 622-3477 (not a toll-free number).

Part IV. Items of General Interest

Notice of Proposed Rulemaking and Notice of Public Hearing

Nondiscrimination Requirements for Certain Defined Contribution Retirement Plans

REG–114697–00

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations that would prescribe conditions under which certain defined contribution retirement plans (sometimes referred to as "new comparability" plans) are permitted to demonstrate compliance with applicable nondiscrimination requirements based on plan benefits rather than plan contributions. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments, requests to speak and outlines of oral comments to be discussed at the public hearing scheduled for January 25, 2001, at 10 a.m., must be received by January 5, 2001.

ADDRESSES: Send submissions to: CC:M&SP:RU (REG–114697–00) room 5226, 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 5 p.m. to: CC:M&SP:RU (REG–114697–00), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option of the IRS Home Page, or by submitting comments directly to the IRS Internet site at: http://www.irs.gov/tax_regs/reglist.html. The public hearing will be held in the IRS Auditorium (7th Floor), Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, John T. Ricotta, 202-622-6060 or Linda S. F. Marshall, 202-622-6090; concerning submissions and the hearing, and/or to be placed on the building access list to attend the hearing, LaNita VanDyke, 202-622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to 26 CFR part 1 under section 401(a)(4) of the Internal Revenue Code of 1986 (Code).

Section 401(a)(4) provides that a plan or trust forming part of a stock bonus, pension or profit-sharing plan of an employer shall not constitute a qualified plan under section 401(a) of the Code unless the contributions or benefits provided under the plan do not discriminate in favor of highly compensated employees (HCEs) (within the meaning of section 414(q)). Whether a plan satisfies this requirement depends on the form of the plan and its effect in operation.

Section 415(b)(6)(A) provides that the computation of benefits under a defined contribution plan, for purposes of section 401(a)(4), shall not be made on a basis inconsistent with regulations prescribed by the Secretary. The legislative history of this provision explains that, in the case of target benefit and other defined contribution plans, "regulations may establish reasonable earnings assumptions and other factors for these plans to prevent discrimination." Conf. Rep. No. 1280, 93d Cong., 2d Sess. 277 (1974).

Under the section 401(a)(4) regulations, a plan can demonstrate that either the contributions or the benefits provided under the plan are nondiscriminatory in amount. Defined contribution plans generally satisfy the regulations by demonstrating that contributions are nondiscriminatory in amount, through certain safe harbors provided for under the regulations or through general testing.

A defined contribution plan (other than an ESOP) may, however, satisfy the regulations on the basis of benefits by using "cross-testing" pursuant to rules provided in §1.401(a)(4)–8 of the regulations. Under this cross-testing method, contributions are converted to equivalent benefits payable at normal retirement age and tested on the basis of these equivalent benefits. The conversion is done by making an actuarial projection of the benefits payable at normal retirement age that are attributable to the contributions. Thus, this cross-testing method effectively permits nonelective employer contributions under a defined contribution plan to be tested on the basis of the benefits attributable to those contributions, in a manner similar to the testing of employer-provided benefits under a defined benefit plan.

In Notice 2000–14 (2000–10 I.R.B. 737), released February 24, 2000, the IRS and the Treasury Department initiated a review of issues related to use of the cross-testing method by so-called "new comparability plans" and requested public comments on this plan design from plan sponsors, plan participants and other interested parties. In general, new comparability plans are defined contribution plans that have built-in disparities between the allocation rates for classifications of participants consisting entirely or predominately of HCEs and the allocation rates for other employees.

In a typical new comparability plan, HCEs receive high allocation rates, while nonhighly compensated employees (NHCEs), regardless of their age or years of service, receive comparatively low allocation rates. For example, HCEs in such a plan might receive allocations of 18 or 20% of compensation, while NHCEs might receive allocations of 3% of compensation. A similar plan design, sometimes known as a "super-integrated" plan, provides for an additional allocation rate that applies only to compensation in excess of a specified threshold, but the specified threshold (e.g., $100,000) or the additional allocation rate (e.g., 10%) is higher than the maximum threshold and rate allowed under the permitted disparity rules of section 401(*l*).

These new comparability and similar plans rely on the cross-testing method to demonstrate compliance with the nondiscrimination rules by comparing the actuarially projected value of the employer contributions for the younger NHCEs with the actuarial projections of the larger contributions (as a percentage of compensation) for the older HCEs. As a result, these plans are able generally to provide

higher rates of employer contributions to HCEs, while NHCEs are not allowed to earn the higher allocation rates as they work additional years for the employer or grow older. Notwithstanding the analytical underpinnings of cross-testing, the IRS and the Treasury Department are concerned whether new comparability and similar plans are consistent with the basic purpose of the nondiscrimination rules under section 401(a)(4).

A variety of public comments were submitted in response to Notice 2000–14. Some comments expressed the view that changes in the application of the nondiscrimination rules to new comparability plans are unnecessary. These comments noted that in some cases such plans are adopted by employers that previously had no retirement plan for their employees. At the same time, many of these comments advanced suggestions as to the types of conditions that might be imposed on new comparability plans if changes in the rules are in fact proposed.

Other comments expressed the view that the rules need to be changed to increase the contributions made for NHCEs in new comparability plans and similar tax-qualified plan designs. These comments suggested various methods for ensuring that NHCEs receive larger allocations of employer contributions under new comparability plans, including imposing a maximum ratio of the allocation rates for HCEs to those for NHCEs or requiring a minimum allocation rate for the NHCEs.

Still other comments questioned the policy justification for permitting new comparability plans under the nondiscrimination rules governing tax-qualified plans because new comparability plan designs often provide such an overwhelming percentage of total plan allocations to HCEs, with only a modest percentage of the plan allocations going to the NHCEs. Some of these comments expressed concern that new comparability plans in some instances have been marketed as a technique for limiting most employees to lower allocation rates than they would receive under other defined contribution plan designs (such as salary ratio or age-weighted) and allocating the difference to one or more HCEs. They noted that, in some cases, the percentage of total plan allocations provided to the HCEs can exceed 90%.

After consideration of the comments received, the IRS and Treasury are issuing these proposed regulations, which would prescribe conditions that new comparability and similar plans must satisfy if they are to use the cross-testing method. The proposed regulations preserve the existing cross-testing rules of the section 401(a)(4) regulations, and would not affect cross-tested defined contribution plans that provide broadly available allocation rates, as defined in the proposed regulations. The definition of broadly available allocation rates includes plans that base allocations or allocation rates on age or service. In contrast to new comparability plans, these plans provide an opportunity for participants to "grow into" higher allocation rates as they age or accumulate additional service.

These proposed regulations would continue to permit new comparability plans. As suggested in various comments, the proposed regulations would set forth a minimum allocation "gateway" that would constrain the plan designs with the greatest disparity in favor of HCEs, while leaving many new comparability plan designs unchanged. A new comparability plan that satisfies the minimum allocation gateway could continue to use the existing cross-testing rules of the section 401(a)(4) regulations.

The proposed regulations also would prevent circumvention of the minimum allocation gateway by aggregating (for purposes of satisfying the nondiscrimination rules) a new comparability defined contribution plan with a defined benefit plan that provides only minimal benefits or covers only a relatively small number of the employees, or by aggregating a defined contribution plan with a defined benefit plan that benefits primarily HCEs. However, an aggregated defined contribution and defined benefit plan that is primarily defined benefit in character (as defined in the proposed regulations) could test for nondiscrimination on the basis of benefits in the same manner as under current law. Similarly, the ability to test for nondiscrimination on a benefits basis as under current law would be unrestricted if each of the defined contribution and defined benefit portions of the aggregated plan is a broadly available separate plan (as defined in the proposed regulations).

The proposed regulations would not affect defined benefit plans except where a defined contribution plan is aggregated with a defined benefit plan for nondiscrimination purposes and thus is a part of a DB/DC plan (as defined in §1.401(a)(4)–9). The proposed regulations would not apply merely because a plan sponsor maintains both a defined contribution plan and a defined benefit plan. The proposed regulations would not require aggregation of a defined contribution plan with a defined benefit plan or otherwise modify the existing rules regarding when plans are required or permitted to be aggregated.

Explanation of Provisions

A. *Overview*

The basic structure of the proposed regulations permits defined contribution plans with broadly available allocation rates to test on a benefits basis ("cross-test") in the same manner as under current law, and permits other defined contribution plans to cross-test once they pass a gateway that prescribes minimum allocation rates for NHCEs. Similarly, the proposed regulations permit a DB/DC plan to test on a benefits basis in the same manner as under current law if the DB/DC plan either is primarily defined benefit in character or consists of broadly available separate plans. Other DB/DC plans are permitted to test on a benefits basis once they pass a corresponding gateway prescribing minimum aggregate normal allocation rates for NHCEs.

B. *Gateway for Cross-Testing of New Comparability and Similar Plans*

The proposed regulations would require that a defined contribution plan that does not provide broadly available allocation rates (as defined in these proposed regulations) satisfy a gateway in order to be eligible to use the cross-testing rules to meet the nondiscrimination requirements of section 401(a)(4). A plan would satisfy this minimum allocation gateway if each NHCE in the plan has an allocation rate that is at least one third of the allocation rate of the HCE with the highest alloca-

tion rate[1]; however, a plan would be deemed to satisfy this minimum allocation gateway if each NHCE received an allocation of at least 5% of the NHCE's compensation (within the meaning of section 415(c)(3)).

The proposed regulations would not change the general rule prohibiting aggregation of a 401(k) plan or 401(m) plan with a plan providing nonelective contributions. Accordingly, elective contributions and matching contributions would not be taken into account for purposes of the gateway. If an employer also provides a 401(k) plan, however, then to the extent the HCEs are electing contributions under that plan, the highest HCE allocation rate may be lower than it otherwise would be, which, in turn would lower the minimum required allocation for the NHCEs under the gateway. Further, if the employer sponsors a safe harbor 401(k) plan that provides for 3% nonelective contributions, then, as noted in Notice 98–52 (1998–2 C.B. 632), those nonelective contributions may be taken into account in determining the allocation rates for the NHCEs under section 401(a)(4), including the minimum allocation gateway.

C. *Plans with Broadly Available Allocation Rates*

As suggested in Notice 2000–14, a plan that has broadly available allocation rates would not need to satisfy the minimum allocation gateway and may continue to be tested for nondiscrimination on the basis of benefits as under current law. In order to be broadly available, each allocation rate under the plan must be currently available to a group of employees that satisfies section 410(b) (without regard to the average benefit percentage test). Thus, for example, if within one plan an employer provides different allocation rates for nondiscriminatory groups of employees at different locations or different profit centers, the plan would not need to satisfy the minimum allocation gateway in order to use cross testing.

In addition, a plan that provides allocation rates that increase as an employee ages or accumulates additional service would be treated as having broadly available allocation rates, if the schedule of allocation rates satisfies certain conditions that permit participants to "grow into" higher allocation rates. The conditions are that the same schedule of allocation rates is available to all employees in the plan and that the schedule provides for smoothly increasing allocation rates at regular intervals of age or service.

The proposed regulation would provide that in order for a schedule of allocation rates to increase smoothly, the allocation rate for each age or service band cannot be more than 5 percentage points higher than the allocation rate for the immediately preceding band and cannot be more than twice that allocation rate. For example, if the allocation rate for an age or service band were 6%, the allocation rate for the next higher age or service band could not exceed 11% (i.e., the lesser of 11% (6% plus 5%) and 12% (2 times 6%)).

Further, in order for a schedule of allocation rates to be considered to be increasing smoothly, the ratio of the allocation rate for any age or service band to the allocation rate for the immediately preceding band cannot exceed the ratio of the allocation rates between the two immediately preceding bands. The proposed regulations would provide that the intervals for the age or service bands are regular if they are all of the same length (although this requirement generally would not apply to the first and last bands).

The definition of broadly available allocation rates is designed to be sufficiently flexible to accommodate a wide variety of age- and service-based plans (including age-weighted profit-sharing plans that provide for allocations that result in the same equivalent accrual rate for all employees).

The conditions described above relating to a plan's schedule of age-based or service-based allocation rates are intended to exempt from the minimum allocation gateway those plans in which NHCEs actually receive the benefit of higher rates as they attain higher ages or complete additional years of service. Without conditions such as these, plans can be designed to backload allocation rates excessively, providing for lengthy plateau periods in which rates increase little if at all, followed by sharp increases.

Comments are invited on whether there are plans using schedules of allocation rates (such as schedules of rates based on points or otherwise combining age and service) that would fall outside the definition of broadly available allocation rates but that do afford sufficient opportunity for NHCEs to "grow into" higher allocation rates.

D. *Application to Defined Contribution Plans That Are Combined with Defined Benefit Plans*

The proposed regulations would prescribe rules for testing defined contribution plans that are aggregated with defined benefit plans for purposes of sections 401(a)(4) and 410(b). These rules would apply in situations in which the employer aggregates the plans because one of the plans does not satisfy sections 401(a)(4) and 410(b) standing alone.

1. *Gateway for benefits testing of combined plans*

Under the proposed regulations, the combination of a defined contribution plan and a defined benefit plan may demonstrate nondiscrimination on the basis of benefits if the combined plan is primarily defined benefit in character, consists of broadly available separate plans (as these terms are defined in the proposed regulations), or satisfies a gateway requirement. This minimum aggregate allocation gateway is generally similar to the minimum allocation gateway for defined contribution plans that are not combined with a defined benefit plan. To apply this minimum aggregate allocation gateway, the employee's aggregate normal allocation rate is determined by adding the employee's allocation under the defined contribution plan to the employee's equivalent allocation under the defined benefit plan. The use of aggregation would allow an employer that provides both a defined contribution and a defined benefit plan to the NHCEs to take both plans into account in determining whether the minimum aggregate allocation gateway is met.

Under the gateway, if the aggregate normal allocation rate of the HCE with the highest aggregate normal allocation rate under the plan (HCE rate) is less than 15%, the aggregate normal allocation rate for all NHCEs must be at least 1/3 of the

[1]For example, if any HCE had an allocation of 12% of compensation, all NHCEs in the plan would be required to have an allocation of at least 4% of compensation.

HCE rate. If the HCE rate is between 15% and 25%, the aggregate normal allocation rate for all NHCEs must be at least 5%. If the HCE rate exceeds 25%, then the aggregate normal allocation rate for each NHCE must be at least 5% plus one percentage point for each 5-percentage-point increment (or portion thereof) by which the HCE rate exceeds 25% (e.g., the NHCE minimum is 6% for an HCE rate that exceeds 25% but not 30%, and 7% for an HCE rate that exceeds 30% but not 35%, etc.).

In addition, in determining the equivalent allocation rate for an NHCE under a defined benefit plan, a plan is permitted to treat each NHCE who benefits under the defined benefit plan as having an equivalent allocation rate equal to the average of the equivalent allocation rates under the defined benefit plan for all NHCEs benefitting under that plan. This averaging rule recognizes the "grow-in" feature inherent in traditional defined benefit plans (i.e., the defined benefit plan provides higher equivalent allocation rates at higher ages).

Comments are invited on possible special situations involving DB/DC plans, such as situations arising as a result of a merger or acquisition or a situation in which some HCEs in a DB/DC plan have unusually high equivalent normal allocation rates for reasons other than the design of the plan. Comments are invited as to whether the regulations should address such special circumstances and, if so, how (e.g., through a maximum required rate for NHCEs under a DB/DC plan or other approaches).

2. *Primarily defined benefit in character*

A combined plan that is primarily defined benefit in character would not be subject to the gateway requirement and may continue to be tested for nondiscrimination on the basis of benefits as under current law. A combined plan would be primarily defined benefit in character if, for more than 50% of the NHCEs benefitting under the plan, the normal accrual rate attributable to benefits provided under defined benefit plans for the NHCE exceeds the equivalent accrual rate attributable to contributions under defined contribution plans for the NHCE. For example, a DB/DC plan would be primarily defined benefit in character where the defined contribution plan covers only salaried employees, the defined benefit plan covers only hourly employees, and more than half of the NHCEs participating in the DB/DC plan are hourly employees participating only in the defined benefit plan.

3. *Broadly available separate plans*

A combined plan that consists of broadly available separate plans would not be subject to the gateway requirement and may continue to be tested for nondiscrimination on the basis of benefits as under current law. A DB/DC plan consists of broadly available separate plans if the defined contribution plan and the defined benefit plan each would satisfy the requirements of section 410(b) and the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) if each plan were tested separately, assuming satisfaction of the average benefit percentage test of §1.410(b)–5. Thus, the defined contribution plan must separately satisfy the nondiscrimination requirements (taking into account these proposed regulations as applicable), but for this purpose assuming satisfaction of the average benefit percentage test. Similarly, the defined benefit plan must separately satisfy the nondiscrimination requirements, assuming for this purpose satisfaction of the average benefit percentage test. In conducting the required separate testing, all plans of a single type (defined contribution or defined benefit) within the DB/DC plan are aggregated, but those plans are tested without regard to plans of the other type.

This alternative would be useful, for example, where an employer maintains a defined contribution plan that provides a uniform allocation rate for all covered employees at one business unit and a safe harbor defined benefit plan for all covered employees at another unit, where the group of employees covered by each plan is a group that satisfies the nondiscriminatory classification requirement of section 410(b). Because the employer provides broadly available separate plans, it may continue to aggregate the plans and test for nondiscrimination on the basis of benefits, as an alternative to using the qualified separate line of business rules or demonstrating satisfaction of the average benefit percentage test.

E. *Use of Component Plans and Permitted Disparity*

Component plans under the restructuring rules cannot be used for the determination of whether a defined contribution plan provides broadly available allocation rates or satisfies the minimum allocation gateway, or the determination of whether a DB/DC plan satisfies the minimum aggregate allocation gateway, is primarily defined benefit in character, or consists of broadly available separate plans. For purposes of the two gateways and determining whether a DB/DC plan is primarily defined benefit in character, allocation rates and equivalent allocation rates are determined without the use of permitted disparity. For purposes of determining whether a DB/DC plan consists of broadly available separate plans, permitted disparity may be used in the defined contribution plan or the defined benefit plan but not in both plans with respect to each employee who participates in both.

Proposed Effective Date

The regulations are proposed to be applicable for plan years beginning on or after January 1, 2002.

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

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any electronic or

written comments (preferably a signed original and eight (8) copies) that are submitted timely to the IRS. In addition to the other requests for comments set forth in this document, the IRS and Treasury also request comments on the clarity of the proposed rule and how it may be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for January 25, 2001, at 10 a.m. in the IRS Auditorium (7th Floor), Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC. Due to building security procedures, visitors must enter at the 10th street entrance, located between Constitution and Pennsylvania Avenues, NW. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 15 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "FOR FURTHER INFORMATION CONTACT" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons who wish to present oral comments at the hearing must submit written comments and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by January 5, 2001.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal authors of these regulations are John T. Ricotta and Linda S. F. Marshall of the Office of the Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury participated in their development.

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Proposed Amendments to the Regulations

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

PART 1 — INCOME TAXES

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

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

Par. 2. In §1.401(a)(4)–8, paragraph (b)(1) is revised to read as follows:

§1.401(a)(4)–8 Cross-testing.

* * * * *

(b) *Nondiscrimination in amount of benefits provided under a defined contribution plan*—(1) *General rule and gateway*—(i) *General rule*. Equivalent benefits under a defined contribution plan (other than an ESOP) are nondiscriminatory in amount for a plan year if—

(A) The plan would satisfy §1.401(a)(4)–2(c)(1) for the plan year if an equivalent accrual rate, as determined under paragraph (b)(2) of this section, were substituted for each employee's allocation rate in the determination of rate groups; and

(B) For plan years beginning on or after January 1, 2002, if the plan does not have broadly available allocation rates (within the meaning of paragraph (b)(1)(iii) of this section) for the plan year, the plan satisfies the minimum allocation gateway of paragraph (b)(1)(iv) of this section for the plan year.

(ii) *Allocations after testing age*. A plan does not fail to satisfy paragraph (b)(1)(i)(A) of this section merely because allocations are made at the same rate for employees who are older than their testing age (determined without regard to the current-age rule in paragraph (4) of the definition of *testing age* in §1.401(a)(4)–12), as they are made for employees who are at that age.

(iii) *Broadly available allocation rates*—(A) *In general*. A plan has broadly available allocation rates for the plan year if each allocation rate under the plan is currently available during the plan year (within the meaning of §1.401(a)(4)–4(b)(2)), to a group of employees that satisfies section 410(b) (without regard to the average benefit percentage test of §1.410(b)–5). For this purpose, the disregard of age and service conditions described in §1.401(a)(4)–4(b)(2)(ii)(A) applies only if the plan provides an allocation formula under which the allocation rates for all employees benefitting under the plan are determined using a single schedule of rates that are based solely on either age or service, and only if the allocation rates under the schedule increase smoothly at regular intervals, within the meaning of paragraphs (b)(1)(iii)(B) and (C) of this section. A plan does not fail to provide broadly available allocation rates merely because it provides the minimum benefit described in section 416(c)(2).

(B) *Smoothly increasing schedule of allocation rates*. A plan uses a single schedule of allocation rates that are based solely on age or service if it uses a single schedule of allocation rates that consists of a series of either age or service bands under which the same allocation rate applies to all employees whose age is within each age band or whose years of service are within each service band. A schedule of allocation rates increases smoothly if the allocation rate for each age or service band within the schedule is greater than the allocation rate for the immediately preceding band (i.e., the age or service band with the next lower number of years of age or service) but by no more than 5 percentage points. However, a schedule of allocation rates will not be treated as increasing smoothly if the ratio of the allocation rate for any age or service band to the rate for the immediately preceding band is more than 2.0 or if it exceeds the ratio of allocation rates between the two immediately preceding bands.

(C) *Regular intervals*. A schedule of allocation rates has regular intervals of age or service if each age or service band, other than the band associated with the highest age or years of service, is the same length. For this purpose, if the schedule is based on age, the first age band will be deemed to be of the same length as the other bands if it ends at or before age 25. If the first age band ends after age 25, then, in determining whether the length of the first band is the same as the length of other bands, the starting age for the first age band is permitted to be treated as age 25 or any age earlier than 25.

(iv) *Minimum allocation gateway*. A plan satisfies the minimum allocation gateway of this paragraph (b)(1)(iv) if each NHCE has an allocation rate that is at least one third of the allocation rate of the HCE with the highest allocation rate. However, a plan is deemed to satisfy this minimum allocation gateway if each NHCE receives an allocation of at least 5% of the

NHCE's compensation within the meaning of section 415(c)(3).

(v) *Determination of allocation rates.* For purposes of this paragraph (b)(1), allocations and allocation rates are determined under §1.401(a)(4)–2(c)(2), but without taking into account the imputation of permitted disparity under §1.401(a)(4)–7 in applying the minimum allocation gateway of paragraph (b)(1)(iv) of this section.

(vi) *Examples.* The following examples illustrate the rules in this paragraph (b)(1):

Example 1. (i) Plan M is a defined contribution plan that provides an allocation formula under which allocations are provided to all employees according to the following schedule:

Years of Service	Allocation Rate	Ratio of Allocation Rate for Band to Allocation Rate for Immediately Preceding Band
0- 5	3.0%	not applicable
6-10	4.5%	1.50
11-15	6.5%	1.44
16-20	8.5%	1.31
21-25	10.0%	1.18
26 or more	11.5%	1.15

(ii) Because Plan M provides that allocation rates for all employees are determined using a single schedule based solely on service, the plan is permitted to disregard the service requirement in determining whether the allocation rates are broadly available (within the meaning of paragraph (b)(1)(iii) of this section), if the allocation rates under the schedule increase smoothly at regular intervals.

(iii) The schedule of allocation rates under Plan M does not increase by more than 5 percentage points between adjacent bands and the ratio of the allocation rate for any band to the allocation rate for the immediately preceding band is never more than 2.0 and does not increase. Therefore, the allocation rates increase smoothly. In addition, the bands (other than the highest band) are all 5 years long, so the increases occur at regular intervals. Accordingly, the service requirement is disregarded and each allocation rate is broadly available within the meaning of paragraph (b)(1)(iii) of this section, as each allocation rate is currently available to all employees in the Plan.

(iv) Under paragraph (b)(1)(i) of this section, Plan M satisfies the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits if it satisfies paragraph (b)(1)(i)(A) of this section, regardless of whether it satisfies the minimum allocation gateway of paragraph (b)(1)(iv) of this section.

Example 2. (i) Plan N is a defined contribution plan that provides an allocation formula under which allocations are provided to all employees according to the following schedule:

Age	Allocation rate	Ratio of Allocation Rate for Band to Allocation Rate for Immediately Preceding Band
under 25	3.0 %	not applicable
25-34	6.0 %	2.00
35-44	9.0 %	1.50
45-54	12.0%	1.33
55-64	16.0%	1.33
65 or older	21.0%	1.31

(ii) Because Plan N provides that allocation rates for all employees are determined using a single schedule based solely on age, the plan is permitted to disregard the age requirement in determining whether the allocation rates are broadly available (within the meaning of paragraph (b)(1)(iii) of this section), if the allocation rates under the schedule increase smoothly at regular intervals.

(iii) The schedule of allocation rates under Plan N does not increase by more than 5 percentage points between adjacent bands and the ratio of the allocation rate for any band to the allocation rate for the immediately preceding band is never more than 2.0 and does not increase. Therefore, the allocation rates increase smoothly. In addition, the bands are all 10 years long (other than the highest band and the first band, which is deemed to be the same length as the other bands because it ends prior to age 25), so the increases occur at regular intervals. Accordingly, the age requirement is disregarded and each allocation rate is broadly available within the meaning of paragraph (b)(1)(iii) of this section, as each allocation rate is currently available to all employees in the Plan.

(iv) Under paragraph (b)(1)(i) of this section, Plan N satisfies the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits if it satisfies paragraph (b)(1)(i)(A) of this section, regardless of whether it satisfies the minimum allocation gateway of paragraph (b)(1)(iv) of this section.

Example 3. (i) Plan O is a profit-sharing plan maintained by Employer A that covers all of Em-

ployer A's employees, consisting of two HCEs, X and Y, and 7 NHCEs. Employee X's compensation is $170,000 and Employee Y's compensation is $150,000. The allocation for Employees X and Y is $30,000 each, resulting in an allocation rate of 17.6% for Employee X and 20% for Employee Y. Under Plan O, each NHCE receives an allocation of 5% of compensation within the meaning of section 415(c)(3).

(ii) Because the allocation rate for X is not currently available to any NHCE, Plan O does not have broadly available allocation rates and must satisfy the minimum allocation gateway of paragraph (b)(1)(iv) of this section.

(iii) The highest allocation rate for any HCE under Plan O is 20%. Accordingly, Plan O would satisfy the minimum allocation gateway of paragraph (b)(1)(iv) of this section if all NHCEs have an allocation rate of at least 6.67%, or if all NHCEs receive an allocation of at least 5% of compensation within the meaning of section 415(c)(3).

(iv) Under Plan O, each NHCE receives an allocation of 5% of compensation within the meaning of section 415(c)(3). Accordingly, Plan O satisfies the minimum allocation gateway of paragraph (b)(1)(iv) of this section.

(v) Under paragraph (b)(1)(i) of this section, Plan O satisfies the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits if it satisfies paragraph (b)(1)(i)(A) of this section.

* * * * *

Par. 3. Section 1.401(a)(4)–9 is amended by adding paragraph (b)(2)(v) and revising paragraph (c)(3)(ii) to read as follows:

§1.401(a)(4)–9 Plan aggregation and restructuring.

* * * * *

(b) * * *

(2) * * *

(v) *Eligibility for testing on a benefits basis*—(A) *General rule*. For plan years beginning on or after January 1, 2002, unless, for the plan year, a DB/DC plan is primarily defined benefit in character (within the meaning of paragraph (b)(2)(v)(B) of this section) or consists of broadly available separate plans (within the meaning of paragraph (b)(2)(v)(C) of this section), the DB/DC plan must satisfy the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section for the plan year in order to be permitted to demonstrate satisfaction of the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits.

(B) *Primarily defined benefit in character*. A DB/DC plan is primarily defined benefit in character if, for more than 50% of the NHCEs benefitting under the plan, the normal accrual rate for the NHCE attributable to benefits provided under defined benefit plans that are part of the DB/DC plan exceeds the equivalent accrual rate for the NHCE attributable to contributions under defined contribution plans that are part of the DB/DC plan.

(C) *Broadly available separate plans*. A DB/DC plan consists of broadly available separate plans if the defined contribution plan and the defined benefit plan that are part of the DB/DC plan each would satisfy the requirements of section 410(b) and the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) if each plan were tested separately and assuming that the average benefit percentage test of §1.410(b)–5 were satisfied. For this purpose, all defined contribution plans that are part of the DB/DC plan are treated as a single defined contribution plan and all defined benefit plans that are part of the DB/DC plan are treated as a single defined benefit plan. In addition, if permitted disparity is used for an employee for purposes of satisfying the separate testing requirement of this paragraph (b)(2)(v)(C) for plans of one type, it may not be used in satisfying the separate testing requirement for plans of the other type for the employee.

(D) *Minimum aggregate allocation gateway*. A DB/DC plan satisfies the minimum aggregate allocation gateway of this paragraph (b)(2)(v)(D) if each NHCE has an aggregate normal allocation rate that is at least one third of the aggregate normal allocation rate of the HCE with the highest such rate (HCE rate), or, if less, 5% of the NHCE's compensation, provided that the HCE rate does not exceed 25% of compensation. If the HCE rate exceeds 25% of compensation, then the aggregate normal allocation rate for each NHCE must be 5% increased by one percentage point for each 5-percentage-point increment (or portion thereof) by which the HCE rate exceeds 25% (e.g., the NHCE minimum is 6% for an HCE rate that exceeds 25% but not 30%, and 7% for an HCE rate that exceeds 30% but not 35%). For purposes of this paragraph (b)(2)(v)(D), a plan is permitted to treat each NHCE who benefits under the defined benefit plan as having an equivalent normal allocation rate equal to the average of the equivalent normal allocation rates under the defined benefit plan for all NHCEs benefitting under that plan.

(E) *Determination of rates*. For purposes of this paragraph (b)(2)(v), the normal accrual rate and the equivalent normal allocation rate attributable to defined benefit plans, the equivalent accrual rate attributable to defined contribution plans and the aggregate normal allocation rate are determined under paragraph (b)(2)(ii) of this section, but without taking into account the imputation of permitted disparity under §1.401(a)(4)–7, except as otherwise permitted under paragraph (b)(2)(v)(C) of this section.

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

Example 1. (i) Employer A maintains Plan M, a defined benefit plan, and Plan N, a defined contribution plan. All HCEs of Employer A are covered by Plan M (at a 1% accrual rate), but not covered by Plan N. All NHCEs of Employer A are covered by Plan N (at a 3% allocation rate), but not covered by Plan M. Because Plan M does not satisfy section 410(b) standing alone, Plans M and N are aggregated for purposes of satisfying sections 410(b) and 401(a)(4).

(ii) Because none of the NHCEs participate in the defined benefit plan, the aggregated DB/DC plan is not primarily defined benefit in character within the meaning of paragraph (b)(2)(v)(B) of this section nor does it consist of broadly available separate plans within the meaning of paragraph (b)(2)(v)(C) of this section. Accordingly, the aggregated Plan M and Plan N must satisfy the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section in order to satisfy the nondiscrimination in amount requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits.

Example 2. (i) Employer B maintains Plan O, a defined benefit plan, and Plan P, a defined contribution plan. All of the six employees of Employer B are covered under both Plan O and Plan P. Under Plan O, all employees have a uniform normal accrual rate of 1% of compensation. Under Plan P, Employees A and B, who are HCEs, receive an allocation rate of 15%, and participants C, D, E and F, who are NHCEs, receive an allocation rate of 3%. Employer B aggregates Plans O and P for purposes of satisfying sections 410(b) and 401(a)(4). The equivalent normal allocation and normal accrual rates under Plans O and P are as follows:

Employee	Equivalent Normal Allocation Rates for the 1% Accrual under Plan O (defined benefit plan)	Equivalent Normal Accrual Rates for the 15%/3% Allocations under Plan P (defined contribution plan)
HCE A (age 55)	3.93%	3.82%
HCE B (age 50)	2.61%	5.74%
C (age 60)	5.91%	.51%
D (age 45)	1.73%	1.73%
E (age 35)	.77%	3.90%
F (age 25)	.34%	8.82%

(ii) Although all of the NHCEs benefit under the Plan O (the defined benefit plan), the aggregated DB/DC plan is not primarily defined benefit in character because the normal accrual rate attributable to defined benefit plans (which is 1% for all the NHCEs) is greater than the equivalent accrual rate under defined contribution plans only for Employee C. In addition, because the 15% allocation rate is only available to HCEs, the defined contribution plan cannot satisfy the requirements of §1.401(a)(4)–2 and does not have broadly available allocation rates within the meaning of §1.401(a)(4)–8(b)(1)(iii). Further, the defined contribution plan does not satisfy the minimum allocation gateway of §1.401(a)(4)–8(b)(1)(iv) (3% is less than 1/3 of the 15% HCE rate). Therefore, the defined contribution plan within the DB/DC plan cannot separately satisfy §1.401(a)(4)–1(b)(2) and does not constitute a broadly available separate plan within the meaning of paragraph (b)(2)(v)(C) of this section. Accordingly, the aggregated plans can satisfy the nondiscrimination in amounts requirement of §1.401(a)(4)–1(b)(2) on the basis of benefits only if the aggregated plans satisfy the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section.

(iii) Employee A has an aggregate normal allocation rate of 18.93% under the aggregated plans (3.93% from Plan O plus 15% from Plan P), which is the highest aggregate normal allocation rate for any HCE under the plans. Employee F has an aggregate normal allocation rate of 3.34% under the aggregated plans (.34% from Plan O plus 3% from Plan P) which is less than the 5% aggregate normal allocation rate that Employee F would be required to have to satisfy the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section.

(iv) However, for purposes of satisfying the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section, Employer B is permitted to treat each NHCE who benefits under the Plan O (the defined benefit plan) as having an equivalent allocation rate equal to the average of the equivalent allocation rates under Plan O for all NHCEs benefitting under that plan. The average of the equivalent allocation rates for all the NHCEs under Plan O is 2.19% (the sum of 5.91%, 1.73%, .77%, and .34%, divided by 4). Accordingly, Employer B is permitted to treat all the NHCEs as having an equivalent allocation rate attributable to Plan O equal to 2.19%. Thus, all NHCEs can be treated as having an aggregate normal allocation rate of 5.19% for this purpose (3% from the defined contribution plan and 2.19% from the defined benefit plan) and the aggregated DB/DC plan satisfies the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section.

* * * * *

(c) * * *

(3) * * *

(ii) *Restructuring not available for certain testing purposes*. The safe harbor in §1.401(a)(4)–2(b)(3) for plans with uniform points allocation formulas is not available in testing (and thus cannot be satisfied by) contributions under a component plan. Similarly, component plans cannot be used for purposes of determining whether a plan provides broadly available allocation rates (as defined in §1.401(a)(4)–8(b)(1)(iii)), or determining whether a plan is primarily defined benefit in character or consists of broadly available separate plans (as defined in paragraphs (b)(2)(v)(B) and (C) of this section). In addition, the minimum allocation gateway of §1.401(a)(4)–8(b)(1)(iv) and the minimum aggregate allocation gateway of paragraph (b)(2)(v)(D) of this section cannot be satisfied on the basis of component plans. See §§1.401(k)–1(b)(3)(iii) and 1.401(m)–1(b)(3)(iii) for rules regarding the inapplicability of restructuring to section 401(k) plans and section 401(m) plans.

* * * * *

David A. Mader,
Acting Deputy Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on October 5, 2000, 8:45 a.m., and published in the issue of the Federal Register for October 6, 2000, 65 F.R. 59774)

Monthly Limit for Transit Passes and Transportation in a Commuter Highway Vehicle Provided by an Employer to Employees Under Section 132(f) of the Internal Revenue Code

Announcement 2000–78

This announcement sets forth a clarification to the proposed Treasury Regulations dealing with qualified transportation fringes (Prop. Treas. Reg. § 1.132–9, 65 F.R. 4388). Specifically, when finalized, the regulations will clarify that transit passes may be distributed in advance for more than one month (such as for a calendar quarter). The applicable statutory monthly limit under section 132(f)(2) on the combined amount of transit passes and transportation in a commuter highway vehicle may be calculated by taking into account the monthly limits for all months for which the transit passes are distributed. Thus, for example, the employer may distribute advance transit passes for a subsequent calendar quarter with a value equal to the statutory monthly limit times three months (for 2000, $65 times three equals $195). However, if transit passes are provided in advance and the employee's employment terminates before the beginning of the last month of the period for which the transit passes are provided, the value of transit passes covering the month(s) that begin after the employee's employment terminates is included in the employee's wages for income tax purposes and for employment tax purposes (income tax withholding, FICA and FUTA) to the extent the employer does not recover those transit passes or the value of those passes.

Pending issuance of the final regulations, taxpayers may rely on this announcement. An employer will not be considered to have failed to satisfy employment tax requirements under this announcement for advance transit pass distributions occurring before January 1, 2001.

Prior to issuing final regulations, the Service is requesting comments concerning this announcement. Written comments should be sent to the following address:

Internal Revenue Service
CC:DOM:CORP (ANN 2000–78; CC:TEGE:EOEG:ET2)
P.O. Box 7604, Ben Franklin Station
Washington, DC 20044

In the alternative, comments may be hand delivered between the hours of 8:00 a.m. and 5:00 p.m. to the courier's desk at 1111 Constitution Avenue, NW., Washington, DC, or submitted electronically via the IRS Internet site at http://www.irs.utreas.gov/tax_regs/regslist.html.

Because the Service and Treasury would like to receive comments with sufficient time to consider them in developing the final regulations, comments should be submitted by November 15, 2000. However, to the extent possible, consideration will be given to comments received after that date.

The principal author of this announcement is John Richards of the Office of Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this announcement contact John Richards at (202) 622-6040 (not a toll-free call).

Recognition of Gain on Certain Transfers to Certain Foreign Trusts and Estates; Correction

Announcement 2000–85

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Correction to notice of proposed rulemaking.

SUMMARY: This document contains a correction to a notice of proposed rulemaking that was published in the **Federal Register** on Monday, August 7, 2000 (65 F.R. 48198) relating to the recognition of gain on certain transfers to certain foreign trusts and estates.

FOR FURTHER INFORMATION CONTACT: Karen A. Rennie Quarrie at (202) 622-3880 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

The notice of proposed rulemaking that is the subject of this correction is under section 684 of the Internal Revenue Code.

Need for Correction

As published, the notice of proposed rulemaking contains errors that may prove to be misleading and are in need of clarification.

Correction of Publication

Accordingly, the publication of the notice of proposed rulemaking (REG–108522–00, 2000–34 I.R.B. 187), that was the subject of FR Doc. 00–19896, is corrected as follows:

§1.684–3 [Corrected]

On page 48202, column 1, §1.684–3(f), the first line in *Example 1*, the language "*Example 1. Transfer to owner trust*. In" is corrected to read "*Example 1. Transfer to grantor trust*. In"

Cynthia E. Grigsby,
Chief, Regulations Unit,
Office of Special Counsel
(Modernization and Strategic Planning).

(Filed by the Office of the Federal Register on October 2, 2000, 8:45 a.m., and published in the issue of the Federal Register for October 3, 2000, 65 F.R. 58973)

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 law 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 the 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.—Statements 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.

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