Internal Revenue
bulletin

Bulletin No. 2002–24
June 17, 2002

HIGHLIGHTS OF THIS ISSUE

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

INCOME TAX

Rev. Rul. 2002–36, page 1148.
Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate. For purposes of sections 382, 1274, 1288, and other sections of the Code, tables set forth the rates for June 2002.

Rev. Rul. 2002–37, page 1147.
LIFO; price indexes; department stores. The April 2002 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 2002.

T.D. 8996, page 1127.
Final regulations under sections 441 and 442 of the Code relate to certain adoptions, changes, and retentions of annual accounting periods. The final regulations primarily affect taxpayers that want to adopt an annual accounting period or that must receive approval from the Commissioner to adopt, change, or retain an annual accounting period. In addition, the regulations provide guidance relating to the taxable years of partnerships and S corporations. Rev. Ruls. 57–589, 65–316, 68–125, 69–563, 74–326, and 78–179 obsolete.

Notice 2002–41, page 1153.
This notice contains guidance for entering into a withholding foreign partnership or withholding foreign trust agreement with the service.

EMPLOYEE PLANS

Rev. Proc. 2002–29, page 1176.
Minimum distributions; regulations; model amendments. This procedure describes the final and temporary regulations under section 401(a)(9) of the Code and provides model amendments for qualified defined contribution plans and for qualified defined benefit plans. Rev. Procs. 2000–20 and 2002–6 modified.

Rev. Proc. 2002–35, page 1187.
Retroactive plan amendments; GUST late amenders. This document establishes streamlined procedures to avoid the disqualification of plans intended to satisfy sections 401(a) or 403(a) of the Code on account of the plans' failure to be timely amended for GUST. Rev. Proc. 2001–17 modified.

EXCISE TAX

Rev. Rul. 2002–34, page 1150.
Segment Tax. This ruling provides guidance on how to calculate the tax under section 4261(b) of the Code on domestic segments if an aircraft is chartered and one or more persons are transported on that aircraft.

ADMINISTRATIVE

Notice 2002–40, page 1152.
This notice supplements the relief granted in Notice 2001–61, 2001–40 I.R.B. 305, and Notice 2001–68, 2001–47 I.R.B. 504, for taxpayers affected by the September 11, 2001, terrorist attack by expanding relief from interest and penalties. The notice implements changes that were made to section 7508A of the Code by the Victims of Terrorism Tax Relief Act of 2001.

(Continued on the next page)

Finding Lists begin on page ii.

Department of the Treasury
Internal Revenue Service

Rev. Proc. 2002–30, page 1184.
This procedure provides for a pilot program that will test whether the process for issuing Technical Advice Memoranda (TAM) can be streamlined. The new advice will be known as a Technical Expedited Advice Memorandum (TEAM). Rev. Proc. 2002–2 modified.

Rev. Proc. 2002–42, page 1188.
This procedure sets forth a process whereby taxpayers who purchase motor vehicles propelled by both a gasoline internal combustion engine and an electric motor that is recharged as the motor vehicles operate (hybrid vehicles) may rely on the original equipment manufacturer's (or, in the case of a foreign original equipment manufacturer, its domestic distributor's) certification of the incremental cost of the motor vehicles' clean-fuel vehicle property for purposes of section 179A of the Code.

Announcement 2002–54, page 1190.
This announcement contains the annual report concerning the Pre-Filing Agreement Program of the Large and Mid-Size Division of the Service for calendar year 2001.

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 Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

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

Part IV.—Items of General Interest.

This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The 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.

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

Section 30.—Credit for Qualified Electric Vehicles

If a hybrid motor vehicle is a "qualified electric vehicle", does the motor vehicle constitute "clean-fuel vehicle property" for purposes of section 179A(c) of the Internal Revenue Code? See Rev. Proc. 2002–42, page 1188.

Section 42.—Low-Income Housing Credit

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 50.—Other Special Rules

If a hybrid motor vehicle is used predominantly outside the United States, is a clean-fuel vehicle property deduction allowed with respect to the motor vehicle under section 179A(a) of the Internal Revenue Code? See Rev. Proc. 2002–42, page 1188.

Section 179.—Election to Expense Certain Depreciable Business Assets

If a taxpayer elects to treat the cost of the clean-fuel vehicle property in a hybrid motor vehicle as an expense which is not chargeable to capital account, is a clean-fuel vehicle property deduction allowed with respect to the motor vehicle under section 179A(a) of the Internal Revenue Code? See Rev. Proc. 2002–42, page 1188.

Section 179A.—Deduction for Clean-Fuel Vehicles and Certain Refueling Property

If a motor vehicle is propelled by both a gasoline internal combustion engine and an electric motor that is recharged as the motor vehicle operates and the motor vehicle otherwise meets the requirements of section 179A of the Internal Revenue Code, may taxpayers rely on the manufacturer's certification of the incremental cost of the motor vehicle's clean-fuel vehicle property for purposes of the clean-fuel vehicle property deduction under section 179A of the Internal Revenue Code? See Rev. Proc. 2002–42, page 1188.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted applicable federal long-term rate is set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 401.—Qualified Pension, Profit-Sharing and Stock Bonus Plans

26 CFR 1.401(a)(9)–1: Required distributions from trusts and plans.

A revenue procedure provides model amendments that may be used in conjunction with the final and temporary Income Tax Regulations published under § 401(a)(9) of the Code which are effective for years beginning on or after January 1, 2003. See Rev. Proc. 2002–29, page 1176.

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26 CFR 1.401(b)–1: Certain retroactive changes in plan.

A revenue procedure describes how retroactive remedial plan amendments may be made after the end of the GUST remedial amendment period if certain criteria are met. See Rev. Proc. 2002–35, page 1187.

Section 412.—Minimum Funding Standards

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 441.—Period for Computation of Taxable Income

26 CFR 1.441–1: Period for computation of taxable income.

T.D. 8996

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1, 5c, 5f, 18, and 602

Changes in Accounting Periods

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations relating to certain adoptions, changes, and retentions of annual accounting periods. The final regulations are necessary to update, clarify, and reorganize the rules and procedures for adopting, changing, and retaining a taxpayer's annual accounting period. The final regulations primarily affect taxpayers that want to adopt an annual accounting period under section 441 or that must receive approval from the Commissioner to adopt, change, or retain their annual accounting periods under section 442.

DATES: *Effective Date*: These regulations are effective May 17, 2002.

Applicability Date: These regulations are applicable for taxable years ending on or after May 17, 2002.

FOR FURTHER INFORMATION CONTACT: Michael Schmit or Roy Hirschhorn at (202) 622-4960 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in these final regulations have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545-1748. Responses to these collections of information are required for certain taxpayers to adopt, change, or retain an annual accounting period.

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

The estimated annual burden per respondent varies from 20 minutes to one hour, depending on individual circumstances, with an estimated average of 30 minutes.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, W:CAR: MP:FP:S, Washington, DC 20224, and to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

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

Background

On June 12, 2001, the IRS and Treasury Department published in the **Federal Register** proposed amendments to regulations under section 441 (period for computing taxable income), and sections 442, 706, 898, and 1378 (regarding the requirement to obtain the approval of the Commissioner to adopt, change, or retain an annual accounting period) (REG–106917–99, 2001–27 I.R.B. 4 [66 FR 31850]). Written and electronic comments were solicited, and a public hearing was scheduled for October 2, 2001. Several comments were received, and are discussed below. Because no requests to speak were received, the public hearing was cancelled. After consideration of all comments, the proposed regulations under sections 441, 442, 706, and 1378 are adopted as revised by this Treasury decision.

Summary of Comments and Explanation of Revisions

1. *Comments and Changes Relating to § 1.441 of the Proposed Regulations*

A. *Definition of 52–53-week taxable year*

The proposed regulations both define the term *taxable year consisting of 52–53-weeks* and provide an *Example* illustrating a 52–53-week taxable year that ends on a particular day of the week that last occurs in a calendar month or that is nearest to the last day of that calendar month. A commentator observed that many taxpayers have difficulty correctly applying the rules for 52–53-week taxable years, and suggested that certain explanatory text contained in the *Example* be moved to the regulations text itself where it would be more apparent and helpful. This suggestion has been adopted in the final regulations.

B. *Changes to or from a 52–53-week taxable year*

The proposed regulations generally provide that changes to or from a 52–53-week taxable year are treated as changes in annual accounting periods that require the approval of the Commissioner, and describe some specific instances in which such approval may be obtained automatically under administrative procedures to be published by the Commissioner. Consistent with the general framework of the regulations, the descriptions of these specific changes have been removed from the final regulations. Taxpayers should see Rev. Proc. 2002–37, 2002–22 I.R.B. 1030 and Rev. Proc. 2002–38, 2002–22 I.R.B. 1037, for situations in which automatic approval for changes to or from a 52–53-week taxable year will be granted. The final regulations clarify that a taxpayer will not be granted automatic approval for a change from one 52–53-week taxable year to another 52–53-week taxable year, even if both years reference the same calendar month.

C. *Short periods of 6 days or less*

The proposed regulations provide special rules for certain short periods required to effect a change in annual accounting period to (or from) a 52–53-week taxable year. The proposed regulations provide that if the short period is 6 days or less, such short period is not a separate taxable year but is instead added to and deemed a part of the following taxable year.

One commentator suggested that taxpayers be permitted the option of adding such a short period to either: (1) the following taxable year (as the proposed regulations would require); or (2) the prior taxable year, whichever convention is used by the taxpayer for financial accounting purposes.

The IRS and Treasury Department believe that adopting the commentator's suggestion in this case would present certain administrative difficulties, complicate tax administration, and possibly encourage the use of hindsight in tax reporting. After careful consideration, the IRS and Treasury have concluded that it is in the best interests of sound tax administration to have a uniform and certain rule applicable in all such situations. Thus, the final regulations do not adopt this suggestion.

D. *Application of effective date rules to 52–53 week-taxable years*

The proposed regulations provide a general rule concerning the application of certain effective dates as they apply to taxpayers employing 52–53-week taxable years. In response to comments, the final regulations clarify that this rule also applies to administrative guidance published by the Commissioner.

A comment was received suggesting that additional *Examples* be provided illustrating how particular terms other than those "expressed in terms of taxable years beginning, including, or ending with reference to the first or last day of a specified calendar month," apply to 52–53-week fiscal-year taxpayers. In response to this comment, clarifying language and an additional *Example* have been provided in the final regulations.

E. *Definitions of "pass-through entity" and "owner of a pass-through entity"*

The proposed regulations provide rules for certain pass-through entities and owners of pass-through entities relating to the treatment of certain taxable years ending with reference to the same calendar month. These rules are designed to prevent substantial deferral and distortion of income reporting.

The IRS and Treasury have become aware of a potentially abusive situation involving the deferral of income reporting in the case of closely-held Real Estate Investment Trusts (REITs) (within the meaning of section 6655(e)(5)(B)) and certain owners of interests in closely-held REITs (within the meaning of section 6655(e)(5)(A)).

For estimated tax purposes, certain owners of interests in closely-held REITs are required to recognize income from the REIT in a manner similar to partners in a partnership. Unlike a partnership, however, REITs are not required to use a taxable year that conforms to the taxable year of their owners but rather are required to use a taxable year ending December 31 pursuant to section 859. Thus, the potential for deferral of estimated taxes exists with respect to certain owners of interests in closely-held REITs, including owners with 52–53-week taxable years that reference December 31, as well as fiscal-year owners.

In an attempt to reduce the potential for deferral of estimated taxes in the case of certain owners of interests in closely-held REITs, the final regulations have been modified to add: (1) a closely-held REIT (within the meaning of section 6655(e)(5)(B)) to the definition of a *pass-through entity*; and (2) an owner of an interest (within the meaning of section 6655(e)(5)(A)) in a closely-held REIT to the definition of an *owner of a pass-through entity*. Thus, these owners of interests in a closely-held REIT with 52–53-week taxable years that reference December 31 will be required under the final regulations to recognize income from the closely-held REIT as if their taxable year ends on December 31.

F. *Accrual of foreign taxes*

The IRS recognizes that changes to the taxable year of a taxpayer may shift the taxable year in which foreign taxes are treated as accruing for U.S. purposes. The IRS also recognizes that similar results may occur in the case of taxpayers that use a 52–53-week taxable year, which will not always include the last day of the taxpayer's taxable year in a foreign jurisdiction. The IRS is working on guidance that it expects will be issued this year to ensure that changes in U.S. taxable years, or the use of a 52–53-week taxable year, do not result in unintended and inappropriate consequences for foreign tax credit purposes. Comments are requested on the changes necessary and appropriate to address the accrual of foreign taxes in these situations.

2. *Comments and Changes Relating to § 1.442 of the Proposed Regulations*

A. *Time and manner for filing an application*

The proposed regulations provide specific rules for the time and manner of filing an application to adopt, change, or retain an annual accounting period. Consistent with the general framework of the regulations, the IRS and Treasury have concluded that it is more appropriate to remove the specific time and manner requirements for filing applications for adoptions, changes, and retentions in annual accounting period from the final regulations, and provide them instead in administrative procedures published by the Commissioner. See Rev. Proc. 2002–37, Rev. Proc. 2002–38, and Rev. Proc. 2002–39, 2002–22 I.R.B. 1046. The IRS and Treasury believe that providing these rules in administrative guidance, rather than in regulations, allows the IRS more flexibility to respond in the future to the changing needs of taxpayers and the IRS.

The proposed regulations provide that an application for non-automatic approval of an annual accounting period change may be filed no earlier than the day following the close of the first effective year and no later than the 15th day of the third calendar month following the close of the first effective year. One commentator suggested that such applications be permitted to be filed no earlier than the later of: (1) the first day of the short period resulting from the proposed tax year change; or (2) 60 days prior to the end of the short period.

The IRS currently allows taxpayers to file applications with the national office within the referenced 60-day period and believes that many taxpayers take advantage of early filing, even knowing that their applications lack adequate information, in an effort to obtain priority over other applications processed by the national office. However, the lack of adequate financial and other required information common to such early applications requires that the IRS devote additional resources to properly develop and process the applications. Ultimately, this causes a delay in processing both the early applications, and other applications as well. For this reason, the administrative guidance issued concurrently with these final regulations do not adopt this suggestion. However, the IRS and Treasury Department intend to study filing patterns under the new rules, and will consider expanding or modifying the time frame for filing applications with the national office if circumstances warrant.

One commentator recommended that instead of requiring all taxpayers to file the application by the 15th day of the third calendar month following the close of the first taxable year in which the taxpayer wants the adoption, change, or retention to be effective (the first effective year), as the proposed regulations provide, the due date for the application should be the due date of the taxpayer's return for the short period, without extensions. The IRS and Treasury believe that such a rule will be simpler for taxpayers (such as individuals and partnerships) and the IRS. Accordingly, this change is adopted in the administrative guidance issued concurrently with these final regulations.

B. *Changes to required taxable years by pass-through entities*

One commentator suggested that the proposed regulations be modified to waive the Form 1128, *Application to Adopt, Change, or Retain a Tax Year*, filing requirement in the case of partnerships, S corporations, and personal service corporations (PSCs) changing to a "required taxable year" for the first taxable year for which such change is required. Alternatively, the commentator recommended use of an "automatic consent" procedure similar to the procedure

outlined in the proposed regulations for subsidiaries changing tax years to conform to the periods of their affiliated groups. The commentator reasoned that changes to statutorily required taxable years should not require the Commissioner's prior approval through any filing or application process.

Except in very limited circumstances (*e.g.*, adoptions of required years, certain section 444 terminations, and certain section 859 changes) applications historically have been required for changes to a required taxable year by a pass-through entity. The IRS and Treasury Department believe that the statutes that require such entities to use or change to a particular taxable year must be read in conjunction with the general requirement under section 442 to obtain the prior approval of the Commissioner to change an existing taxable year. Moreover, the applications serve to provide the IRS with necessary information about the entity's annual accounting period. Accordingly, this comment was not adopted in the final regulations or the administrative guidance issued concurrently with these regulations.

C. *Book conformity requirements*

The proposed regulations conform the recordkeeping requirement for taxpayers using a fiscal year to that of § 1.446–1(a)(4), which allows for a reconciliation between the taxpayer's books and return. However, the preamble to the proposed regulations noted that, as a term and condition of obtaining approval to adopt, change to, or retain an annual accounting period under section 442, certain taxpayers nevertheless may be required, under administrative procedures published by the Commissioner, to compute income and keep their books (including financial statements and reports to creditors) on the basis of the requested annual accounting period. In fact, strict book conformity is a general requirement in the administrative procedures for approval to make many changes. See, *e.g.*, Rev. Proc. 2002–37.

One commentator objected to the proposed elimination of procedures contained in the existing regulations under section 442 under which certain corporations are granted automatic approval to change their taxable year without a strict book conformity requirement (*i.e.*, by satisfying the general book conformity rules of section 446). The commentator recommended that either the final regulations retain these automatic consent rules or, alternatively, that the administrative procedures eliminate the strict book conformity requirement.

The IRS and Treasury Department believe it is appropriate to apply the more lenient book conformity rule of section 446 in the case of a taxpayer adopting, changing to, or retaining a required or ownership taxable year and in the case of a foreign corporation that is required by foreign law to use a particular year for financial accounting purposes. See, *e.g.*, Rev. Proc. 2002–39. However, for all other changes under the administrative procedures, the IRS and Treasury Department continue to believe that strict book conformity is an appropriate term and condition of a voluntary change in annual accounting period, as it provides assurance that the change is motivated by business, as opposed to tax, considerations. In addition, the IRS and Treasury believe, for reasons stated in the preamble to the proposed regulations, that tax administration and taxpayers are better served by providing the specific rules for adoptions, changes, and retentions of annual accounting periods in administrative pronouncements, rather than regulations. Accordingly, the comment has not been adopted.

3. *Comments and Changes Relating to Partnerships, S Corporations, and Personal Service Corporations (PSCs)*

A comment was received recommending that the limitation on additional required taxable year changes in the proposed regulations for partnerships using a majority-interest taxable years, be extended to partnerships using other required taxable years (*e.g.*, to principal partners' taxable years and to least-aggregate-deferral taxable years). The limitation for changes to a majority interest taxable year is specifically provided in section 706(b)(4)(B). No such statutory authority exists for providing similar limitations in the case of other required taxable year changes by partnerships. Accordingly, this comment was not adopted in the final regulations. However, the Treasury Department is considering this comment in connection with a legislative simplification study.

The proposed regulations (consistent with the existing temporary regulations) generally provide for a 1-year testing period for determining whether a taxpayer is a PSC. In the preamble to the proposed regulations, the IRS and Treasury Department responded to a comment received in connection with the original notice of proposed rulemaking cross-referenced by the temporary regulations. The original commentator suggested that the testing period be expanded to the three preceding taxable years in order to minimize instances in which taxpayers become PSCs due to temporary or aberrational conditions. In response, the IRS and Treasury Department indicated that they would consider alternatives to the current 1-year period if similar requests were received in comments to the proposed regulations now that taxpayers have significantly more experience with the 1-year rule.

Although some comments were received recommending a general 3-year testing period for both PSCs and S corporations, the suggestions were not directed to particular taxpayer burdens stemming from the 1-year testing period for a PSC or the original concern about taxpayers becoming a PSC because of temporary or aberrational conditions. Rather, commentators suggested that a general 3-year testing period rule would reduce repetitive "required tax year" changes, and promote tax-year certainty.

The IRS and Treasury Department believe that these reasons do not warrant extending the 1-year testing period for PSCs and S corporations because the current required taxable year framework for PSCs and S corporations should not result in repetitive required taxable year changes. Once a PSC or S corporation has changed to its required taxable year (*i.e.*, a calendar year), any further changes would be voluntary rather than required. Accordingly, this suggestion has not been adopted in the final regulations.

Effect on Other Documents

Rev. Rul. 57–589 is obsolete.

Rev. Rul. 65–316 (1965–2 C.B. 149) is obsolete.

Rev. Rul. 68–125 (1968–1 C.B. 189) is obsolete.

Rev. Rul. 69–563 is obsolete.
Rev. Rul. 74–326 (1974–2 C.B. 142) is obsolete.
Rev. Rul. 78–179 (1978–1 C.B. 132) is obsolete.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collections of information in these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that few small entities are expected to adopt a 52–53-week taxable year, triggering the collection of information, and that for those who do, the burden imposed under § 1.441–2(b)(1)(ii) will be minimal. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal authors of these regulations are Roy A. Hirschhorn and Michael F. Schmit of the Office of Associate Chief Counsel (Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1, 5c, 5f, 18, and 602 are amended as follows:

PART 1—INCOME TAXES

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

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

Par. 2. In the list below, for each section indicated in the left column, remove the old language in the middle column and add the new language in the right column.

Affected Section	Remove	Add
1.46–1(p)(2)(iv)	paragraph (b)(1) of § 1.441–2	§ 1.441–2
1.48–3(d)(1)(iii)	paragraph (b)(1) of § 1.441–2	§ 1.441–2
1.280H–1T(a), last sentence	§ 1.441–4T(d)	§ 1.441–3(c)
1.443–1(b)(1)(ii)	and paragraph (c)(5) of § 1.441–2	and § 1.441–2(b)(2)(ii).
1.444–1T(a)(1), first sentence	§ 1.441–4T(d)	§ 1.441–3(c)
1.444–2T(a), last sentence	§ 1.441–4T(d)	§ 1.441–3(c)
1.448–1(h)(2)(ii)(B)(*1*)	§ 1.441–2T(b)(1)	§ 1.441–2(c)
1.469–1(h)(4)(ii)(D)	§ 1.441–4T(f)	§ 1.441–3(e)
1.469–1T(g)(2)(i)	§ 1.441–4T(d)	§ 1.441–3(c)
1.1561–1(c)(2)	See paragraph (b)(1) of § 1.441–2	See § 1.441–2
1.6654–2(a), concluding text	paragraph (b) of § 1.441–2	§ 1.441–2(c)
1.6655–2(a)(4), first sentence	paragraph (b) of § 1.441–2	§ 1.441-2(c)
301.7701(b)–6(a), third sentence	§ 1.441–1(e)	§ 1.441–1(b)

Par. 3. Sections 1.441–0, 1.441–1, 1.441–2, 1.441–3, and 1.441–4 are added to read as follows:

§ 1.441–0 Table of contents.

This section lists the captions contained in §§ 1.441–1 through 1.441–4 as follows:

§ 1.441–1 Period for computation of taxable income.

(a) Computation of taxable income.
(1) In general.
(2) Length of taxable year.
(b) General rules and definitions.
(1) Taxable year.
(2) Required taxable year.
(i) In general.
(ii) Exceptions.
(A) 52–53-week taxable years.
(B) Partnerships, S corporations, and PSCs.
(C) Specified foreign corporations.
(3) Annual accounting period.
(4) Calendar year.
(5) Fiscal year.
(i) Definition.
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(6) Grandfathered fiscal year.
(7) Books.
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(c) Adoption of taxable year.
(1) In general.
(2) Approval required.
(i) Taxpayers with required taxable years.
(ii) Taxpayers without books.
(d) Retention of taxable year.
(e) Change of taxable year.
(f) Obtaining approval of the Commissioner or making a section 444 election.

§ 1.441–2 Election of taxable year consisting of 52–53 weeks.

(a) In general.
(1) Election.
(2) Effect.
(3) Eligible taxpayer.
(4) Example.
(b) Procedures to elect a 52–53-week taxable year.
(1) Adoption of a 52–53-week taxable year.
(i) In general.
(ii) Filing requirement.
(2) Change to (or from) a 52–53-week taxable year.
(i) In general.
(ii) Special rules for short period required to effect the change.
(3) Examples.
(c) Application of effective dates.
(1) In general.
(2) Examples.
(3) Changes in tax rates.
(4) Examples.
(d) Computation of taxable income.
(e) Treatment of taxable years ending with reference to the same calendar month.
(1) Pass-through entities.
(2) Personal service corporations and employee-owners.
(3) Definitions.
(i) Pass-through entity.
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(4) Examples.
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§ 1.441–3 Taxable year of a personal service corporation.

(a) Taxable year.
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§ 1.441–4 Effective date.

§ 1.441–1 Period for computation of taxable income.

(a) *Computation of taxable income*—(1) *In general*. Taxable income must be computed and a return must be made for a period known as the taxable year. For rules relating to methods of accounting, the taxable year for which items of gross income are included and deductions are taken, inventories, and adjustments, see parts II and III (section 446 and following), subchapter E, chapter 1 of the Internal Revenue Code, and the regulations thereunder.

(2) *Length of taxable year*. Except as otherwise provided in the Internal Revenue Code and the regulations thereunder (*e.g.*, § 1.441–2 regarding 52–53-week taxable years), a taxable year may not cover a period of more than 12 calendar months.

(b) *General rules and definitions*. The general rules and definitions in this paragraph (b) apply for purposes of sections 441 and 442 and the regulations thereunder.

(1) *Taxable year*. *Taxable year* means—

(i) The period for which a return is made, if a return is made for a period of less than 12 months (short period). See section 443 and the regulations thereunder;

(ii) Except as provided in paragraph (b)(1)(i) of this section, the taxpayer's required taxable year (as defined in paragraph (b)(2) of this section), if applicable;

(iii) Except as provided in paragraphs (b)(1)(i) and (ii) of this section, the taxpayer's annual accounting period (as defined in paragraph (b)(3) of this section), if it is a calendar year or a fiscal year; or

(iv) Except as provided in paragraphs (b)(1)(i) and (ii) of this section, the calendar year, if the taxpayer keeps no books, does not have an annual accounting period, or has an annual accounting period that does not qualify as a fiscal year.

(2) *Required taxable year*—(i) *In general*. Certain taxpayers must use the particular taxable year that is required under the Internal Revenue Code and the regulations thereunder (the required taxable year). For example, the required taxable year is—

(A) In the case of a foreign sales corporation or domestic international sales corporation, the taxable year determined under section 441(h) and § 1.921–1T(a)(11), (b)(4), and (b)(6);

(B) In the case of a personal service corporation (PSC), the taxable year determined under section 441(i) and § 1.441–3;

(C) In the case of a nuclear decommissioning fund, the taxable year determined under § 1.468A–4(c)(1);

(D) In the case of a designated settlement fund or a qualified settlement fund, the taxable year determined under § 1.468B–2(j);

(E) In the case of a common trust fund, the taxable year determined under section 584(i);

(F) In the case of certain trusts, the taxable year determined under section 644;

(G) In the case of a partnership, the taxable year determined under section 706 and § 1.706–1;

(H) In the case of an insurance company, the taxable year determined under section 843 and § 1.1502–76(a)(2);

(I) In the case of a real estate investment trust, the taxable year determined under section 859;

(J) In the case of a real estate mortgage investment conduit, the taxable year determined under section 860D(a)(5) and § 1.860D–1(b)(6);

(K) In the case of a specified foreign corporation, the taxable year determined under section 898(c)(1)(A);

(L) In the case of an S corporation, the taxable year determined under section 1378 and § 1.1378–1; or

(M) In the case of a member of an affiliated group that makes a consolidated return, the taxable year determined under § 1.1502–76.

(ii) *Exceptions*. Notwithstanding paragraph (b)(2)(i) of this section, the following taxpayers may have a taxable year other than their required taxable year:

(A) *52–53-week taxable years*. Certain taxpayers may elect to use a 52–53-week taxable year that ends with reference to their required taxable year. See, for example, §§ 1.441–3 (PSCs), 1.706–1 (partnerships), 1.1378–1 (S corporations), and 1.1502–76(a)(1) (members of a consolidated group).

(B) *Partnerships, S corporations, and PSCs*. A partnership, S corporation, or PSC may use a taxable year other than its required taxable year if the taxpayer elects to use a taxable year other than its required taxable year under section 444, elects a 52–53-week taxable year that ends with reference to its required taxable year as provided in paragraph (b)(2)(ii)(A) of this section or to a taxable year elected under section 444, or establishes a business purpose to the satisfaction of the Commissioner under section 442 (such as a grandfathered fiscal year).

(C) *Specified foreign corporations*. A specified foreign corporation (as defined in section 898(b)) may use a taxable year other than its required taxable year if it elects a 52–53-week taxable year that ends with reference to its required taxable year as provided in paragraph (b)(2)(ii)(A) of this section or makes a one-month deferral election under section 898(c)(1)(B).

(3) *Annual accounting period*. *Annual accounting period* means the annual period (calendar year or fiscal year) on the basis of which the taxpayer regularly computes its income in keeping its books.

(4) *Calendar year*. *Calendar year* means a period of 12 consecutive months ending on December 31. A taxpayer who has not established a fiscal year must make its return on the basis of a calendar year.

(5) *Fiscal year*—(i) *Definition*. *Fiscal year* means—

(A) A period of 12 consecutive months ending on the last day of any month other than December; or

(B) A 52–53-week taxable year, if such period has been elected by the taxpayer. See § 1.441–2.

(ii) *Recognition*. A fiscal year will be recognized only if the books of the taxpayer are kept in accordance with such fiscal year.

(6) *Grandfathered fiscal year*. *Grandfathered fiscal year* means a fiscal year (other than a year that resulted in a three month or less deferral of income) that a partnership or an S corporation received permission to use on or after July 1, 1974, by a letter ruling (*i.e.*, not by automatic approval).

(7) *Books*. *Books* include the taxpayer's regular books of account and such other records and data as may be necessary to support the entries on the taxpayer's books and on the taxpayer's return, as for example, a reconciliation of any difference between such books and the taxpayer's return. Records that are sufficient to reflect income adequately and clearly on the basis of an annual accounting period will be regarded as the keeping of books. See section 6001 and the regulations thereunder for rules relating to the keeping of books and records.

(8) *Taxpayer. Taxpayer* has the same meaning as the term *person* as defined in section 7701(a)(1) (*e.g.*, an individual, trust, estate, partnership, association, or corporation) rather than the meaning of the term taxpayer as defined in section 7701(a)(14) (any person subject to tax).

(c) *Adoption of taxable year*—(1) *In general*. Except as provided in paragraph (c)(2) of this section, a new taxpayer may adopt any taxable year that satisfies the requirements of section 441 and the regulations thereunder without the approval of the Commissioner. A taxable year of a new taxpayer is adopted by filing its first Federal income tax return using that taxable year. The filing of an application for automatic extension of time to file a Federal income tax return (*e.g.*, Form 7004, *"Application for Automatic Extension of Time To File Corporation Income Tax Return"*), the filing of an application for an employer identification number (*i.e.*, Form SS-4, "*Application for Employer Identification Number")*, or the payment of estimated taxes, for a particular taxable year do not constitute an adoption of that taxable year.

(2) *Approval required*—(i) *Taxpayers with required taxable years*. A newly-formed partnership, S corporation, or PSC that wants to adopt a taxable year other than its required taxable year, a taxable year elected under section 444, or a 52–53-week taxable year that ends with reference to its required taxable year or a taxable year elected under section 444 must establish a business purpose and obtain the approval of the Commissioner under section 442.

(ii) *Taxpayers without books*. A taxpayer that must use a calendar year under section 441(g) and paragraph (f) of this section may not adopt a fiscal year without obtaining the approval of the Commissioner.

(d) *Retention of taxable year*. In certain cases, a partnership, S corporation, electing S corporation, or PSC will be required to change its taxable year unless it obtains the approval of the Commissioner under section 442, or makes an election under section 444, to retain its current taxable year. For example, a corporation using a June 30 fiscal year that either becomes a PSC or elects to be an S corporation and, as a result, is required to use the calendar year under section 441(i) or 1378, respectively, must obtain the approval of the Commissioner to retain its current fiscal year. Similarly, a partnership using a taxable year that corresponds to its required taxable year must obtain the approval of the Commissioner to retain such taxable year if its required taxable year changes as a result of a

change in ownership. However, a partnership that previously established a business purpose to the satisfaction of the Commissioner to use a taxable year is not required to obtain the approval of the Commissioner if its required taxable year changes as a result of a change in ownership.

(e) *Change of taxable year*. Once a taxpayer has adopted a taxable year, such taxable year must be used in computing taxable income and making returns for all subsequent years unless the taxpayer obtains approval from the Commissioner to make a change or the taxpayer is otherwise authorized to change without the approval of the Commissioner under the Internal Revenue Code (*e.g.*, section 444 or 859) or the regulations thereunder.

(f) *Obtaining approval of the Commissioner or making a section 444 election*. See § 1.442–1(b) for procedures for obtaining approval of the Commissioner (automatically or otherwise) to adopt, change, or retain an annual accounting period. See §§ 1.444–1T and 1.444–2T for qualifications, and 1.444–3T for procedures, for making an election under section 444.

§ 1.441–2 Election of taxable year consisting of 52–53 weeks.

(a) *In general*—(1) *Election*. An eligible taxpayer may elect to compute its taxable income on the basis of a fiscal year that—

(i) Varies from 52 to 53 weeks;

(ii) Ends always on the same day of the week; and

(iii) Ends always on—

(A) Whatever date this same day of the week last occurs in a calendar month; or

(B) Whatever date this same day of the week falls that is the nearest to the last day of the calendar month.

(2) *Effect*. In the case of a taxable year described in paragraph (a)(1)(iii)(A) of this section, the year will always end within the month and may end on the last day of the month, or as many as six days before the end of the month. In the case of a taxable year described in paragraph (a)(1)(iii)(B) of this section, the year may end on the last day of the month, or as many as three days before or three days after the last day of the month.

(3) *Eligible taxpayer*. A taxpayer is eligible to elect a 52–53-week taxable year if such fiscal year would otherwise satisfy the requirements of section 441 and the regulations thereunder. For example, a taxpayer that is required to use a calendar year under § 1.441–1(b)(2)(i)(D) is not an eligible taxpayer.

(4) *Example*. The provisions of this paragraph (a) are illustrated by the following example:

Example. If the taxpayer elects a taxable year ending always on the last Saturday in November, then for the year 2001, the taxable year would end on November 24, 2001. On the other hand, if the taxpayer had elected a taxable year ending always on the Saturday nearest to the end of November, then for the year 2001, the taxable year would end on December 1, 2001.

(b) *Procedures to elect a 52–53-week taxable year*—(1) *Adoption of a 52–53-week taxable year*—(i) *In general*. A new eligible taxpayer elects a 52–53-week taxable year by adopting such year in accordance with § 1.441–1(c). A newly-formed partnership, S corporation or personal service corporation (PSC) may adopt a 52–53-week taxable year without the approval of the Commissioner if such year ends with reference to either the taxpayer's required taxable year (as defined in § 1.441-1(b)(2)) or the taxable year elected under section 444. See §§ 1.441–3, 1.706–1, and 1.1378–1. Similarly, a newly-formed specified foreign corporation (as defined in section 898(b)) may adopt a 52–53-week taxable year if such year ends with reference to the taxpayer's required taxable year, or, if the one-month deferral election under section 898(c)(1)(B) is made, with reference to the month immediately preceding the required taxable year. See § 1.1502–76(a)(1) for special rules regarding subsidiaries adopting 52–53-week taxable years.

(ii) *Filing requirement*. A taxpayer adopting a 52–53-week taxable year must file with its Federal income tax return for its first taxable year a statement containing the following information—

(A) The calendar month with reference to which the 52–53-week taxable year ends;

(B) The day of the week on which the 52–53-week taxable year always will end; and

(C) Whether the 52–53-week taxable year will always end on the date on which that day of the week last occurs in the calendar month, or on the date on which that day of the week falls that is nearest to the last day of that calendar month.

(2) *Change to (or from) a 52–53-week taxable year*—(i) *In general*. An election of a 52–53-week taxable year by an existing eligible taxpayer with an established taxable year is treated as a change in annual accounting period that requires the approval of the Commissioner in accordance with § 1.442–1. Thus, a taxpayer must obtain approval to change from its current taxable year to a 52–53-week taxable year, even if such 52–53-week taxable year ends with reference to the same calendar month. Similarly, a taxpayer must obtain approval to change from a 52–53-week taxable year, or to change from one 52–53-week taxable year to another 52–53-week taxable year. However, a taxpayer may obtain approval for 52–53-week taxable year changes automatically to the extent provided in administrative procedures published by the Commissioner. See § 1.442–1(b) for procedures for obtaining such approval.

(ii) *Special rules for the short period required to effect the change*. If a change to or from a 52–53-week taxable year results in a short period (within the meaning of § 1.443–1(a)) of 359 days or more, or six days or less, the tax computation under § 1.443–1(b) does not apply. If the short period is 359 days or more, it is treated as a full taxable year. If the short period is six days or less, such short period is not a separate taxable year but instead is added to and deemed a part of the following taxable year. (In the case of a change to or from a 52–53-week taxable year not involving a change of the month with reference to which the taxable year ends, the tax computation under § 1.443–1(b) does not apply because the short period will always be 359 days or more, or six days or less.) In the case of a short period which is more than six days and less than 359 days, taxable income for the short period is placed on an annual basis for purposes of § 1.443–1(b) by multiplying such income by 365 and dividing the result by the number of days in the short period. In such case, the tax for the short period is the same part of the tax computed on such income placed on an annual basis as the number of days in the short period is of 365 days (unless § 1.443–1(b)(2), relating to the alternative

tax computation, applies). For an adjustment in deduction for personal exemption, see § 1.443–1(b)(1)(v).

(3) *Examples*. The following examples illustrate paragraph (b)(2)(ii) of this section:

Example 1. A taxpayer having a fiscal year ending April 30, obtains approval to change to a 52–53-week taxable year ending the last Saturday in April for taxable years beginning after April 30, 2001. This change involves a short period of 362 days, from May 1, 2001, to April 27, 2002, inclusive. Because the change results in a short period of 359 days or more, it is not placed on an annual basis and is treated as a full taxable year.

Example 2. Assume the same conditions as *Example 1*, except that the taxpayer changes for taxable years beginning after April 30, 2002, to a taxable year ending on the Thursday nearest to April 30. This change results in a short period of two days, May 1 to May 2, 2002. Because the short period is less than seven days, tax is not separately computed. This short period is added to and deemed part of the following 52–53-week taxable year, which would otherwise begin on May 3, 2002, and end on May 1, 2003.

(c) *Application of effective dates*—(1) *In general*. Except as provided in paragraph (c)(3) of this section, for purposes of determining the effective date (*e.g.*, of legislative, regulatory, or administrative changes) or the applicability of any provision of the internal revenue laws that is expressed in terms of taxable years beginning, including, or ending with reference to the first or last day of a specified calendar month, a 52–53-week taxable year is deemed to begin on the first day of the calendar month nearest to the first day of the 52–53-week taxable year, and is deemed to end or close on the last day of the calendar month nearest to the last day of the 52–53-week taxable year, as the case may be. Examples of provisions of this title, the applicability of which is expressed in terms referred to in the preceding sentence, include the provisions relating to the time for filing returns and other documents, paying tax, or performing other acts, and the provisions of part II, subchapter B, chapter 6 (section 1561 and following) relating to surtax exemptions of certain controlled corporations.

(2) *Examples*. The provisions of paragraph (c)(1) of this section may be illustrated by the following examples:

Example 1. Assume that an income tax provision is applicable to taxable years beginning on or after January 1, 2001. For that purpose, a 52–53-week taxable year beginning on any day within the period December 26, 2000, to January 4, 2001, inclusive, is treated as beginning on January 1, 2001.

Example 2. Assume that an income tax provision requires that a return must be filed on or before the 15th day of the third month following the close of the taxable year. For that purpose, a 52–53-week taxable year ending on any day during the period May 25 to June 3, inclusive, is treated as ending on May 31, the last day of the month ending nearest to the last day of the taxable year, and the return, therefore, must be made on or before August 15.

Example 3. Assume that a revenue procedure requires the performance of an act by the taxpayer within "the first 90 days of the taxable year," by "the 75th day of the taxable year," or, alternately, by "the last day of the taxable year." The taxpayer employs a 52–53-week taxable year that ends always on the Saturday closest to the last day of December. These requirements are not expressed in terms of taxable years beginning, including, or ending with reference to the first or last day of a specified calendar month, and are accordingly outside the scope of the rule stated in § 1.441–2(c)(1). Accordingly, the taxpayer must perform the required act by the 90th, 75th, or last day, respectively, of its taxable year.

Example 4. X, a corporation created on January 1, 2001, elects a 52–53-week taxable year ending on the Friday nearest the end of December. Thus, X's first taxable year begins on Monday, January 1, 2001, and ends on Friday, December 28, 2001; its next taxable year begins on Saturday, December 29, 2001, and ends on Friday, January 3, 2003; and its next taxable year begins on Saturday, January 4, 2003, and ends on Friday, January 2, 2004. For purposes of applying the provisions of Part II, subchapter B, chapter 6 of the Internal Revenue Code, X's first taxable year is deemed to end on December 31, 2001; its next taxable year is deemed to begin on January 1, 2002, and end on December 31, 2002, and its next taxable year is deemed to begin on January 1, 2003, and end on December 31, 2003. Accordingly, each such taxable year is treated as including one and only one December 31st.

(3) *Changes in tax rates*. If a change in the rate of tax is effective during a 52–53-week taxable year (other than on the first day of such year as determined under paragraph (c)(1) of this section), the tax for the 52–53-week taxable year must be computed in accordance with section 15, relating to effect of changes, and the regulations thereunder. For the purpose of the computation under section 15, the determination of the number of days in the period before the change, and in the period on and after the change, is to be made without regard to the provisions of paragraph (b)(1) of this paragraph.

(4) *Examples*. The provisions of paragraph (c)(3) of this section may be illustrated by the following examples:

Example 1. Assume a change in the rate of tax is effective for taxable years beginning after June 30, 2002. For a 52–53-week taxable year beginning on Friday, November 2, 2001, the tax must be computed on the basis of the old rates for the actual number of days from November 2, 2001, to June 30, 2002, inclusive, and on the basis of the new rates for the actual number of days from July 1, 2002, to Thursday, October 31, 2002, inclusive.

Example 2. Assume a change in the rate of tax is effective for taxable years beginning after June 30, 2001. For this purpose, a 52–53-week taxable year beginning on any of the days from June 25 to July 4, inclusive, is treated as beginning on July 1. Therefore, no computation under section 15 will be required for such year because of the change in rate.

(d) *Computation of taxable income*. The principles of section 451, relating to the taxable year for inclusion of items of gross income, and section 461, relating to the taxable year for taking deductions, generally are applicable to 52–53-week taxable years. Thus, except as otherwise provided, all items of income and deduction must be determined on the basis of a 52–53-week taxable year. However, a taxpayer may determine particular items as though the 52–53-week taxable year were a taxable year consisting of 12 calendar months, provided that practice is consistently followed by the taxpayer and clearly reflects income. For example, an allowance for depreciation or amortization may be determined on the basis of a 52–53-week taxable year, or as though the 52–53-week taxable year is a taxable year consisting of 12 calendar months, provided the taxpayer consistently follows that practice with respect to all depreciable or amortizable items.

(e) *Treatment of taxable years ending with reference to the same calendar month*—(1) *Pass-through entities*. If a pass-through entity (as defined in paragraph (e)(3)(i) of this section) or an owner of a pass-through entity (as defined in paragraph (e)(3)(ii) of this section), or both, use a 52–53-week taxable year and the taxable year of the pass-through entity and the owner end with reference to the same calendar month, then, for purposes of determining the taxable year in which items of income, gain, loss, deductions, or credits from the pass-through entity are taken into account by the owner of the pass-through, the owner's taxable year will be deemed to end on the last day of the pass-through's taxable year. Thus, if the taxable year of a partnership and a partner end with reference to the same calendar month, then for purposes of determining the taxable year in which that partner takes into account items described in section 702 and items that are deductible by the partnership (including items

described in section 707(c)) and includible in the income of that partner, that partner's taxable year will be deemed to end on the last day of the partnership's taxable year. Similarly, if the taxable year of an S corporation and a shareholder end with reference to the same calendar month, then for purposes of determining the taxable year in which that shareholder takes into account items described in section 1366(a) and items that are deductible by the S corporation and includible in the income of that shareholder, that shareholder's taxable year will be deemed to end on the last day of the S corporation's taxable year.

(2) *Personal service corporations and employee-owners*. If the taxable year of a PSC (within the meaning of § 1.441–3(c)) and an employee-owner (within the meaning of § 1.441–3(g)) end with reference to the same calendar month, then for purposes of determining the taxable year in which an employee-owner takes into account items that are deductible by the PSC and includible in the income of the employee-owner, the employee-owner's taxable year will be deemed to end on the last day of the PSC's taxable year.

(3) *Definitions*—(i) *Pass-through entity*. For purposes of this section, a pass-through entity means a partnership, S corporation, trust, estate, closely-held real estate investment trust (within the meaning of section 6655(e)(5)(B)), common trust fund (within the meaning of section 584(i)), controlled foreign corporation (within the meaning of section 957), foreign personal holding company (within the meaning of section 552), or passive foreign investment company that is a qualified electing fund (within the meaning of section 1295).

(ii) *Owner of a pass-through entity*. For purposes of this section, an owner of a pass-through entity generally means a taxpayer that owns an interest in, or stock of, a pass-through entity. For example, an owner of a pass-through entity includes a partner in a partnership, a shareholder of an S corporation, a beneficiary of a trust or an estate, an owner of a closely-held real estate investment trust (within the meaning of section 6655(e)(5)(A)), a participant in a common trust fund, a U.S. shareholder (as defined in section 951(b)) of a controlled foreign corporation, a U.S. shareholder (as defined in section 551(a)) of a foreign personal holding company, or a U.S. person that holds stock in a passive foreign investment company that is a qualified electing fund with respect to that shareholder.

(4) *Examples*. The provisions of paragraph (e)(2) of this section may be illustrated by the following examples:

Example 1. ABC Partnership uses a 52–53-week taxable year that ends on the Wednesday nearest to December 31, and its partners, A, B, and C, are individual calendar year taxpayers. Assume that, for ABC's taxable year ending January 3, 2001, each partner's distributive share of ABC's taxable income is $10,000. Under section 706(a) and paragraph (e)(1) of this section, for the taxable year ending December 31, 2000, A, B, and C each must include $10,000 in income with respect to the ABC year ending January 3, 2001. Similarly, if ABC makes a guaranteed payment to A on January 2, 2001, A must include the payment in income for A's taxable year ending December 31, 2000.

Example 2. X, a PSC, uses a 52–53-week taxable year that ends on the Wednesday nearest to December 31, and all of the employee-owners of X are individual calendar year taxpayers. Assume that, for its taxable year ending January 3, 2001, X pays a bonus of $10,000 to each employee-owner on January 2, 2001. Under paragraph (e)(2) of this section, each employee-owner must include its bonus in income for the taxable year ending December 31, 2000.

(5) *Transition rule*. In the case of an owner of a pass-through entity (other than the owner of a partnership or S corporation) that is required by this paragraph (e) to include in income for its first taxable year ending on or after May 17, 2002, amounts attributable to two taxable years of a pass-through entity, the amount that otherwise would be required to be included in income for such first taxable year by reason of this paragraph (e) should be included in income ratably over the four-taxable-year period beginning with such first taxable year under principles similar to § 1.702–3T, unless the owner of the pass-through entity elects to include all such income in its first taxable year ending on or after May 17, 2002.

§ 1.441–3 Taxable year of a personal service corporation.

(a) *Taxable year*—(1) *Required taxable year*. Except as provided in paragraph (a)(2) of this section, the taxable year of a personal service corporation (PSC) (as defined in paragraph (c) of this section) must be the calendar year.

(2) *Exceptions*. A PSC may have a taxable year other than its required taxable year (*i.e.*, a fiscal year) if it makes an election under section 444, elects to use a 52–53-week taxable year that ends with reference to the calendar year or a taxable year elected under section 444, or establishes a business purpose for such fiscal year and obtains the approval of the Commissioner under section 442.

(b) *Adoption, change, or retention of taxable year*—(1) *Adoption of taxable year*. A PSC may adopt, in accordance with § 1.441–1(c), the calendar year, a taxable year elected under section 444, or a 52–53-week taxable year ending with reference to the calendar year or a taxable year elected under section 444 without the approval of the Commissioner. See § 1.441–1. A PSC that wants to adopt any other taxable year must establish a business purpose and obtain the approval of the Commissioner under section 442.

(2) *Change in taxable year*. A PSC that wants to change its taxable year must obtain the approval of the Commissioner under section 442 or make an election under section 444. However, a PSC may obtain automatic approval for certain changes, including a change to the calendar year or to a 52–53-week taxable year ending with reference to the calendar year, pursuant to administrative procedures published by the Commissioner.

(3) *Retention of taxable year*. In certain cases, a PSC will be required to change its taxable year unless it obtains the approval of the Commissioner under section 442, or makes an election under section 444, to retain its current taxable year. For example, a corporation using a June 30 fiscal year that becomes a PSC and, as a result, is required to use the calendar year must obtain the approval of the Commissioner to retain its current fiscal year.

(4) *Procedures for obtaining approval or making a section 444 election*. See § 1.442–1(b) for procedures to obtain the approval of the Commissioner (automatically or otherwise) to adopt, change, or retain a taxable year. See §§ 1.444–1T and 1.444–2T for qualifications, and 1.444–3T for procedures, for making an election under section 444.

(5) *Examples*. The provisions of paragraph (b)(4) of this section may be illustrated by the following examples:

Example 1. X, whose taxable year ends on January 31, 2001, becomes a PSC for its taxable year beginning February 1, 2001, and does not obtain the approval of the Commissioner for using a fiscal

year. Thus, for taxable years ending before February 1, 2001, this section does not apply with respect to X. For its taxable year beginning on February 1, 2001, however, X will be required to comply with paragraph (a) of this section. Thus, unless X obtains approval of the Commissioner to use a January 31 taxable year, or makes a section 444 election, X will be required to change its taxable year to the calendar year under paragraph (b) of this section by using a short taxable year that begins on February 1, 2001, and ends on December 31, 2001. Under paragraph (b)(1) of this section, X may obtain automatic approval to change its taxable year to a calendar year. See § 1.442–1(b).

Example 2. Assume the same facts as in *Example 1*, except that X desires to change to a 52–53-week taxable year ending with reference to the month of December. Under paragraph (b)(1) of this section X may obtain automatic approval to make the change. See § 1.442–1(b).

(c) *Personal service corporation defined*—(1) *In general*. For purposes of this section and section 442, a taxpayer is a PSC for a taxable year only if—

(i) The taxpayer is a C corporation (as defined in section 1361(a)(2)) for the taxable year;

(ii) The principal activity of the taxpayer during the testing period is the performance of personal services;

(iii) During the testing period, those services are substantially performed by employee-owners (as defined in paragraph (g) of this section); and

(iv) Employee-owners own (as determined under the attribution rules of section 318, except that the language "any" applies instead of "50 percent" in section 318(a)(2)(C)) more than 10 percent of the fair market value of the outstanding stock in the taxpayer on the last day of the testing period.

(2) *Testing period*—(i) *In general*. Except as otherwise provided in paragraph (c)(2)(ii) of this section, the testing period for any taxable year is the immediately preceding taxable year.

(ii) *New corporations*. The testing period for a taxpayer's first taxable year is the period beginning on the first day of that taxable year and ending on the earlier of—

(A) The last day of that taxable year; or

(B) The last day of the calendar year in which that taxable year begins.

(3) *Examples*. The provisions of paragraph (c)(2)(ii) of this section may be illustrated by the following examples:

Example 1. Corporation A's first taxable year begins on June 1, 2001, and A desires to use a September 30 taxable year. However, if A is a personal service corporation, it must obtain the Commissioner's approval to use a September 30 taxable year. Pursuant to paragraph (c)(2)(ii) of this section, A's testing period for its first taxable year beginning June 1, 2001, is the period June 1, 2001, through September 30, 2001. Thus, if, based upon such testing period, A is a personal service corporation, A must obtain the Commissioner's permission to use a September 30 taxable year.

Example 2. The facts are the same as in *Example 1*, except that A desires to use a March 31 taxable year. Pursuant to paragraph (c)(2)(ii) of this section, A's testing period for its first taxable year beginning June 1, 2001, is the period June 1, 2001, through December 31, 2001. Thus, if, based upon such testing period, A is a personal service corporation, A must obtain the Commissioner's permission to use a March 31 taxable year.

(d) *Performance of personal services*—(1) *Activities described in section 448(d)(2)(A)*. For purposes of this section, any activity of the taxpayer described in section 448(d)(2)(A) or the regulations thereunder will be treated as the performance of personal services. Therefore, any activity of the taxpayer that involves the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting (as such fields are defined in § 1.448–1T) will be treated as the performance of personal services for purposes of this section.

(2) *Activities not described in section 448(d)(2)(A)*. For purposes of this section, any activity of the taxpayer not described in section 448(d)(2)(A) or the regulations thereunder will not be treated as the performance of personal services.

(e) *Principal activity*—(1) *General rule*. For purposes of this section, the principal activity of a corporation for any testing period will be the performance of personal services if the cost of the corporation's compensation (the compensation cost) for such testing period that is attributable to its activities that are treated as the performance of personal services within the meaning of paragraph (d) of this section (*i.e.*, the total compensation for personal service activities) exceeds 50 percent of the corporation's total compensation cost for such testing period.

(2) *Compensation cost*—(i) *Amounts included*. For purposes of this section, the compensation cost of a corporation for a taxable year is equal to the sum of the following amounts allowable as a deduction, allocated to a long-term contract, or otherwise chargeable to a capital account by the corporation during such taxable year—

(A) Wages and salaries; and

(B) Any other amounts, attributable to services performed for or on behalf of the corporation by a person who is an employee of the corporation (including an owner of the corporation who is treated as an employee under paragraph (g)(2) of this section) during the testing period. Such amounts include, but are not limited to, amounts attributable to deferred compensation, commissions, bonuses, compensation includible in income under section 83, compensation for services based on a percentage of profits, and the cost of providing fringe benefits that are includible in income.

(ii) *Amounts excluded*. Notwithstanding paragraph (e)(2)(i) of this section, compensation cost does not include amounts attributable to a plan qualified under section 401(a) or 403(a), or to a simplified employee pension plan defined in section 408(k).

(3) *Attribution of compensation cost to personal service activity*—(i) *Employees involved only in the performance of personal services*. The compensation cost for employees involved only in the performance of activities that are treated as personal services under paragraph (d) of this section, or employees involved only in supporting the work of such employees, are considered to be attributable to the corporation's personal service activity.

(ii) *Employees involved only in activities that are not treated as the performance of personal services*. The compensation cost for employees involved only in the performance of activities that are not treated as personal services under paragraph (d) of this section, or for employees involved only in supporting the work of such employees, are not considered to be attributable to the corporation's personal service activity.

(iii) *Other employees*. The compensation cost for any employee who is not described in either paragraph (e)(3)(i) or (ii) of this section (a mixed-activity employee) is allocated as follows—

(A) *Compensation cost attributable to personal service activity*. That portion of the compensation cost for a mixed activity employee that is attributable to the corporation's personal service activity

equals the compensation cost for that employee multiplied by the percentage of the total time worked for the corporation by that employee during the year that is attributable to activities of the corporation that are treated as the performance of personal services under paragraph (d) of this section. That percentage is to be determined by the taxpayer in any reasonable and consistent manner. Time logs are not required unless maintained for other purposes;

(B) *Compensation cost not attributable to personal service activity*. That portion of the compensation cost for a mixed activity employee that is not considered to be attributable to the corporation's personal service activity is the compensation cost for that employee less the amount determined in paragraph (e)(3)(iii)(A) of this section.

(f) *Services substantially performed by employee-owners*—(1) *General rule*. Personal services are substantially performed during the testing period by employee-owners of the corporation if more than 20 percent of the corporation's compensation cost for that period attributable to its activities that are treated as the performance of personal services within the meaning of paragraph (d) of this section (*i.e.*, the total compensation for personal service activities) is attributable to personal services performed by employee-owners.

(2) *Compensation cost attributable to personal services*. For purposes of paragraph (f)(1) of this section—

(i) The corporation's compensation cost attributable to its activities that are treated as the performance of personal services is determined under paragraph (e)(3) of this section; and

(ii) The portion of the amount determined under paragraph (f)(2)(i) of this section that is attributable to personal services performed by employee-owners is to be determined by the taxpayer in any reasonable and consistent manner.

(3) *Examples*. The provisions of this paragraph (f) may be illustrated by the following examples:

Example 1. For its taxable year beginning February 1, 2001, Corp A's testing period is the taxable year ending January 31, 2000. During that testing period, A's only activity was the performance of personal services. The total compensation cost of A (including compensation cost attributable to employee-owners) for the testing period was $1,000,000. The total compensation cost attributable to employee-owners of A for the testing period was $210,000. Pursuant to paragraph (f)(1) of this section, the employee-owners of A substantially performed the personal services of A during the testing period because the compensation cost of A's employee-owners was more than 20 percent of the total compensation cost for all of A's employees (including employee-owners).

Example 2. Corp B has the same facts as corporation A in *Example 1*, except that during the taxable year ending January 31, 2001, B also participated in an activity that would not be characterized as the performance of personal services under this section. The total compensation cost of B (including compensation cost attributable to employee-owners) for the testing period was $1,500,000 ($1,000,000 attributable to B's personal service activity and $500,000 attributable to B's other activity). The total compensation cost attributable to employee-owners of B for the testing period was $250,000 ($210,000 attributable to B's personal service activity and $40,000 attributable to B's other activity). Pursuant to paragraph (f)(1) of this section, the employee-owners of B substantially performed the personal services of B during the testing period because more than 20 percent of B's compensation cost during the testing period attributable to its personal service activities was attributable to personal services performed by employee-owners ($210,000).

(g) *Employee-owner defined*—(1) *General rule*. For purposes of this section, a person is an employee-owner of a corporation for a testing period if—

(i) The person is an employee of the corporation on any day of the testing period; and

(ii) The person owns any outstanding stock of the corporation on any day of the testing period.

(2) *Special rule for independent contractors who are owners*. Any person who is an owner of the corporation within the meaning of paragraph (g)(1)(ii) of this section and who performs personal services for, or on behalf of, the corporation is treated as an employee for purposes of this section, even if the legal form of that person's relationship to the corporation is such that the person would be considered an independent contractor for other purposes.

(h) *Special rules for affiliated groups filing consolidated returns*—(1) *In general*. For purposes of applying this section to the members of an affiliated group of corporations filing a consolidated return for the taxable year—

(i) The members of the affiliated group are treated as a single corporation;

(ii) The employees of the members of the affiliated group are treated as employees of such single corporation; and

(iii) All of the stock of the members of the affiliated group that is not owned by any other member of the affiliated group is treated as the outstanding stock of that corporation.

(2) *Examples*. The provisions of this paragraph (h) may be illustrated by the following examples:

Example 1. The affiliated group AB, consisting of corporation A and its wholly owned subsidiary B, filed a consolidated Federal income tax return for the taxable year ending January 31, 2001, and AB is attempting to determine whether it is affected by this section for its taxable year beginning February 1, 2001. During the testing period (*i.e.*, the taxable year ending January 31, 2001), A did not perform personal services. However, B's only activity was the performance of personal services. On the last day of the testing period, employees of A did not own any stock in A. However, some of B's employees own stock in A. In the aggregate, B's employees own 9 percent of A's stock on the last day of the testing period. Pursuant to paragraph (h)(1) of this section, this section is effectively applied on a consolidated basis to members of an affiliated group filing a consolidated Federal income tax return. Because the only employee-owners of AB are the employees of B, and because B's employees do not own more than 10 percent of AB on the last day of the testing period, AB is not a PSC subject to the provisions of this section. Thus, AB is not required to determine on a consolidated basis whether, during the testing period, its principal activity is the providing of personal services, or the personal services are substantially performed by employee-owners.

Example 2. The facts are the same as in *Example 1*, except that on the last day of the testing period A owns only 80 percent of B. The remaining 20 percent of B is owned by employees of B. The fair market value of A, including its 80 percent interest in B, as of the last day of the testing period, is $1,000,000. In addition, the fair market value of the 20 percent interest in B owned by B's employees is $50,000 as of the last day of the testing period. Pursuant to paragraphs (c)(1)(iv) and (h)(1) of this section, AB must determine whether the employee-owners of A and B (*i.e.*, B's employees) own more than 10 percent of the fair market value of A and B as of the last day of the testing period. Because the $140,000 [($1,000,000 x .09) + $50,000] fair market value of the stock held by B's employees is greater than 10 percent of the aggregate fair market value of A and B as of the last day of the testing period, or $105,000 [$1,000,000 + $50,000 x .10], AB may be subject to this section if, on a consolidated basis during the testing period, the principal activity of AB is the performance of personal services and the personal services are substantially performed by employee-owners.

§ 1.441–4 Effective date.

Sections 1.441–0 through 1.441–3 are applicable for taxable years ending on or after May 17, 2002.

§§ 1.441–1T, 1.441–2T, 1.441–3T and 1.441–4T [Removed]

Par. 4. Sections 1.441–1T, 1.441–2T, 1.441–3T and 1.441–4T are removed.

Par 5. Section 1.442–1 is revised to read as follows:

§ 1.442–1 Change of annual accounting period.

(a) *Approval of the Commissioner*. A taxpayer that has adopted an annual accounting period (as defined in § 1.441–1(b)(3)) as its taxable year generally must continue to use that annual accounting period in computing its taxable income and for making its Federal income tax returns. If the taxpayer wants to change its annual accounting period and use a new taxable year, it must obtain the approval of the Commissioner, unless it is otherwise authorized to change without the approval of the Commissioner under either the Internal Revenue Code (*e.g.*, section 444 and section 859) or the regulations thereunder (*e.g.*, paragraph (c) of this section). In addition, as described in § 1.441–1(c) and (d), a partnership, S corporation, electing S corporation, or personal service corporation (PSC) generally is required to secure the approval of the Commissioner to adopt or retain an annual accounting period other than its required taxable year. The manner of obtaining approval from the Commissioner to adopt, change, or retain an annual accounting period is provided in paragraph (b) of this Section. However, special rules for obtaining approval may be provided in other sections.

(b) *Obtaining approval*—(1) *Time and manner for requesting approval*. In order to secure the approval of the Commissioner to adopt, change, or retain an annual accounting period, a taxpayer must file an application, generally on Form 1128, "*Application To Adopt, Change, or Retain a Tax Year*", with the Commissioner within such time and in such manner as is provided in administrative procedures published by the Commissioner.

(2) *General requirements for approval*. An adoption, change, or retention in annual accounting period will be approved where the taxpayer establishes a business purpose for the requested annual accounting period and agrees to the Commissioner's prescribed terms, conditions, and adjustments for effecting the adoption, change, or retention. In determining whether a taxpayer has established a business purpose and which terms, conditions, and adjustments will be required, consideration will be given to all the facts and circumstances relating to the adoption, change, or retention, including the tax consequences resulting therefrom. Generally, the requirement of a business purpose will be satisfied, and adjustments to neutralize any tax consequences will not be required, if the requested annual accounting period coincides with the taxpayer's required taxable year (as defined in § 1.441–1(b)(2)), ownership taxable year, or natural business year. In the case of a partnership, S corporation, electing S corporation, or PSC, deferral of income to partners, shareholders, or employee-owners will not be treated as a business purpose.

(3) *Administrative procedures*. The Commissioner will prescribe administrative procedures under which a taxpayer may be permitted to adopt, change, or retain an annual accounting period. These administrative procedures will describe the business purpose requirements (including an ownership taxable year and a natural business year) and the terms, conditions, and adjustments necessary to obtain approval. Such terms, conditions, and adjustments may include adjustments necessary to neutralize the tax effects of a substantial distortion of income that would otherwise result from the requested annual accounting period including: a deferral of a substantial portion of the taxpayer's income, or shifting of a substantial portion of deductions, from one taxable year to another; a similar deferral or shifting in the case of any other person, such as a beneficiary in an estate; the creation of a short period in which there is a substantial net operating loss, capital loss, or credit (including a general business credit); or the creation of a short period in which there is a substantial amount of income to offset an expiring net operating loss, capital loss, or credit. See, for example, Rev. Proc. 2002–39, 2002–22 I.R.B. 1046, procedures for obtaining the Commissioner's prior approval of an adoption, change, or retention in annual accounting period through application to the national office; Rev. Proc. 2002–37, 2002–22 I.R.B. 1030, automatic approval procedures for certain corporations; Rev. Proc. 2002–38, 2002–22 I.R.B. 1037, automatic approval procedures for partnerships, S corporations, electing S corporations, and PSCs; and Rev. Proc. 66–50, 1966–2 C.B. 1260, automatic approval procedures for individuals. For availability of Revenue Procedures and Notices, see § 601.601(d)(2) of this chapter.

(4) *Taxpayers to whom Section 441(g) applies*. If section 441(g) and § 1.441–1(b)(1)(iv) apply to a taxpayer, the adoption of a fiscal year is treated as a change in the taxpayer's annual accounting period under Section 442. Therefore, that fiscal year can become the taxpayer's taxable year only with the approval of the Commissioner. In addition to any other terms and conditions that may apply to such a change, the taxpayer must establish and maintain books that adequately and clearly reflect income for the short period involved in the change and for the fiscal year proposed.

(c) *Special rule for change of annual accounting period by subsidiary corporation*. A subsidiary corporation that is required to change its annual accounting period under § 1.1502–76, relating to the taxable year of members of an affiliated group that file a consolidated return, does not need to obtain the approval of the Commissioner or file an application on Form 1128 with respect to that change.

(d) *Special rule for newly married couples*. (1) A newly married husband or wife may obtain automatic approval under this paragraph (d) to change his or her annual accounting period in order to use the annual accounting period of the other spouse so that a joint return may be filed for the first or second taxable year of that spouse ending after the date of marriage. Such automatic approval will be granted only if the newly married husband or wife adopting the annual accounting period of the other spouse files a Federal income tax return for the short period required by that change on or before the 15th day of the 4th month following the close of the short period. See Section 443 and the regulations thereunder. If the due date for any such short-period return occurs before the date of marriage, the first taxable year of the other spouse ending after the date of marriage cannot be

adopted under this paragraph (d). The short-period return must contain a statement at the top of page one of the return that it is filed under the authority of this paragraph (d). The newly married husband or wife need not file Form 1128 with respect to a change described in this paragraph (d). For a change of annual accounting period by a husband or wife that does not qualify under this paragraph (d), see paragraph (b) of this section.

(2) The provisions of this paragraph (d) may be illustrated by the following example:

Example. H & W marry on September 25, 2001. H is on a fiscal year ending June 30, and W is on a calendar year. H wishes to change to a calendar year in order to file joint returns with W. W's first taxable year after marriage ends on December 31, 2001. H may not change to a calendar year for 2001 since, under this paragraph (d), he would have had to file a return for the short period from July 1 to December 31, 2000, by April 16, 2001. Since the date of marriage occurred subsequent to this due date, the return could not be filed under this paragraph (d). Therefore, H cannot change to a calendar year for 2001. However, H may change to a calendar year for 2002 by filing a return under this paragraph (d) by April 15, 2002, for the short period from July 1 to December 31, 2001. If H files such a return, H and W may file a joint return for calendar year 2002 (which is W's second taxable year ending after the date of marriage).

(e) *Effective date*. The rules of this Section are applicable for taxable years ending on or after May 17, 2002.

§§ 1.442–2T and 1.442–3T [Removed]

Par. 6. Sections 1.442–2T and 1.442–3T are removed.

Par. 7. Section 1.706–1 is amended by revising paragraphs (a) and (b) and adding paragraph (d) to read as follows:

§ 1.706–1 Taxable years of partner and partnership.

(a) *Year in which partnership income is includible*. (1) In computing taxable income for a taxable year, a partner is required to include the Partner's distributive share of partnership items set forth in section 702 and the regulations thereunder for any partnership taxable year ending within or with the partner's taxable year. A partner must also include in taxable income for a taxable year guaranteed payments under Section 707(c) that are deductible by the partnership under its method of accounting in the partnership taxable year ending within or with the Partner's taxable year.

(2) The rules of this paragraph (a)(1) may beillustrated by the following example:

Example. Partner A reports income using a calendar year, while the partnership of which A is a member reports its income using a fiscal year ending May 31. The partnership reports its income and deductions under the cash method of accounting. During the partnership taxable year ending May 31, 2002, the Partnership makes guaranteed payments of $120,000 to A for services and for the use of capital. Of this amount, $70,000 was paid to A between June 1 and December 31, 2001, and the remaining $50,000 was paid to A between January 1 and May 31, 2002. The entire $120,000 paid to A is includible in A's taxable income for the calendar year 2002 (together with A's distributive share of partnership items set forth in section 702 for the partnership taxable year ending May 31, 2002).

(3) If a Partner receives distributions under section 731 or sells or exchanges all or part of a partnership interest, any gain or loss arising therefrom does not constitute partnership income.

(b) *Taxable year*—(1) *Partnership treated as a taxpayer*. The taxable year of a partnership must be determined as though the partnership were a taxpayer.

(2) *Partnership's taxable year*—(i) *Required taxable year*. Except as provided in paragraph (b)(2)(ii) of this section, the taxable year of a partnership must be—

(A) The majority interest taxable year, as defined in section 706(b)(4);

(B) If there is no majority interest taxable year, the taxable year of all of the principal partners of the partnership, as defined in 706(b)(3) (the principal partners' taxable year); or

(C) If there is no majority interest taxable year or principal partners' taxable year, the taxable year that produces the least aggregate deferral of income as determined under paragraph (b)(3) of this section.

(ii) *Exceptions*. A partnership may have a taxable year other than its required taxable year if it makes an election under section 444, elects to use a 52–53-week taxable year that ends with reference to its required taxable year or a taxable year elected under section 444, or establishes a business purpose for such taxable year and obtains approval of the Commissioner under section 442.

(3) *Least aggregate deferral*—(i) *Taxable year that results in the least aggregate deferral of income*. The taxable year that results in the least aggregate deferral of income will be the taxable year of one or more of the partners in the partnership which will result in the least aggregate deferral of income to the partners. The aggregate deferral for a particular year is equal to the sum of the products determined by multiplying the month(s) of deferral for each partner that would be generated by that year and each partner's interest in partnership profits for that year. The partner's taxable year that produces the lowest sum when compared to the other partner's taxable years is the taxable year that results in the least aggregate deferral of income to the partners. If the calculation results in more than one taxable year qualifying as the taxable year with the least aggregate deferral, the partnership may select any one of those taxable years as its taxable year. However, if one of the qualifying taxable years is also the partnership's existing taxable year, the partnership must maintain its existing taxable year. The determination of the taxable year that results in the least aggregate deferral of income generally must be made as of the beginning of the partnership's current taxable year. The director, however, may determine that the first day of the current taxable year is not the appropriate testing day and require the use of some other day or period that will more accurately reflect the ownership of the partnership and thereby the actual aggregate deferral to the partners where the partners engage in a transaction that has as its principal purpose the avoidance of the principles of this section. Thus, for example the preceding sentence would apply where there is a transfer of an interest in the partnership that results in a temporary transfer of that interest principally for purposes of qualifying for a specific taxable year under the principles of this section. For purposes of this section, deferral to each partner is measured in terms of months from the end of the partnership's taxable year forward to the end of the partner's taxable year.

(ii) *Determination of the taxable year of a partner or partnership that uses a 52–53-week taxable year*. For purposes of the calculation described in paragraph (b)(3)(i) of this section, the taxable year of a partner or partnership that uses a 52–53-week taxable year must be the same year determined under the rules of

section 441(f) and the regulations thereunder with respect to the inclusion of income by the partner or partnership.

(iii) *Special de minimis rule*. If the taxable year that results in the least aggregate deferral produces an aggregate deferral that is less than .5 when compared to the aggregate deferral of the current taxable year, the Partnership's current taxable year will be treated as the taxable year with the least aggregate deferral. Thus, the partnership will not be permitted to change its taxable year.

(iv) *Examples*. The principles of this section may be illustrated by the following examples:

Example 1. Partnership P is on a fiscal year ending June 30. Partner A reports income on the fiscal year ending June 30 and Partner B reports income on the fiscal year ending July 31. A and B each have a 50 percent interest in partnership profits. For its taxable year beginning July 1, 1987, the partnership will be required to retain its taxable year since the fiscal year ending June 30 results in the least aggregate deferral of income to the partners. This determination is made as follows:

Test 6/30	**Year End**	**Interest in Partnership Profits**	**Months of Deferral for 6/30 Year End**	**Interest x Deferral**
Partner A	6/30	.5	0	0
Partner B	7/31	.5	1	.5
Aggregate deferral				.5

Test 7/31	**Year End**	**Interest in Partnership Profits**	**Months of Deferral for 7/31 Year End**	**Interest x Deferral**
Partner A	6/30	.5	11	5.5
Partner B	7/31	.5	0	0
Aggregate deferral				5.5

Example 2. The facts are the same as in *Example 1* except that A reports income on the calendar year and B reports on the fiscal year ending November 30. For the partnership's taxable year beginning July 1, 1987, the partnership is required to change its taxable year to a fiscal year ending November 30 because such year results in the least aggregate deferral of income to the partners. This determination is made as follows:

Test 12/31	**Year End**	**Interest in Partnership Profits**	**Months of Deferral for 12/31 Year End**	**Interest x Deferral**
Partner A	12/31	.5	0	0
Partner B	11/30	.5	11	5.5
Aggregate deferral				5.5

Test 11/30	**Year End**	**Interest in Partnership Profits**	**Months of Deferral for 11/30 Year End**	**Interest x Deferral**
Partner A	12/31	.5	1	.5
Partner B	11/30	.5	0	0
Aggregate deferral				.5

Example 3. The facts are the same as in *Example 2* except that B reports income on the fiscal year ending June 30. For the partnership's taxable year beginning July 1, 1987, each partner's taxable year will result in identical aggregate deferral of income. If the partnership's current taxable year was neither a fiscal year ending June 30 nor the calendar year, the partnership would select either the fiscal year ending June 30 or the calendar year as its taxable year. However, since the partnership's current taxable year ends June 30, it must retain its current taxable year. The determination is made as follows:

Test 12/31	Year End	Interest in Partnership Profits	Months of Deferral for 12/31 Year End	Interest x Deferral
Partner A	12/31	.5	0	0
Partner B	6/30	.5	6	3.0
Aggregate deferral				3.0

Test 6/30	Year End	Interest in Partnership Profits	Months of Deferral for 6/30 Year End	Interest x Deferral
Partner A	12/31	.5	6	3.0
Partner B	6/30	.5	0	0
Aggregate deferral				3.0

Example 4. The facts are the same as in *Example 1* except that on December 31, 1987, partner A sells a 4 percent interest in the Partnership to Partner C, who reports income on the fiscal year ending June 30, and a 40 percent interest in the partnership to Partner D, who also reports income on the fiscal year ending June 30. The taxable year beginning July 1, 1987, is unaffected by the sale. However, for the taxable year beginning July 31, 1988, the partnership must determine the taxable year resulting in the least aggregate deferral as of July 1, 1988. In this case, the partnership will be required to retain its taxable year since the fiscal year ending June 30 continues to be the taxable year that results in the least aggregate deferral of income to the partners.

Example 5. The facts are the same as in *Example 4* except that Partner D reports income on the fiscal year ending April 30. As in *Example 4*, the taxable year during which the sale took place is unaffected by the shifts in interests. However, for its taxable year beginning July 1, 1988, the partnership will be required to change its taxable year to the fiscal year ending April 30. This determination is made as follows:

Test 7/31	Year End	Interest in Partnership Profits	Months of Deferral for 7/31 Year End	Interest x Deferral
Partner A	6/30	.06	11	.66
Partner B	7/31	.5	0	0
Partner C	6/30	.04	11	.44
Partner D	4/30	.4	9	3.60
Aggregate deferral				4.70

Test 6/30	Year End	Interest in Partnership Profits	Months of Deferral for 6/30 Year End	Interest x Deferral
Partner A	6/30	.06	0	0
Partner B	7/31	.5	1	.5
Partner C	6/30	.04	0	0
Partner D	4/30	.4	10	4.0
				4.5
Aggregate deferral				

Test 4/30	Year End	Interest in Partnership Profits	Months of Deferral for 4/30 Year End	Interest x Deferral
Partner A	6/30	.06	2	.12
Partner B	7/31	.5	3	1.50
Partner C	6/30	.04	2	.08
Partner D	4/30	.4	0	0
Aggregate deferral				1.70

§ 1.706–1(b)(3) Test:	
Current taxable year (June 30)	4.5
Less: Taxable year producing the least aggregate deferral (April 30)	1.7
Additional aggregate deferral (greater than .5)	2.8

Example 6. (i) Partnership P has two partners, A who reports income on the fiscal year ending March 31, and B who reports income on the fiscal year ending July 31. A and B share profits equally. P has determined its taxable year under paragraph (b)(3) of this section to be the fiscal year ending March 31 as follows:

Test 3/31	Year End	Interest in Partnership Profits	Months of Deferral for 3/31 Year End	Interest x Deferral
Partner A	3/31	.5	0	0
Partner B	7/31	.5	4	2
Aggregate deferral				2

Test 7/31	Year End	Interest in Partnership Profits	Deferral for 7/31 Year End	Interest x Deferral
Partner A	3/31	.5	8	4
Partner B	7/31	.5	0	0
Aggregate deferral				4

(ii) In May 1988, Partner A sells a 45 percent interest in the partnership to C, who reports income on the fiscal year ending April 30. For the taxable period beginning April 1, 1989, the fiscal year ending April 30 is the taxable year that produces the least aggregate deferral of income to the partners. However, under paragraph (b)(3)(iii) of this section the partnership is required to retain its fiscal year ending March 31. This determination is made as follows:

Test 3/31	Year End	Interest in Partnership Profits	Deferral for 3/31 Year End	Interest x Deferral
Partner A	3/31	.05	0	0
Partner B	7/31	.5	4	2.0
Partner C	4/30	.45	1	.45
Aggregate deferral				2.45

Test 7/31	Year End	Interest in Partnership Profits	Deferral for 7/31 Year End	Interest Deferral
Partner A	3/31	.05	8	.40
Partner B	7/31	.5	0	0
Partner C	4/30	.45	9	4.05
Aggregate deferral				4.45

Test 4/30	Year End	Interest in Partnership Profits	Deferral for 4/30 Year End	Interest Deferral
Partner A	3/31	.05	11	.55
Partner B	7/31	.5	3	1.50
Partner C	4/30	.45	0	0
Aggregate deferral				2.05

§ 1.706–1(b)(3) Test:	
Current taxable year (3/31)	2.45
Less: Taxable year producing the leastaggregate deferral (4/30).	2.05
	.40
Additional aggregate deferral (greater than .5)	

(4) *Measurement of partner's profits and capital interest*— (i) *In general*. The rules of this paragraph (b)(4) apply in determining the majority interest taxable year, the principal partners' taxable year, and the least aggregate deferral taxable year.

(ii) *Profits interest*—(A) *In general*. For purposes of section 706(b), a partner's interest in partnership profits is generally the partner's percentage share of partnership profits for the current partnership taxable year. If the partnership does not expect to have net income for the current partnership taxable year, then a partner's interest in partnership profits instead must be the partner's percentage share of partnership net income for the first taxable year in which the partnership expects to have net income.

(B) *Percentage share of partnership net income*. The partner's percentage share of partnership net income for a partnership taxable year is the ratio of: the partner's distributive share of partnership net income for the taxable year, to the partnership's net income for the year. If a partner's percentage share of partnership net income for the taxable year depends on the amount or nature of partnership income for that year (due to, for example, preferred returns or special allocations of specific partnership items), then the partnership must make a reasonable estimate of the amount and nature of its income for the taxable year. This estimate must be based on all facts and circumstances known to the partnership as of the first day of the current partnership taxable year. The partnership must then use this estimate in determining the partners' interests in partnership profits for the taxable year.

(C) *Distributive share*. For purposes of this paragraph (b)(4)(ii), a partner's distributive share of partnership net income is determined by taking into account all rules and regulations affecting that determination, including, without limitation, sections 704(b), (c), and (e), 736, and 743.

(iii) *Capital interest*. Generally, a partner's interest in partnership capital is determined by reference to the assets of the partnership that the partner would be entitled to upon withdrawal from the partnership or upon liquidation of the partnership. If the partnership maintains capital accounts in accordance with § 1.704–1(b)(2)(iv), then for purposes of section 706(b), the partnership may assume that a partner's interest in partnership capital is the ratio of the partner's capital account to all partners' capital accounts as of the first day of the partnership taxable year.

(5) *Certain tax-exempt partners disregarded*. [Reserved]

(6) *Foreign Partners*. [Reserved]

(7) *Adoption of taxable year*. A newly-formed partnership may adopt, in accordance with § 1.441–1(c), its required taxable year, a taxable year elected under section 444, or a 52–53-week taxable year ending with reference to its required taxable year or a taxable year elected under section 444 without securing the approval of the Commissioner. If a newly-formed partnership wants to adopt any other taxable year, it must establish a business purpose and secure the approval of the Commissioner under section 442.

(8) *Change in taxable year*—(i) *Partnerships—(A) Approval required*. An existing partnership may change its taxable year only by securing the approval of the Commissioner under section 442 or making an election under Section 444. However, a partnership may obtain automatic approval for certain changes, including a change to its required taxable

year, pursuant to administrative procedures published by the Commissioner.

(B) *Short period tax return*. A partnership that changes its taxable year must make its return for a short period in accordance with section 443, but must not annualize the partnership taxable income.

(C) *Change in required taxable year*. If a partnership is required to change to its majority interest taxable year, then no further change in the partnership's required taxable year is required for either of the two years following the year of the change. This limitation against a second change within a three-year period applies only if the first change was to the majority interest taxable year and does not apply following a change in the partnership's taxable year to the principal partners' taxable year or the least aggregate deferral taxable year.

(ii) *Partners*. Except as otherwise provided in the Internal Revenue Code or the regulations thereunder (*e.g.*, section 859 regarding real estate investment trusts or § 1.442–2(c) regarding a subsidiary changing to its consolidated parent's taxable year), a partner may not change its taxable year without securing the approval of the Commissioner under section 442. However, certain partners may be eligible to obtain automatic approval to change their taxable years pursuant to the regulations or administrative procedures published by the Commissioner. A partner that changes its taxable year must make its return for a short period in accordance with section 443.

(9) *Retention of taxable year*. In certain cases, a partnership will be required to change its taxable year unless it obtains the approval of the Commissioner under section 442, or makes an election under section 444, to retain its current taxable year. For example, a partnership using a taxable year that corresponds to its required taxable year must obtain the approval of the Commissioner to retain such taxable year if its required taxable year changes as a result of a change in ownership, unless the partnership previously obtained approval for its current taxable year or, if appropriate, makes an election under section 444.

(10) *Procedures for obtaining approval or making a section 444 election*. See § 1.442–1(b) for procedures to obtain the approval of the Commissioner (automatically or otherwise) to adopt, change, or retain a taxable year. See §§ 1.444–1T and 1.444–2T for qualifications, and § 1.444–3T for procedures, for making an election under section 444.

* * * * *

(d) *Effective date*. The rules of this section are applicable for taxable years ending on or after May 17, 2002, except for paragraph (c), which applies for taxable years beginning after December 31, 1953.

§ 1.706–1T [Removed]

Par. 8. Section 1.706–1T is removed.

Par. 9. Section 1.1378–1 is added under the undesignated centerheading "Small Business Corporations and Their Shareholders" to read as follows:

§ 1.1378–1 Taxable year of S corporation.

(a) *In general*. The taxable year of an S corporation must be a permitted year. A permitted year is the required taxable year (*i.e.*, a taxable year ending on December 31), a taxable year elected under section 444, a 52–53-week taxable year ending with reference to the required taxable year or a taxable year elected under section 444, or any other taxable year for which the corporation establishes a business purpose to the satisfaction of the Commissioner under section 442.

(b) *Adoption of taxable year*. An electing S corporation may adopt, in accordance with § 1.441–1(c), its required taxable year, a taxable year elected under section 444, or a 52–53-week taxable year ending with reference to its required taxable year or a taxable year elected under section 444 without the approval of the Commissioner. See § 1.441–1. An electing S corporation that wants to adopt any other taxable year, must establish a business purpose and obtain the approval of the Commissioner under section 442.

(c) *Change in taxable year*—(1) *Approval required*. An S corporation or electing S corporation that wants to change its taxable year must obtain the approval of the Commissioner under section 442 or make an election under section 444. However, an S corporation or electing S corporation may obtain automatic approval for certain changes, including a change to its required taxable year, pursuant to administrative procedures published by the Commissioner.

(2) *Short period tax return*. An S corporation or electing S corporation that changes its taxable year must make its return for a short period in accordance with section 443, but must not annualize the corporation's taxable income.

(d) *Retention of taxable year*. In certain cases, an S corporation or electing S corporation will be required to change its taxable year unless it obtains the approval of the Commissioner under section 442, or makes an election under Section 444, to retain its current taxable year. For example, a corporation using a June 30 fiscal year that elects to be an S corporation and, as a result, is required to use the calendar year must obtain the approval of the Commissioner to retain its current fiscal year.

(e) *Procedures for obtaining approval or making a section 444 election*—(1) *In general*. See § 1.442–1(b) for procedures to obtain the approval of the Commissioner (automatically or otherwise) to adopt, change, or retain a taxable year. See §§ 1.444–1T and 1.444–2T for qualifications, and 1.444–3T for procedures, for making an election under section 444.

(2) *Special rules for electing S corporations*. An electing S corporation that wants to adopt, change to, or retain a taxable year other than its required taxable year must request approval of the Commissioner on Form 2553, *Election by a Small Business Corporation*, when the election to be an S corporation is filed pursuant to section 1362(b) and § 1.1362–6. See § 1.1362–6(a)(2)(i) for the manner of making an election to be an S corporation. If such corporation receives permission to adopt, change to, or retain a taxable year other than its required taxable year, the election to be an S corporation will be effective. Denial of the request renders the election ineffective unless the corporation agrees that, in the event the request to adopt, change to, or retain a taxable year other than its required taxable year is denied, it will adopt, change to, or retain its required taxable year or, if applicable, make an election under section 444.

(f) *Effective date*. The rules of this Section are applicable for taxable years ending on or after May 17, 2002.

PART 5c—TEMPORARY INCOME TAX REGULATIONS UNDER THE ECONOMIC RECOVERY TAX ACT OF 1981

Par. 10. The authority citation for part 5c continues to read as follows:

Authority 26 U.S.C. 168(f)(8)(G) and 7805.

§ 5c.442–1 [Removed]

Par. 11. Section 5c.442–1 is removed.

PART 5f—TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982

Par. 12. The authority citation for part 5f continues to read in part as follows:

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

§ 5f.442–1 [Removed]

Par. 13. Section 5f.442–1 is removed.

PART 18—TEMPORARY INCOME TAX REGULATIONS UNDER THE SUBCHAPTER S REVISION ACT OF 1982

Par. 14. The authority citation for part 18 continues to read as follows:

Authority 26 U.S.C. 7805.

§ 18.1378–1T [Removed]

Par. 15. Section 18.1378–1 is removed.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 16. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 17. In § 602.101, paragraph (b) is amended by adding an entry for "1.441–2", removing the entries for "1.441–3T", "1.442–2T", and "1.442–3T", revising the entry for "1.442–1", and adding an entry for "1.1378–1" in numerical order to read as follows:

§ 602.101 OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
1.441–2	1545–1748
* * * * *	
1.442–1	1545–0074
	1545–0123
	1545–0134
	1545–0152
	1545–1748
* * * * *	
1.1378–1	1545–1748
* * * * *	

Robert E. Wenzel,
Deputy Commissioner of Internal Revenue.

Approved May 3, 2002.

Pamela F. Olson,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on May 16, 2002, 8:45 a.m., and published in the issue of the Federal Register for May 17, 2002, 67 F.R. 35009)

Section 442.—Change of Annual Accounting Period

26 CFR 1.442–1: Change of annual accounting period.

Final regulations relate to obtaining approval of the Commissioner to adopt, change, or retain an annual accounting period under section 442 of the Code. See T.D. 8996, page 1127.

Section 467.—Certain Payments for the Use of Property or Services

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

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

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

LIFO; price indexes; department stores. The April 2002 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 2002.

Rev. Rul. 2002–37

The following Department Store Inventory Price Indexes for April 2002 were issued by the Bureau of Labor Statistics. The indexes are accepted by the Internal Revenue Service, under § 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 86–46, 1986–2 C.B. 739, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, April 30, 2002.

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

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

Groups	Apr. 2001	Apr. 2002	Percent Change from Apr. 2001 to Apr. 2002[1]
1. Piece Goods	497.9	488.7	-1.8
2. Domestics and Draperies	606.5	597.7	-1.5
3. Women's and Children's Shoes	657.4	652.6	-0.7
4. Men's Shoes	895.3	902.7	0.8
5. Infants' Wear	626.8	622.2	-0.7
6. Women's Underwear	565.5	554.0	-2.0
7. Women's Hosiery	344.8	356.0	3.2
8. Women's and Girls' Accessories	557.3	565.6	1.5
9. Women's Outerwear and Girls' Wear	414.5	395.0	-4.7
10. Men's Clothing	591.8	600.2	1.4
11. Men's Furnishings	618.7	604.4	-2.3
12. Boys' Clothing and Furnishings	485.0	504.2	4.0
13. Jewelry	938.6	905.6	-3.5
14. Notions	793.4	794.8	0.2
15. Toilet Articles and Drugs	991.0	974.7	-1.6
16. Furniture and Bedding	650.3	627.7	-3.5
17. Floor Coverings	626.8	618.7	-1.3
18. Housewares	773.8	756.6	-2.2
19. Major Appliances	224.8	222.6	-1.0
20. Radio and Television	55.2	50.8	-8.0
21. Recreation and Education[2]	90.3	87.2	-3.4
22. Home Improvements[2]	127.0	125.8	-0.9
23. Auto Accessories[2]	109.0	110.8	1.7
Groups 1 — 15: Soft Goods	603.2	591.9	-1.9
Groups 16 — 20: Durable Goods	426.5	413.9	-3.0
Groups 21 — 23: Misc. Goods[2]	98.9	97.1	-1.8
Store Total[3]	537.5	526.3	-2.1

[1] Absence of a minus sign before the percentage change in this column signifies a price increase.
[2] Indexes on a January 1986=100 base.
[3] The store total index covers all departments, including some not listed separately, except for the following: candy, food, liquor, tobacco, and contract departments.

DRAFTING INFORMATION

The principal author of this revenue ruling is Michael Burkom of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue ruling, contact Mr. Burkom at (202) 622–7718 (not a toll-free call).

Section 482.—Allocation of Income and Deductions Among Taxpayers

Federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 483.—Interest on Certain Deferred Payments

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 642.—Special Rules for Credits and Deductions

Federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 706.—Taxable Years of Partner and Partnership

26 CFR 1.706–1: Taxable years of partner and partnership.

Final regulations relate to taxable years of partnerships under section 706 of the Code. See T.D. 8996, page 1127.

Section 807.—Rules for Certain Reserves

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 846.—Discounted Unpaid Losses Defined

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also sections 42, 280G, 382, 412, 467, 468, 482, 483, 642, 807, 846, 1288, 7520, 7872.)

Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate. For purposes of sections 382, 1274, 1288, and other sections of the Code, tables set forth the rates for June 2002.

Rev. Rul. 2002–36

This revenue ruling provides various prescribed rates for federal income tax purposes for June 2002 (the current month). Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section 1288(b). Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropriate percentages for determining the low-income housing credit described in section 42(b)(2) for buildings placed in service during the current month. Finally, Table 5 contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 2002–36 TABLE 1

Applicable Federal Rates (AFR) for June 2002

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	2.91%	2.89%	2.88%	2.87%
110% AFR	3.21%	3.18%	3.17%	3.16%
120% AFR	3.50%	3.47%	3.46%	3.45%
130% AFR	3.80%	3.76%	3.74%	3.73%
Mid-Term				
AFR	4.74%	4.69%	4.66%	4.64%
110% AFR	5.23%	5.16%	5.13%	5.11%
120% AFR	5.71%	5.63%	5.59%	5.57%
130% AFR	6.19%	6.10%	6.05%	6.02%
150% AFR	7.16%	7.04%	6.98%	6.94%
175% AFR	8.38%	8.21%	8.13%	8.07%

REV. RUL. 2002–36 TABLE 1—CONTINUED

Applicable Federal Rates (AFR) for June 2002

Period for Compounding

	Annual	*Semiannual*	*Quarterly*	*Monthly*
Long-Term				
AFR	5.70%	5.62%	5.58%	5.56%
110% AFR	6.28%	6.18%	6.13%	6.10%
120% AFR	6.85%	6.74%	6.68%	6.65%
130% AFR	7.44%	7.31%	7.24%	7.20%

REV. RUL. 2002–36 TABLE 2

Adjusted AFR for June 2002

Period for Compounding

	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-term adjusted AFR	2.45%	2.44%	2.43%	2.43%
Mid-term adjusted AFR	3.67%	3.64%	3.62%	3.61%
Long-term adjusted AFR	4.89%	4.83%	4.80%	4.78%

REV. RUL. 2002–36 TABLE 3

Rates Under Section 382 for June 2002

Adjusted federal long-term rate for the current month	4.89%
Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.)	5.01%

REV. RUL. 2002–36 TABLE 4

Appropriate Percentages Under Section 42(b)(2) for June 2002

Appropriate percentage for the 70% present value low-income housing credit	8.22%
Appropriate percentage for the 30% present value low-income housing credit	3.52%

REV. RUL. 2002–36 TABLE 5	
Rate Under Section 7520 for June 2002	
Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest	5.8%

Section 1288.—Treatment of Original Issue Discounts on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 1378.—Taxable Year of S Corporation

26 CFR 1.1378–1: Taxable year of S corporation.

Final regulations relate to taxable years of S corporations under section 1378 of the Code. See T.D. 8996, page 1127.

Section 4261.—Imposition of Tax

26 CFR 49.4261–1: Imposition of tax; in general. (Also §§ 4281.)

Segment Tax. This ruling provides guidance on how to calculate the tax on domestic segments under section 4261(b) of the Code if an aircraft is chartered and one or more persons are transported on that aircraft.

Rev. Rul. 2002–34

ISSUE

How is the tax on domestic segments under § 4261(b) of the Internal Revenue Code calculated if an aircraft is chartered and one or more persons are transported on that aircraft?

FACTS

X operates an air charter service that provides taxable air transportation. Each of *X*'s aircraft has a certificated takeoff weight in excess of 6,000 pounds. The amount *X* charges for the charter of an aircraft is not affected by the number of passengers transported on the aircraft. Passengers transported on the aircraft do not pay for the transportation.

LAW AND ANALYSIS

Section 4261(a) imposes a tax on the amount paid for taxable transportation (as defined in § 4262) of any person by air (the percentage tax) equal to 7.5 percent of the amount paid.

Section 4262(a)(1) provides that the term "taxable transportation" includes transportation by air which begins in the United States and ends in the United States.

Section 4261(b)(1), enacted by § 1031(c)(1) of the Taxpayer Relief Act of 1997, 1997–4 (Vol. 1) C.B. 1, 143, imposes a tax on the amount paid for each domestic segment of taxable transportation (the segment tax) equal to a fixed amount determined in accordance with the table contained in that section. For segments beginning in 2002, that amount is $3.00 per segment. The term "domestic segment" is defined in § 4261(b)(2) as any segment consisting of one takeoff and one landing that is taxable transportation described in § 4262(a)(1).

Section 4261(c) imposes a tax on any amount paid for any transportation of any person by air if the transportation begins or ends in the United States (the international facilities tax). Generally, the amount of the tax was set at $12.00 for amounts paid in 1997. Section 4261(e)(4) provides that the amount of the tax imposed by § 4261(c) is to be adjusted for inflation; generally, the amount of the tax for amounts paid in 2002 is $13.20.

Section 4281 provides an exemption from the tax imposed by § 4261 for aircraft having a certificated takeoff weight of 6,000 pounds or less, except when that aircraft is operated on an established line.

Rev. Rul. 72–309, 1972–1 C.B. 348, addresses the calculation of the international facilities tax imposed by § 4261(c) in the context of a single payment for a charter. The revenue ruling concludes that, if a single amount is paid for a charter, the § 4261(c) international facilities tax applies with respect to each passenger because implicit in the charter fee is an amount paid for the transportation of each passenger actually on the flight.

The § 4261(b) segment tax is similar to the § 4261(c) international facilities tax inasmuch as it is not calculated as a percentage of the amount paid, but is a fixed amount imposed on the amount paid for the transportation. Rev. Rul. 72–309 establishes that implicit in a charter payment is an amount paid for each passenger actually on the flight. Thus, as in the case of the § 4261(c) international facilities tax, the § 4261(b) segment tax is to be calculated on a per-passenger basis. Accordingly, for each segment, *X* must calculate the § 4261(b) segment tax by multiplying the amount of tax set forth in § 4261(b)(1) by the number of passengers transported on the chartered aircraft. (The segment tax so determined is not an amount paid for taxable transportation for purposes of calculating the § 4261(a) percentage tax.)

HOLDING

If an aircraft is chartered and one or more persons are transported on that aircraft, for each segment the tax under § 4261(b) is calculated by multiplying the amount of tax set forth in § 4261(b)(1) by the number of passengers transported on the aircraft.

DRAFTING INFORMATION

The principal author of this revenue ruling is Patrick S. Kirwan of the Office of Associate Chief Counsel (Passthroughs

and Special Industries). For further information regarding this revenue ruling, contact Mr. Kirwan at (202) 622–3130 (not a toll-free call).

Section 7520.—Valuation Tables

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Section 7872.—Treatment of Loans With Below-Market Interest Rates

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of June 2002. See Rev. Rul. 2002–36, page 1148.

Part III. Administrative, Procedural, and Miscellaneous

Additional Relief for Certain Taxpayers Affected by the September 11, 2001 Terrorist Attack

Notice 2002–40

PURPOSE

This notice supplements and expands the relief granted under section 7508A of the Internal Revenue Code (Code) in Notice 2001–61, 2001–40 I.R.B. 305, and Notice 2001–68, 2001–47 I.R.B. 504, for taxpayers affected by the September 11, 2001, Terrorist Attack. In Notice 2001–61 and Notice 2001–68, the Department of the Treasury and the IRS extended and postponed filing and payment due dates for affected taxpayers. At the time those notices were issued, the Code limited the amount of interest relief the IRS could provide to an affected taxpayer. Under section 6404(h), interest was abated only for income taxes due from an affected taxpayer located in the Presidentially declared disaster area and only if both an extension of time to file under section 6081 and an extension of time to pay under section 6161 were granted to the taxpayer. The Secretary's authority to provide relief under section 7508A was specifically limited to items other than interest. In addition, section 7508A permitted the Secretary to disregard no more than 120 days in the calculation of penalties.

On January 23, 2002, the President signed into law the Victims of Terrorism Tax Relief Act of 2001 (the Act). Section 112 of the Act repealed section 6404(h) and amended section 7508A (effective September 11, 2001), by providing, in part, that the Secretary may disregard up to one year in determining the amount of any interest or penalty. Under this increased authority, the Department of the Treasury and the IRS are providing relief from interest and expanded relief from the failure to pay penalty for certain affected taxpayers.

GRANT OF RELIEF

(1) For affected taxpayers with an original income tax return due date on or after September 11, 2001, and on or before November 30, 2001, that were previously granted a six-month extension of time to file and pay and a 120 day postponement of time to file and pay by paragraphs (1) and (2) of the Grant of Relief Section of Notice 2001–61, and for certain taxpayers who had difficulty in filing their federal income tax returns due on or after September 11, 2001, and on or before October 31, 2001, because of disruptions in the transportation and delivery of documents by mail or private delivery services resulting from the terrorist attack, that were previously granted a postponement of time to file and pay until November 15, 2001, by paragraph (5) of the Grant of Relief Section of Notice 2001–61, interest will not be due for the period of time that the payment is extended and postponed. For example, an affected fiscal year taxpayer with an original due date of September 17, 2001, has until July 15, 2002, to file and pay as a result of the relief granted by Notice 2001–61. Under this notice, no interest will accrue from September 17, 2001, through July 15, 2002. Additionally, no failure to file or pay penalty will accrue from September 17, 2001, through July 15, 2002. This relief applies to all affected taxpayers (as defined in Notice 2001–61 and Announcement 2001–124 2001–52 I.R.B. 630) no matter where they are located.

(2) For affected taxpayers with an extended income tax return due date on or after September 11, 2001, and on or before November 30, 2001, that were previously granted a 120 day postponement of time to file by Notice 2001–61, and for taxpayers with an extended due date on or after December 1, 2001, and on or before January 31, 2002, that were previously granted a postponement of time to file until February 15, 2002, by paragraph (1) of the Additional Grant of Relief section of Notice 2001–68, interest will not be due for the period beginning September 11, 2001, and ending with the postponed due date of the return. In addition, the relief from the failure to pay penalty provided by Notice 2001–61 for the period September 11, 2001, through January 9, 2002 (120 days) is expanded to cover the period beginning September 11, 2001, and ending with the postponed due date of the return. For example, an individual income taxpayer with an extended due date of October 15, 2001, has a postponed filing due date of February 12, 2002, as a result of the relief granted by Notice 2001–61. Under this notice, no interest or failure to pay penalty will accrue from September 11, 2001, through February 12, 2002, on any balance originally due on April 16, 2001. Interest and the failure to pay penalty will be owed on any balance due for the period April 16, 2001, through September 10, 2001, and on any balance remaining due after February 12, 2002.

(3) Under paragraph (6) of the Grant of Relief section of Notice 2001–61, certain taxpayers were granted a reasonable cause waiver from the failure to deposit penalty if third quarter tax deposits due from September 11, 2001, through September 30, 2001, were deposited by November 15, 2001. For these taxpayers, the third quarter return and payment were generally due on October 31, 2001. In the absence of relief under section 7508A (as amended), interest would be imposed for the period from November 1, 2001, through November 15, 2001, on any balance due on October 31, 2001. Under this notice, taxpayers will not owe interest for this period on any employment and excise tax liability for which the failure to deposit penalty has been waived.

(4) The IRS may have already assessed interest and penalties relieved under this notice and taxpayers may have already paid these amounts. The IRS has identified taxpayers located in the covered disaster area specified in Notice 2001–61 who are eligible for the additional relief and have adjusted those accounts accordingly. If you were located in the covered disaster area and are entitled to receive a refund, you should receive a notice by May 28, 2002. Taxpayers not located in the covered disaster area who are entitled to this additional relief (or anyone else with any questions regarding the status of an adjustment or

refund because of this notice), should contact the IRS at (866) 562–5227 (a toll-free call).

DRAFTING INFORMATION

This notice was authored by the Office of Associate Chief Counsel, Procedure and Administration (Administrative Provisions and Judicial Practice Division). For further information regarding this notice, you may call (202) 622–4940 (not a toll-free call).

Application Procedures for Withholding Foreign Partnership or Withholding Foreign Trust Status Under Section 1441; Proposed Withholding Foreign Partnership and Withholding Foreign Trust Agreements

Notice 2002–41

SECTION 1. PURPOSE

.01 *Proposed Guidance to Simplify Partnership and Trust Withholding and Reporting Obligations*. This notice contains proposed guidance for entering into a withholding foreign partnership (WP) or withholding foreign trust (WT) agreement with the Internal Revenue Service (IRS). Similar to the qualified intermediary (QI) withholding agreement,[1] the proposed WP and WT agreements are designed to simplify withholding and reporting obligations for payments of income made to partners of a WP and beneficiaries or owners of a WT. The IRS recognizes that foreign partnerships and trusts differ significantly from each other, as well as from foreign financial institutions that receive amounts subject to withholding as intermediaries for account holders. These proposed agreements attempt to address the unique features of partnerships and trusts by adopting tailored procedures for documentation, reporting and audit that facilitate compliance and reduce administrative and audit cost for the WP or WT. As discussed further in Section 7 of this notice, Treasury and the IRS request comments on these proposed agreements. Treasury and the IRS will review any comments received and intend thereafter to publish a revenue procedure containing the final text of the WP and WT agreements.

Under applicable Treasury regulations, a foreign partnership or foreign simple or grantor trust that is not a WP or WT is required to provide each withholding agent from whom it receives an amount subject to withholding under sections 1441 and 1442 of the Internal Revenue Code (Code) and the regulations thereunder with a Form W-8IMY, along with documentation from each of its partners, beneficiaries, or owners, and a withholding statement allocating the amount attributable to each partner, beneficiary, or owner. The withholding agent is required to withhold tax from payments to the partnership or trust and to report on Forms 1042-S and 1099 payments to, and tax withheld from, each partner, beneficiary, or owner.

Under the provisions of the WP and WT agreements, a WP or WT is permitted to provide the withholding agent with a Form W-8IMY as a WP or WT without attached documentation from partners, beneficiaries, or owners. The WP or WT receives payments from the withholding agent in gross and withholds and deposits tax, if any, based on the Forms W-8 or W-9 that it receives from its partners, beneficiaries, or owners. The WP or WT reports payments to, and tax withheld from, its direct foreign partners, beneficiaries or owners on Form 1042-S on an individual basis or, by election, on a pooled basis. Thus, a WP or WT is relieved of the requirement to disclose to a withholding agent any documentation and payment information for partners, beneficiaries or owners. A withholding agent is relieved of the responsibility for collecting documentation, withholding and reporting payment information for partners, beneficiaries and owners of a WP or WT.

.02 *Key Provisions*. The following key provisions, explained in greater detail in Section 4.02, are intended to work together to produce a simple and administrable agreement for withholding foreign partnerships and trusts.

Direct partners, beneficiaries or owners. A foreign partnership or simple or grantor trust that has entered into a WP or WT agreement may act as a WP or WT only with respect to amounts subject to NRA withholding that are distributed to, or included in the distributive share of, direct partners, beneficiaries, or owners. WP or WT must act as a nonwithholding foreign partnership or trust with respect to partners, beneficiaries, or owners that hold through intermediaries or passthrough entities. The foreign partnership or foreign simple or grantor trust may, however, act as a WP or WT with respect to amounts distributed to, or included in the distributive share of, another WP or WT.

Forms W-8 and W-9. WP or WT is required to document each direct partner, beneficiary or owner with Form W-8 or W-9.

Withholding and reporting—direct foreign partners, beneficiaries or owners. WP or WT is required to withhold and deposit tax, to file a tax return on Form 1042, and, absent a pooled reporting election, to report on Form 1042-S for each direct foreign partner, beneficiary or owner.

Reporting—pooled reporting election. WP or WT may elect to report on Form 1042-S on a pooled basis (using the recipient codes for QI pooling until such time that there are recipient codes for WPs and WTs that make an election to report on a pooled basis). Whether WP or WT elects pooled reporting will affect both the timing of audits and the term of the agreement.

Reporting—direct U.S. partners, beneficiaries or owners. WP or WT is not required to report on Form 1099 for U.S. partners, beneficiaries, or owners. However, if WP has U.S. partners, WP generally is required to file Form 1065 with Schedules K-1 for each U.S. partner. If WT is a grantor trust with U.S. owners, WT is required to file Form 3520-A and

[1] See Rev. Proc. 2000–12, 2000–1 C.B. 387.

to provide statements to each U.S. beneficiary or owner. If WT makes a distribution to a U.S. person, WT must provide an information statement to that U.S. person pursuant to section 6048(c) of the Code.

Audit. Unless WP or WT has elected to report on Form 1042-S on a pooled basis, it will be subject to audit only if selected for audit by the IRS. In that case, WP or WT will be subject to audit by an external auditor unless WP or WT requests an IRS audit. If WP or WT elects pooled reporting it must agree to have the external auditor conduct an audit after the close of every other calendar year, which will examine the two previous calendar years.

Term of the agreement. The WP or WT agreement will continue in force indefinitely unless WP or WT has elected to report on Form 1042-S on a pooled basis. In that case, the agreement will expire after a term of six years.

Automatic termination. If WP or WT fails to document any partner, beneficiary or owner with Form W-8 or W-9 by the time withholding is required under the agreement, then, unless WP or WT cures its failure, the agreement will automatically terminate effective December 31st of the year in which the failure is discovered.

SECTION 2. SCOPE

.01 *Foreign Partnerships and Foreign Simple and Grantor Trusts*. This Notice applies to a foreign partnership seeking to qualify as a withholding foreign partnership under Treas. Reg. §1.1441–5(c)(2)(ii).[2] The proposed withholding foreign partnership agreement applies to amounts subject to NRA withholding that the partnership distributes to, or includes in the distributive shares of, its direct partners.

This Notice also applies to a foreign trust seeking to qualify as a withholding foreign trust under Treas. Reg. §1.1441–5(e)(5)(v). The proposed withholding foreign trust agreement applies to amounts subject to NRA withholding that are required to be distributed to the beneficiaries of a simple trust or that are includable in the income of the owners of a grantor trust ("distributive shares" of beneficiaries or owners).

The IRS intends that the WP and WT agreements will be available in all circumstances in which a foreign entity acting on behalf of its partners, beneficiaries or owners provides Form W-8IMY as proper documentation. For example, a WP or WT agreement would be available for an entity that is properly claiming treaty benefits for its owners under section 894 of the Code (notwithstanding that the entity may be treated as a corporation for U.S. tax purposes).

This Notice does not apply to intermediaries seeking to become QIs. Instead, see Rev. Proc. 2000–12, 2000–1 C.B. 387. The QI agreement applies to amounts subject to NRA withholding that are collected by an intermediary and paid to its account holders.

The QI agreement is not available to foreign partnerships or foreign trusts. As outlined below, the relationship of an intermediary and its account holders addressed in the QI agreement differs fundamentally from the relationship of a partnership and its partners and the relationship of a trust and its beneficiaries or owners.

.02 *Notice 2001–4*. Pending the development of these agreements, Notice 2001–4, 2001–1 C.B. 267, provided a transition rule for foreign partnerships for calendar year 2001. Under the transition rule, for calendar year 2001, partnerships were permitted to provide to withholding agents Form W-8IMY with partner documentation attached together with a withholding statement that furnished payment information on the basis of withholding rate pools. Because that relief is unavailable for payments after December 31, 2001, the IRS intends that subscribing partnerships will apply the WP agreement for calendar years after 2001.

Notice 2001–4 also permitted a QI to treat the beneficiaries of a foreign simple trust or the owners of a foreign grantor trust as direct account holders for purposes of the QI agreement if certain criteria were met. This rule will continue in effect after the WT agreement becomes available. Alternatively, foreign simple and grantor trusts, including those that meet the criteria set forth in Notice 2001–4, may choose to enter a WT agreement when the WT agreement is finalized.

SECTION 3. BACKGROUND

.01 *Withholding and Reporting on Payments to Foreign Persons*. Under sections 1441 and 1442 of the Internal Revenue Code (Code), a person that makes a payment of U.S. source interest, dividends, royalties, and certain other types of income to a foreign person generally must deduct and withhold 30 percent from the payment. A lower rate of withholding may apply under the Code (*e.g.*, section 1443), the regulations, or an income tax treaty. Generally, a payor of these types of income also must report the payments on Forms 1042-S. See Treas. Reg. § 1.1461–1(c).

Under sections 6041, 6042, 6045, 6049, and 6050N of the Code (the Form 1099 reporting provisions), payors of interest, dividends, royalties, gross proceeds from the sale of securities, and other fixed or determinable income must report payments on Form 1099 unless an exception applies. If a payment is reportable on Form 1099, a payor must generally obtain a Form W-9 from the payee. If the payor does not receive the Form W-9, it generally must backup withhold under section 3406 of the Code and report the payment on Form 1099.

An exception to the Form 1099 reporting provisions applies if the payee is a foreign person. A payor can treat a person as foreign if the payor can reliably associate the payment with a Form W-8 or other documentation that establishes that the person is the foreign beneficial owner of the income or a foreign payee. See Treas. Reg. §§ 1.1441–1, 1.6041–4(a),1.6042–3(b)(1)(iii), 1.6045–1(g)(1)(i), 1.6049–5(b)(12), and 1.6050N–1(c)(1)(i). Moreover, a payor does not backup withhold on payments to foreign beneficial owners or foreign payees because backup withholding applies only to amounts that the payor must report on Form 1099.

[2]All citations to income tax regulations in this revenue procedure are to the regulations as amended by T.D. 8734, 1997–2 C.B. 109 [62 FR 53387], T.D. 8804, 1999–1 C.B. 793 [63 FR 72183], and T.D. 8856, 2000–1 C.B. 298 [64 FR 73408].

In general, the beneficial owners or payees of a payment to a person that is treated as a nonwithholding foreign partnership are the partners (looking through partners that are foreign intermediaries or flow-through entities). However, a payment to a withholding foreign partnership is treated as a payment to the partnership and not to the partners. See Treas. Reg. § 1.1441–5(c). Similarly, the beneficial owners of a payment to a nonwithholding foreign simple or grantor trust are the beneficiaries or owners of the trust (looking through beneficiaries or owners that are foreign intermediaries or flow-through entities). However, a payment to a withholding foreign trust is treated as a payment to the trust and not to its beneficiaries or owners. See Treas. Reg. § 1.1441–5(e).

A nonwithholding foreign partnership or nonwithholding foreign simple or grantor trust must forward documentation for each of its partners, beneficiaries or owners to each withholding agent making a payment to the partnership or trust so that the withholding agent can correctly withhold and report on Forms 1042-S and 1099, as appropriate. If a withholding agent does not receive that documentation, the withholding agent generally will withhold and report based on presumptions provided in the regulations. See Treas. Reg. §§ 1.1441–1, 1.1441–5 and 1.6049–5.

A foreign partnership or foreign trust is a withholding agent under sections 1441 and 1442 of the Code for amounts subject to withholding that it pays to foreign persons, including partners, beneficiaries and owners, and therefore must file Forms 1042 and 1042-S in the same manner as a U.S. withholding agent. However, a foreign partnership or foreign trust is not required to file Forms 1042 and 1042-S if another withholding agent has reported the same amount to the same recipient for which the foreign partnership or foreign trust would be required to file a return and the proper amount has been withheld. See Treas. Reg. § 1.1461–1(b) and (c)(4).

Under section 6031 of the Code, a foreign partnership that has gross income that is effectively connected with the conduct of a trade or business within the United States (ECI) is required to file a partnership return on Form 1065 with Schedules K-1 (*Statement of Partner's Share of Income, Credit, Deduction, Etc.*) for each partner. Also, a foreign partnership that has U.S. source gross income that is not ECI and that has U.S. partners is generally required to file Form 1065 and Schedules K-1 for each of its direct U.S. partners and for its passthrough partners through which U.S. partners hold an interest in the foreign partnership. See Treas. Reg. § 1.6031(a)–1(b). A foreign trust generally is not engaged in any trade or business. However, if it has gross income that is treated as effectively connected with the conduct of a U.S. trade or business, it must file a return on Form 1040NR. Under section 6048(b), a foreign trust that has a U.S. owner must file Form 3520-A, *Annual Information Return of a Foreign Trust with a U.S. Owner*. Under section 6048(c), a U.S. person that receives a distribution from a foreign trust must file Form 3520. The trust must provide an information statement to the U.S. distributee. See Form 3520, *Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*.

SECTION 4. OVERVIEW OF PROPOSED AGREEMENTS

.01 *Comparison with QI Agreement*. The IRS recognizes that foreign partnerships and foreign simple and grantor trusts differ significantly from each other as well as from foreign financial institutions that act as intermediaries for their account holders. For instance, foreign partnerships and trusts generally (1) have unique governing provisions and allocations, (2) are not subject to any extensive government regulation and oversight (including know-your-customer laws), and (3) do not have staffing and systems comparable to financial institutions that are intermediaries. Thus, certain provisions in the QI agreement become problematic in the context of foreign partnerships and trusts, such as: the treatment of indirect account holders, collection and examination of documentary evidence, application of the presumption rules, and Form 1099 reporting. In addition, such entities often have special allocations that generally are not an issue with account holders of financial institutions.

.02 *Simplified Requirements and Procedures*. The proposed agreements attempt to minimize the difficulties unique to partnerships and trusts by adopting procedures that reduce the administrative and audit cost for the WP and WT, as well as the risk of error in performing under the agreements.

(i) *Limitation to direct partners, beneficiaries, or owners*. The WP and WT agreements apply only to payments from a WP or WT to its direct partners, beneficiaries, or owners. This limitation eliminates the need (1) for the WP or WT to apply the presumption rules on payments it makes to indirect partners, beneficiaries, or owners who failed to provide adequate documentation; (2) for the WP or WT to gather and review documentation and withholding information for indirect partners, beneficiaries, and owners; and (3) for the WP or WT to bear the expense of having an auditor review such documentation and withholding information for indirect partners. The presumption rules generally require a withholding agent to withhold at the highest rate, which often requires subsequent reimbursements or refunds, and also results in duplicative reporting. A WP or WT, nevertheless, may act as a WP or WT for payments it makes to a partner, beneficiary, or owner that is, itself, a WP or WT because, for payments to such entities, it is never necessary to apply the presumption rules, or review documentation for the partners, beneficiaries, or owners of such entities. Because the IRS and Treasury expect that many foreign partnerships and trusts will enter into WP and WT agreements with the IRS, it is expected that the number of WPs and WTs that have partners, beneficiaries, or owners that are nonwithholding foreign partnerships and nonwithholding foreign trusts will be relatively small.

(ii) *Documentation*. The agreements require a WT and WP to obtain Forms W-8 and W-9 from its direct partners, beneficiaries, or owners. Obtaining documentary evidence in lieu of Forms W-8 and W-9 is not permitted. Although this requirement is imposed primarily for simplicity, it is also necessary because a WP or WT generally is not subject to the know-your-customer (KYC) rules in its jurisdiction. Therefore, the IRS is unable

to rely on the regulators in that jurisdiction to ensure that a WP or WT is properly documenting its partners, beneficiaries, or owners. The IRS believes that this requirement should not unduly burden a WP or WT because, unlike a QI, which may have had large percentages of its account base already documented with KYC-type documentation for other regulatory purposes, a WP or WT generally will not.

(iii) *Automatic termination*. The agreements provide that, if on audit the IRS or external auditor discovers that the WP or WT was not in possession of a valid Form W-8 or W-9, as applicable, for any direct partner, beneficiary, or owner, the agreement will automatically terminate unless cured. This provision operates in conjunction with the documentation provisions described above to eliminate completely the application of the presumption rules by WP or WT. The extended date for withholding on undistributed income under the WP or WT agreements, as noted below, provides the WP or WT with more time to obtain documentation. Thus, it is expected that WP or WT will have ample time to comply with the documentation requirements to avoid automatic termination.

(iv) *Withholding*. Because information regarding special allocations among partners, beneficiaries, or owners often is unavailable at the time withholding is required, a WP or WT may find it difficult to determine the correct amount of withholding at the time a payment is received by WP or WT. To address this concern, the agreements provide that, where an actual distribution has not been made, a WP or WT is not required to withhold until the earlier of the date that the statements required under section 6031 (for partnerships) or section 6048 (for simple and grantor trusts) are mailed or otherwise provided to the partner, beneficiary or owner, or the due date for furnishing such statements (whether or not WP or WT is required to prepare and furnish such statements). With this delay in the time for withholding on undistributed income, the foreign partnership or trust who enters into the WP or WT agreement should be able to withhold accurately, thereby avoiding the need to correct withholding errors. This provision also will ease the audit burden by eliminating the need for the auditor to review numerous setoffs or reimbursements.

(v) *Pooled reporting*. Under the regulations, a foreign partnership or trust is required to provide the U.S. withholding agent with sufficient information so that it can properly report on Form 1042-S for each foreign partner, beneficiary, or owner. Under the agreements, the WP or WT assumes the Form 1042-S reporting requirement for each direct foreign partner, beneficiary, or owner. The IRS understands, however, that reporting on a beneficial owner basis is a concern for some foreign partnerships and trusts. To accommodate this concern, the agreements allow a WP or WT to elect pooled-basis reporting for those amounts distributed to, or includible in the income of, its direct foreign partners, beneficiaries, or owners. If a WP or WT makes the pooled reporting election, the term of the agreement will be limited and the WP or WT will be subject to external audit every other year.

(vi) *Elimination of Form 1099 reporting*. To avoid duplication of reporting to a WP's or WT's direct U.S. partners, beneficiaries, or owners, (*e.g.*, a Form 1099 and K-1 issued to the same U.S. partner of a foreign partnership for the same income), the agreements eliminate the requirement that a WP or WT file Form(s) 1099 for its direct U.S. partners, beneficiaries, or owners. The WP or WT must file the necessary forms, schedules, and statements required by sections 6031 and 6048, as applicable.

(vii) *Amendment and Termination of Agreement*. The agreements may be amended by the IRS if the IRS determines that such amendment is needed for the sound administration of the applicable laws or regulations. For example, the IRS may amend the agreement as needed to address changes in law or administrative practice. The agreement also may be modified by mutual agreement of the parties. Either party can terminate the agreement prior to the end of its term by delivering a notice of termination. However, the IRS will terminate the agreement only in certain specified circumstances involving a "significant change in circumstances" or an "event of default" (as defined in the agreement).

SECTION 5. APPLICATION FOR WP or WT STATUS

.01 *Where to Apply*. To apply for WP or WT status, a foreign partnership or trust must submit the information required by this Section 5 to:

Internal Revenue Service
LMSB:FS:QI
290 Broadway
New York, NY 10007–1867
USA

.02 *Contents of the Application*. A prospective WP or WT must submit an application to become a WP or WT. An application must include the information specified in this section 5.02, and any additional information and documentation requested by the IRS:

(1) A statement identifying what type of entity the applicant is (*i.e.*, a foreign partnership or a foreign simple or grantor trust) and that it requests to enter into a WP or WT agreement with the IRS.

(2) The applicant's name, address, and employer identification number(s) (EIN), if any.

(3) The country in which the applicant was created or organized and a description of the applicant's business.

(4) A list of the titles of those persons who will be the responsible parties for performance under the Agreement and the names, addresses, and telephone numbers of those persons as of the date the application is submitted.

(5) A list describing, as of the date the application is submitted, the type of partners, beneficiaries or owners (*e.g.*, U.S., foreign, treaty benefit claimant, or intermediary or flow-through), the number (and percentage interest in partnership capital, partnership profits, and partnership losses (noting any special allocations or similar provisions)) of partners, beneficiaries or owners within each type, and the estimated value of U.S. investments that the WP or WT agreement will cover.

(6) A general description, as of the date the application is submitted, of U.S. assets by type (*e.g.*, U.S. securities, U.S. real estate), including assets held by U.S. custodians, and their approximate aggregate value by type.

(7) A completed Form SS-4 (*Application for Employer Identification Number*)

to apply for a withholding foreign partnership or trust Employer Identification Number (WP-EIN, WT-EIN) to be used solely for WP or WT reporting and filing purposes. An applicant must apply for a WP-EIN or WT-EIN even if it already has another EIN. The WP-EIN or WT-EIN will be in addition to any EIN the WP or WT already has, which should be retained.

(8) A completed WP or WT agreement, as set forth in Appendix 1 or 2, executed as provided in section 6.

SECTION 6. EXECUTING THE WP OR WT AGREEMENT

The text of the WP agreement is set forth in Appendix 1. The text of the WT agreement is set forth in Appendix 2. Upon receipt and review of an application to become a WP or WT, the IRS will complete the agreement based on the information provided by WP or WT (*e.g.*, insertion of the WP's name, etc.). Therefore, a prospective WP or WT should ensure that it has provided to the IRS all of the information that is required to complete the agreement. It may be necessary for the IRS to contact the potential WP or WT, or its authorized representative, to obtain additional information. Once the IRS has obtained all the information required to complete the agreement, the IRS will send two unsigned copies of the agreement to the prospective WP or WT for signature. Both copies of the agreement should be signed by a person with the authority to sign the agreement and should be returned to the IRS at the address specified in section 5.01. The IRS will sign the agreement and return one of the originals to the WP or WT.

SECTION 7. REQUEST FOR COMMENTS

Treasury and the IRS request comments on the proposed withholding foreign partnership and withholding foreign trust agreements attached as appendices to this notice. After consideration of any comments received, Treasury and the IRS intend to publish a revenue procedure containing the final text of these agreements. In addition, the IRS may consider adapting the proposed withholding foreign partnership and withholding foreign trust agreements to the unique circumstances of certain classes of foreign partnerships and trusts. For instance, the IRS may consider incorporating documentation provisions similar to the provisions in the QI agreement in the case of certain foreign partnerships and trusts that are required by law in the jurisdiction of organization to comply with know-your-customer rules for obtaining documentation confirming the identity of partners, beneficiaries, or owners (or the interests in which are generally held through institutions that are subject to know-your-customer rules); and

(i) the offer and sale of interests in which are subject to securities regulation in that jurisdiction; or

(ii) the interests in which are publicly traded on an established securities exchange or continuously offered and sold to the general public (and the partnership is not classified as a corporation pursuant to section 7704).

In addition, the IRS understands that certain small partnerships or small family trusts may find the WP or WT agreement to be a desirable alternative to acting as a nonwithholding partnership or trust but may nevertheless require adaptations to the agreements as drafted.

The IRS specifically requests comments identifying such classes of foreign partnerships or trusts, suggesting possible adaptations of the agreements for such cases and analyzing the feasibility of any such suggestions.

Written comments must be received by July 22, 2002. Send comments to CC:DOM:CORP:R (NOT–151112–01), Room 5228, Internal Revenue Service, Ben Franklin Station, Washington, DC 20224. Alternatively, comments may be hand delivered between the hours of 8:00 AM and 5:00 PM to: CC:DOM:CORP:R (NOT–151112–01), Courier's Desk, Internal Revenue Service, 1111 Constititution Ave. NW, Washington, DC.

SECTION 8. CONTACT INFORMATION

For further information regarding this Notice, contact Carl Cooper or Laurie Hatten-Boyd of the Office of the Associate Chief Counsel (International), Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Mr. Cooper and Ms. Hatten-Boyd may be contacted by telephone at 202–622–3840 (not a toll-free call).

APPENDIX 1

Withholding Foreign Partnership Agreement

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SECTION 10. MISCELLANEOUS PROVISIONS

THIS AGREEMENT is made in duplicate under and in pursuance of section 1441 of the Internal Revenue Code of 1986, as amended, (the "Code") and Treasury Regulation § 1.1441–5(c)(2) by and between ______________, (referred to as "WP"), and the INTERNAL REVENUE SERVICE (the "IRS"):

WHEREAS, WP has submitted an application in accordance with **Revenue Procedure 2002–xx** to be a withholding foreign partnership for purposes of Treas. Reg. § 1.1445–5(c)(2);

WHEREAS, WP and the IRS desire to enter into an agreement to establish WP's rights and obligations regarding documentation, withholding, information reporting, tax return filing, deposits, and adjustment procedures under sections 1441, 1442, 1443, 1461, 6031, 6302, 6402, and 6414 of the Code with respect to certain types of payments;

NOW, THEREFORE, in consideration of the following terms, representations, and conditions, the parties agree as follows:

SECTION 1. PURPOSE AND SCOPE

Sec. 1.01. General Obligations. Except as otherwise provided in this Agreement, WP's obligations with respect to income distributed to, or included in the distributive shares of, its partners are governed by the Code and the regulations thereunder. WP may act in its capacity as a withholding foreign partnership pursuant to this Agreement only for payments of amounts subject to NRA withholding that are distributed to, or included in the distributive shares of, its direct partners. WP is required to act as a withholding foreign partnership for all such amounts paid to WP, or included in WP's distributive share, by any withholding agent to which WP has provided a Form W-8IMY that represents that WP is acting as a withholding foreign partnership with respect to such amounts. WP must act as a withholding foreign partnership for any such amounts paid with respect to such a Form W-8IMY that are distributed to, or included in the distributive shares of, its direct foreign partners. WP may also act as a withholding foreign partnership for such amounts that are distributed to, or included in the distributive shares of, its direct partners that are U.S. persons. In no event may WP act as a withholding foreign partnership for amounts subject to NRA withholding that are distributed to, or included in the distributive shares of, passthrough partners or indirect partners. For passthrough partners and indirect partners, WP must act as a nonwithholding foreign partnership.

Sec. 1.02. Parties to the Agreement. This Agreement applies to WP and the IRS.

SECTION 2. DEFINITIONS

For purposes of this Agreement, the terms listed below are defined as follows:

Sec. 2.01. Agreement. "Agreement" means this Agreement between WP and the IRS. All appendices to this Agreement and WP's application to become a withholding foreign partnership are incorporated into this Agreement by reference.

Sec. 2.02. Amounts Subject to NRA Withholding. An "amount subject to NRA withholding" is an amount described in Treas. Reg. § 1.1441–2(a). An amount subject to NRA withholding shall not include interest paid as part of

the purchase price of an obligation sold between interest payment dates or original issue discount paid as part of the purchase price of an obligation sold in a transaction other than the redemption of such obligation, unless the sale is part of a plan the principal purpose of which is to avoid tax and WP has actual knowledge or reason to know of such plan.

Sec. 2.03. Chapter 3 of the Code. Any reference to "chapter 3 of the Code" means sections 1441, 1442, 1443, 1461, 1463, and 1464 of the Code.

Sec. 2.04. Chapter 61 of the Code. Any reference to "chapter 61 of the Code" means sections 6031, 6041, 6042, 6045, 6049, and 6050N of the Code.

Sec. 2.05. External Auditor. An "external auditor" is any approved auditor listed in Appendix A of this Agreement that WP engages to perform the audits required by section 8 of this Agreement.

Sec. 2.06. Flow-Through Entity. A flow-through entity is a foreign partnership described in Treas. Reg. § 301.7701–2 or 3 (other than a withholding foreign partnership), a foreign trust that is described in section 651(a) of the Code, or a foreign trust all or a portion of which is treated as owned by the grantor or other person under sections 671 through 679 of the Code (other than a withholding foreign trust). For an item of income for which a treaty benefit is claimed, an entity is also a flow-through entity to the extent it is treated as fiscally transparent under section 894 and the regulations thereunder.

Sec. 2.07. Foreign Person. A "foreign person" is any person that is not a "United States person" and includes a "nonresident alien individual," a "foreign corporation," a "foreign partnership," a "foreign trust," and a "foreign estate," as those terms are defined in section 7701 of the Code.

Sec. 2.08. Form W-8. "Form W-8" means a valid IRS Form W-8BEN, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding*; IRS Form W-8ECI, *Certificate of Foreign Person's Claim for Exemption From Withholding on Income Effectively Connected With the Conduct of a Trade or Business in the United States*; IRS Form W-8EXP, *Certificate of Foreign Governments and Other Foreign Organizations for United States Tax Withholding*; and IRS Form W-8IMY, *Certificate of Foreign Intermediary, Foreign Partnership, and Certain U.S. Branches for United States Tax Withholding*, as appropriate. It also includes any acceptable substitute form.

Sec. 2.09. Form W-9. "Form W-9" means a valid IRS Form W-9, *Request for Taxpayer Identification Number and Certification*, or any acceptable substitute.

Sec. 2.10. Form 1042. "Form 1042" means an IRS Form 1042, *Annual Withholding Tax Return for U.S. Source Income of Foreign Persons*.

Sec. 2.11. Form 1042-S. "Form 1042-S" means an IRS Form 1042-S, *Foreign Person's U.S. Source Income Subject to Withholding*.

Sec. 2.12. Form 1065. "Form 1065" means an IRS Form 1065, *U.S. Return of Partnership Income*, and the Schedules K-1 associated with that form.

Sec. 2.13. Intermediary. An "intermediary" means any person that acts on behalf of another person, such as a custodian, broker, nominee, or other agent.

Sec. 2.14. Nonwithholding Foreign Partnership. A "nonwithholding foreign partnership" is any foreign partnership that is not acting as a withholding foreign partnership.

Sec. 2.15. NRA Withholding. For purposes of this agreement, "nonresident alien (NRA) withholding" is any withholding required under chapter 3 of the Code (other than sections 1445 or 1446), whether the payment subject to withholding is made to an individual or to an entity.

Sec. 2.16. Overwithholding. The term "overwithholding" means the excess of the amount actually withheld over the amount required to be withheld under chapter 3 of the Code.

Sec. 2.17. Partnership and Partner. The terms "partnership" and "partner" are defined in section 7701(a)(2) of the Code and the regulations thereunder. A direct partner is a partner, other than an intermediary or flow-through entity, that is not itself a withholding foreign partnership or withholding foreign trust, for which WP acts as a withholding foreign partnership. An indirect partner is a person that owns a partnership interest in WP though one or more passthrough partners. A passthrough partner is a direct or indirect partner in WP that is an intermediary or flow-through entity. As provided in Section 2.06 of this Agreement, a withholding foreign partnership or withholding foreign trust is not a flow-through entity and thus is not a passthrough partner.

Sec. 2.18. Payment. A "payment" is considered made to a person if that person realizes income whether or not such income results from an actual transfer of cash or other property. See Treas. Reg. § 1.1441–2(e).

Sec. 2.19. Reduced Rate of Withholding. A "reduced rate of withholding" means a rate of withholding that is less than 30 percent, either as a result of a reduction in withholding under the Code or as a result of a reduction in withholding under an income tax treaty.

Sec. 2.20. Reportable Amount. A "reportable amount" means an amount subject to NRA withholding (as defined in section 2.02 of this Agreement); U.S. source deposit interest; and U.S. source interest or original issue discount paid on the redemption of short-term obligations. The term does not include payments on deposits with banks and other financial institutions that remain on deposit for two weeks or less. It also does not include amounts of original issue discount arising from a sale and repurchase transaction completed within a period of two weeks or less, or amounts described in Treas. Reg. § 1.6049–5(b)(7), (10), or (11) (relating to certain foreign targeted registered obligations and certain obligations issued in bearer form).

Sec. 2.21. Reporting Pool. A reporting pool is defined in section 5.03 of this Agreement.

Sec. 2.22. Schedule K-1. "Schedule K-1" or "K-1" is the schedule associated with the Form 1065 that itemizes an individual Partner's Share of Income, Credits, Deductions, etc.

Sec. 2.23. TIN. A "TIN" is a U.S. taxpayer identification number.

Sec. 2.24. Underwithholding. "Underwithholding" means the excess of the amount required to be withheld under chapter 3 of the Code over the amount actually withheld.

Sec. 2.25. U.S. Person. A "United States (or U.S.) person" is a person described in section 7701(a)(30) of the Code, the U.S. government (including an agency or instrumentality thereof), a State of the United States (including an agency

or instrumentality thereof), or the District of Columbia (including an agency or instrumentality thereof).

Sec. 2.26. Withholding Agent. A "withholding agent" has the same meaning as set forth in Treas. Reg. § 1.1441–7(a) and includes a payor. As used in this Agreement, the term generally refers to the person making a payment to a withholding foreign partnership.

Sec. 2.27. Withholding Foreign Partnership (or WP). A "withholding foreign partnership" is a person, described in Treas. Reg. § 1.1441–5(c)(2), that has entered into a withholding agreement with the IRS to be treated as a withholding foreign partnership and is acting in its capacity as a withholding foreign partnership.

Sec. 2.28. Withholding Foreign Partnership (or WP) EIN. A "withholding foreign partnership EIN" or "WP-EIN" means the employer identification number assigned by the IRS to a withholding foreign partnership. WP's WP-EIN is only to be used when WP is acting as a withholding foreign partnership. For example, WP must give a withholding agent its non-WP EIN, if any, rather than its WP-EIN, if it is not acting as a withholding foreign partnership and a taxpayer identification number is required.

Sec. 2.29. Withholding Statement. The term "withholding statement" is defined in section 5.02 of this Agreement.

Sec. 2.30. Other Terms. Any term not defined in this section has the same meaning that it has under the Code, the income tax regulations under the Code, or any applicable income tax treaty.

SECTION 3. WITHHOLDING RESPONSIBILITY

Sec. 3.01. NRA Withholding Responsibility. WP is subject to the withholding and reporting provisions applicable to withholding agents under chapter 3 of the Code. Under chapter 3, a withholding agent must withhold 30 percent of any payment of an amount subject to NRA withholding made to a partner that is a foreign person unless the withholding agent can reliably associate the payment with documentation upon which it can rely to treat the payment as made to a payee that is a U.S. person or as made to a beneficial owner that is a foreign person entitled to a reduced rate of withholding. When it is acting as a withholding foreign partnership, WP must assume NRA withholding responsibility for amounts subject to NRA withholding that are distributed to, or included in the distributive share of, any direct partner, and WP must withhold the amount required to be withheld under chapter 3 of the Code. WP must provide a Form W-8IMY that certifies to a withholding agent that makes a payment of such amounts that WP is acting as a withholding foreign partnership, and WP must identify such amounts on the withholding statement associated with that Form W-8IMY. WP is not required to withhold when it pays such amounts to another withholding foreign partnership or withholding foreign trust that has certified to WP on Form W-8IMY that it is acting as a withholding foreign partnership or withholding foreign trust with respect to such identified amounts. WP is not required to act as a withholding foreign partnership for all amounts that it receives from a withholding agent. WP may not act as a withholding foreign partnership for amounts distributed to, or included in the distributive share of, passthrough partners or indirect partners. WP must act as a nonwithholding foreign partnership for such amounts. When WP is not acting as a withholding foreign partnership, WP must: 1) provide to the withholding agent a Form W-8IMY with Part VI completed; 2) identify such amounts on the withholding statement associated with that Form W-8IMY; and 3) provide the documentation and information required by Treas. Reg. §1.1441–5(c)(3)(iii) and (iv).

Sec. 3.02. Timing of Withholding. WP must withhold on the date it makes a distribution to a direct foreign partner that includes an amount subject to NRA withholding. To the extent a direct foreign partner's distributive share of income subject to withholding has not actually been distributed to the direct foreign partner, WP must withhold on the direct foreign partner's distributive share on the earlier of the date that the statement required under section 6031(b) (schedule K-1) is mailed or otherwise provided to the partner or the due date for furnishing the statement (whether or not WP is required to prepare and furnish the statement).

Sec. 3.03. Deposit Requirements. WP must deposit amounts withheld under chapter 3 of the Code with a Federal Reserve bank or authorized financial institution at the time and in the manner provided under section 6302 of the Code (see Treas. Reg. § 1.6302–2(a) or § 31.6302–1(h)).

SECTION 4. DOCUMENTATION REQUIREMENTS

Sec. 4.01. Documentation Requirements. WP agrees to obtain, review, and maintain Forms W-8 and W-9 in accordance with this section 4. WP must obtain a Form W-8 or W-9 from every direct partner prior to the time that withholding is required. WP agrees to make documentation (together with any associated withholding statements and other documents or information) available upon request for inspection by WP's external auditor. WP represents that none of the laws to which it is subject prohibits disclosure of the identity of any partner or corresponding partner information to WP's external auditor. WP may rely on the Forms W-8 and W-9 it obtains under this section 4 as the basis for determining its withholding and reporting obligations.

Sec. 4.02. Documentation for Foreign Partners. WP may treat a direct partner as a foreign beneficial owner if the direct partner provides a Form W-8 that supports such status. WP may treat a direct partner that has provided a Form W-8 as entitled to a reduced rate of NRA withholding if all the requirements for a reduced rate are met and the Form W-8 provided by the direct partner supports entitlement to a reduced rate. Sections 4.03 through 4.06 of this Agreement describe the specific documentation requirements necessary for obtaining a reduced rate of withholding in certain circumstances.

Sec. 4.03. Treaty Claims. WP may not reduce the rate of withholding based on a direct partner's claim of treaty benefits unless WP obtains from the partner a Form W-8BEN with Part II of the form properly completed, including the appropriate limitation on benefits and section 894 certifications.

Sec. 4.04. Documentation for International Organizations. WP may not treat a direct partner as an international organization entitled to an exemption from withholding under section 892 of the Code unless WP obtains a Form

W-8EXP from the international organization and the name provided on the Form W-8EXP is the name of an entity designated as an international organization by executive order pursuant to 22 United States Code 288 through 288(f). If an international organization is not claiming benefits under section 892 of the Code but under another Code exception, the provisions of sections 4.02 of this Agreement apply rather than the provisions of this section 4.04.

Sec. 4.05. Documentation for Foreign Governments and Foreign Central Banks of Issue.

(**A**) **Documentation For a Foreign Government or Foreign Central Bank of Issue Claiming an Exemption From Withholding Under Section 892 or Section 895**. WP may not treat a direct partner as a foreign government or foreign central bank of issue exempt from withholding under section 892 or 895 of the Code unless—

(**1**) WP receives from the direct partner a Form W-8EXP establishing that the direct partner is a foreign government or foreign central bank of issue;

(**2**) The income distributed to, or included in the distributive share of, the direct partner is the type of income that qualifies for an exemption from withholding under section 892 or 895; and

(**3**) WP does not know, or have reason to know, that the direct partner is a controlled commercial entity, that the income owned by the foreign government or foreign central bank of issue is being received from a controlled commercial entity, or that the income is from the disposition of an interest in a controlled commercial entity.

(**B**) **Treaty Exemption**. WP may not treat a direct partner as a foreign government or foreign central bank of issue entitled to a reduced rate of withholding under an income tax treaty unless it obtains a Form W-8BEN that, under section 4.03 of this Agreement, is sufficient to obtain a reduced rate of withholding under a treaty.

(**C**) **Other Code Exception**. If a foreign government or foreign central bank of issue is not claiming benefits under section 892 or section 895 of the Code but under another Code exception (*e.g.*, the portfolio interest exception under sections 871(h) or 881(c) of the Code), the provisions of section 4.02 of this Agreement apply rather than the provisions of this section 4.05.

Sec. 4.06. Documentation for Foreign Tax-Exempt Organizations.

(**A**) **Reduced Rate of Withholding Under Section 501**. WP may not treat a direct partner as a foreign organization described under section 501(c) of the Code, and therefore exempt from withholding (or, if the direct partner is a foreign private foundation, subject to withholding at a 4-percent rate under section 1443(b) of the Code) unless WP obtains a valid Form W-8EXP on which Part III of the form is completed.

(**B**) **Treaty Exemption**. WP may not treat a direct partner as a foreign organization that is tax exempt or entitled to a reduced rate of withholding under an income tax treaty unless WP obtains a Form W-8BEN that, under section 4.03 of this Agreement, is sufficient to obtain a reduced rate of withholding under a treaty.

(**C**) **Other Exceptions**. If a tax-exempt entity is not claiming a reduced rate of withholding because it is an organization described under section 501(c) of the Code or under an income tax treaty, but is claiming a reduced rate of withholding under another Code exception, the provisions of section 4.02 of this Agreement apply rather than the provisions of this section 4.06.

Sec. 4.07. Documentation for Passthrough Partners. WP shall not act as a withholding foreign partnership with respect to an amount subject to withholding distributed to, or included in the distributive share of, a passthrough partner. WP must forward that passthrough partner's documentation (and associated withholding statement and documentation of indirect partners) to the withholding agent from whom WP receives the amount subject to withholding. WP may act as a withholding foreign partnership for payments made to partners that are themselves withholding foreign partnerships or withholding foreign trusts.

Sec. 4.08. Documentation for U.S. Exempt Recipients. WP shall not treat a partner as a U.S. exempt recipient unless WP obtains a Form W-9 from the partner on which the partner writes "Exempt" in Part II of the Form.

Sec. 4.09. Documentation for U.S. Non-Exempt Recipients. WP shall not treat a partner as a U.S. non-exempt recipient unless WP obtains a Form W-9 from the partner.

Sec. 4.10. Documentation Validity. WP may not rely on Forms W-8 or W-9 if WP has actual knowledge or reason to know that the information or statements contained in the forms are unreliable or incorrect. Once WP knows, or has reason to know, that a Form W-8 or W-9 provided by a direct partner is unreliable or incorrect, WP must obtain a new Form W-8 or W-9 prior to the time withholding is required.

Sec. 4.11. Documentation Validity Period.

(**A**) **Form W-8**. WP may rely on a properly completed Form W-8 until its validity expires under Treas. Reg. § 1.1441–1(e)(4)(ii).

(**B**) **Form W-9**. WP may rely on a properly completed Form W-9 as long as it has not been informed by the IRS or another withholding agent that the form is unreliable.

Sec. 4.12. Maintenance and Retention of Documentation.

(**A**) **Maintaining Documentation**. WP shall maintain Forms W-8 and W-9 by retaining the original documentation, a certified copy, a photocopy, a microfiche, or by electronic storage or similar means of record retention.

(**B**) **Retention Period**. WP shall retain a direct partner's Form W-8 or W-9 obtained under this section 4 for as long as it may be relevant to the determination of WP's tax liability under this agreement.

SECTION 5. WITHHOLDING FOREIGN PARTNERSHIP WITHHOLDING CERTIFICATE

Sec. 5.01. WP Withholding Certificate. WP agrees to furnish a withholding foreign partnership withholding certificate to each withholding agent from which it receives amounts subject to NRA withholding as a withholding foreign partnership. The withholding foreign partnership withholding certificate is a Form W-8IMY (or acceptable substitute form) that certifies that WP is acting as a withholding foreign partnership, contains WP's WP-EIN, and provides all other information required by the form. WP is

not required to disclose, as part of that Form W-8IMY or its withholding statement, any information regarding the identity of a direct partner.

Sec. 5.02. Withholding Statement. WP agrees to provide to each withholding agent from which WP receives amounts subject to NRA withholding as a withholding foreign partnership a written statement (the "withholding statement") identifying the amounts for which WP acts as a withholding foreign partnership. The statement forms an integral part of the Form W-8IMY. The withholding statement may be provided in any manner, and in any form, to which WP and the withholding agent mutually agree.

Sec. 5.03. Withholding Rate Pools. When it is acting as a withholding foreign partnership, WP must assume withholding responsibility for amounts subject to withholding that are distributed to, or included in the distributive shares of, its direct partners. Accordingly, withholding rate pool information is not required as part of WP's withholding statement.

SECTION 6. TAX RETURN OBLIGATIONS

Sec. 6.01. Form 1042 Filing Requirement.

(**A**) **In General**. WP shall file a return on Form 1042, whether or not WP withheld any amounts under chapter 3 of the Code, on or before March 15 of the year following any calendar year in which WP acts as a withholding foreign partnership. In addition to the information specifically requested on Form 1042 and the accompanying instructions, WP shall attach a statement setting forth the amounts of any overwithholding or underwithholding adjustments made under Treas. Reg. § 1.1461–2 and sections 7.01 and 7.03 of this Agreement, and an explanation of the circumstances that resulted in the over- or under- withholding.

(**B**) **Extensions for Filing Returns**. WP may request an extension of the time for filing Form 1042, or any of the information required to be attached to the form, by submitting Form 2758, *Application for Extension of Time to File Certain Excise, Income, Information, and Other Returns*, on or before the due date of the return. The application must be in writing, properly signed by a duly authorized agent of WP, and shall clearly set forth the following:

(**1**) The calendar year for which the extension is requested; and

(**2**) A full explanation of the reason(s) for requesting the extension to assist the IRS in determining the period of extension, if any, that will be granted.

Sec. 6.02. Form 1042-S Reporting: General Rule. Unless WP has made a pooled reporting (PR) election pursuant to section 6.03 of this Agreement, WP is required to file separate Forms 1042-S for each direct partner to whom WP distributes, or in whose distributive share is included, an amount subject to NRA withholding. WP must file separate Forms 1042-S by income code, exemption code, recipient code, and withholding rate. WP must file its Forms 1042-S in the manner required by the regulations under chapter 3 of the Code and the instructions to the form, including any requirement to file the forms magnetically or electronically. Any Form 1042-S required by this section 6 shall be filed on or before March 15 following the calendar year in which withholding, if any, was required under section 3.02 of this agreement. WP may request an extension of time to file Forms 1042-S by submitting Form 8809, *Request for Extension of Time to File Information Returns*, by the due date of Forms 1042-S in the manner required by Form 8809.

Sec. 6.03. Form 1042-S Reporting: Special Rule for PR Election. If WP has made the PR election pursuant to this section 6.03, WP is not required to file Forms 1042-S for amounts distributed to, or included in the distributive share of, each separate direct partner for whom such reporting would otherwise be required. Instead, WP shall file a separate Form 1042-S for each reporting pool. A reporting pool consists of income that falls within a particular withholding rate and within a particular income code, exemption code, and recipient code as determined on Form 1042-S. WP may use a single recipient code for all reporting pools except for amounts paid to foreign tax-exempt recipients, for which a separate recipient code must be used. For this purpose, a foreign tax-exempt recipient includes any organization that is not subject to NRA withholding and is not liable to tax in its country of residence because it is a charitable organization, a pension fund, or a foreign government. WP must make the PR election at the time this agreement is executed by signing the election statement on the signature page of this agreement. Once made, the PR election remains in effect for the entire term of this agreement beginning on the date the agreement becomes effective and ending on the date of its expiration or termination under section 9 of the Agreement. WP must make a new election for each renewal term of this agreement. If WP makes the PR election, WP cannot revoke it prior to the end of the term for which WP has made the PR election. If WP did not make the PR election at the time this agreement was executed, then WP may make a PR election only by terminating this agreement pursuant to section 9.03 and requesting to enter into a new agreement.

Sec. 6.04. Form 1065 Filing Requirement. If WP is required to file Form 1065 and Schedules K-1 under Treas. Reg. § 1.6031(a)–1, then WP shall file Form 1065 and Schedules K-1 in accordance with the regulations and the instructions for the form.

Sec. 6.05. Retention of Returns. WP shall retain Forms 1065 and 1042 for the period of the applicable statute of limitations on assessments and collection under the Code.

SECTION 7. ADJUSTMENTS FOR OVER- AND UNDER-WITHHOLDING; REFUNDS

Sec. 7.01. Adjustments for NRA Overwithholding by WP. WP may make an adjustment for amounts paid to its direct partners that it has overwithheld under chapter 3 of the Code by applying either the reimbursement or set-off procedures described in this section within the time period prescribed for those procedures.

(**A**) **Reimbursement Procedure**. WP may repay its partners for an amount overwithheld and reimburse itself by reducing, by the amount of tax actually repaid to the partners, the amount of any subsequent deposit of tax required to be made by WP under section 3.03 of this Agreement. For purposes of this section 7.01(A), an amount that is overwithheld shall be applied in order of time to each

of WP's subsequent deposit periods in the same calendar year to the extent that the withholding taxes required to be deposited for a subsequent deposit period exceed the amount actually deposited. An amount overwithheld in a calendar year may be applied to deposit periods in the calendar year following the calendar year of overwithholding only if:

(**1**) WP states on a Form 1042-S filed by March 15 of the calendar year following the calendar year of overwithholding, the amount of tax withheld and the amount of any actual repayments; and

(**2**) WP states on a Form 1042, filed by March 15 of the calendar year following the calendar year of overwithholding, that the filing of the Form 1042 constitutes a claim for credit in accordance with Treas. Reg. § 1.6414–1.

(**B**) **Set-Off Procedure**. WP may repay its partners by applying the amount overwithheld against any amount which otherwise would be required under chapter 3 of the Code to be withheld by WP before the earlier of March 15 of the calendar year following the calendar year of overwithholding or the date that the Form 1042-S is actually filed with the IRS. For purposes of making a return on Form 1042 or 1042-S for the calendar year of overwithholding, and for purposes of making a deposit of the amount withheld, the reduced amount shall be considered the amount required to be withheld from such income under chapter 3 of the Code.

Sec. 7.02. Collective Credit or Refund Procedures for NRA Overwithholding. If WP has made a PR election and it has overwithheld under chapter 3 of the Code on amounts subject to NRA withholding paid to WP's direct partners during a calendar year and the amount has not been recovered under the reimbursement or set-off procedures under sections 7.01 of this Agreement, WP may request a credit or refund of the total amount overwithheld by following the procedures of this section 7.02. WP shall follow the procedures set forth under sections 6402 and 6414 of the Code, and the regulations thereunder, to claim the credit or refund. No credit or refund will be allowed after the expiration of the statutory period of limitation for refunds under section 6511 of the Code. WP may use the collective refund procedures under this section 7.02 only if the following conditions are met:

(**A**) WP must not have issued Forms 1042-S to the direct partners who were subjected to overwithholding;

(**B**) WP must submit together with its amended return on which it claims a credit or refund a statement of the reason for the overwithholding;

(**C**) WP must submit together with its amended return on which it claims a credit or refund a statement that it has repaid the amount of overwithholding to the appropriate direct partners prior to filing the claim for credit or refund; and

(**D**) WP must retain a record showing that it repaid the direct partners the amount of the overwithholding.

Sec. 7.03. Adjustments for NRA Underwithholding. If WP knows that an amount should have been withheld under chapter 3 of the Code from a previous payment to a direct partner but was not withheld, WP may either withhold from future payments made to the same direct partner or satisfy the tax from the direct partner's proportionate share of assets over which it has control. The additional withholding or satisfaction of the tax owed may only be made before the due date of the Form 1042 (not including extensions) for the calendar year in which the underwithholding occurred.

Sec. 7.04. NRA Underwithholding after Form 1042 Filed. If, after a Form 1042 has been filed for a calendar year, WP, WP's external auditor, or the IRS determines that, due to WP's failure to carry out its obligations under this Agreement, WP has underwithheld tax for such year, WP shall file an amended Form 1042 to report and pay the underwithheld tax. WP shall pay the underwithheld tax, the interest due on the underwithheld tax, and any applicable penalties, at the time of filing the amended Form 1042. If WP fails to file an amended return, the IRS shall make such return under section 6020 of the Code.

Sec. 7.05. Special Rule Regarding Failure to Deposit Penalties. Solely for purposes of applying section 6656 of the Code (failure to make deposit of taxes), WP will not be considered to have made an underpayment of a deposit of NRA withholding taxes if the conditions of this paragraph are met. The conditions of this paragraph are that—

(**A**) WP makes its deposits within the time (deposit period) required by section 6302 of the Code;

(**B**) The deposit is not less than 90 percent of the aggregate amount of the tax required to be withheld under chapter 3 of the Code during the deposit period applicable to WP; and

(**C**) WP determines the difference between the total amount required to be deposited and the amount actually deposited as of the end of the 3rd, 6th, 9th, and 12th months of the calendar year and the difference is deposited no later than the 15th day of the second following month (*i.e.*, May 15, August 15, November 15 and February 15, respectively). In determining whether there has been an underpayment, reimbursements and set-offs shall be taken into account.

SECTION 8. EXTERNAL AUDIT PROCEDURES

Sec. 8.01. In General. Unless WP requests an IRS audit in lieu of an external audit, the IRS agrees not to conduct an on-site audit of WP with respect to withholding and reporting obligations covered by this Agreement provided that an external auditor designated in Appendix A of this Agreement conducts an audit of WP in accordance with this section 8. WP shall permit the external auditor to have access to all relevant records of WP for purposes of performing the external audit, including information regarding specific partners. WP shall permit the IRS to communicate directly with the external auditor and to review the audit procedures followed by the external auditor. WP represents that there are no legal prohibitions that prevent the external auditor from examining any information relevant to the external audit to be performed under this section 8 and that there are no legal prohibitions that prevent the IRS from communicating directly with the auditor. WP shall permit the IRS to examine the external auditor's work papers and reports.

Sec. 8.02. Designation of External Auditor. WP's external auditor must be one of the auditors listed in Appendix A of this Agreement, unless WP and the IRS agree, prior to the audit, to substitute another auditor. WP shall not propose an external auditor unless it has a reasonable belief that the auditor is subject to laws, regulations, or rules that impose sanctions

for failure to exercise its independence and to perform the audit competently. The IRS has the right to reject a proposed external auditor, or to revoke its acceptance of an external auditor, if the IRS, in its sole discretion, reasonably believes that the auditor is not independent or cannot perform an effective audit under this Agreement.

Sec. 8.03. Timing External Audits: General Rule. Unless WP has made a PR election, WP shall have the external auditor conduct an external audit only at such time and only for such calendar years as the IRS directs.

Sec. 8.04. Timing External Audits: Special Rule for PR Election. If WP has made a PR election, WP shall have the external auditor conduct an audit after the close of every other calendar year that this Agreement is in effect. The auditor shall examine the two previous calendar years. For example, the first audit will occur in the third calendar year that the agreement is in effect and the external auditor will examine calendar years one and two.

Sec. 8.05. Scope of External Audit. The external auditor shall verify whether WP is in compliance with this Agreement by conducting an audit that meets the requirements of this section 8.05. The report, described in section 8.06 of this Agreement, must disclose that the external auditor has, at a minimum, performed the following checks listed in this section 8.05, and set forth how each of those checks was performed and the results of the checks. WP's external auditor is encouraged to contact the IRS at the address set forth in section 10.06 of this Agreement and submit an audit plan (which includes, if relevant, the extent to which the external auditor proposes to rely on WP's internal audit procedures) prior to performing the audit so that the audit may be conducted in the most efficient and least costly manner possible.

(**A**) **Documentation**. The external auditor must review information contained in partner files to determine whether the documentation requirements of section 4 of this Agreement are being met.

(**B**) **Withholding Responsibilities**. The external auditor must—

(**1**) Perform test checks of direct partners, to verify that WP is withholding the proper amounts.

(**2**) Verify that amounts withheld were timely deposited in accordance with section 3.03 of this Agreement.

(**C**) **Return Filing and Information Reporting**. The external auditor must—

(**1**) Obtain copies of original and amended Forms 1042, and any schedules, statements, or attachments required to be filed with those forms, and determine whether the amounts of income, taxes, and other information reported on those forms are accurate by—

(**i**) Reviewing work papers;

(**ii**) Reviewing Forms W-8IMY, together with the associated withholding statements, that WP has provided to withholding agents;

(**iii**) Reviewing copies of Forms 1042-S that withholding agents have provided WP;

(**iv**) Reviewing account statements from withholding agents;

(**v**) Reviewing correspondence between WP and withholding agents; and

(**vi**) Interviewing personnel responsible for preparing the Form 1042 and the work papers used to prepare those forms.

(**2**) Obtain copies of original and corrected Forms 1042-S and Schedules K-1 together with the work papers used to prepare those forms and determine whether the amounts reported on those forms are accurate by—

(**i**) Reviewing the Forms 1042-S received from withholding agents;

(**ii**) Reviewing the Form 1065, if required;

(**iii**) Reviewing a valid sample of earnings statements issued by WP to direct partners, if any.

(**3**) Thoroughly review the statements attached to amended Forms 1042 filed to claim a refund, ascertain their veracity, and determine the causes of any overwithholding reported and ensure WP did not issue Forms 1042-S to persons whom it included as part of its collective credit or refund.

(**4**) Determine, in the case of collective credits or refunds, that WP repaid the appropriate partners prior to requesting a collective refund or credit.

(**E**) **Change in Circumstances**. The external auditor must verify that in the course of the audit it has not discovered any significant change in circumstances, as described in section 9.05 (A) or (D) of this Agreement.

Sec. 8.06. External Auditor's Report. Upon completion of the audit of WP, the external auditor shall issue a report, or reports, of audit findings directly to the IRS by sending the original report to the IRS at the address set forth in section 10.06 of this Agreement. This report is due by December 31 following the calendar year being audited, or if that date falls on a Saturday or Sunday, the next U.S. business day. The IRS may, however, upon request by the external auditor, extend the due date of the audit report upon good cause. The report must be in writing, in English, and currency amounts must be stated in U.S. dollars. The report must fully describe the scope of the audit, the methodologies (including sampling techniques) used to determine whether WP is in compliance with the provisions of this Agreement, and the result of each such determination. The report must also specifically address each of the items in section 8.05 of this Agreement.

Sec. 8.07. Expanding Scope and Timing of External Audit. Upon review of the external auditor's report, the IRS may request, and WP must permit, the external auditor to perform additional audit procedures.

SECTION 9. EXPIRATION, TERMINATION AND DEFAULT

Sec. 9.01. Term of Agreement: General Rule. If WP has not made a PR election, this Agreement shall be in effect on ______________ and shall continue in force until terminated under 9.03 or 9.04 of this Agreement.

Sec. 9.02. Term of Agreement: Special Rule for PR Election. If WP has made a PR election, this Agreement shall be in effect on ______________ and shall expire on December 31 of the fifth full calendar year after the year in which this Agreement first takes effect. This Agreement may be renewed for additional terms as provided in section 9.08 of this Agreement.

Sec. 9.03. Termination of Agreement. This Agreement may be terminated by either the IRS or WP prior to the end of

its term by delivery of a notice of termination to the other party in accordance with section 10.06 of this Agreement. The IRS, however, shall not terminate the Agreement unless there has been a significant change in circumstances, as defined in section 9.05 of this Agreement, or an event of default has occurred, as defined in section 9.06 of this Agreement, and the IRS determines, in its sole discretion, that the significant change in circumstances or the event of default warrants termination of this Agreement. In addition, the IRS shall not terminate this Agreement in the event of default if WP can establish to the satisfaction of the IRS that all events of default for which it has received notice have been cured within the time period agreed upon. The IRS shall notify WP, in accordance with section 9.07 of this Agreement, that an event of default has occurred and that the IRS intends to terminate the Agreement unless WP cures the default. A notice of termination sent by either party shall take effect on the date specified in the notice.

Sec 9.04. Automatic Termination of Agreement. Notwithstanding Section 9.03 of this Agreement, this Agreement will terminate automatically in the event that the external auditor or the IRS on audit discovers that WP was not in possession of Forms W-8 or W-9, as applicable, for any direct partner at any time that withholding or reporting was required under section 3.02 of this Agreement. The automatic termination will be effective as of December 31 of the year in which the external auditor or the IRS makes that discovery. This Agreement will be reinstated, effective the same date it was automatically terminated, if WP obtains appropriate Forms W-8 or W-9 (that relate to the time withholding or reporting was required) for each such partner before January 31 of the year following the year in which the agreement automatically terminated. In the event of automatic termination of this agreement, WP must pay any underwithholding of tax, interest, and penalties that the IRS determines is attributable to each undocumented direct partner for the period during which the partner was undocumented, and, if WP has made a PR election, WP must file partner specific Forms 1042-S for every foreign direct partner from the earliest time the Forms W-8 or W-9 were required for any undocumented direct partner through the date of termination. After the date of automatic termination of this agreement, WP may not act as a withholding foreign partnership, and must so notify any persons to which WP has furnished a withholding foreign partnership certificate. After the date of automatic termination of this agreement, the IRS may reinstate this agreement (or the IRS may require WP to enter into a new withholding foreign partnership agreement) on such terms and conditions and with such modifications as the IRS may determine.

Sec. 9.05. Significant Change in Circumstances. For purposes of this Agreement, a significant change in circumstances includes, but is not limited to—

(**A**) any merger, consolidation or division of WP or any change in circumstances that would result in a termination of WP under section 708 of the Code;

(**B**) A change in U.S. federal law or policy, or applicable foreign law or policy, that affects the validity of any provision of this Agreement, materially affects the procedures contained in this Agreement, or affects WP's ability to perform its obligations under this Agreement;

(**C**) A ruling of any court that affects the validity of any provision of this Agreement; or

(**D**) A significant change in WP's business practices that affects WP's ability to meet its obligations under this Agreement.

Sec. 9.06. Events of Default. For purposes of this Agreement, an event of default occurs if WP fails to perform any material duty or obligation required under this Agreement, and includes, but is not limited to, the occurrence of any of the following:

(**A**) WP fails to implement adequate procedures, accounting systems, and internal controls to ensure compliance with this Agreement;

(**B**) WP underwithholds an amount that WP is required to withhold under chapter 3 of the Code and fails to correct the underwithholding or to file an amended Form 1042 reporting, and paying, the appropriate tax;

(**C**) WP makes excessive refund claims;

(**D**) WP fails to file Forms 1042, 1042-S, 1065 (if required), or Schedules K-1 (if required) by the due date specified on such forms or files forms that are materially incorrect or fraudulent;

(**E**) WP fails to have an external audit performed when required, WP's external auditor fails to provide its report directly to the IRS on a timely basis, WP fails to cooperate with the external auditor, or WP or its external auditor fails to cooperate with the IRS;

(**F**) WP fails to inform the IRS within 90 days of any significant change in its business practices to the extent that change affects WP's obligations under this Agreement;

(**G**) WP fails to cure a default identified by the IRS or by an external auditor;

(**H**) WP makes any fraudulent statement or a misrepresentation of material fact with regard to this Agreement to the IRS, a withholding agent, or WP's external auditor;

(**I**) The IRS determines that WP's external auditor is not sufficiently independent to adequately perform its audit function or the external auditor fails to provide an audit report that complies with section 8 of this Agreement;

(**J**) WP is prohibited by any law from disclosing the identity of a partner or partner information to WP's external auditor;

(**K**) WP fails to make deposits in the time and manner required by section 3.03 of this Agreement or fails to make adequate deposits, taking into account the procedures of 7.05 of this Agreement; or

(**L**) WP fails to permit the external auditor to perform additional audit procedures under the provisions of section 8.07 of this Agreement.

Sec. 9.07. Notice and Cure. Upon the occurrence of an event of default, the IRS may deliver to WP a notice of default specifying the event of default that has occurred. WP shall respond to the notice of default within 60 days (60-day response) from the date of the notice of default. The 60-day response shall contain an offer to cure the event of default and the time period in which the cure will be accomplished or shall state the reasons why WP does not agree that an event of default has occurred. If WP does not provide a 60-day response, the IRS may deliver a notice of termination as provided in section 9.03 of this Agreement. If WP provides a 60-day response, the

IRS shall either accept or reject WP's statement that no default has occurred or accept or reject WP's proposal to cure an event of default. If the IRS rejects WP's contention that no default has occurred or rejects WP's proposal to cure a default, the IRS will offer a counter-proposal to cure the event of default. Within 30 days of receiving the IRS's counter-proposal, WP shall notify the IRS (30-day response) whether it continues to maintain that no default has occurred or whether it rejects the IRS's counter-proposal to cure an event of default. If WP's 30-day response states that no default has occurred or it rejects the IRS's counter-proposal to cure, the parties shall seek to resolve their disagreement within 30 days of the IRS's receipt of WP's 30-day response. If a satisfactory resolution has not been achieved at the end of this latter 30-day period, or if WP fails to provide a 30-day response, the IRS may terminate this Agreement by providing a notice of termination in accordance with section 9.03 of this Agreement. If WP receives a notice of termination from the IRS, it may appeal the determination within 30 days of the date of the notice of termination by sending a written notice to the address specified in section 10.06 of this Agreement. If WP appeals the notice of termination, this Agreement shall not terminate until the appeal has been decided. If an event of default is discovered in the course of an external audit, the WP may cure the default, without following the procedures of this section 9.07, if the external auditor's report describes the default and the actions that WP took to cure the default and the IRS determines that the cure procedures followed by WP were sufficient. If the IRS determines that WP's actions to cure the default were not sufficient, the IRS shall issue a notice of default and the procedures described in this section 9.07 shall be followed.

Sec. 9.08. Renewal. If WP has made the PR election under section 6.03 of this agreement and intends to renew this Agreement for an additional term, it shall submit an application for renewal to the IRS no earlier than one year and no later than six months prior to the expiration of this Agreement. Any such application for renewal must contain an update of the information provided by WP to the IRS in connection with the application to enter into this Agreement, and any other information the IRS may request in connection with the renewal process. This Agreement shall be renewed only upon the signatures of both WP and the IRS. Either the IRS or WP may seek to negotiate a new withholding foreign partnership agreement rather than renew this Agreement.

SECTION 10. MISCELLANEOUS PROVISIONS

Sec. 10.01. WP's application to become a withholding foreign partnership and the Appendix to this Agreement are hereby incorporated into and made an integral part of this Agreement. This Agreement, WP's application, and the Appendix to this Agreement constitute the complete agreement between the parties.

Sec. 10.02. This Agreement may be amended by the IRS if the IRS determines that such amendment is needed for the sound administration of the internal revenue laws or internal revenue regulations. The agreement may also be modified by either WP or the IRS upon mutual agreement. Such amendments or modifications shall be in writing.

Sec. 10.03. Any waiver of a provision of this Agreement by the IRS is a waiver solely of that provision. The waiver does not obligate the IRS to waive other provisions of this Agreement or the same provision at a later date.

Sec. 10.04. This Agreement shall be governed by the laws of the United States. Any legal action brought under this Agreement shall be brought only in a U.S. court with jurisdiction to hear and resolve matters under the internal revenue laws of the United States. For this purpose, WP agrees to submit to the jurisdiction of such U.S. court.

Sec. 10.05. WP's rights and responsibilities under this Agreement cannot be assigned to another person.

Sec. 10.06. Notices provided under this Agreement shall be mailed registered, first class airmail. Notice shall be directed as follows:

To the IRS:

Internal Revenue Service
LMSB:FS:QI
290 Broadway
New York, NY 10007–1867
USA

All notices sent to the IRS must include the WP's WP-EIN.

To WP:

____
____
____
____

Sec. 10.07. WP, acting in its capacity as a withholding foreign partnership or in any other capacity, does not act as an agent of the IRS, nor does it have the authority to hold itself out as an agent of the IRS.

IN WITNESS WHEREOF, the above parties have subscribed their names to these presents, in duplicate.

Signed this day of ,

____

(name and title of person signing for WP)

____

(name and title of person signing for IRS)

PR Election Statement

By signing hereunder, WP makes the PR election under section 6.03 of this Agreement.

____

(name and title of person signing for WP)

Appendix A

WP and the IRS agree that any of the following auditors may be used by WP to perform the external audits required by section 8 of this Agreement.

[Names, addresses, telephone and fax numbers of external auditors.]

APPENDIX 2

Withholding Foreign Trust Agreement

SECTION 1. PURPOSE AND SCOPE

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Sec. 1.02. Parties to the Agreement

SECTION 2. DEFINITIONS

Sec. 2.01. Agreement
Sec. 2.02. Amounts Subject to NRA Withholding

Sec. 2.03. Chapter 3 of the Code
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Sec. 2.08. Foreign Person
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Sec. 6.02. Form 1042-S Reporting: General Rule
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SECTION 9. EXPIRATION, TERMINATION AND DEFAULT

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Sec. 9.02. Term of Agreement: Special Rule for PR Election
Sec. 9.03. Termination of Agreement
Sec. 9.04. Automatic Termination of Agreement
Sec. 9.05. Significant Change in Circumstances
Sec. 9.06. Events of Default
Sec. 9.07. Notice and Cure
Sec. 9.08. Renewal

SECTION 10. MISCELLANEOUS PROVISIONS

THIS AGREEMENT is made in duplicate under and in pursuance of section 1441 of the Internal Revenue Code of 1986, as amended, (the "Code") and Treasury Regulation § 1.1441–5(e)(5)(v) by and between ______________, (referred to as "WT"), and the INTERNAL REVENUE SERVICE (the "IRS"):

WHEREAS, WT has submitted an application in accordance with **Revenue Procedure 2002–xx** to be a withholding foreign trust for purposes of Treas. Reg. § 1.1445–5(e)(5)(v);

WHEREAS, WT and the IRS desire to enter into an agreement to establish WT's rights and obligations regarding documentation, withholding, information reporting, tax return filing, deposits, and adjustment procedures under sections 1441, 1442, 1443, 1461, 6048, 6302, 6402, and 6414 of the Code with respect to certain types of payments;

NOW, THEREFORE, in consideration of the following terms, representations, and conditions, the parties agree as follows:

SECTION 1. PURPOSE AND SCOPE

Sec. 1.01. General Obligations. Except as otherwise provided in this Agreement, WT's obligations with respect to income distributed to, or included in the distributive shares of, its beneficiaries or owners are governed by the Code and the regulations thereunder. WT may act in its capacity as a withholding foreign trust pursuant to this Agreement only for payments of amounts subject to NRA withholding that are distributed to, or included in the distributive shares of, its direct beneficiaries or

owners. WT is required to act as a withholding foreign trust for all such amounts paid to WT, or included in WT's distributive share, by any withholding agent to which WT has provided a Form W-8IMY that represents that WT is acting as a withholding foreign trust with respect to such amounts. WT must act as a withholding foreign trust for any such amounts paid with respect to such a Form W-8IMY that are distributed to, or included in the distributive shares of, its direct foreign beneficiaries or owners. WT may act as a withholding foreign trust for such amounts that are distributed to, or included in the distributive shares of, its direct beneficiaries or owners that are U.S. persons. WT may also act as a withholding foreign trust and may treat itself as a direct foreign beneficiary if (i) WT is a trust the terms of which described in section 651(a)(1) and (2) of the Code and (ii) in any taxable year, WT distributes amounts other than amounts of income described in section 651(a)(1). In no event may WT act as a withholding foreign trust for amounts subject to NRA withholding that are distributed to, or included in the distributive shares of, passthrough beneficiaries or owners or indirect beneficiaries or owners. For passthrough beneficiaries or owners and indirect beneficiaries or owners, WT must act as a nonwithholding foreign trust.

Sec. 1.02. Parties to the Agreement. This Agreement applies to WT and the IRS.

SECTION 2. DEFINITIONS

For purposes of this Agreement, the terms listed below are defined as follows:

Sec. 2.01. Agreement. "Agreement" means this Agreement between WT and the IRS. All appendices to this Agreement and WT's application to become a withholding foreign trust are incorporated into this Agreement by reference.

Sec. 2.02. Amounts Subject to NRA Withholding. An "amount subject to NRA withholding" is an amount described in Treas. Reg. § 1.1441–2(a). An amount subject to NRA withholding shall not include interest paid as part of the purchase price of an obligation sold between interest payment dates or original issue discount paid as part of the purchase price of an obligation sold in a transaction other than the redemption of such obligation, unless the sale is part of a plan the principal purpose of which is to avoid tax and WT has actual knowledge or reason to know of such plan.

Sec. 2.03. Chapter 3 of the Code. Any reference to "chapter 3 of the Code" means sections 1441, 1442, 1443, 1461, 1463, and 1464 of the Code.

Sec. 2.04. Chapter 61 of the Code. Any reference to "chapter 61 of the Code" means sections 6041, 6042, 6045, 6048, 6049, and 6050N of the Code.

Sec. 2.05. Distributive share. "Distributive share" means an amount subject to withholding that is required to be distributed to the beneficiaries of a simple trust and an amount subject to withholding that is includable in the income of the owners of a grantor trust.

Sec. 2.06. External Auditor. An "external auditor" is any approved auditor listed in Appendix A of this Agreement that WT engages to perform the audits required by section 8 of this Agreement.

Sec. 2.07. Flow-Through Entity. A flow-through entity is a foreign partnership described in Treas. Reg. § 301.7701–2 or 3 (other than a withholding foreign partnership), a foreign trust that is described in section 651(a) of the Code, or a foreign trust all or a portion of which is treated as owned by the grantor or other person under sections 671 through 679 of the Code (other than a withholding foreign trust). For an item of income for which a treaty benefit is claimed, an entity is also a flow-through entity to the extent it is treated as fiscally transparent under section 894 and the regulations thereunder.

Sec. 2.08. Foreign Person. A "foreign person" is any person that is not a "United States person" and includes a "nonresident alien individual," a "foreign corporation," a "foreign partnership," a "foreign trust," and a "foreign estate," as those terms are defined in section 7701 of the Code.

Sec. 2.09. Form W-8. "Form W-8" means a valid IRS Form W-8BEN, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding*; IRS Form W-8ECI, *Certificate of Foreign Person's Claim for Exemption From Withholding on Income Effectively Connected With the Conduct of a Trade or Business in the United States*; IRS Form W-8EXP, *Certificate of Foreign Governments and Other Foreign Organizations for United States Tax Withholding*; and IRS Form W-8IMY, *Certificate of Foreign Intermediary, Foreign Partnership, and Certain U.S. Branches for United States Tax Withholding*, as appropriate. It also includes any acceptable substitute form.

Sec. 2.10. Form W-9. "Form W-9" means a valid IRS Form W-9, *Request for Taxpayer Identification Number and Certification*, or any acceptable substitute.

Sec. 2.11. Form 1042. "Form 1042" means an IRS Form 1042, *Annual Withholding Tax Return for U.S. Source Income of Foreign Persons*.

Sec. 2.12. Form 1042-S. "Form 1042-S" means an IRS Form 1042-S, *Foreign Person's U.S. Source Income Subject to Withholding*.

Sec. 2.13. Form 3520. "Form 3520" means an IRS Form 3520, *Annual Return to Report Transaction With Foreign Trust and Receipt of Certain Foreign Gifts*.

Sec. 2.14. Form 3520-A. "Form 3520-A" means an IRS Form 3520-A, *Annual Information Return of Foreign Trust With a U.S. Owner*.

Sec. 2.15. Intermediary. An "intermediary" means any person that acts on behalf of another person, such as a custodian, broker, nominee, or other agent.

Sec. 2.16. Nonwithholding Foreign Trust. A "nonwithholding foreign trust" is any foreign trust that is not acting as a withholding foreign trust.

Sec. 2.17. NRA Withholding. For purposes of this agreement "nonresident alien (NRA) withholding" is any withholding required under chapter 3 of the Code (other than sections 1445 or 1446), whether the payment subject to withholding is made to an individual or to an entity.

Sec. 2.18. Overwithholding. The term "overwithholding" means the excess of the amount actually withheld over the amount required to be withheld under chapter 3 of the Code.

Sec. 2.19. Trust, Beneficiary and Owner. The term "trust" is defined in Treas. Reg. § 301.7701–4. The term "beneficiary" is defined in section 643(c) of the Code and the regulations thereunder. An "owner" is a person treated as a grantor or owner under Subpart C of Subchapter J of the Code. A direct beneficiary or owner is a beneficiary or owner,

other than an intermediary or flow-through entity that is not itself a withholding foreign trust or withholding foreign partnership, for which WT acts as a withholding foreign trust. An indirect beneficiary or owner is a person that owns a trust interest in WT though one or more passthrough beneficiaries or owners. A passthrough beneficiary or owner is a direct or indirect beneficiary or owner in WT that is an intermediary or flow-through entity. As provided in Section 2.07 of this Agreement, a withholding foreign partnership or withholding foreign trust is not a flow-through entity and thus is not a passthrough beneficiary or owner.

Sec. 2.20. Payment. A "payment" is considered made to a person if that person realizes income whether or not such income results from an actual transfer of cash or other property. See Treas. Reg. § 1.1441–2(e).

Sec. 2.21. Reduced Rate of Withholding. A "reduced rate of withholding" means a rate of withholding that is less than 30 percent, either as a result of a reduction in withholding under the Code or as a result of a reduction in withholding under an income tax treaty.

Sec. 2.22. Reportable Amount. A "reportable amount" means an amount subject to NRA withholding (as defined in section 2.02 of this Agreement); U.S. source deposit interest; and U.S. source interest or original issue discount paid on the redemption of short-term obligations. The term does not include payments on deposits with banks and other financial institutions that remain on deposit for two weeks or less. It also does not include amounts of original issue discount arising from a sale and repurchase transaction completed within a period of two weeks or less, or amounts described in Treas. Reg. § 1.6049–5(b)(7), (10), or (11) (relating to certain foreign targeted registered obligations and certain obligations issued in bearer form).

Sec. 2.23. Reporting Pool. A "reporting pool" is defined in section 5.03 of this Agreement.

Sec. 2.24. TIN. A "TIN" is a U.S. taxpayer identification number.

Sec. 2.25. Underwithholding. "Underwithholding" means the excess of the amount required to be withheld under chapter 3 of the Code over the amount actually withheld.

Sec. 2.26. U.S. Person. A "United States (or U.S.) person" is a person described in section 7701(a)(30) of the Code, the U.S. government (including an agency or instrumentality thereof), a State of the United States (including an agency or instrumentality thereof), or the District of Columbia (including an agency or instrumentality thereof).

Sec. 2.27. Withholding Agent. A "withholding agent" has the same meaning as set forth in Treas. Reg. § 1.1441–7(a) and includes a payor. As used in this Agreement, the term generally refers to the person making a payment to a withholding foreign trust.

Sec. 2.28. Withholding Foreign Trust (or WT). A "withholding foreign trust" is a person, described in Treas. Reg. § 1.1441–5(e)(5)(v), that has entered into a withholding agreement with the IRS to be treated as a withholding foreign trust and is acting in its capacity as a withholding foreign trust.

Sec. 2.29. Withholding Foreign Trust (or WT) EIN. A "withholding foreign trust EIN" or "WT-EIN" means the employer identification number assigned by the IRS to a withholding foreign trust. WT's WT-EIN is only to be used when WT is acting as a withholding foreign trust. For example, WT must give a withholding agent its non-WT EIN, if any, rather than its WT-EIN, if it is not acting as a withholding foreign trust and a taxpayer identification number is required.

Sec. 2.30. Withholding Statement. The term "withholding statement" is defined in section 5.02 of this Agreement.

Sec. 2.31. Other Terms. Any term not defined in this section has the same meaning that it has under the Code, the income tax regulations under the Code, or any applicable income tax treaty.

SECTION 3. WITHHOLDING RESPONSIBILITY

Sec. 3.01. NRA Withholding Responsibility. WT is subject to the withholding and reporting provisions applicable to withholding agents under chapter 3 of the Code. Under chapter 3, a withholding agent must withhold 30 percent of any payment of an amount subject to NRA withholding made to a beneficiary or owner that is a foreign person unless the withholding agent can reliably associate the payment with documentation upon which it can rely to treat the payment as made to a payee that is a U.S. person or as made to a beneficial owner that is a foreign person entitled to a reduced rate of withholding. When it is acting as a withholding foreign trust, WT must assume NRA withholding responsibility for amounts subject to NRA withholding that are distributed to, or included in the distributive share of, any direct beneficiary or owner, and WT must withhold the amount required to be withheld under chapter 3 of the Code. WT must provide a Form W-8IMY that certifies to a withholding agent that makes a payment of such amounts that WT is acting as a withholding foreign trust, and WT must identify such amounts on the withholding statement associated with that Form W-8IMY. WT is not required to withhold when it pays such amounts to another withholding foreign trust or withholding foreign partnership that has certified to WT on Form W-8IMY that it is acting as a withholding foreign trust or withholding foreign partnership with respect to such identified amounts. WT is not required to act as a withholding foreign trust for all amounts that it receives from a withholding agent. WT may not act as a withholding foreign trust for amounts distributed to, or included in the distributive share of, passthrough beneficiaries or owners or indirect beneficiaries or owners. WT must act as a nonwithholding foreign trust for such amounts. When WT is not acting as a withholding foreign trust, WT must: 1) provide to the withholding agent a Form W-8IMY with Part VI completed; 2) identify such amounts on the withholding statement associated with that Form W-8IMY; and 3) provide the documentation and information required by Treas. Reg. §1.1441–5(e)(5)(iii) and (iv).

Sec. 3.02. Timing of Withholding. WT must withhold on the date it makes a distribution to a direct foreign beneficiary or owner that includes an amount subject to NRA withholding. To the extent a direct foreign beneficiary's or owner's distributive share of income subject to withholding has not actually been distributed to the direct foreign beneficiary or owner, WT must withhold on the direct beneficiary's or owner's distributive share on the earlier of the date the statement required under section 6048 is mailed or otherwise provided to the beneficiary or owner or the due date for furnishing the statement (whether or not WT is required to prepare and furnish the statement).

Sec. 3.03. Deposit Requirements. WT must deposit amounts withheld under chapter 3 of the Code with a Federal Reserve bank or authorized financial institution at the time and in the manner provided under section 6302 of the Code (see Treas. Reg. §§ 1.6302–2(a) or 31.6302–1(h)).

SECTION 4. DOCUMENTATION REQUIREMENTS

Sec. 4.01. Documentation Requirements. WT agrees to obtain, review, and maintain Forms W-8 and W-9 in accordance with this section 4. WT must obtain a Form W-8 or W-9 from every direct beneficiary or owner prior to the time that withholding is required. WT agrees to make documentation (together with any associated withholding statements and other documents or information) available upon request for inspection by WT's external auditor. WT represents that none of the laws to which it is subject prohibits disclosure of the identity of any beneficiary or owner or corresponding beneficiary or owner information to WT's external auditor. WT may rely on the Forms W-8 and W-9 it obtains under this section 4 as the basis for determining its withholding and reporting obligations.

Sec. 4.02. Documentation for Foreign Beneficiaries or Owners. WT may treat a direct beneficiary or owner as a foreign beneficial owner if the direct beneficiary or owner provides a Form W-8 that supports such status. WT may treat a direct beneficiary or owner that has provided a Form W-8 as entitled to a reduced rate of NRA withholding if all the requirements for a reduced rate are met and the Form W-8 provided by the direct beneficiary or owner supports entitlement to a reduced rate. Sections 4.03 through 4.06 of this Agreement describe the specific documentation requirements necessary for obtaining a reduced rate of withholding in certain circumstances.

Sec. 4.03. Treaty Claims. WT may not reduce the rate of withholding based on a direct beneficiary's or owner's claim of treaty benefits unless WT obtains from the beneficiary or owner a Form W-8BEN with Part II of the form properly completed, including the appropriate limitation on benefits and section 894 certifications.

Sec. 4.04. Documentation for International Organizations. WT may not treat a direct beneficiary or owner as an international organization entitled to an exemption from withholding under section 892 of the Code unless WT obtains a Form W-8EXP from the international organization and the name provided on the Form W-8EXP is the name of an entity designated as an international organization by executive order pursuant to 22 United States Code 288 through 288(f). If an international organization is not claiming benefits under section 892 of the Code but under another Code exception, the provisions of sections 4.02 of this Agreement apply rather than the provisions of this section 4.04.

Sec. 4.05. Documentation for Foreign Governments and Foreign Central Banks of Issue.

(**A**) **Documentation For a Foreign Government or Foreign Central Bank of Issue Claiming an Exemption From Withholding Under Section 892 or Section 895**. WT may not treat a direct beneficiary or owner as a foreign government or foreign central bank of issue exempt from withholding under section 892 or 895 of the Code unless—

(**1**) WT receives from the direct beneficiary or owner a Form W-8EXP establishing that the direct beneficiary or owner is a foreign government or foreign central bank of issue;

(**2**) The income distributed to, or included in the distributive share of, the direct beneficiary or owner is the type of income that qualifies for an exemption from withholding under section 892 or 895; and

(**3**) WT does not know, or have reason to know, that the direct beneficiary or owner is a controlled commercial entity, that the income owned by the foreign government or foreign central bank of issue is being received from a controlled commercial entity, or that the income is from the disposition of an interest in a controlled commercial entity.

(**B**) **Treaty Exemption**. WT may not treat a direct beneficiary or owner as a foreign government or foreign central bank of issue entitled to a reduced rate of withholding under an income tax treaty unless it obtains a Form W-8BEN that, under section 4.03 of this Agreement, is sufficient to obtain a reduced rate of withholding under a treaty.

(**C**) **Other Code Exception**. If a foreign government or foreign central bank of issue is not claiming benefits under section 892 or 895 of the Code but under another Code exception (*e.g.*, the portfolio interest exception under sections 871(h) or 881(c) of the Code), the provisions of section 4.02 of this Agreement apply rather than the provisions of this section 4.05.

Sec. 4.06. Documentation for Foreign Tax-Exempt Organizations.

(**A**) **Reduced Rate of Withholding Under Section 501**. WT may not treat a direct beneficiary or owner as a foreign organization described under section 501(c) of the Code, and therefore exempt from withholding (or, if the direct beneficiary or owner is a foreign private foundation, subject to withholding at a 4-percent rate under section 1443(b) of the Code) unless WT obtains a valid Form W-8EXP on which Part III of the form is completed.

(**B**) **Treaty Exemption**. WT may not treat a direct beneficiary or owner as a foreign organization that is tax exempt, or entitled to a reduced rate of withholding under an income tax treaty unless it obtains a Form W-8BEN from the beneficiary or owner that, under section 4.03 of this Agreement, is sufficient to obtain a reduced rate of withholding under a treaty.

(**C**) **Other Exceptions**. If a tax-exempt entity is not claiming a reduced rate of withholding because it is an organization described under section 501(c) of the Code or under an income tax treaty, but is

claiming a reduced rate of withholding under another Code exception, the provisions of section 4.02 of this Agreement apply rather than the provisions of this section 4.06.

Sec. 4.07. Documentation For Passthrough Beneficiaries or Owners. WT shall not act as a withholding foreign trust with respect to an amount subject to withholding distributed to, or included in the distributive share of, a passthrough beneficiary or owner. WT must forward that passthrough beneficiary's or owner's documentation (and associated withholding statement and documentation of indirect beneficiaries or owners) to the withholding agent from whom WT receives the amount subject to withholding. WT may act as a withholding foreign trust for payments made to beneficiaries or owners that are themselves withholding foreign trusts or withholding foreign partnerships.

Sec. 4.08. Documentation For U.S. Exempt Recipients. WT shall not treat a beneficiary or owner as a U.S. exempt recipient unless WT obtains from the beneficiary or owner a Form W-9 on which the beneficiary or owner writes "Exempt" in Part II of the Form.

Sec. 4.09. Documentation for U.S. Non-Exempt Recipients. WT shall not treat a beneficiary or owner as a U.S. non-exempt recipient unless WT obtains a Form W-9 from the beneficiary or owner.

Sec. 4.10. Documentation Validity. WT may not rely on Forms W-8 or W-9 if WT has actual knowledge or reason to know that the information or statements contained in the forms are unreliable or incorrect. Once WT knows, or has reason to know, that a Form W-8 or W-9 provided by a direct beneficiary or owner is unreliable or incorrect, WT must obtain a new Form W-8 or W-9 prior to the time withholding is required.

Sec. 4.11. Documentation Validity Period.

(**A**) **Form W-8**. WT may rely on a properly completed Form W-8 until its validity expires under Treas. Reg. § 1.1441–1(e)(4)(ii).

(**B**) **Form W-9**. WT may rely on a properly completed Form W-9 as long as it has not been informed by the IRS or another withholding agent that the form is unreliable.

Sec. 4.12. Maintenance and Retention of Documentation.

(**A**) **Maintaining Documentation**. WT shall maintain Forms W-8 and W-9 by retaining the original documentation, a certified copy, a photocopy, a microfiche, or by electronic storage or similar means of record retention.

(**B**) **Retention Period**. WT shall retain a direct beneficiary's or owner's Form W-8 or W-9 obtained under this section 4 for as long as it may be relevant to the determination of WT's tax liability under this agreement.

SECTION 5. WITHHOLDING FOREIGN TRUST WITHHOLDING CERTIFICATE

Sec. 5.01. WT Withholding Certificate. WT agrees to furnish a withholding foreign trust withholding certificate to each withholding agent from which it receives amounts subject to NRA withholding as a withholding foreign trust. The withholding foreign trust withholding certificate is a Form W-8IMY (or acceptable substitute form) that certifies that WT is acting as a withholding foreign trust, contains WT's WT-EIN, and provides all other information required by the form. WT is not required to disclose, as part of that Form W-8IMY or its withholding statement, any information regarding the identity of a direct beneficiary or owner.

Sec. 5.02. Withholding Statement. WT agrees to provide to each withholding agent from which WT receives amounts subject to NRA withholding as a withholding foreign trust a written statement (the "withholding statement") identifying the amounts for which WT acts as a withholding foreign trust. The statement forms an integral part of the Form W-8IMY. The withholding statement may be provided in any manner, and in any form, to which WT and the withholding agent mutually agree.

Sec. 5.03. Withholding Rate Pools. When it is acting as a withholding foreign trust, WT must assume withholding responsibility for amounts subject to withholding that are distributed to, or included in the distributive shares of, its direct beneficiaries or owners. Accordingly, withholding rate pool information is not required as part of WT's withholding statement.

SECTION 6. TAX RETURN OBLIGATIONS

Sec. 6.01. Form 1042 Filing Requirement.

(**A**) **In general**. WT shall file a return on Form 1042, whether or not WT withheld any amounts under chapter 3 of the Code, on or before March 15 of the year following any calendar year in which WT acts as a withholding foreign trust. In addition to the information specifically requested on Form 1042 and the accompanying instructions, WT shall attach a statement setting forth the amounts of any overwithholding or underwithholding adjustments made under Treas. Reg. § 1.1461–2 and sections 7.01 and 7.03 of this Agreement, and an explanation of the circumstances that resulted in the over- or under- withholding.

(**B**) **Extensions for Filing Returns**. WT may request an extension of the time for filing Form 1042, or any of the information required to be attached to the form, by submitting Form 2758, *Application for Extension of Time to File Certain Excise, Income, Information, and Other Returns*, on or before the due date of the return. The application must be in writing, properly signed by a duly authorized agent of WT, and shall clearly set forth the following:

(**1**) The calendar year for which the extension is requested; and

(**2**) A full explanation of the reason(s) for requesting the extension to assist the IRS in determining the period of extension, if any, that will be granted.

Sec. 6.02. Form 1042-S Reporting: General Rule. Unless WT has made a pooled reporting (PR) election pursuant to section 6.03 of this Agreement, WT is required to file separate Forms 1042-S for each direct beneficiary or owner to whom WT distributes, or in whose distributive share is included, an amount subject to NRA withholding. WT must file separate Forms 1042-S by income code, exemption code, recipient code, and withholding rate. WT must file its Forms 1042-S in the manner required by the regulations under chapter 3 of the Code and the instructions to the form, including any requirement to file the forms magnetically or electronically. Any Form 1042-S required by this section 6 shall be filed on

or before March 15 following the calendar year in which withholding, if any, was required under section 3.02 of this agreement. WT may request an extension of time to file Forms 1042-S by submitting Form 8809, *Request for Extension of Time to File Information Returns*, by the due date of Forms 1042-S in the manner required by Form 8809.

Sec. 6.03. Form 1042-S Reporting: Special Rule for PR Election. If WT has made the PR election pursuant to this section 6.03, WT is not required to file Forms 1042-S for amounts distributed to, or included in the distributive share of, each separate direct beneficiary or owner for whom such reporting would otherwise be required. Instead, WT shall file a separate Form 1042-S for each reporting pool. A reporting pool consists of income that falls within a particular withholding rate and within a particular income code, exemption code, and recipient code as determined on Form 1042-S. WT may use a single recipient code for all reporting pools except for amounts paid to foreign tax-exempt recipients, for which a separate recipient code must be used. For this purpose, a foreign tax-exempt recipient includes any organization that is not subject to NRA withholding and is not liable to tax in its country of residence because it is a charitable organization, a pension fund, or a foreign government. WT must make the PR election at the time this agreement is executed by signing the election statement on the signature page of this agreement. Once made, the PR election remains in effect for the entire term of this agreement beginning on the date the agreement becomes effective and ending on the date of its expiration or termination under section 9 of this Agreement. WT must make a new election for each renewal term of this agreement. If WT makes the PR election, WT cannot revoke it prior to the end of the term for which WT has made the PR election. If WT did not make the PR election at the time this agreement was executed, then WT may make a PR election only by terminating this agreement pursuant to section 9.03 and requesting to enter into a new agreement.

Sec. 6.04. Form 3520–A Filing Requirement. If WT is required to file Form 3520-A under section 6048 of the Code, then WT shall file Form 3520-A and furnish any required statements to U.S. beneficiaries or owners in accordance with the instructions for the form.

Sec. 6.05. Retention of Returns. WT shall retain 1042 and Form 3520-A, if required, for the period of the applicable statute of limitations on assessments and collection under the Code.

SECTION 7. ADJUSTMENTS FOR OVER- AND UNDER-WITHHOLDING; REFUNDS

Sec. 7.01. Adjustments for NRA Overwithholding by WT. WT may make an adjustment for amounts paid to its direct beneficiaries or owners that it has overwithheld under chapter 3 of the Code by applying either the reimbursement or set-off procedures described in this section within the time period prescribed for those procedures.

(**A**) **Reimbursement Procedure**. WT may repay its beneficiaries or owners for an amount overwithheld and reimburse itself by reducing, by the amount of tax actually repaid to the beneficiaries or owners, the amount of any subsequent deposit of tax required to be made by WT under section 3.03 of this Agreement. For purposes of this section 7.01(A), an amount that is overwithheld shall be applied in order of time to each of WT's subsequent deposit periods in the same calendar year to the extent that the withholding taxes required to be deposited for a subsequent deposit period exceed the amount actually deposited. An amount overwithheld in a calendar year may be applied to deposit periods in the calendar year following the calendar year of overwithholding only if:

(**1**) WT states on a Form 1042-S, filed by March 15 of the calendar year following the calendar year of overwithholding, the amount of tax withheld and the amount of any actual repayments; and

(**2**) WT states on a Form 1042, filed by March 15 of the calendar year following the calendar year of overwithholding, that the filing of the Form 1042 constitutes a claim for credit in accordance with Treas. Reg. § 1.6414–1.

(**B**) **Set-Off Procedure**. WT may repay its beneficiaries or owners by applying the amount overwithheld against any amount which otherwise would be required under chapter 3 of the Code to be withheld by WT before the earlier of March 15 of the calendar year following the calendar year of overwithholding or the date that the Form 1042-S is actually filed with the IRS. For purposes of making a return on Form 1042 or 1042-S for the calendar year of overwithholding, and for purposes of making a deposit of the amount withheld, the reduced amount shall be considered the amount required to be withheld from such income under chapter 3 of the Code.

Sec. 7.02. Collective Credit or Refund Procedures for NRA Overwithholding. If WT has made a PR election and it has overwithheld under chapter 3 of the Code on amounts subject to NRA withholding paid to WT's direct beneficiaries or owners during a calendar year and the amount has not been recovered under the reimbursement or set-off procedures under sections 7.01 of this Agreement, WT may request a credit or refund of the total amount overwithheld by following the procedures of this section 7.02. WT shall follow the procedures set forth under sections 6402 and 6414 of the Code, and the regulations thereunder, to claim the credit or refund. No credit or refund will be allowed after the expiration of the statutory period of limitation for refunds under section 6511 of the Code. WT may use the collective refund procedures under this section 7.02 only if the following conditions are met:

(**A**) WT must not have issued Forms 1042-S to the direct beneficiaries or owners who were subjected to overwithholding;

(**B**) WT must submit together with its amended return on which it claims a credit or refund a statement of the reason for the overwithholding;

(**C**) WT must submit together with its amended return on which it claims a credit or refund a statement that it has repaid the amount of overwithholding to the appropriate direct beneficiaries or owners prior to filing the claim for credit or refund; and

(**D**) WT must retain a record showing that it repaid the direct beneficiaries or owners the amount of the overwithholding.

Sec. 7.03. Adjustments for NRA Underwithholding. If WT knows that an amount should have been withheld under chapter 3 of the Code from a previous payment to a direct beneficiary or owner

but was not withheld, WT may either withhold from future payments made to the same direct beneficiary or owner or satisfy the tax from the direct beneficiary's or owner's proportionate share of assets over which it has control. The additional withholding or satisfaction of the tax owed may only be made before the due date of the Form 1042 (not including extensions) for the calendar year in which the underwithholding occurred.

Sec. 7.04. NRA Underwithholding after Form 1042 Filed. If, after a Form 1042 has been filed for a calendar year, WT, WT's external auditor, or the IRS determines that, due to WT's failure to carry out its obligations under this Agreement, WT has underwithheld tax for such year, WT shall file an amended Form 1042 to report and pay the underwithheld tax. WT shall pay the underwithheld tax, the interest due on the underwithheld tax, and any applicable penalties, at the time of filing the amended Form 1042. If WT fails to file an amended return, the IRS shall make such return under section 6020 of the Code.

Sec. 7.05. Special Rule Regarding Failure to Deposit Penalties. Solely for purposes of applying section 6656 of the Code (failure to make deposit of taxes), WT will not be considered to have made an underpayment of a deposit of NRA withholding taxes if the conditions of this paragraph are met. The conditions of this paragraph are that—

(**A**) WT makes its deposits within the time (deposit period) required by section 6302 of the Code;

(**B**) The deposit is not less than 90 percent of the aggregate amount of the tax required to be withheld under chapter 3 of the Code during the deposit period applicable to WT; and

(**C**) WT determines the difference between the total amount required to be deposited and the amount actually deposited as of the end of the 3rd, 6th, 9th, and 12th months of the calendar year and the difference is deposited no later than the 15th day of the second following month (*i.e.*, May 15, August 15, November 15 and February 15, respectively). In determining whether there has been an underpayment, reimbursements and set-offs shall be taken into account.

SECTION 8. EXTERNAL AUDIT PROCEDURES

Sec. 8.01. In General. Unless WT requests an IRS audit in lieu of an external audit, the IRS agrees not to conduct an on-site audit of WT with respect to withholding and reporting obligations covered by this Agreement provided that an external auditor designated in Appendix A of this Agreement conducts an audit of WT in accordance with this section 8. WT shall permit the external auditor to have access to all relevant records of WT for purposes of performing the external audit, including information regarding specific beneficiaries or owners. WT shall permit the IRS to communicate directly with the external auditor and to review the audit procedures followed by the external auditor. WT represents that there are no legal prohibitions that prevent the external auditor from examining any information relevant to the external audit to be performed under this section 8 and that there are no legal prohibitions that prevent the IRS from communicating directly with the auditor. WT shall permit the IRS to examine the external auditor's work papers and reports.

Sec. 8.02. Designation of External Auditor. WT's external auditor must be one of the auditors listed in Appendix A of this Agreement, unless WT and the IRS agree, prior to the audit, to substitute another auditor. WT shall not propose an external auditor unless it has a reasonable belief that the auditor is subject to laws, regulations, or rules that impose sanctions for failure to exercise its independence and to perform the audit competently. The IRS has the right to reject a proposed external auditor, or to revoke its acceptance of an external auditor, if the IRS, in its sole discretion, reasonably believes that the auditor is not independent or cannot perform an effective audit under this Agreement.

Sec. 8.03. Timing External Audits: General Rule. Unless WT has made a PR election, WT shall have the external auditor conduct an external audit only at such time and only for such calendar years as the IRS directs.

Sec. 8.04. Timing External Audits: Special Rule for PR Election. If WT has made a PR election, WT shall have the external auditor conduct an audit after the close of every other calendar year that this Agreement is in effect. The auditor shall examine the two previous calendar years. For example, the first audit will occur in the third calendar year that the agreement is in effect and the external auditor will examine calendar years one and two.

Sec. 8.05. Scope of External Audit. The external auditor shall verify whether WT is in compliance with this Agreement by conducting an audit that meets the requirements of this section 8.05. The report, described in section 8.06 of this Agreement, must disclose that the external auditor has, at a minimum, performed the following checks listed in this section 8.05, and set forth how each of those checks was performed and the results of the checks. WT's external auditor is encouraged to contact the IRS at the address set forth in section 10.06 of this Agreement and submit an audit plan (which includes, if relevant, the extent to which the external auditor proposes to rely on WT's internal audit procedures) prior to performing the audit so that the audit may be conducted in the most efficient and least costly manner possible.

(**A**) **Documentation**. The external auditor must review information contained in beneficiary or owner files to determine whether the documentation requirements of section 4 of this Agreement are being met.

(**B**) **Withholding Responsibilities**. The external auditor must—

(**1**) Perform test checks of direct beneficiaries or owners, to verify that WT is withholding the proper amounts.

(**2**) Verify that amounts withheld were timely deposited in accordance with section 3.03 of this Agreement.

(**C**) **Return Filing and Information Reporting**. The external auditor must-

(**1**) Obtain copies of original and amended Forms 1042, and any schedules, statements, or attachments required to be filed with those forms, and determine whether the amounts of income, taxes, and other information reported on those forms are accurate by—

(**i**) Reviewing work papers;

(**ii**) Reviewing Forms W-8IMY, together with the associated withholding statements, that WT has provided to withholding agents;

(**iii**) Reviewing copies of Forms 1042-S that withholding agents have provided WT;

(**iv**) Reviewing account statements from withholding agents;

(**v**) Reviewing correspondence between WT and withholding agents; and

(**vi**) Interviewing personnel responsible for preparing the Form 1042 and the work papers used to prepare those forms.

(**2**) Obtain copies of original and corrected Forms 1042-S and Forms 3520-A together with the work papers used to prepare those forms and determine whether the amounts reported on those forms are accurate by—

(**i**) Reviewing the Forms 1042-S received from withholding agents;

(**ii**) Reviewing a valid sample of earnings statements issued by WT to direct beneficiaries or owners, if any.

(**3**) Thoroughly review the statements attached to amended Forms 1042 filed to claim a refund, ascertain their veracity, and determine the causes of any overwithholding reported and ensure WT did not issue Forms 1042-S to persons whom it included as part of its collective credit or refund.

(**4**) Determine, in the case of collective credits or refunds, that WT repaid the appropriate beneficiaries or owners prior to requesting a collective refund or credit.

(**E**) **Change in Circumstances**. The external auditor must verify that in the course of the audit it has not discovered any significant change in circumstances, as described in section 9.05 (A) or (D) of this Agreement.

Sec. 8.06. External Auditor's Report. Upon completion of the audit of WT, the external auditor shall issue a report, or reports, of audit findings directly to the IRS by sending the original report to the IRS at the address set forth in section 10.06 of this Agreement. This report is due by December 31 following the calendar year being audited, or if that date falls on a Saturday or Sunday, the next U.S. business day. The IRS may, however, upon request by the external auditor, extend the due date of the audit report upon good cause. The report must be in writing, in English, and currency amounts must be stated in U.S. dollars. The report must fully describe the scope of the audit, the methodologies (including sampling techniques) used to determine whether WT is in compliance with the provisions of this Agreement, and the result of each such determination. The report must also specifically address each of the items in section 8.05 of this Agreement.

Sec. 8.07. Expanding Scope and Timing of External Audit. Upon review of the external auditor's report, the IRS may request, and WT must permit, the external auditor to perform additional audit procedures.

SECTION 9. EXPIRATION, TERMINATION AND DEFAULT

Sec. 9.01. Term of Agreement: General Rule. If WT has not made a PR election, this Agreement shall be in effect on ________________ and shall continue in force until terminated under 9.03 or 9.04 of this Agreement.

Sec. 9.02. Term of Agreement: Special Rule for PR Election. If WT has made a PR election, this Agreement shall be in effect on ______________ and shall expire on December 31 of the fifth full calendar year after the year in which this Agreement first takes effect. This Agreement may be renewed for additional terms as provided in section 9.08 of this Agreement.

Sec. 9.03. Termination of Agreement. This Agreement may be terminated by either the IRS or WT prior to the end of its term by delivery of a notice of termination to the other party in accordance with section 10.06 of this Agreement. The IRS, however, shall not terminate the Agreement unless there has been a significant change in circumstances, as defined in section 9.05 of this Agreement, or an event of default has occurred, as defined in section 9.06 of this Agreement, and the IRS determines, in its sole discretion, that the significant change in circumstances or the event of default warrants termination of this Agreement. In addition, the IRS shall not terminate this Agreement in the event of default if WT can establish to the satisfaction of the IRS that all events of default for which it has received notice have been cured within the time period agreed upon. The IRS shall notify WT, in accordance with section 9.07 of this Agreement, that an event of default has occurred and that the IRS intends to terminate the Agreement unless WT cures the default. A notice of termination sent by either party shall take effect on the date specified in the notice.

Sec 9.04. Automatic Termination of Agreement. Notwithstanding Section 9.03 of this Agreement, this Agreement will terminate automatically in the event that the external auditor or the IRS discovers that WT was not in possession of Forms W-8 or W-9, as applicable, for any direct beneficiary or owner at any time that withholding or reporting was required under section 3.02 of this agreement. The automatic termination will be effective as of December 31 of the year in which the external auditor or the IRS makes such discovery. This Agreement will be reinstated, effective the same date it was automatically terminated, if WT obtains appropriate Forms W-8 or W-9 (that relate to the time withholding or reporting was required) for each such partner before January 31 of the year following the year in which the agreement automatically terminated. In the event of automatic termination of this agreement, WT must pay any underwithholding of tax, interest, and penalties that the IRS determines is attributable to each undocumented direct beneficiary or owner for the period during which the beneficiary or owner was undocumented, and, if WT has made a PR election, WT must file beneficiary or owner specific Forms 1042-S for every foreign direct beneficiary or owner from the earliest time the Forms W-8 or W-9 were required for any undocumented direct beneficiary or owner through the date of termination. After the date of automatic termination of this agreement, WT may not act as a withholding foreign trust, and must so notify any persons to which WT has furnished a withholding foreign trust certificate. After the date of automatic termination of this agreement, the IRS may reinstate this agreement (or the IRS may require WT to enter into a new withholding foreign trust agreement) on such terms and conditions and with such modifications as the IRS may determine.

Sec. 9.05. Significant Change in Circumstances. For purposes of this Agreement, a significant change in circumstances includes, but is not limited to—

(**A**) A change in U.S. federal law or policy, or applicable foreign law or policy, that affects the validity of any provision of this Agreement, materially

affects the procedures contained in this Agreement, or affects WT's ability to perform its obligations under this Agreement;

(**B**) A ruling of any court that affects the validity of any provision of this Agreement; or

(**C**) A significant change in WT's business practices that affects WT's ability to meet its obligations under this Agreement.

Sec. 9.06. Events of Default. For purposes of this Agreement, an event of default occurs if WT fails to perform any material duty or obligation required under this Agreement, and includes, but is not limited to, the occurrence of any of the following:

(**A**) WT fails to implement adequate procedures, accounting systems, and internal controls to ensure compliance with this Agreement;

(**B**) WT underwithholds an amount that WT is required to withhold under chapter 3 of the Code and fails to correct the underwithholding or to file an amended Form 1042 reporting, and paying, the appropriate tax;

(**C**) WT makes excessive refund claims;

(**D**) WT fails to file Forms 1042, 1042-S, 3520-A (if required), 1041 (if required), and Schedules K-1 (if required) by the due date specified on such forms or files forms or schedules that are materially incorrect or fraudulent;

(**E**) WT fails to have an external audit performed when required, WT's external auditor fails to provide its report directly to the IRS on a timely basis, WT fails to cooperate with the external auditor, or WT or its external auditor fails to cooperate with the IRS;

(**F**) WT fails to inform the IRS within 90 days of any significant change in its business practices to the extent that change affects WT's obligations under this Agreement;

(**G**) WT fails to cure a default identified by the IRS or by an external auditor;

(**H**) WT makes any fraudulent statement or a misrepresentation of material fact with regard to this Agreement to the IRS, a withholding agent, or WT's external auditor;

(**I**) The IRS determines that WT's external auditor is not sufficiently independent to adequately perform its audit function or the external auditor fails to provide an audit report that complies with section 8 of this Agreement;

(**J**) WT is prohibited by any law from disclosing the identity of a beneficiary or owner or beneficiary or owner information to WT's external auditor;

(**K**) WT fails to make deposits in the time and manner required by section 3.03 of this Agreement or fails to make adequate deposits, taking into account the procedures of 7.05 of this Agreement; or

(**L**) WT fails to permit the external auditor to perform additional audit procedures under the provisions of section 8.07 of this Agreement.

Sec. 9.07. Notice and Cure. Upon the occurrence of an event of default, the IRS may deliver to WT a notice of default specifying the event of default that has occurred. WT shall respond to the notice of default within 60 days (60-day response) from the date of the notice of default. The 60-day response shall contain an offer to cure the event of default and the time period in which the cure will be accomplished or shall state the reasons why WT does not agree that an event of default has occurred. If WT does not provide a 60-day response, the IRS may deliver a notice of termination as provided in section 9.03 of this Agreement. If WT provides a 60-day response, the IRS shall either accept or reject WT's statement that no default has occurred or accept or reject WT's proposal to cure an event of default. If the IRS rejects WT's contention that no default has occurred or rejects WT's proposal to cure a default, the IRS will offer a counter-proposal to cure the event of default. Within 30 days of receiving the IRS's counter-proposal, WT shall notify the IRS (30-day response) whether it continues to maintain that no default has occurred or whether it rejects the IRS's counter-proposal to cure an event of default. If WT's 30-day response states that no default has occurred or it rejects the IRS's counter-proposal to cure, the parties shall seek to resolve their disagreement within 30 days of the IRS's receipt of WT's 30-day response. If a satisfactory resolution has not been achieved at the end of this latter 30-day period, or if WT fails to provide a 30-day response, the IRS may terminate this Agreement by providing a notice of termination in accordance with section 9.03 of this Agreement. If WT receives a notice of termination from the IRS, it may appeal the determination within 30 days of the date of the notice of termination by sending a written notice to the address specified in section 10.06 of this Agreement. If WT appeals the notice of termination, this Agreement shall not terminate until the appeal has been decided. If an event of default is discovered in the course of an external audit, the WT may cure the default, without following the procedures of this section 9.07, if the external auditor's report describes the default and the actions that WT took to cure the default and the IRS determines that the cure procedures followed by WT were sufficient. If the IRS determines that WT's actions to cure the default were not sufficient, the IRS shall issue a notice of default and the procedures described in this section 9.07 shall be followed.

Sec. 9.08. Renewal. If WT has made the PR election under section 6.03 of this agreement and intends to renew this Agreement for an additional term, it shall submit an application for renewal to the IRS no earlier than one year and no later than six months prior to the expiration of this Agreement. Any such application for renewal must contain an update of the information provided by WT to the IRS in connection with the application to enter into this Agreement, and any other information the IRS may request in connection with the renewal process. This Agreement shall be renewed only upon the signatures of both WT and the IRS. Either the IRS or WT may seek to negotiate a new withholding foreign trust agreement rather than renew this Agreement.

SECTION 10. MISCELLANEOUS PROVISIONS

Sec. 10.01. WT's application to become a withholding foreign trust and the Appendix to this Agreement are hereby incorporated into and made an integral part of this Agreement. This Agreement, WT's application, and the Appendix to this Agreement constitute the complete agreement between the parties.

Sec. 10.02. This Agreement may be amended by the IRS if the IRS determines that such amendment is needed for the sound administration of the internal

revenue laws or internal revenue regulations. The agreement may also be modified by either WT or the IRS upon mutual agreement. Such amendments or modifications shall be in writing.

Sec. 10.03. Any waiver of a provision of this Agreement is a waiver solely of that provision. The waiver does not obligate the IRS to waive other provisions of this Agreement or the same provision at a later date.

Sec. 10.04. This Agreement shall be governed by the laws of the United States. Any legal action brought under this Agreement shall be brought only in a U.S. court with jurisdiction to hear and resolve matters under the internal revenue laws of the United States. For this purpose, WT agrees to submit to the jurisdiction of such U.S. court.

Sec. 10.05. WT's rights and responsibilities under this Agreement cannot be assigned to another person.

Sec. 10.06. Notices provided under this Agreement shall be mailed registered, first class airmail. Notice shall be directed as follows:

To the IRS:

Internal Revenue Service
LMSB:FS:QI
290 Broadway
New York, NY 10007–1867
USA

All notices sent to the IRS must include the WT's WT-EIN.

To WT:

____
____
____
____

Sec. 10.07. WT, acting in its capacity as a withholding foreign trust or in any other capacity, does not act as an agent of the IRS, nor does it have the authority to hold itself out as an agent of the IRS.

IN WITNESS WHEREOF, the above parties have subscribed their names to these presents, in duplicate.

Signed this day of ,

____

(name and title of person signing for WT)

____

(name and title of person signing for IRS)

PR Election Statement

By signing hereunder, WT makes the PR election under section 6.03 of this Agreement.

____

(name and title of person signing for WT)

Appendix A

WT and the IRS agree that any of the following auditors may be used by WT to perform the external audits required by section 8 of this Agreement.
[Names, addresses, telephone and fax numbers of external auditors.]

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26 CFR 601.201: Rulings and determination letters. (Also, Part I, §§ 401; 1.401(a)(9)–1.)

Rev. Proc. 2002–29

SECTION 1. PURPOSE

This revenue procedure provides that qualified retirement plans generally must be amended by the end of the first plan year beginning on or after January 1, 2003, to the extent necessary to comply with final and temporary regulations under § 401(a)(9) of the Internal Revenue Code, relating to required minimum distributions. The revenue procedure contains model plan amendments that sponsors of master and prototype (M&P), volume submitter and individually designed plans may adopt to satisfy this requirement. The revenue procedure also provides that determination letter applications filed on or after the first day of the 2003 plan year will be reviewed with respect to whether the form of the plan satisfies the requirements of the final and temporary regulations under § 401(a)(9).

SECTION 2. BACKGROUND

.01 Section 401(a)(9) provides rules for required minimum distributions from plans qualified under § 401(a). The rules also apply to § 403(b) annuity contracts, § 408 IRAs, § 408A Roth IRAs, and § 457 eligible deferred compensation plans.

.02 Proposed regulations (EE–113–82, 1987–2 C.B. 881) under § 401(a)(9) were published in the **Federal Register** on July 27, 1987, 52 FR 28070, and January 17, 2001, 66 FR 3928. The proposed regulations published in 2001 (the § 401(a)(9) 2001 Proposed Regulations) substantially simplified many of the rules in regulations that had been proposed in 1987 (the § 401(a)(9) 1987 Proposed Regulations) and also incorporated other guidance published after 1987, including guidance relating to the changes to § 401(a)(9) made by the Small Business Job Protection Act of 1996, Pub. L. 104–188 (SBJPA).

.03 The preamble to the § 401(a)(9) 2001 Proposed Regulations stated that taxpayers could rely on the § 401(a)(9) 1987 Proposed Regulations or the § 401(a)(9) 2001 Proposed Regulations for determining required minimum distributions for calendar year 2001 and subsequent calendar years prior to the effective date of the final regulations. The preamble also contained a model amendment that sponsors of qualified plans could adopt if they wished to apply the § 401(a)(9) 2001 Proposed Regulations in making all required minimum distributions for 2001 and subsequent calendar years prior to the effective date of the final regulations. After publication in the **Federal Register**, the model amendment was republished in Announcement 2001–18, 2001–1 C.B. 791, with minor corrections, and appeared (as corrected in the I.R.B.) in the preamble to the § 401(a)(9) 2001 Proposed Regulations (REG–130477–00; REG–130481–00, 2001–1 C.B. 865).

.04 An alternative model amendment was published in Announcement 2001–82, 2001–32 I.R.B. 123. This additional model amendment was provided in response to the concerns of qualified plan sponsors that intended to use the § 401(a)(9) 2001 Proposed Regulations for distributions for 2001 but made required minimum distributions for 2001 under the § 401(a)(9) 1987 Proposed Regulations prior to the date in 2001 on which the plan began operating under the § 401(a)(9) 2001 Proposed Regulations. The alternative model amendment in Announcement 2001–82 allowed required minimum distributions made for 2001 prior to the date in 2001 on which the

plan began operating under the § 401(a)(9) 2001 Proposed Regulations to be made under the § 401(a)(9) 1987 Proposed Regulations.

.05 The alternative model amendment in Announcement 2001–82 provided the following rules with respect to distributees who received 2001 required distributions prior to the date in 2001 on which the plan began operating under the § 401(a)(9) 2001 Proposed Regulations. If the total amount of 2001 required minimum distributions made to a participant prior to the date on which the plan began operating in accordance with the § 401(a)(9) 2001 Proposed Regulations equaled or exceeded the required minimum distributions determined under the § 401(a)(9) 2001 Proposed Regulations, then no additional distributions were required for that participant for 2001 on or after such date. If the total amount of 2001 required minimum distributions made to a participant prior to the date on which the plan began operating in accordance with the § 401(a)(9) 2001 Proposed Regulations was less than the amount determined under the § 401(a)(9) 2001 Proposed Regulations, then required minimum distributions for 2001 on and after such date would be determined so that the total amount of required minimum distributions for 2001 for that participant would be the amount determined under the § 401(a)(9) 2001 Proposed Regulations.

.06 In order for a qualified plan sponsor to use either the original model amendment in Announcement 2001–18 or the alternative model amendment in Announcement 2001–82, the plan sponsor was required to adopt the amendment by the deadline for amending its plan for GUST. See Rev. Proc. 2001–55, 2001–49 I.R.B. 552.

.07 Final and temporary regulations (T.D. 8987, 2002–19 I.R.B. 852) under § 401(a)(9) were published in the Federal Register on April 17, 2002, 74 FR 18987 (the § 401(a)(9) Final and Temporary Regulations). The § 401(a)(9) Final and Temporary Regulations generally adopt the simplifications proposed in 2001 and provide additional simplifications. The § 401(a)(9) Final and Temporary regulations apply for determining required minimum distributions for calendar years beginning on or after January 1, 2003. For determining required minimum distributions for calendar year 2002, taxpayers may rely on the § 401(a)(9) Final and Temporary Regulations, the § 401(a)(9) 2001 Proposed Regulations, or the § 401(a)(9) 1987 Proposed Regulations.

.08 Section 401(b) and the regulations thereunder provide a remedial amendment period during which an amendment to a disqualifying provision may be made retroactively effective, under certain circumstances, to comply with the requirements of § 401(a). Section 1.401(b)–1(b) provides that a disqualifying provision includes an amendment to an existing plan that causes the plan to fail to satisfy the requirements of § 401(a). Notice 2001–42, 2001–30 I.R.B. 70, provides a remedial amendment period under § 401(b) ending not prior to the last day of the first plan year beginning on or after January 1, 2005, in which any needed retroactive amendment with regard to the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107–16, (EGTRRA), may be adopted. The availability of this remedial amendment period is conditioned on the adoption of a good faith EGTRRA plan amendment no later than the later of: (i) the end of the plan year in which the EGTRRA change in the qualification requirement is required to be, or is optionally, put into effect under the plan; or (ii) the end of the GUST remedial amendment period for the plan.

.09 Rev. Proc. 2000–20, 2000–1 C.B. 553, as modified by Rev. Proc. 2000–27, 2000–1 C.B. 1272, Notice 2001–42, 2001–30 I.R.B. 70, and Rev. Proc. 2001–55, contains the Service's procedures for issuing opinion letters regarding the acceptability of the form of M&P plans.

.10 Rev. Proc. 2002–6, 2002–1 I.R.B. 203, contains the Service's procedures for issuing determination letters on the qualified status of employee plans under §§ 401(a), 403(a), 409 and 4975(e)(7) of the Code and the exempt status of related trusts or custodial accounts under § 501(a).

.11 Section 1.401(a)(9)–1, Q&A–3, describes the provisions that a plan must contain in order to satisfy § 401(a)(9). The plan must generally set forth the statutory rules of § 401(a)(9), including the incidental death benefit requirement in § 401(a)(9)(G), and must provide that distributions must be made in accordance with the § 401(a)(9) Final and Temporary Regulations. The plan must provide that its provisions reflecting § 401(a)(9) override any inconsistent distribution options in the plan and must include such other provisions as the Commissioner may prescribe in guidance published in the Internal Revenue Bulletin.

SECTION 3. REQUIRED PLAN AMENDMENTS

.01 In general, qualified plans must be amended by the last day of the first plan year beginning on or after January 1, 2003, to the extent necessary to comply with the requirements of the § 401(a)(9) Final and Temporary Regulations. Whether and the extent to which a particular plan must be amended depends on the plan's current terms. Any plan amendments for the § 401(a)(9) Final and Temporary Regulations must apply in determining required minimum distributions under the plan for calendar years beginning on or after January 1, 2003. If a plan sponsor begins operating its plan under the § 401(a)(9) Final and Temporary Regulations on a date in 2002, then the amendments must also apply in determining required minimum distributions under the plan for 2002 that are made on or after such date, although the amendments are not required to be adopted before the last day of the first plan year beginning on or after January 1, 2003.

.02 If a plan sponsor begins operating its plan under the § 401(a)(9) Final and Temporary Regulations on a date in 2002 and prior to such date the plan sponsor has made required minimum distributions for 2002 under the § 401(a)(9) 1987 Proposed Regulations or the § 401(a)(9) 2001 Proposed Regulations, then the plan must also be amended to provide the transitional rule for 2002 required minimum distributions that is set forth in section 1.2 of the model amendments in the Appendix to this revenue procedure.

.03 Every M&P plan must allow the M&P plan sponsor to amend the plan on behalf of all adopting employers so that changes in the Code, regulations, revenue rulings, other statements published by the Internal Revenue Service, or corrections of prior approved plans may be applied to all employers who have adopted the plan. Therefore, by December 31, 2003, every sponsor of an M&P plan must amend its

plan to the extent necessary to comply with the requirements of the § 401(a)(9) Final and Temporary Regulations and must furnish copies of the amendments to all employers who have adopted the plan. A favorable opinion letter may not be relied upon after December 31, 2003, unless the M&P plan sponsor satisfies this requirement.

.04 Practitioners that sponsor volume submitter plans generally are not authorized to amend the plan on behalf of adopting employers. In this case, employers that have adopted the plan must individually amend their plans by the last day of the first plan year beginning on or after January 1, 2003, to the extent necessary to comply with the requirements of the § 401(a)(9) Final and Temporary Regulations. Nevertheless, volume submitter practitioners must amend their specimen plans for the § 401(a)(9) Final and Temporary Regulations by December 31, 2003, so that the amendments will apply to future adopters of the plan. A favorable advisory letter may not be relied upon after December 31, 2003, unless the volume submitter practitioner satisfies this requirement.

.05 Until further notice, sponsors of pre-approved plans are not required to request opinion or advisory letters that consider whether their plans satisfy the requirements of the § 401(a)(9) Final and Temporary Regulations. However, opinion and advisory letter applications filed on or after January 1, 2003, will be reviewed with respect to whether the form of the plan satisfies these requirements. Opinion and advisory letter applications filed before January 1, 2003, will be reviewed with respect to whether the form of the plan satisfies the requirements of the § 401(a)(9) Final and Temporary Regulations if a plan amendment to comply with the § 401(a)(9) Final and Temporary Regulations is submitted in conjunction with and at the same time as the request for the opinion or advisory letter.

.06 Determination letter applications for individually designed plans filed on or after the first day of the first plan year beginning on or after January 1, 2003, will be reviewed with respect to whether the form of the plan satisfies the requirements of the § 401(a)(9) Final and Temporary Regulations. Determination letter applications for individually designed plans filed before the first day of the first plan year beginning on or after January 1, 2003, will be reviewed with respect to whether the form of the plan satisfies the requirements of the § 401(a)(9) Final and Temporary Regulations if a plan amendment to comply with the § 401(a)(9) Final and Temporary Regulations is submitted in conjunction with and at the same time as the request for the determination letter. In both cases, determination letters issued for such applications may be relied on with respect to the requirements of the § 401(a)(9) Final and Temporary Regulations. Determination letters issued for pre-approved plans may be relied on with respect to the requirements of the § 401(a)(9) Final and Temporary Regulations if those requirements were considered in issuing the opinion or advisory letter.

.07 If a plan is timely amended to comply with the § 401(a)(9) Final and Temporary Regulations and, as a result of the amendment, there is a disqualifying provision under § 401(b), the remedial amendment period with respect to the disqualifying provision will end at the end of the EGTRRA remedial amendment period. Therefore, an application for a determination letter regarding the effect of the plan amendment need not be filed earlier than the last day of the EGTRRA remedial amendment period. The timely adoption of the appropriate model amendment in the Appendix will provide reliance, without the need to request a letter, that the plan has been amended to comply with the § 401(a)(9) Final and Temporary Regulations and will not result in a disqualifying provision.

.08 The Appendix provides two model plan amendments to facilitate the amendment of qualified plans to comply with the requirements of the § 401(a)(9) Final and Temporary Regulations. The model amendments may be adopted by M&P plans sponsors and volume submitter practitioners and also by sponsors of individually designed plans. The model amendments are "snap-on" amendments designed to work with a plan's existing minimum distribution provisions by superseding those that are inconsistent with the provisions of the model amendment and retaining those (such as the plan's definition of required beginning date) that are not inconsistent. Plans that are amended to adopt the model amendments must retain their existing required minimum distribution provisions in order to have reliance that the form of the plan has been properly amended to comply with the § 401(a)(9) Final and Temporary Regulations. Adoption of one of the model amendments will not amend a plan for the changes to § 401(a)(9) made by § 1404 of SBJPA or to provide that 2001 or 2002 required minimum distributions will be determined in accordance with the § 401(a)(9) 2001 Proposed Regulations.

The first model amendment is for defined contribution plans. The second model amendment is for defined benefit plans. A plan sponsor or a sponsor of a pre-approved plan that timely adopts the appropriate model amendment verbatim (or with only minor changes) will have reliance that the form of its plan satisfies the requirements of the § 401(a)(9) Final and Temporary Regulations, and the adoption of the model amendment will not adversely affect the plan sponsor's reliance on a favorable determination, opinion or advisory letter, or cause a pre-approved plan to be treated as an individually designed plan. For this purpose, changes to either of the model amendments to incorporate the adoption agreement elective provisions into the body of the amendment or to remove the elective provisions in favor of the default rules in the body of the amendment are minor changes.

SECTION 4. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 2000–20 and Rev. Proc. 2002–6 are modified.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective June 17, 2002.

DRAFTING INFORMATION

The principal authors of this revenue procedure are James Flannery and Steven Linder of Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue procedure, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 between the hours of 8:00 a.m. and 6:30 p.m. Eastern

time, Monday through Friday (a toll-free number). Mr. Flannery and Mr. Linder may be reached at 1–202–283–9888 (not a toll-free call).

APPENDIX — MODEL AMENDMENTS

The following are model plan amendments that sponsors of pre-approved plans and sponsors of individually designed plans may adopt to comply with the § 401(a)(9) Final and Temporary Regulations. Except as provided below, a plan that is amended to adopt one of the model amendments will satisfy, in form, the requirements of § 401(a)(9) and the § 401(a)(9) Final and Temporary Regulations in determining required minimum distributions for calendar years beginning on or after January 1, 2003 (as well as required minimum distributions for calendar year 2002 made on or after the date the plan sponsor begins to operate its plan in accordance with the § 401(a)(9) Final and Temporary Regulations). Adoption of the model amendments will not amend a plan to reflect the change to the definition of required beginning date in § 401(a)(9)(C) that was made by § 1404 of SBJPA or to provide the actuarial adjustment that may be required in a defined benefit plan that is so amended. A plan sponsor that wishes to amend its plan to reflect the provisions of § 1404 of SBJPA must do so through a separate amendment. Consequently, the model amendments may not be relied upon with respect to whether a plan's definition of required beginning date is correct or whether a defined benefit plan makes the correct actuarial adjustment required by § 401(a)(9)(C)(iii). Adoption of the model amendments also will not amend a plan to provide that 2001 or 2002 required minimum distributions will be determined in accordance with the § 401(a)(9) 2001 Proposed Regulations. A plan sponsor that has operated its plan in accordance with the § 401(a)(9) 2001 Proposed Regulations must adopt the model amendment in Announcement 2001–18 or the alternative model amendment in Announcement 2001–82 within the plan's GUST remedial amendment period. Plans that are amended to adopt the model amendments must retain their existing required minimum distribution provisions in order to have reliance that the form of the plan has been properly amended to comply with the § 401(a)(9) Final and Temporary Regulations.

MODEL PLAN AMENDMENT 1 — DEFINED CONTRIBUTION PLANS

Article _______. MINIMUM DISTRIBUTION REQUIREMENTS.

Section 1. General Rules

1.1. Effective Date. Unless an earlier effective date is specified in the adoption agreement, the provisions of this article will apply for purposes of determining required minimum distributions for calendar years beginning with the 2003 calendar year.

1.2. Coordination with Minimum Distribution Requirements Previously in Effect. If the adoption agreement specifies an effective date of this article that is earlier than calendar years beginning with the 2003 calendar year, required minimum distributions for 2002 under this article will be determined as follows. If the total amount of 2002 required minimum distributions under the plan made to the distributee prior to the effective date of this article equals or exceeds the required minimum distributions determined under this article, then no additional distributions will be required to be made for 2002 on or after such date to the distributee. If the total amount of 2002 required minimum distributions under the plan made to the distributee prior to the effective date of this article is less than the amount determined under this article, then required minimum distributions for 2002 on and after such date will be determined so that the total amount of required minimum distributions for 2002 made to the distributee will be the amount determined under this article.

1.3. Precedence. The requirements of this article will take precedence over any inconsistent provisions of the plan.

1.4. Requirements of Treasury Regulations Incorporated. All distributions required under this article will be determined and made in accordance with the Treasury regulations under section 401(a)(9) of the Internal Revenue Code.

1.5. TEFRA Section 242(b)(2) Elections. Notwithstanding the other provisions of this article, distributions may be made under a designation made before January 1, 1984, in accordance with section 242(b)(2) of the Tax Equity and Fiscal Responsibility Act (TEFRA) and the provisions of the plan that relate to section 242(b)(2) of TEFRA.

Section 2. Time and Manner of Distribution.

2.1. Required Beginning Date. The participant's entire interest will be distributed, or begin to be distributed, to the participant no later than the participant's required beginning date.

2.2. Death of Participant Before Distributions Begin. If the participant dies before distributions begin, the participant's entire interest will be distributed, or begin to be distributed, no later than as follows:

(a) If the participant's surviving spouse is the participant's sole designated beneficiary, then, except as provided in the adoption agreement, distributions to the surviving spouse will begin by December 31 of the calendar year immediately following the calendar year in which the participant died, or by December 31 of the calendar year in which the participant would have attained age 70½, if later.

(b) If the participant's surviving spouse is not the participant's sole designated beneficiary, then, except as provided in the adoption agreement, distributions to the designated beneficiary will begin by December 31 of the calendar year immediately following the calendar year in which the participant died.

(c) If there is no designated beneficiary as of September 30 of the year following the year of the participant's death, the participant's entire interest will be distributed by December 31 of the calendar year containing the fifth anniversary of the participant's death.

(d) If the participant's surviving spouse is the participant's sole designated beneficiary and the surviving spouse dies after the participant but before distributions to the surviving spouse begin, this section 2.2, other than section 2.2(a), will apply as if the surviving spouse were the participant.

For purposes of this section 2.2 and section 4, unless section 2.2(d) applies, distributions are considered to begin on the participant's required beginning date. If section 2.2(d) applies, distributions are

considered to begin on the date distributions are required to begin to the surviving spouse under section 2.2(a). If distributions under an annuity purchased from an insurance company irrevocably commence to the participant before the participant's required beginning date (or to the participant's surviving spouse before the date distributions are required to begin to the surviving spouse under section 2.2(a)), the date distributions are considered to begin is the date distributions actually commence.

2.3. Forms of Distribution. Unless the participant's interest is distributed in the form of an annuity purchased from an insurance company or in a single sum on or before the required beginning date, as of the first distribution calendar year distributions will be made in accordance with sections 3 and 4 of this article. If the participant's interest is distributed in the form of an annuity purchased from an insurance company, distributions thereunder will be made in accordance with the requirements of section 401(a)(9) of the Code and the Treasury regulations.

Section 3. Required Minimum Distributions During Participant's Lifetime.

3.1. Amount of Required Minimum Distribution For Each Distribution Calendar Year. During the participant's lifetime, the minimum amount that will be distributed for each distribution calendar year is the lesser of:

(a) the quotient obtained by dividing the participant's account balance by the distribution period in the Uniform Lifetime Table set forth in section 1.401(a)(9)–9 of the Treasury regulations, using the participant's age as of the participant's birthday in the distribution calendar year; or

(b) if the participant's sole designated beneficiary for the distribution calendar year is the participant's spouse, the quotient obtained by dividing the participant's account balance by the number in the Joint and Last Survivor Table set forth in section 1.401(a)(9)–9 of the Treasury regulations, using the participant's and spouse's attained ages as of the participant's and spouse's birthdays in the distribution calendar year.

3.2. Lifetime Required Minimum Distributions Continue Through Year of Participant's Death. Required minimum distributions will be determined under this section 3 beginning with the first distribution calendar year and up to and including the distribution calendar year that includes the participant's date of death

Section 4. Required Minimum Distributions After Participant's Death.

4.1. Death On or After Date Distributions Begin.

(a) Participant Survived by Designated Beneficiary. If the participant dies on or after the date distributions begin and there is a designated beneficiary, the minimum amount that will be distributed for each distribution calendar year after the year of the participant's death is the quotient obtained by dividing the participant's account balance by the longer of the remaining life expectancy of the participant or the remaining life expectancy of the participant's designated beneficiary, determined as follows:

(1) The participant's remaining life expectancy is calculated using the age of the participant in the year of death, reduced by one for each subsequent year.

(2) If the participant's surviving spouse is the participant's sole designated beneficiary, the remaining life expectancy of the surviving spouse is calculated for each distribution calendar year after the year of the participant's death using the surviving spouse's age as of the spouse's birthday in that year. For distribution calendar years after the year of the surviving spouse's death, the remaining life expectancy of the surviving spouse is calculated using the age of the surviving spouse as of the spouse's birthday in the calendar year of the spouse's death, reduced by one for each subsequent calendar year.

(3) If the participant's surviving spouse is not the participant's sole designated beneficiary, the designated beneficiary's remaining life expectancy is calculated using the age of the beneficiary in the year following the year of the participant's death, reduced by one for each subsequent year.

(b) No Designated Beneficiary. If the participant dies on or after the date distributions begin and there is no designated beneficiary as of September 30 of the year after the year of the participant's death, the minimum amount that will be distributed for each distribution calendar year after the year of the participant's death is the quotient obtained by dividing the participant's account balance by the participant's remaining life expectancy calculated using the age of the participant in the year of death, reduced by one for each subsequent year.

4.2. Death Before Date Distributions Begin.

(a) Participant Survived by Designated Beneficiary. Except as provided in the adoption agreement, if the participant dies before the date distributions begin and there is a designated beneficiary, the minimum amount that will be distributed for each distribution calendar year after the year of the participant's death is the quotient obtained by dividing the participant's account balance by the remaining life expectancy of the participant's designated beneficiary, determined as provided in section 4.1.

(b) No Designated Beneficiary. If the participant dies before the date distributions begin and there is no designated beneficiary as of September 30 of the year following the year of the participant's death, distribution of the participant's entire interest will be completed by December 31 of the calendar year containing the fifth anniversary of the participant's death.

(c) Death of Surviving Spouse Before Distributions to Surviving Spouse Are Required to Begin. If the participant dies before the date distributions begin, the participant's surviving spouse is the participant's sole designated beneficiary, and the surviving spouse dies before distributions are required to begin to the surviving spouse under section 2.2(a), this section 4.2 will apply as if the surviving spouse were the participant.

Section 5. Definitions.

5.1. Designated beneficiary. The individual who is designated as the beneficiary under section _______ of the plan and is the designated beneficiary under section 401(a)(9) of the Internal Revenue Code and section 1.401(a)(9)–1, Q&A-4, of the Treasury regulations.

5.2. Distribution calendar year. A calendar year for which a minimum distribution is required. For distributions beginning before the participant's death, the

first distribution calendar year is the calendar year immediately preceding the calendar year which contains the participant's required beginning date. For distributions beginning after the participant's death, the first distribution calendar year is the calendar year in which distributions are required to begin under section 2.2. The required minimum distribution for the participant's first distribution calendar year will be made on or before the participant's required beginning date. The required minimum distribution for other distribution calendar years, including the required minimum distribution for the distribution calendar year in which the participant's required beginning date occurs, will be made on or before December 31 of that distribution calendar year.

5.3. Life expectancy. Life expectancy as computed by use of the Single Life Table in section 1.401(a)(9)–9 of the Treasury regulations.

5.4. Participant's account balance. The account balance as of the last valuation date in the calendar year immediately preceding the distribution calendar year (valuation calendar year) increased by the amount of any contributions made and allocated or forfeitures allocated to the account balance as of dates in the valuation calendar year after the valuation date and decreased by distributions made in the valuation calendar year after the valuation date. The account balance for the valuation calendar year includes any amounts rolled over or transferred to the plan either in the valuation calendar year or in the distribution calendar year if distributed or transferred in the valuation calendar year.

5.5 Required beginning date. The date specified in section _______ of the plan.

Adoption Agreement

(Check and complete section 1 below if any required minimum distributions for the 2002 distribution calendar year were made in accordance with the § 401(a)(9) Final and Temporary Regulations.)

Section 1. Effective Date of Plan Amendment for Section 401(a)(9) Final and Temporary Treasury Regulations.

_______. Article _______, Minimum Distribution Requirements, applies for purposes of determining required minimum distributions for distribution calendar years beginning with the 2003 calendar year, as well as required minimum distributions for the 2002 distribution calendar year that are made on or after _______.

(Check and complete any of the remaining sections if you wish to modify the rules in sections 2.2 and 4.2 of Article _______ of the plan.)

Section 2. Election to Apply 5-Year Rule to Distributions to Designated Beneficiaries.

_______ If the participant dies before distributions begin and there is a designated beneficiary, distribution to the designated beneficiary is not required to begin by the date specified in section 2.2 of Article _____ of the plan, but the participant's entire interest will be distributed to the designated beneficiary by December 31 of the calendar year containing the fifth anniversary of the participant's death. If the participant's surviving spouse is the participant's sole designated beneficiary and the surviving spouse dies after the participant but before distributions to either the participant or the surviving spouse begin, this election will apply as if the surviving spouse were the participant.

This election will apply to:

_______All distributions.
_______The following distributions:
_________________________.

Section 3. Election to Allow Participants or Beneficiaries to Elect 5-Year Rule.

_______ Participants or beneficiaries may elect on an individual basis whether the 5-year rule or the life expectancy rule in sections 2.2 and 4.2 of Article _______ of the plan applies to distributions after the death of a participant who has a designated beneficiary. The election must be made no later than the earlier of September 30 of the calendar year in which distribution would be required to begin under section 2.2 of Article _______ of the plan, or by September 30 of the calendar year which contains the fifth anniversary of the participant's (or, if applicable, surviving spouse's) death. If neither the participant nor beneficiary makes an election under this paragraph, distributions will be made in accordance with sections 2.2 and 4.2 of Article of the plan and, if applicable, the elections in section 2 above.

Section 4. Election to Allow Designated Beneficiary Receiving Distributions Under 5-Year Rule to Elect Life Expectancy Distributions.

_______ A designated beneficiary who is receiving payments under the 5-year rule may make a new election to receive payments under the life expectancy rule until December 31, 2003, provided that all amounts that would have been required to be distributed under the life expectancy rule for all distribution calendar years before 2004 are distributed by the earlier of December 31, 2003, or the end of the 5-year period.

MODEL PLAN AMENDMENT 2 — DEFINED BENEFIT PLANS

Article _______. MINIMUM DISTRIBUTION REQUIREMENTS.

Section 1. General Rules

1.1. Effective Date. Unless an earlier effective date is specified in the adoption agreement, the provisions of this article will apply for purposes of determining required minimum distributions for calendar years beginning with the 2003 calendar year.

1.2. Coordination with Minimum Distribution Requirements Previously in Effect. If the adoption agreement specifies an effective date of this article that is earlier than calendar years beginning with the 2003 calendar year, required minimum distributions for 2002 under this article will be determined as follows. If the total amount of 2002 required minimum distributions under the plan made to the distributee prior to the effective date of this article equals or exceeds the required minimum distributions determined under this article, then no additional distributions will be required to be made for 2002 on or after such date to the distributee. If the total amount of 2002 required minimum distributions under the

plan made to the distributee prior to the effective date of this article is less than the amount determined under this article, then required minimum distributions for 2002 on and after such date will be determined so that the total amount of required minimum distributions for 2002 made to the distributee will be the amount determined under this article.

1.3. Precedence. The requirements of this article will take precedence over any inconsistent provisions of the plan.

1.4. Requirements of Treasury Regulations Incorporated. All distributions required under this article will be determined and made in accordance with the Treasury regulations under section 401(a)(9) of the Internal Revenue Code.

1.5. TEFRA Section 242(b)(2) Elections. Notwithstanding the other provisions of this article, other than section 1.4, distributions may be made under a designation made before January 1, 1984, in accordance with section 242(b)(2) of the Tax Equity and Fiscal Responsibility Act (TEFRA) and the provisions of the plan that relate to section 242(b)(2) of TEFRA.

Section 2. Time and Manner of Distribution.

2.1. Required Beginning Date. The participant's entire interest will be distributed, or begin to be distributed, to the participant no later than the participant's required beginning date.

2.2. Death of Participant Before Distributions Begin. If the participant dies before distributions begin, the participant's entire interest will be distributed, or begin to be distributed, no later than as follows:

(a) If the participant's surviving spouse is the participant's sole designated beneficiary, then, except as provided in the adoption agreement, distributions to the surviving spouse will begin by December 31 of the calendar year immediately following the calendar year in which the participant died, or by December 31 of the calendar year in which the participant would have attained age 70½, if later.

(b) If the participant's surviving spouse is not the participant's sole designated beneficiary, then, except as provided in the adoption agreement, distributions to the designated beneficiary will begin by December 31 of the calendar year immediately following the calendar year in which the participant died.

(c) If there is no designated beneficiary as of September 30 of the year following the year of the participant's death, the participant's entire interest will be distributed by December 31 of the calendar year containing the fifth anniversary of the participant's death.

(d) If the participant's surviving spouse is the participant's sole designated beneficiary and the surviving spouse dies after the participant but before distributions to the surviving spouse begin, this section 2.2, other than section 2.2(a), will apply as if the surviving spouse were the participant.

For purposes of this section 2.2 and section 5, distributions are considered to begin on the participant's required beginning date (or, if section 2.2(d) applies, the date distributions are required to begin to the surviving spouse under section 2.2(a)). If annuity payments irrevocably commence to the participant before the participant's required beginning date (or to the participant's surviving spouse before the date distributions are required to begin to the surviving spouse under section 2.2(a)), the date distributions are considered to begin is the date distributions actually commence.

2.3. Form of Distribution. Unless the participant's interest is distributed in the form of an annuity purchased from an insurance company or in a single sum on or before the required beginning date, as of the first distribution calendar year distributions will be made in accordance with sections 3, 4 and 5 of this article. If the participant's interest is distributed in the form of an annuity purchased from an insurance company, distributions thereunder will be made in accordance with the requirements of section 401(a)(9) of the Code and the Treasury regulations. Any part of the participant's interest which is in the form of an individual account described in section 414(k) of the Code will be distributed in a manner satisfying the requirements of section 401(a)(9) of the Code and the Treasury regulations that apply to individual accounts.

Section 3. Determination of Amount to be Distributed Each Year.

3.1. General Annuity Requirements. If the participant's interest is paid in the form of annuity distributions under the plan, payments under the annuity will satisfy the following requirements:

(a) the annuity distributions will be paid in periodic payments made at intervals not longer than one year;

(b) the distribution period will be over a life (or lives) or over a period certain not longer than the period described in section 4 or 5;

(c) once payments have begun over a period certain, the period certain will not be changed even if the period certain is shorter than the maximum permitted;

(d) payments will either be nonincreasing or increase only as follows:

(1) by an annual percentage increase that does not exceed the annual percentage increase in a cost-of-living index that is based on prices of all items and issued by the Bureau of Labor Statistics;

(2) to the extent of the reduction in the amount of the participant's payments to provide for a survivor benefit upon death, but only if the beneficiary whose life was being used to determine the distribution period described in section 4 dies or is no longer the participant's beneficiary pursuant to a qualified domestic relations order within the meaning of section 414(p);

(3) to provide cash refunds of employee contributions upon the participant's death; or

(4) to pay increased benefits that result from a plan amendment.

3.2. Amount Required to be Distributed by Required Beginning Date. The amount that must be distributed on or before the participant's required beginning date (or, if the participant dies before distributions begin, the date distributions are required to begin under section 2.2(a) or (b)) is the payment that is required for one payment interval. The second payment need not be made until the end of the next payment interval even if that payment interval ends in the next calendar year. Payment intervals are the periods for which payments are received, *e.g.*, bi-monthly, monthly, semi-annually, or annually. All of the participant's benefit

accruals as of the last day of the first distribution calendar year will be included in the calculation of the amount of the annuity payments for payment intervals ending on or after the participant's required beginning date.

3.3. Additional Accruals After First Distribution Calendar Year. Any additional benefits accruing to the participant in a calendar year after the first distribution calendar year will be distributed beginning with the first payment interval ending in the calendar year immediately following the calendar year in which such amount accrues.

Section 4. Requirements For Annuity Distributions That Commence During Participant's Lifetime.

4.1. Joint Life Annuities Where the Beneficiary Is Not the Participant's Spouse. If the participant's interest is being distributed in the form of a joint and survivor annuity for the joint lives of the participant and a nonspouse beneficiary, annuity payments to be made on or after the participant's required beginning date to the designated beneficiary after the participant's death must not at any time exceed the applicable percentage of the annuity payment for such period that would have been payable to the participant using the table set forth in Q&A-2 of section 1.401(a)(9)–6T of the Treasury regulations. If the form of distribution combines a joint and survivor annuity for the joint lives of the participant and a nonspouse beneficiary and a period certain annuity, the requirement in the preceding sentence will apply to annuity payments to be made to the designated beneficiary after the expiration of the period certain.

4.2. Period Certain Annuities. Unless the participant's spouse is the sole designated beneficiary and the form of distribution is a period certain and no life annuity, the period certain for an annuity distribution commencing during the participant's lifetime may not exceed the applicable distribution period for the participant under the Uniform Lifetime Table set forth in section 1.401(a)(9)–9 of the Treasury regulations for the calendar year that contains the annuity starting date. If the annuity starting date precedes the year in which the participant reaches age 70, the applicable distribution period for the participant is the distribution period for age 70 under the Uniform Lifetime Table set forth in section 1.401(a)(9)–9 of the Treasury regulations plus the excess of 70 over the age of the participant as of the participant's birthday in the year that contains the annuity starting date. If the participant's spouse is the participant's sole designated beneficiary and the form of distribution is a period certain and no life annuity, the period certain may not exceed the longer of the participant's applicable distribution period, as determined under this section 4.2, or the joint life and last survivor expectancy of the participant and the participant's spouse as determined under the Joint and Last Survivor Table set forth in section 1.401(a)(9)–9 of the Treasury regulations, using the participant's and spouse's attained ages as of the participant's and spouse's birthdays in the calendar year that contains the annuity starting date.

Section 5. Requirements For Minimum Distributions Where Participant Dies Before Date Distributions Begin.

5.1. Participant Survived by Designated Beneficiary. Except as provided in the adoption agreement, if the participant dies before the date distribution of his or her interest begins and there is a designated beneficiary, the participant's entire interest will be distributed, beginning no later than the time described in section 2.2(a) or (b), over the life of the designated beneficiary or over a period certain not exceeding:

(a) unless the annuity starting date is before the first distribution calendar year, the life expectancy of the designated beneficiary determined using the beneficiary's age as of the beneficiary's birthday in the calendar year immediately following the calendar year of the participant's death; or

(b) if the annuity starting date is before the first distribution calendar year, the life expectancy of the designated beneficiary determined using the beneficiary's age as of the beneficiary's birthday in the calendar year that contains the annuity starting date.

5.2. No Designated Beneficiary. If the participant dies before the date distributions begin and there is no designated beneficiary as of September 30 of the year following the year of the participant's death, distribution of the participant's entire interest will be completed by December 31 of the calendar year containing the fifth anniversary of the participant's death.

5.3. Death of Surviving Spouse Before Distributions to Surviving Spouse Begin. If the participant dies before the date distribution of his or her interest begins, the participant's surviving spouse is the participant's sole designated beneficiary, and the surviving spouse dies before distributions to the surviving spouse begin, this section 5 will apply as if the surviving spouse were the participant, except that the time by which distributions must begin will be determined without regard to section 2.2(a).

Section 6. Definitions.

6.1. Designated beneficiary. The individual who is designated as the beneficiary under section _______ of the plan and is the designated beneficiary under section 401(a)(9) of the Internal Revenue Code and section 1.401(a)(9)–1, Q&A-4, of the Treasury regulations.

6.2. Distribution calendar year. A calendar year for which a minimum distribution is required. For distributions beginning before the participant's death, the first distribution calendar year is the calendar year immediately preceding the calendar year which contains the participant's required beginning date. For distributions beginning after the participant's death, the first distribution calendar year is the calendar year in which distributions are required to begin pursuant to section 2.2.

6.3 Life expectancy. Life expectancy as computed by use of the Single Life Table in section 1.401(a)(9)–9 of the Treasury regulations.

6.4. Required beginning date. The date specified in section _______ of the plan.

Adoption Agreement

(Check and complete section 1 below if any required minimum distributions for the 2002 distribution calendar year were made in accordance with the § 401(a)(9) Final and Temporary Regulations.)

Section 1. Effective Date of Plan Amendment for Section 401(a)(9) Final and Temporary Treasury Regulations.

_______ Article _______, Minimum Distribution Requirements, applies for purposes of determining required minimum distributions for distribution calendar years beginning with the 2003 calendar year, as well as required minimum distributions for the 2002 distribution calendar year that are made on or after .

(Check and complete any of the remaining sections if you wish to modify the rules in sections 2.2 and 5 of Article _______ of the plan.)

Section 2. Election to Apply 5-Year Rule to Distributions to Designated Beneficiaries.

_______ If the participant dies before distributions begin and there is a designated beneficiary, distribution to the designated beneficiary is not required to begin by the date specified in section 2.2 of Article _______ of the plan, but the participant's entire interest will be distributed to the designated beneficiary by December 31 of the calendar year containing the fifth anniversary of the participant's death. If the participant's surviving spouse is the participant's sole designated beneficiary and the surviving spouse dies after the participant but before distributions to either the participant or the surviving spouse begin, this election will apply as if the surviving spouse were the participant.

This election will apply to:

_______All distributions.
_______The following distributions:
________________________.

Section 3. Election to Allow Participants or Beneficiaries to Elect 5-Year Rule.

_______ Participants or beneficiaries may elect on an individual basis whether the 5-year rule or the life expectancy rule in sections 2.2 and 5 of Article _______ of the plan applies to distributions after the death of a participant who has a designated beneficiary. The election must be made no later than the earlier of September 30 of the calendar year in which distribution would be required to begin under section 2.2 of Article of the plan, or by September 30 of the calendar year which contains the fifth anniversary of the participant's (or, if applicable, surviving spouse's) death. If neither the participant nor beneficiary makes an election under this paragraph, distributions will be made in accordance with sections 2.2 and 5 of Article_______ of the plan and, if applicable, the elections in section 2 above.

Section 4. Election to Allow Designated Beneficiary Receiving Distributions Under 5-Year Rule to Elect Life Expectancy Distributions.

_______ A designated beneficiary who is receiving payments under the 5-year rule may make a new election to receive payments under the life expectancy rule until December 31, 2003, provided that all amounts that would have been required to be distributed under the life expectancy rule for all distribution calendar years before 2004 are distributed by the earlier of December 31, 2003, or the end of the 5-year period.

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

Rev. Proc. 2002–30

SECTION 1. PURPOSE

This revenue procedure provides for a pilot program that will test whether the process for issuing Technical Advice Memoranda (TAMs) can be streamlined. The new advice will be known as a Technical Expedited Advice Memorandum (TEAM). During the TEAM pilot program, only issues under the jurisdiction of the Associate Chief Counsel (Income Tax & Accounting) will be eligible for a TEAM.

The purpose of the new TEAM pilot program is to expedite certain aspects of the TAM process and to eliminate certain requirements (taxpayer and field agreement on facts) that may delay or frustrate the process. Accordingly, the Office of Chief Counsel will provide an answer even if the taxpayer and the field disagree on the facts. The Office of Chief Counsel, in appropriate circumstances, may issue two separate answers: one based on the field's factual submission and the other based on the taxpayer's.

If the TEAM pilot program is successful, the Office of Chief Counsel expects to expand it to cover other types of issues and all Associate offices. The program also may be made permanent in Rev. Proc. 2003–2 or a subsequent annual revenue procedure. To that end, comments from taxpayers and practitioners regarding the TEAM pilot program are solicited and may be mailed to:

Internal Revenue Service
CC:ITA:RU (RP–124153–02)
Room 5226
POB 7604
Ben Franklin Station
Washington, DC 20044
Attn: A. Lawan Jackson

Submissions may also be delivered Monday through Friday between the hours of 8 a.m. and 5 p.m to CC:ITA:RU (RP–124153–02), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may submit comments electronically by submitting comments directly to the following IRS e-mail address: *Notice.Comments@irscounsel.treas.gov*.

SECTION 2. EFFECT OF A TEAM

A TEAM issued under this revenue procedure will have the same force and legal effect as a TAM requested under Rev. Proc. 2002–2, 2002–1 I.R.B. 82, except as described in sections 8, 10, and 11 of this revenue procedure. Therefore, the field must process the taxpayer's case on the basis of the conclusions in the TEAM, subject to the conditions and limitations described in Rev. Proc. 2002–2, and sections 8, 10, and 11 of this revenue procedure.

SECTION 3. DEFINITIONS

For purposes of this revenue procedure—

(1) The term "taxpayer" includes all persons subject to any provision of the Internal Revenue Code (including issuers of section 103 obligations) and, when appropriate, their representatives;

(2) The term "Associate" means the Associate Chief Counsel (Income Tax & Accounting);

(3) The term "field" refers to field counsel and exam and appeals personnel;

(**4**) The term "field counsel" refers to any attorney with the Office of Chief Counsel who is not part of the national office or Division Counsel Headquarters;

(**5**) The term "director" refers to the Director, Field Operations, LMSB; the Territory Manager, Field Compliance, SB/SE; or the Director, Compliance, W&I, as appropriate, and their respective offices; and

(**6**) The term "area director, appeals" refers to the Area Director, Appeals LBSP, or the Area Director, General Appeals Programs, as appropriate.

SECTION 4. SCOPE

The TEAM pilot program is limited to TAM requests originating during the examination or appeals process that are submitted to the Associate Chief Counsel (Income Tax & Accounting). All TAM requests with issues under the jurisdiction of the Associate will be eligible for the TEAM procedures, except for requests that require coordination outside of the Associate's office. If the request requires coordination outside of the Associate's office, the TAM procedures set forth in Rev. Proc. 2002–2 will apply. During the pendency of the TEAM pilot program, all TAM requests to the Associate (whether or not eligible for the pilot program) must be submitted through the presubmission procedures set forth in section 6 of this revenue procedure. TEAM treatment will be available only after the taxpayer, the field and the Associate agree that such treatment is appropriate following the presubmisson conference described in section 6.

SECTION 5. WHO IS RESPONSIBLE FOR REQUESTING A TEAM?

Requests for a TEAM. A request for a TEAM can originate with the taxpayer, exam or appeals personnel, or field counsel. All requests for a TEAM must be submitted through the supervisory chain for exam or appeals and must be approved by the director or equivalent official in the respective operating divisions or by the area director, appeals (or by an official authorized to act on their behalf) before submission to the Associate. If the director or equivalent official declines to approve the request, then the denial can be appealed to the Division Commissioner for that Operating Division or to the Deputy Director, General Appeals Programs or Director, Appeals, LBSP.

Taxpayer initiated request. While a case is under the jurisdiction of a director or area director, appeals, a taxpayer may make a written or oral request to the examining agent or appeals officer that an issue be referred to the Associate for a TEAM.

Field counsel initiated request. Exam or appeals personnel can request advice from field counsel on issues involved in cases under their jurisdiction. If, during the discussion of an issue with an examining agent or appeals officer, field counsel believes an issue warrants consideration as a TEAM, then field counsel may make a written or oral request to the examining agent or appeals officer that the issue be referred to the Associate for a TEAM.

Resolution of conflicts over requests for a TEAM. If, after considering a request by the taxpayer or field counsel that an issue be submitted for a TEAM, the examining agent or appeals officer disagrees with the request, the taxpayer or the field counsel may raise the request through the examining agent's or the appeals officer's supervisory chain.

SECTION 6. HOW ARE PRESUBMISSION CONFERENCES SCHEDULED?

Field counsel will work closely with the examining agents or appeals officers and the taxpayer in developing the case for a TEAM and in preparing for the presubmission conference. The request for a presubmission conference must be made by FAX to the Associate's office at **202–622–6316**, and must be confirmed in writing by the director or area director, appeals. The receipt of the FAX will be confirmed by the Associate office within one business day. Because the presubmission conference shall involve the taxpayer, as set forth in Rev. Proc. 2002–2, coordination of the request with the taxpayer must begin as soon as reasonably possible after the oral request. Additionally, the field personnel and the taxpayer should agree on what materials to forward to the Associate's office to assist in deciding whether TEAM procedures are appropriate.

Within 5 calendar days of receiving the request, the assigned branch within the Associate's office will contact the field office to schedule the conference. The conference will be held within 15 calendar days of the assigned branch's call to the field office and will be held by telephone, unless the parties specifically request a meeting in person. In no event will a request for an in-person presubmission conference be allowed to delay the conference beyond the 15-day period. The presubmission materials must be received by the assigned branch in the Associate's office no later than 5 calendar days prior to the conference. In order to obtain the protection of taxpayer information offered by the Chief Counsel Intranet "firewall," the presubmission materials shall be electronically transmitted by field counsel to the **CRU-TEAM** e-mail address. To the extent that supporting materials cannot reasonably be submitted, such materials should be sent by FAX, express mail, or private delivery service to avoid any delays in regular mail to the Associate's office.

During the presubmission conference, the parties should determine whether the issue is appropriate for a TEAM, and how the issue should be framed. The participants from the Associate's office will explain the TEAM procedures and the expedited time frames involved. If all parties agree that the TEAM process is desirable, then the request will be processed subject to the TEAM pilot procedures. The parties also should agree on the background documents necessary for the TEAM, and when and how the parties will submit those documents to the Associate.

If the parties do not agree that the TEAM process is appropriate for the issue, the standard TAM procedures of Rev. Proc. 2002–2 may be used.

SECTION 7. WHAT MUST BE INCLUDED IN THE REQUEST FOR A TEAM?

In general, the same procedures should be used for preparing a TEAM request that are used for preparing a TAM request, with the following modifications to Rev. Proc. 2002–2 to expedite the process and to articulate procedures for the TEAM pilot program:

Factual statements. The field, with the assistance of field counsel, will prepare a factual statement. The taxpayer will have 10 calendar days to respond to the field office's facts. If the taxpayer and the field disagree, the parties will have 10 calendar days to attempt to resolve the disagreements. Within 5 calendar days of the expiration of the 10-day period or the day that factual agreement is reached, whichever is earliest, the TEAM request will be forwarded to the Associate. If there is no agreement on the facts, both sets of facts will be forwarded to the Associate. The field, with the assistance of field counsel, will prepare a memorandum highlighting the material factual differences, which memorandum will be provided to the taxpayer.

Submission of documents. All documents will be electronically transmitted by field counsel (followed by hard copy upon the request of the Associate) to the **CRU:TEAM** e-mail address. Additional or supporting documents will be sent by FAX, express mail or private delivery service. The field and the taxpayer are encouraged to provide electronic versions of a proposed TEAM containing the taxpayer's deletions and legends for the Associate's use.

SECTION 8. HOW ARE REQUESTS HANDLED?

If, at the outset, the reviewing branch chief in the Associate's office determines that general guidance should be published regarding the issue presented, the branch chief will immediately notify the Associate. The reviewing branch chief will attempt to make this determination and recommendation as soon as possible, which may occur during the presubmission conference. The criteria for this determination should include whether the issue has a broad application to similarly situated taxpayers or an industry, or resolution of the issue is important to a clear understanding of the tax laws. If the Associate, in consultation with Division Counsel and the Operating Division, agrees that general guidance is desirable, an expedited guidance project will be initiated. The Associate, in consultation with Division Counsel and the Operating Division, also will determine the appropriate resolution of the TEAM request, *i.e.*, whether it may be issued in advance of the general guidance project or must await the publication of guidance. In general, except where policy issues and concerns regarding proper administration of the tax laws require otherwise, the TEAM will be issued in advance of the published guidance.

Within 5 calendar days of the receipt of the TEAM request, the assigned attorney in the Associate's office will contact the field office and the field counsel to confirm the receipt of the request for advice. The assigned Associate attorney and reviewer should also evaluate the issue(s) presented in the TEAM request. If, notwithstanding the presubmission discussion, the Associate concludes that the issue is too complex or otherwise impractical to resolve in the time frames provided below, the Associate may submit a memorandum to the Chief Counsel requesting that the case be excluded from the TEAM process and be treated as a TAM under Rev. Proc. 2002–2. The Associate must discuss this request with both the field and the taxpayer and reflect their views in the memorandum to the Chief Counsel.

Within 20 calendar days of receipt of the TEAM request, the assigned branch in the Associate's office will analyze the facts and offer the taxpayer and the field a conference of right, which will be scheduled for a date within 10 calendar days of the date of the offer for the conference. The conference will be conducted by telephone, unless the taxpayer or the field requests that the conference be held in-person. In no event will the conference be delayed to provide an in person conference rather than a telephone conference.

Following the conference, the taxpayer and the field will have 15 calendar days to provide any supplemental materials. No further conferences will be held. The TEAM will be issued no later than 15 calendar days after the expiration of the 15-day period for supplemental materials.

If two sets of facts are provided to the Associate (*i.e.*, the parties were unable to reach agreement on the facts), the following procedure will be used: If the Associate would rule the same way on either set of facts, a TEAM will be issued, which will note that the factual disagreement is immaterial. If the Associate would rule differently based on which specific set of facts is considered, then a TEAM will be issued describing the resolution of the issue based on each set of facts.

If the TEAM provides alternate responses based on separate sets of facts, the field will not be required to process the case on the basis of the conclusions in the TEAM, as required by section 17.01 of Rev. Proc. 2002–2 in the case of a TAM.

SECTION 9. ISSUANCE OF A TEAM

The Associate will attempt to issue all TEAMs to the field within 60 calendar days of receipt. The Associate will provide the field with the TEAM at the earliest possible date (whether the proposed TEAM is favorable or adverse, in whole or in part, to the taxpayer). The Associate will not provide the taxpayer with the TEAM or advise the taxpayer of a proposed or final conclusion until the Associate has considered a request for reconsideration under section 10 of this revenue procedure or, if no reconsideration is requested, after the expiration of the 30-day period to request reconsideration, whichever occurs later.

SECTION 10. RECONSIDERATION OF A TEAM

The field will have 30 calendar days from issuance to request reconsideration or the TEAM becomes final and will be released to the taxpayer, as is provided in section 17 of Rev. Proc. 2002–2. The request for reconsideration from the field must come from the director or area director, appeals. The request for reconsideration must describe with specificity the errors in the TEAM analysis and conclusions. Requests for reconsideration should not reargue points raised in the initial request, but should instead focus on points that the TEAM overlooked or misconstrued in the field's arguments in support of their request.

The Associate will consider the field's request for reconsideration and rule on that request within 30 calendar days of receipt. The Associate may request further submissions from the field or the taxpayer, but no additional submissions shall be made in the absence of such a request. If the field does not request reconsideration, the TEAM will take effect at the end

of the 30-day period following the issuance of the TEAM to the field. If reconsideration is requested, the TEAM will take effect 5 calendar days after the reconsideration is ruled on.

In the event of a TEAM adverse to the taxpayer, in whole or in part, the taxpayer may request section 7805(b) relief. Such a request will be treated as a separate request subject to the user fee requirements in Rev. Proc. 2002–1. (Similar to section 301.9100 relief.)

SECTION 11. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 2002–2, 2002–1 I.R.B. 82, is modified by the supplemental procedures in this revenue procedure. If the TEAM provides alternate responses based on separate sets of facts, the field will not be required to process the case on the basis of the conclusions in the TEAM, as required by section 17.01 of Rev. Proc. 2002–2 in the case of a TAM.

SECTION 12. EFFECTIVE DATE

This revenue procedure is effective on the date of publication in the Internal Revenue Bulletin, and the TEAM pilot procedures will remain in effect until the issuance of Rev. Proc. 2003–2.

SECTION 13. DRAFTING INFORMATION

The principal author of this revenue procedure is Susan L. Hartford of the Office of Associate Chief Counsel (Procedure and Administration). For further information regarding this revenue procedure, contact Ms. Hartford at 202–622–4940 (not a toll-free call).

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26 CFR 601.201: Rulings and determination letters. (Also, Part I, §§ 401; 1.401(b)–1.)

Rev. Proc. 2002–35

SECTION 1. PURPOSE

This revenue procedure establishes streamlined procedures to avoid the disqualification of plans intended to satisfy § 401(a) or § 403(a) of the Internal Revenue Code on account of failure to be timely amended for GUST.[1] These streamlined procedures are available only if the plan sponsor applies for a determination letter by September 3, 2002.

SECTION 2. BACKGROUND

.01 Plans intended to satisfy § 401(a) or § 403(a) ("Qualified Plans") are required to be amended for GUST within the GUST remedial amendment period. A plan's GUST remedial amendment period generally ends on the later of February 28, 2002, or the last day of the first plan year beginning on or after January 1, 2001. See Rev. Proc. 2001–55, 2001–49 I.R.B. 552. Special rules apply to governmental plans, plans directly affected by the terrorist attack of September 11, 2001, and plans that are eligible for the extended GUST remedial amendment period that applies to master and prototype and volume submitter plans under section 19 of Rev. Proc. 2000–20, 2000–1 C.B. 553, as modified by Rev. Proc. 2000–27, 2000–1 C.B. 1272, Notice 2001–42, 2001–30 I.R.B. 70, and Rev. Proc. 2001–55.

.02 Rev. Proc. 2001–17, 2001–1 C.B. 589, describes the Employee Plans Compliance Resolution System ("EPCRS"), a comprehensive system of correction programs that, with respect to Qualified Plans, permits plan sponsors to correct qualification failures and thereby preserve the plans' tax-favored status.

SECTION 3. STREAMLINED PROCEDURES

.01 The streamlined procedures in this section apply to Eligible Qualified Plans. The term "Eligible Qualified Plan" means a Qualified Plan that has not been amended for GUST within its GUST remedial amendment period and for which an application for a determination letter that considers all of the requirements of GUST is filed by September 3, 2002. However, a plan is not an Eligible Qualified Plan if the plan is a late amender without regard to GUST (for example, in the case of a plan other than a governmental or nonelecting church plan, if the plan was not timely amended for the Tax Reform Act of 1986, the Unemployment Compensation Act of 1992 or the Omnibus Budget and Reconciliation Act of 1993.) For purposes of this revenue procedure, the failure to amend any disqualifying provision for which the GUST remedial amendment period is available will be treated as a failure to amend the plan for GUST.

.02 The procedures in this section apply to Eligible Qualified Plans in lieu of the procedures in Rev. Proc. 2001–17. Rev. Proc. 2001–17 will continue to apply to late amended plans that are not eligible under this revenue procedure, including late amended plans for which determination letter applications are not filed by September 3, 2002.

.03 The Service will, upon resolution of the determination letter application, treat an Eligible Qualified Plan as having been amended for GUST within the GUST remedial amendment period and issue a favorable determination letter if the plan sponsor has submitted payment of the fee described in section 3.04. This fee is in addition to the determination letter user fee, if applicable.

[1] "GUST" refers to the following:

- the Uruguay Round Agreements Act, Pub. L. 103–465;
- the Uniformed Services Employment and Reemployment Rights Act of 1994, Pub. L. 103–353;
- the Small Business Job Protection Act of 1996, Pub. L. 104–188;
- the Taxpayer Relief Act of 1997, Pub L. 105–34;
- the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105–206; and
- the Community Renewal Tax Relief Act of 2000, Pub. L. 106–554.

.04 The amount of the fee is as follows:

Number of Participants (per Form 5300 or Form 5307)	Fee
1 – 100	$1,000
101 – 1000	$3,000
1001 or more	$10,000

.05 If the plan sponsor of a late amended Qualified Plan does not resolve the failure to timely amend the plan under this revenue procedure or under Rev. Proc. 2001–17, the plan will be subject to disqualification.

SECTION 4. APPLICATION PROCEDURES

.01 A plan sponsor of an Eligible Qualified Plan may apply to have the failure to timely amend the plan resolved under this revenue procedure by filing a complete GUST determination letter application by September 3, 2002. If the application is filed on or after July 17, 2002, the application should include a check or money order, made payable to the U.S. Treasury, in the amount of the fee determined under section 3.04. This fee and the appropriate determination letter user fee, if applicable, should be paid using separate checks or money orders, each appropriately annotated. The phrase "Rev. Proc. 2002–35" should be written in bold at the top of the Form 5300 or Form 5307. The application should be sent to the appropriate address in section 6.18 of Rev. Proc. 2002–6, 2002–1 I.R.B. 203.

.02 If the Service determines that a plan for which a GUST determination letter application has been filed by September 3, 2002, is a GUST late amender, and the plan sponsor has not submitted payment of the fee under section 3.04, the Service will contact the plan sponsor to offer the sponsor the opportunity to request consideration under this procedure, or, if the plan is not an Eligible Qualified Plan, under Rev. Proc. 2001–17. Therefore, plan sponsors of late amended plans that have filed GUST determination letter applications before July 17, 2002, need take no further action until contacted by the Service.

SECTION 5. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 2001–17 is modified.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective on June 17, 2002.

DRAFTING INFORMATION

The principal author of this revenue procedure is James Flannery of Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue procedure, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 between the hours of 8:00 a.m. and 6:30 p.m. Eastern time, Monday through Friday (a toll-free number). Mr. Flannery may be reached at 1–202–283–9888 (not a toll-free call).

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26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part I, §§ 30, 50, 179, 179A.)

Rev. Proc. 2002–42

SECTION 1. PURPOSE

This revenue procedure sets forth a process that allows taxpayers who purchase certain clean-fuel vehicle property to rely on a manufacturer's certification of the incremental cost of the property for purposes of the clean-fuel vehicle property deduction provided in § 179A of the Internal Revenue Code. This revenue procedure applies to motor vehicles (other than buses, and trucks and vans with a gross vehicle weight rating greater than 10,000 pounds) that are propelled by both a gasoline internal combustion engine and an electric motor that is recharged as the motor vehicles operate (hybrid vehicles) and that otherwise meet the requirements of § 179A.

SECTION 2. BACKGROUND

.01 *In general*. Section 179A allows a deduction for certain costs of "qualified clean-fuel vehicle property" for the tax year in which the property is placed in service. In the case of hybrid vehicles, only the incremental cost of permitting the use of the clean-burning fuel (electricity) can be taken into account when determining the allowable deduction under § 179A.

The Internal Revenue Service has received numerous inquiries from taxpayers concerning the determination of the incremental cost for specific hybrid vehicles for purposes of § 179A. This revenue procedure sets forth a process allowing a taxpayer who purchases a hybrid vehicle to rely on the original equipment manufacturer's (or, in the case of a foreign original equipment manufacturer, its domestic distributor's) certification of the incremental cost of the property for purposes of § 179A.

.02 *Qualifying Motor Vehicles*. This revenue procedure applies only to motor vehicles that meet the requirements of § 179A. In order to be eligible for the deduction under § 179A, a motor vehicle must: (1) be acquired for use by the taxpayer and not for resale and have its original use commence with the taxpayer; (2) meet the applicable federal and state emissions standards with respect to each fuel by which the vehicle is propelled; (3) be manufactured primarily for use on public streets, roads, and highways; (4) have at least four wheels; and (5) not operate exclusively on a rail or rails. Section 179A and this revenue procedure do not apply to motor vehicles that are primarily powered by electricity and qualify for the credit provided in § 30 or to motor vehicles that are used predominantly outside the United States.

.03 *Deduction Amount Limitations*. Under § 179A, except in the case of any truck or van with a gross vehicle weight rating greater than 10,000 pounds or any bus with a seating capacity of at least 20 adults (not including the driver), the maximum cost that may be taken into account when determining the deduction is $2,000 for motor vehicles placed in service on or before December 31, 2003. The $2,000 maximum is reduced by 25 percent for motor vehicles placed in service in calendar year 2004, 50 percent for motor vehicles placed in service in calendar year 2005, and 75 percent for motor vehicles placed in service in calendar year 2006. No deduction is allowed for motor vehicles placed in service after December 31, 2006. No deduction is allowed with

respect to the portion of the cost of any property taken into account under § 179.

SECTION 3. PROCEDURE

.01 *Original Equipment Manufacturer's Certification*. An original equipment manufacturer (or in the case of a foreign original equipment manufacturer, its domestic distributor) may prepare a certification concerning the incremental cost of permitting the use of electricity to propel its vehicles. The certification should contain the following information:

(1) the name and address of the certifying entity;

(2) the make, model, year, and any other appropriate identifiers of the motor vehicle; and

(3) a statement disclosing the total per-vehicle cost to acquire and install the motor vehicle's electric motor and related generating, storage, and delivery equipment. If the total cost exceeds $2,000, the statement may so indicate without disclosing the specific amount of the cost.

The certification should be signed by an officer of the original equipment manufacturer (or, in the case of a foreign original equipment manufacturer, an officer of its domestic distributor). This original signed certification must be sent to the Internal Revenue Service, Industry Director, Large and Mid-Size Business, Heavy Manufacturing and Transportation, Metro Park Office Complex — LMSB, 111 Wood Avenue, South, Iselin, New Jersey 08830.

.02 *Internal Revenue Service's Acknowledgment*. The Internal Revenue Service will review the original signed certification and issue an acknowledgment letter to the original equipment manufacturer (or, in the case of a foreign original equipment manufacturer, its domestic distributor). This acknowledgment letter will state whether purchasers may rely on the certification.

.03 *Purchaser's Reliance*. Copies of the certification and acknowledgment may be made available to purchasers. Except as otherwise provided in the acknowledgment, a purchaser of a hybrid vehicle may rely on the certification concerning the incremental cost of permitting the use of electricity to propel the vehicle.

SECTION 4. DRAFTING INFORMATION

The principal author of this revenue procedure is Jolene J. Shiraishi of the Office of the Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this revenue procedure, contact Ms. Shiraishi at (202) 622–3120 (not a toll free call).

Part IV. Items of General Interest

Announcement and Report Concerning Pre-Filing Agreements

Announcement 2002–54

Introduction

This Announcement is issued pursuant to the Conference Report to H.R. 4577 (Pub. L. 106–554), *The Community Renewal Tax Relief Act of 2000*, which requires that the Secretary of the Treasury make publicly available an annual report relating to the Pre-Filing Agreement ("PFA") program operations for the preceding calendar year. The Conference Report states that the report is to include: (1) the number of pre-filing agreements completed, (2) the number of applications received, (3) the number of applications withdrawn, (4) the types of issues which are resolved by completed agreements, (5) whether the program is being utilized by taxpayers who were previously subject to audit, (6) the average length of time required to complete an agreement, (7) the number, if any, and subject of technical advice and Chief Counsel advice memoranda issued to address issues arising in connection with any pre-filing agreement, (8) any model agreements, and (9) any other information the Secretary deems appropriate. This is the second annual report and provides information on the four remaining PFA pilot program cases that closed in calendar year 2001. This report also provides similar information concerning case activity that started with the permanent program (Rev. Proc. 2001–22, 2001–1 C.B. 745).

Background

The Large and Mid-Size Business Division ("LMSB") within the Internal Revenue Service serves corporations and partnerships with assets greater than $10 million. In 2001, approximately 170,000 corporations and partnerships filed returns reporting assets in this range. The returns filed by these taxpayers present a wide variety of complex issues. Taxpayers served by LMSB reported a total tax liability of $350 billion during 2001. The largest of the taxpayers deal with the IRS on a continuous basis.

One of LMSB's strategic initiatives is issue management. Through effective issue management, LMSB seeks to resolve issues of tax controversy on a more current basis. This includes, but is not limited to, increasing the efficiency of the examination process and seeking alternative issue resolution tools. The Pre-Filing Agreement program was designed to support LMSB's issue management strategy. LMSB believes the Pre-Filing Agreement program reduces taxpayer burden and make more effective use of IRS resources by resolving or eliminating tax controversy before the tax return is filed.

Pre-Filing Agreement Program

The PFA program is designed to permit a taxpayer to resolve, before the filing of a return, the treatment of an issue that otherwise would likely be disputed in a post-filing examination. The PFA program is intended to produce agreement on factual issues and apply settled legal principles to those facts. A PFA is a specific matter closing agreement under § 7121 of the Internal Revenue Code and resolves the subject of the PFA for a taxable period. Execution of a PFA that resolves issues prior to filing permits taxpayers to avoid a portion of the costs, burdens and delays that are frequently incident to post-filing examination disputes between taxpayers and the IRS.

In calendar year 2000, the pilot program was implemented which resulted in the execution of seven PFAs. Four cases remained in process at the end of calendar year 2000 and all four cases were closed during calendar year 2001. A PFA was executed in three of the four cases. Based upon input from internal and external participants in the pilot program, the IRS expanded the PFA program and made it permanent.

Pilot Pre-Filing Agreement Program Completion

PFA Pilot Program

The PFA pilot program was open to Coordinated Examination Program ("CEP") taxpayers that had a CEP examination team currently on site (CEP cases have been renamed Coordinated Industry Cases (CIC)). Notice 2000–12, 2000–1 C.B. 727, dated February 11, 2000, provided a description of a PFA, the procedures for requesting a PFA, and the procedures for LMSB to select taxpayers for the PFA pilot program. The IRS believed that this PFA pilot program offered significant benefits for taxpayers, as well as for the IRS, and invited large business taxpayers to participate. Notice 2000–12 requested interested taxpayers to submit applications for the PFA pilot program by March 15, 2000, through the on site LMSB team manager. During the PFA pilot, eleven cases were accepted into the pilot program. Of the eleven, seven were closed during calendar year 2000 and reflected in the first report (Announcement 2001–38, 2001–1 C.B. 1138, dated April 23, 2001). The remaining four cases were closed during calendar year 2001. This report reflects the activity of the four pilot cases closed in calendar year 2001.

The taxpayers and the respective Industry Directors, in accordance with the provisions of Notice 2000–12, agreed to continue discussions relating to the four PFAs that were in process at December 31, 2000.

Industry Segment	Issue	In-Process @12/31/00
Heavy Manufacturing & Transportation	Research Credit	1
Heavy Manufacturing & Transportation	Valuation of Assets	1
Communications, Technology & Media	Research Credit	1
Retailers, Food, Pharmaceuticals & Healthcare	Expense vs. Capitalization	1

During calendar year 2001, the four pilot cases were closed in the following manner:

Status of PFAs	Issue
Executed PFA	Research Credit
Executed PFA	Valuation of Assets
Executed PFA	Research Credit
PFA Withdrawn	Expense vs. Capitalization

Executed PFAs — Research Credit

Two applicants sought PFAs regarding the amount of research credit each could claim as a result of various activities undertaken to improve products. In both instances, IRS specialists and other non-Service outside experts were involved in the process of ascertaining what activities qualified for the credit. In one case, the analysis involved consideration of the activities of over 1,500 different departments. Closing agreements were executed in both cases.

Executed PFA — Valuation of Assets

This case involved a determination of value related to the sale of assets and stock of a subsidiary to an unrelated party. An allocation of the net selling price among the assets and stock sold, the basis of the assets sold, and the taxable gain or loss were at issue. A closing agreement was executed regarding all of these issues.

PFA Withdrawn — Expense vs. Capitalization

The issue in this case related to whether certain repairs and maintenance expenditures were deductible or should be capitalized and depreciated over their useful life. A closing agreement with multi-year application which was sought by the taxpayer could not be provided under the terms of the Delegation Order for the PFA program. Consequently, both the Service and the taxpayer mutually agreed to withdraw from the PFA process.

Closing Agreements

The above three PFAs were executed during 2001. A pro forma or model agreement does not exist for a PFA. A PFA represents a specific matter closing agreement under § 7121. The closing agreements entered into under this program were prepared with assistance from the Office of Chief Counsel and conform to the guidance provided in Rev. Proc. 68–16, 1968–1 C.B. 770.

Processing Statistics

The average elapsed time to resolve the four cases described above that were closed in calendar year 2001 was 482.75 days.

Average Processing Time for Four Cases Closed in 2001	Range (Elapsed Days)	Average (Elapsed Days)
Phase I —Application Screening Process	21–86	44.5
Phase II — PFA Evaluation Process	292–533	438.25
Total Time to Close a PFA Case	322–574	482.75

Phase I — Application Screening Process

The initial phase was the screening process to determine if an application was appropriate for inclusion in the PFA pilot program. This screening process included obtaining comments from various LMSB functions and Chief Counsel, the review of these comments, and the decision making process on the acceptance/rejection of an application by the Industry Director. The average elapsed time from the date an application was received by the IRS until the Industry Director rendered a decision to accept or reject an application was 44.5 days.

Phase II — PFA Evaluation Process

The second (and final) phase in the PFA pilot program process was the evaluation phase. This phase began when the Industry Director accepted an application into the PFA program and ended when a PFA was executed or the case was otherwise closed. The average elapsed time for the four cases was 438.25 days.

Program Evaluation

The PFA Program Manager ensures that an evaluation of all of the PFA program cases, based on feedback from LMSB employees and taxpayer participants, is conducted. As a part of this program evaluation, participants were asked to provide the actual direct examination time expended to complete the PFA and an estimate of the direct examination time it would have taken to resolve the issue in a post-filing context.

Cumulative Hours (Executed PFAs)	Taxpayer (Hours) (2 executed PFAs)	LMSB (Hours) (3 executed PFAs)
Actual — PFA Process	25,920	17,192
Estimated — Post-Filing Process	59,500	31,860
Estimated Savings	33,580	14,668
Estimated Savings Percentage (Average)	56.4%	46%
Estimated Savings Percentage (Range)	(28%) – 59%	(12.4%) – 61%

One taxpayer who executed a PFA did not participate in the program evaluation phase of the PFA process.

Pre-Filing Agreement Pilot Program Summary

After evaluating the PFA pilot program and receiving input from internal and external participants, the IRS concluded that the PFA program supports the LMSB issue management strategy by assisting taxpayers to resolve issues in a cost efficient and cooperative environment. Accordingly, the IRS issued Rev. Proc. 2001–22, which expanded the PFA program and made it permanent.

Permanent Pre-Filing Agreement Program

PFA Program

As a result of the success of the pilot program, the Service established a permanent PFA Program with the issuance of Rev. Proc. 2001–22. Although many of the procedures remained the same, there were some significant changes, including:

1. All taxpayers within the jurisdiction of LMSB are eligible to participate;
2. More issues are considered appropriate;
3. There are fewer excludible circumstances;
4. Certain international issues are now considered appropriate; and
5. A user fee was implemented for those taxpayers accepted into the program.

PFA Process

The PFA process is managed and conducted by LMSB Industry Directors and field staff, with support from the Office of Pre-Filing and Technical Guidance in LMSB Headquarters. The PFA Program Manager receives all applications and, with the assistance of the Technical Advisors and the Office of Chief Counsel, ensures that the issues presented are appropriate for inclusion in the PFA program.

The Industry Director with jurisdiction over the taxpayer makes the final decision whether to accept a taxpayer's request for participation in the PFA program. The criteria for selecting a request include:

a. The suitability of the issue presented by the taxpayer;
b. The direct or indirect impact of a PFA upon other years, issues, taxpayers, or related cases;
c. The availability of Service resources;
d. The ability and willingness of the taxpayer to dedicate sufficient resources to the process;
e. The likelihood that the PFA may result in contrary positions with respect to an item or transaction ("whipsaw"); and
f. The probability of completing the examination of the issue and entering into a PFA by the target date.

For the cases selected, a mandatory orientation session for the examination team and the taxpayer is conducted. Subsequently, the taxpayer and examination team convene a joint planning meeting to reach agreement on a proposed timeframe, to identify and arrange for IRS access to relevant records and testimony, and to define the potential scope and nature of the PFA.

The examination team conducts the factual determination and issue development consistent with IRS auditing standards. Based upon an examination of the issue, the Team Manager prepares a PFA recommendation for the Industry Director. The Industry Director's decision to enter into a PFA is based on the Team Manager's recommendation and discussions with the PFA Program Manager, Chief Counsel attorneys, appropriate Technical Advisors and the taxpayer. Following Chief Counsel review to ensure that the proposed PFA conforms with guidance provided in Rev. Proc. 68–16 (regarding closing agreements), the Industry Director could execute a PFA if he or she determines that:

a. Entering into the PFA is consistent with the goals of the PFA program as stated in Rev. Proc. 2001–22;
b. The resolution in the PFA reflects settled legal principles and correctly applies those principles (or positions authorized under Delegation Order Nos. 236 or 247) to facts found by the Examination Team; and
c. There appears to be an advantage in having the issue(s) permanently and conclusively closed for the taxable period covered by the PFA, or that the taxpayer shows good and sufficient reasons for desiring a closing agreement and that the United States would sustain no disadvantage

through consummation of such an agreement (see § 301.7121–1(a) of the Procedure and Administration Regulations).

Program Oversight

A designated PFA Program Manager and an analyst assigned to the Office of Pre-Filing and Technical Guidance in LMSB Headquarters provide oversight for the PFA program. The PFA Program Manager provides assistance to taxpayers, Industry Directors and Team Managers throughout the process.

Pre-Filing Agreement Program Accomplishments

Applications Received

Twenty-six applications were received for the permanent PFA program in calendar year 2001. Applications were received from each LMSB industry segment and involved a variety of issues.

Number of Requests Received by Industry

Industry Segment	***Received***
Financial Services	10
Retailers, Food, Pharmaceuticals & Healthcare	3
Natural Resources & Construction	4
Communications, Technology & Media	3
Heavy Manufacturing, Construction & Transportation	6
Total	26

Types of Issues Received

Issue	Received
Deductibility of interest	1
Fair Market Value of Assets	3
Expense vs. Capitalization	1
Tax Basis & Holding Period	1
Excise Tax Allocation	2
Reorganization & Stock Basis	1
Research & Experiment Credit	3
Bad Debts & Worthless Securities	1
Gain on Sale	1
Amortization of Intangibles	1
Class Life Determination	2
Deductibility of Indemnification Payments	1
Acquiring parent — method of accounting	1
NOL Determination	1
Demutualization & IPO	2
Foreign Business Cessation	1
Acquisition & Liquidation	1
Cost Basis Determination	1
Complete Liquidation & Bankruptcy	1
Total	26

Applications Not Accepted

Eight applications were not considered appropriate for the PFA program.

Reasons for Non-acceptance	Applications
Issue Not Suitable or Ineligible	4
International Issue Not Listed in Rev. Proc. 2001–22	1
Not Well-Settled Law	1
Change of Accounting Method (Form 3115)	1
Not Under Jurisdiction of LMSB	1
Total	8

Applications Accepted

Eighteen applications from the twenty-six taxpayer submissions were accepted into the permanent PFA program. The status of these applications on December 31, 2001, was as follows:

Status of PFAs @ 12/31/01	Applications
PFA Request Withdrawn by Taxpayer	1
PFA Request Withdrawn by IRS	1
PFAs In-process	11
PFAs Executed	5
Total	18

Taxpayer Withdrawal (1)

One taxpayer, in accordance with the procedures set forth in Section 8 of Rev. Proc. 2001–22, withdrew from the PFA program after its request had been accepted. This withdrawal was necessitated, in the view of the taxpayer, due to adverse economic conditions within the company causing a reduction in staffing required to successfully continue the PFA process.

IRS Withdrawal (1)

The Service withdrew from the PFA process in another instance where all issue and factual development had been completed and, after considerable discussions with the taxpayer, it was determined that a closing agreement could not be reached on the issue of the amount of allowable research credit.

PFAs In Process (11)

The taxpayers and the respective Industry Directors, in accordance with the provisions of Rev. Proc. 2001–22, have agreed to continue the PFA process in an effort to reach a closing agreement concerning the 11 in-process cases.

PFAs Executed (5)

Five PFAs were completed in calendar year 2001 under the permanent program.

The Office of Chief Counsel provided advice to the examination teams and assisted in the drafting and review of the PFA closing agreements. No Technical Advice or Chief Counsel Advice Memoranda were issued for issues addressed in the PFA process. The executed PFAs covered the following issues:

PFAs Executed by Issue

Deductibility of Interest	1
Class Life Determination	1
Expense vs. Capitalization	1
Amortization of Intangibles	1
Deductibility of Indemnification Payments	1
Total	5

Deductibility of Interest (1)

An agreement was reached between a taxpayer and the Service that, on the basis of the facts presented, the taxpayer was not subject to disallowance of its interest deductions under § 265(a)(2) because its investment in tax-exempt securities was less than 2 percent of its average total assets and therefore it satisfied the 2 percent safe harbor under § 3.05 of Rev. Proc. 72–18.

Class Life Determination (1)

Taxpayer requested a determination whether they had properly assigned class lives and recovery periods for assets capitalized and placed into service during the taxable year (the PFA year). Additionally, the taxpayer requested a determination as to whether certain assets placed in service in prior periods were properly classified. A closing agreement was executed concerning the assets placed in service during the PFA year. Separately, the taxpayer submitted a request for a change of accounting method to the Office of Chief Counsel concerning the reclassification of assets placed in service in prior tax periods which was consistent with the determination in the PFA year.

Expense vs. Capitalization (1)

Taxpayer requested consideration whether certain expenditures for repairs made during the PFA year were properly deductible or should be capitalized and depreciated over the appropriate recovery period. A closing agreement was executed establishing which portion of the total expenditures was properly expensed and which portion was properly capitalized and subject to depreciation.

Amortization of Intangibles (1)

During the PFA year, the taxpayer entered into a taxable transaction in which it acquired certain amortizable intangible assets. The taxpayer requested a determination as to the value of the intangibles acquired. A closing agreement was executed as to such value.

Deductibility of Indemnification Payments (1)

A majority shareholder made certain payments in settlement of litigation on his own behalf and on behalf of a corporate taxpayer. The corporate taxpayer agreed to indemnify the shareholder a negotiated amount. The corporate taxpayer requested a determination concerning the deductibility of the indemnification payments made to the shareholder during the PFA year. A closing agreement was executed regarding the amounts of deductible and non-deductible payments.

Closing Agreements

Five PFAs were executed in the permanent PFA program during calendar year 2001. A pro forma or model agreement does not exist for a PFA. A PFA represents a specific matter closing agreement under § 7121. The closing agreements entered into under this program were prepared with assistance from the Office of Chief Counsel and conform to the guidance provided in Rev. Proc. 68–16.

Processing Statistics

The average elapsed time to resolve the seven cases (five executed PFAs and two withdrawals) described above that were closed in calendar year 2001 was 172.7 days.

Average Processing Time for Seven Cases Closed in 2001	Range (Elapsed Days)	Average (Elapsed Days)
Phase I — Application Screening Process	16–65	46.6
Phase II — PFA Evaluation Process	54–188	126.1
Total Time to Close a PFA Case	105–253	172.7

Phase I — Application Screening Process

Twenty-six applications were received for the PFA program during calendar year 2001. The initial phase was the screening process to determine if an application was appropriate for inclusion in the PFA program. This screening process included obtaining comments from various LMSB functions and Chief Counsel, the review of these comments, and the decision making process on the acceptance/rejection of an application by the Industry Director. The average time from the date an application was received by the IRS until the Industry Director rendered a decision to accept or reject an application was 63.96 days for all twenty-six applications received in the calendar year 2001 and 46.6 days for the seven cases closed in that year.

Phase II — PFA Evaluation Process

The second (and final) phase in the PFA program process was the evaluation phase. This phase began when the Industry Director accepted an application into the PFA program and ended when a PFA was executed or the case was otherwise closed. The average elapsed time for the seven cases closed in calendar year 2001 was 126.1 days.

Program Evaluation

The PFA Program Manager ensures that an evaluation of all of the PFA program cases, based on feedback from LMSB employees and taxpayer participants, is conducted. As a part of this program evaluation, participants were asked to provide the direct examination time expended to complete the PFA and an estimate of the direct examination time it would have taken to resolve the issue in a post-filing context.

Cumulative Hours (5 Executed PFAs)	Taxpayer (Hours)	LMSB (Hours)
Actual — PFA Process	4,583	6,252
Estimated — Post-Filing Process	13,708	11,873
Estimated Savings	9,125	5,621
Estimated Savings Percentage (Average)	66.6%	47.3%
Estimated Savings Percentage (Range)	50%–98.4%	(8.9)%–92.5%

Comparative Analysis — Processing Statistics

Illustrated below are the average elapsed time (in days) processing statistics for the seven pilot cases that closed in calendar year 2000, the remaining four pilot cases closed in calendar year 2001, and the seven permanent program cases closed in calendar year 2001. In the pilot program, the average total time to conclude the first seven cases, as indicated below, was 164.8 days. The range was from a low of 91 days to a high of 186 days. The four pilot cases that started in calendar year 2000 and closed in calendar year 2001 were concluded in an average total time of 482.75 days. Those cases had a range of 322 to 574 days. The average total time to conclude the seven permanent program cases that started and closed in calendar year 2001 was 172.7 days. The range was from 105 to 253 days.

With regard to the four pilot cases completed in calendar year 2001, the increased time can be attributed to the degree of complexity of the issue and the time necessary to develop the factual aspects of the issue. Generally, the more complex and examination intensive the issue is, the greater the time necessary to complete the process.

Regarding the Phase I — Application Screening Process, we have noted the slight increase in average processing time. With respect to the Phase II and Total Time, the results meet our expectations and may be a positive consequence of the slightly increased Phase I time. Other than the contributing factors stated above, our analysis thus far has not revealed any systemic issues giving rise to this phenomenon.

Average Processing Time for PFAs (Days)	**Pilot CY 2000** (7 cases)	**Pilot CY 2001** (4 cases)	**Overall Pilot** (11 cases)	**Program CY 2001** (7 cases)
Phase I — Application Screening Process	34.7	44.5	38.3	46.6
Phase II — PFA Evaluation Process	130.1	438.25	242.2	126.1
Total Time to Complete a PFA	164.8	482.75	280.5	172.7

Pre-Filing Agreement Program Summary

The PFA program is now available to all LMSB taxpayers, including taxpayers that are not currently under examination. While the PFA program will continue to be limited to issues that involve settled legal principles, the list of recommended issues has been expanded, and now includes certain international issues. Generally, the operational procedures used during the PFA pilot program were adopted and enhanced in the permanent PFA program.

Overall, the PFA program is meeting the LMSB strategic program objectives as contained in its issue management strategic initiative. Issues of potential controversy are being resolved more efficiently and on a more current basis yielding benefits to taxpayers and the IRS.

The principal author of this announcement is J. Michael Mann, in the Office of Pre-Filing and Technical Guidance, Large and Mid-Size Business Division. For further information regarding this announcement, contact Mr. Mann at (202) 283–8424 (not a toll-free call).

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.—Intemal 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.

Numerical Finding List[1]

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2002–16, 2002–7 I.R.B. *541*
2002–17, 2002–8 I.R.B. *561*
2002–18, 2002–10 I.R.B. *621*
2002–19, 2002–8 I.R.B. *561*
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2002–21, 2002–8 I.R.B. *562*
2002–22, 2002–8 I.R.B. *562*
2002–23, 2002–8 I.R.B. *563*
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2002–6, 2002–3 I.R.B. *326*
2002–7, 2002–6 I.R.B. *489*
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2002–9, 2002–5 I.R.B. *450*
2002–10, 2002–6 I.R.B. *490*
2002–11, 2002–7 I.R.B. *526*
2002–12, 2002–7 I.R.B. *526*
2002–13, 2002–8 I.R.B. *547*
2002–14, 2002–8 I.R.B. *548*
2002–15, 2002–8 I.R.B. *548*
2002–16, 2002–9 I.R.B. *567*
2002–17, 2002–9 I.R.B. *567*
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2002–19, 2002–10 I.R.B. *619*
2002–20, 2002–17 I.R.B. *796*
2002–21, 2002–14 I.R.B. *730*
2002–22, 2002–14 I.R.B. *731*
2002–23, 2002–15 I.R.B. *742*
2002–24, 2002–16 I.R.B. *785*
2002–25, 2002–15 I.R.B. *743*
2002–26, 2002–15 I.R.B. *743*
2002–27, 2002–18 I.R.B. *814*
2002–28, 2002–16 I.R.B. *785*
2002–29, 2002–17 I.R.B. *797*
2002–30, 2002–17 I.R.B. *797*
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2002–34, 2002–21 I.R.B. *990*
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REG–167648–01, 2002–16 I.R.B. *790*
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2002–8, 2002–1 I.R.B. *252*
2002–9, 2002–3 I.R.B. *327*
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2002–11, 2002–7 I.R.B. *526*
2002–12, 2002–3 I.R.B. *374*
2002–13, 2002–8 I.R.B. *549*
2002–14, 2002–5 I.R.B. *450*
2002–15, 2002–6 I.R.B. *490*
2002–16, 2002–9 I.R.B. *572*
2002–17, 2002–13 I.R.B. *676*
2002–18, 2002–13 I.R.B. *678*
2002–19, 2002–13 I.R.B. *696*
2002–20, 2002–14 I.R.B. *732*
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2002–22, 2002–14 I.R.B. *733*
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[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2001–27 through 2001–53 is in Internal Revenue Bulletin 2002–1, dated January 7, 2002.

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8974, 2002–3 I.R.B. *318*
8975, 2002–4 I.R.B. *379*
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8978, 2002–7 I.R.B. *500*
8979, 2002–6 I.R.B. *466*
8980, 2002–6 I.R.B. *477*
8981, 2002–7 I.R.B. *496*
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8986, 2002–16 I.R.B. *780*
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97–49
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T.D. 8994, 2002–23 I.R.B. *1078*

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98–43
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2001–68
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Notice 2002–15, 2002–8 I.R.B. *548*

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REG–113526–98
Withdrawn by
REG–105369–00, 2002–18 I.R.B. *828*

REG–107100–00
Corrected by
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REG–107566–00
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Ann. 2002–30, 2002–11 I.R.B. *632*

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Corrected by
Ann. 2002–30, 2002–11 I.R.B. *632*

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Ann. 2002–30, 2002–11 I.R.B. *632*

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Ann. 2002–30, 2002–11 I.R.B. *632*

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85–16
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87–32
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87–50
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89–45
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91–71
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96–13
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Rev. Proc. 2002–1, 2002–1 I.R.B. *1*

97–27
Modified and amplified by
Rev. Proc. 2002–19, 2002–13 I.R.B. *696*

98–23
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98–49
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[2] A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2001–27 through 2001–53 is in Internal Revenue Bulletin 2002–1, dated January 7, 2002.

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Superseded by
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Supplemented by
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2001–41
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Rev. Proc. 2002–2, 2002–1 I.R.B. *82*

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Rev. Proc. 2002–3, 2002–1 I.R.B. *117*

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2002–6
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61–146
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Rev. Rul. 2002–3, 2002–3 I.R.B. *316*

64–328
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73–305
Superseded by
Rev. Proc. 2002–26, 2002–15 I.R.B. *746*

76–270
Amplified and superseded by
Rev. Rul. 2002–20, 2002–17 I.R.B. *794*

79–151
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Rev. Rul. 2002–19, 2002–16 I.R.B. *778*

79–284
Superseded by
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Superseded by
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87–112
Clarified by
Rev. Rul. 2002–22, 2002–19 I.R.B. *849*

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89–29
Obsoleted by
T.D. 8976, 2002–5 I.R.B. *421*

92–19
Supplemented in part by
Rev. Rul. 2002–12, 2002–11 I.R.B. *624*

2002–7
Corrected by
Ann. 2002–13, 2002–7 I.R.B. *540*

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Corrected by
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8973
Corrected by
Ann. 2002–14, 2002–7 I.R.B. *540*

8975
Corrected by
Ann. 2002–21, 2002–8 I.R.B. *562*

8976
Corrected by
Ann. 2002–21, 2002–8 I.R.B. *562*

8978
Corrected by
Ann. 2002–39, 2002–14 I.R.B. *738*

8985
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