INTERNAL REVENUE
BULLETIN

IRS

HIGHLIGHTS OF THIS ISSUE

Bulletin No. 2019–47
November 18, 2019

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.

ADMINISTRATIVE, ESTATE TAX, EXCISE TAX, GIFT TAX, INCOME TAX

Rev. Proc. 2019-44, page 1093.

This procedure provides the 2020 cost-of-living adjustments to certain items due to inflation as required by various provisions of the Code and Service guidance.

EMPLOYEE PLANS

Notice 2019-59, page 1091.

Section 415 of the Internal Revenue Code (the Code) provides for dollar limitations on benefits and contributions under qualified retirement plans. Section 415(d) requires that the Secretary of the Treasury annually adjust these limits for cost of living increases. Other limitations applicable to deferred compensation plans are also affected by these adjustments under § 415. Under § 415(d), the adjustments are to be made under adjustment procedures similar to those used to adjust benefit amounts under § 215(i)(2)(A) of the Social Security Act.

INCOME TAX

REG-123112-19, page 1104.

This document announces that the Department of the Treasury (Treasury Department) and the IRS intend to issue proposed regulations regarding the treatment of certain interests in corporations as stock or indebtedness and requests comments from the public regarding the contemplated rules. This document also announces that, following the expiration of the 2016 Temporary Regulations (described in the Background section of this advance notice of proposed rulemaking), a taxpayer may rely on the 2016 Proposed Regulations (also described in the Background) until further notice is given in the Federal Register, provided that the taxpayer consistently applies the rules in the 2016 Proposed Regulations in their entirety.

T.D. 9879, page 1052.

TD 9879 provides guidance relating to information reporting obligations for reportable policy sales of life insurance contracts under §6050Y, which was added by section 13520 of the 2017 Tax Cuts and Jobs Act (the TCJA). TD 9879 also provides guidance under §101, as amended by section 13522 of the TCJA, for reportable policy sales and to make certain other related changes to the existing regulations under §101.

T.D. 9880, page 1085.

This Treasury Decision removes final regulations identified by the Secretary of the Treasury as imposing an undue financial burden on taxpayers and as being unduly complex. The final regulations being removed set forth minimum documentation requirements that ordinarily must be satisfied in order for certain related-party interests in a corporation to be treated as indebtedness for federal tax purposes. This document also adopts conforming amendments to other final regulations to reflect the removal of those regulations.

Finding Lists begin on page ii.

The IRS Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the 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.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

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

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

Part I

26 CFR 1.101-1; 26 CFR 1.6050Y-1; 26 CFR 1.6050Y-2; 26 CFR 1.6050Y-3; 26 CFR 1.6050Y-4

T.D. 9879

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Information Reporting for Certain Life Insurance Contract Transactions and Modifications to the Transfer for Valuable Consideration Rules

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations providing guidance on new information reporting obligations under section 6050Y related to reportable policy sales of life insurance contracts and payments of reportable death benefits. The final regulations also provide guidance on the amount of death benefits excluded from gross income under section 101 following a reportable policy sale. The final regulations affect parties involved in certain life insurance contract transactions, including reportable policy sales, transfers of life insurance contracts to foreign persons, and payments of reportable death benefits.

DATES: *Effective Date*: These regulations are effective October 31, 2019.

Applicability Date: For dates of applicability, see §§1.101-6 and 1.6050Y-1(b).

FOR FURTHER INFORMATION CONTACT: Kathryn M. Sneade, (202) 317-6995 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 under sections 101 and 6050Y of the Internal Revenue Code (Code). These amendments (final regulations) implement legislative changes to sections 101 and 6050Y of the Code by sections 13520 and 13522 of Pub. L. No. 115-97 (131 Stat. 2054, 2149, 2151), commonly referred to as the Tax Cuts and Jobs Act (TCJA). The final regulations under section 101 amend final regulations under section 101 published in the **Federal Register** on November 26, 1960 (25 FR 11402), as subsequently amended on December 24, 1964 (29 FR 18356), September 27, 1982 (47 FR 42337), and July 26, 2007 (72 FR 41159) (existing regulations).

Section 13520 of the TCJA added section 6050Y to chapter 61 (Information and Returns) of subtitle F of the Code (chapter 61). Section 6050Y imposes information reporting obligations related to certain life insurance contract transactions, including reportable policy sales and payments of reportable death benefits. Section 6050Y provides that each of the returns required by section 6050Y is to be made "at such time and in such manner as the Secretary shall prescribe." The final regulations under section 6050Y implement section 6050Y by specifying the manner in which and time at which the information reporting obligations must be satisfied. The final regulations also provide definitions and rules that govern the application of the information reporting obligations.

Section 13522 of the TCJA amended section 101. New section 101(a)(3) defines the term "reportable policy sale" and provides rules for determining the amount of death benefits excluded from gross income following a reportable policy sale. The final regulations under section 101 provide definitions applicable under sections 101 and 6050Y and guidance for determining the amount of death benefits excluded from gross income following a reportable policy sale.

Notice 2018-41, 2018-20 I.R.B. 584, described sections 13520 and 13522 of the TCJA and the regulations the Department of the Treasury (Treasury Department) and the IRS expected to propose under section 6050Y, requested comments on the definition of "reportable policy sale" set forth in section 101(a)(3)(B), among other things, and identified the need for regulations providing guidance on the application of section 101(a) following the addition of section 101(a)(3) to the Code. The Treasury Department and the IRS received comments in response to the notice and considered these comments in developing the proposed regulations.

The Treasury Department and the IRS published proposed regulations under sections 101 and 6050Y (REG-103083-18) in the **Federal Register** (84 FR 11009) on March 25, 2019 (proposed regulations). The Treasury Department and the IRS received public comments on the proposed regulations and held a public hearing on June 5, 2019.

After consideration of all of the comments on the proposed regulations, the proposed regulations are adopted as amended by this Treasury decision.

Summary of Comments and Explanation of Revisions

This section discusses the public comments received on the proposed regulations and explains the revisions adopted by the final regulations in response to those comments.

1. *Comments and Changes Relating to Applicability Dates*

A. *Applicability date for section 6050Y regulations*

Section 1.6050Y-1 of the proposed regulations provides that the rules in §1.6050Y-1 through 1.6050Y-4 of the proposed regulations apply to reportable policy sales made and reportable death benefits paid after December 31, 2017, and provides transition relief with respect to reporting required on reportable policy sales and payments of reportable death benefits occurring after December 31, 2017, and before the date final regulations under section 6050Y are published in the **Federal Register**.

One commenter recommended that reporting obligations under section 6050Y (as well as application of the rules under section 101 relating to section 6050Y) be delayed until 60 days after the date the final regulations are published in the **Federal Register**. Informal comments also were received requesting transition relief (such as delayed reporting) or permanent relief with respect to the reporting obligations under section 6050Y for reportable policy sales and payments of reportable death benefits occurring after December 31, 2017, and before January 1, 2019 (such as waiving the reporting obligations for this period). One commenter requested that at least an additional 30 days be added to the 90-day relief period provided in §1.6050Y-1(b)(2) and (3) of the proposed regulations for filing returns and furnishing statements required under section 6050Y(b) and (c) and §1.6050Y-3 and 1.6050Y-4 of the proposed regulations, to give issuers at least 60 days to complete their reporting after the 60-day extension period provided to acquirers of an interest in a life insurance contract under §1.6050Y-1(b)(1) of the proposed regulations. The commenter asserted that issuers require significantly more time than the 30 days effectively provided to complete Forms 1099-SB, "Seller's Investment in Life Insurance Contract," and 1099-R "Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.", and to add new forms (such as Form 1099-SB) to their systems. The commenter stated that issuers must identify policies that are subject to reporting once the Forms 1099-LS, "Reportable Life Insurance Sale," are received as well as enhance systems to track these policies over their life and transmit data between various systems in order to accurately report under sections 6050Y(b) and (c).

In response to these comments, and to give acquirers and issuers ample time to develop and implement reporting systems, the final regulations provide that the rules in §§1.6050Y-1 through 1.6050Y-4 of the final regulations apply to reportable policy sales made and reportable death benefits paid after December 31, 2018. *See* §1.6050Y-1(b) of the final regulations. As a result, no reporting is required under section 6050Y for reportable policy sales made and reportable death benefits paid after December 31, 2017, and before January 1, 2019.

Section 1.6050Y-1(a)(12) of the final regulations defines "reportable death benefits" as "amounts paid by reason of the death of the insured under a life insurance contract that are attributable to an interest in the contract that was transferred in a reportable policy sale." Accordingly, because the definition of "reportable policy sale" under §1.6050Y-1(a)(14) of the final regulations applies only to transfers of interests in life insurance contracts made after December 31, 2018, death benefits are "reportable death benefits" under §1.6050Y-1(a)(12) of the final regulations and are subject to the reporting requirements of §1.6050Y-4 of the final regulations only if the death benefits are paid by reason of the death of the insured under a life insurance contract transferred after December 31, 2018, in a reportable policy sale.

The final regulations also provide transition relief as set forth in the proposed regulations with two modifications. First, the transition relief applies with respect to reportable policy sales made and reportable death benefits paid after December 31, 2018, and on or before October 31, 2019. Second, as requested by one of the commenters, §1.6050Y-1(b)(3), (4), and (5) of the final regulations provide issuers with at least 120 days after the final regulations are published in the **Federal Register** to file returns and furnish statements under section 6050Y(b) and (c) and §§1.6050Y-3 and 1.6050Y-4 of the final regulations. These features of the final regulations are intended to give acquirers and issuers ample time to develop and implement reporting systems.

Noting that 250 or more information returns of a single taxpayer must be filed electronically, one commenter requested waivers from electronic filing for 2018 and 2019 issuer reporting under section 6050Y(b) and (c). The Treasury Department and the IRS have determined not to provide the requested waiver in the final regulations under section 6050Y because procedures already exist for any person required to file 250 or more returns during the calendar year to request a waiver from the requirement to file electronically by showing hardship. *See* §301.6011-2(c).

B. *Applicability date for section 101 regulations*

Section 1.101-6(b) of the proposed regulations provides that, for purposes of section 6050Y, §1.101-1(b), (c), (d), (e), (f), and (g) apply to reportable policy sales made after December 31, 2017, and to reportable death benefits paid after December 31, 2017. Section 1.101-6(b) of the proposed regulations further provides that, for any other purpose, §1.101-1(b), (c), (d), (e), (f), and (g) apply to transfers of life insurance contracts, or interests therein, made after the date the Treasury decision adopting the proposed regulations as final regulations is published in the **Federal Register**.

Several commenters requested clarification regarding the applicability dates set forth in §1.101-6(b) of the proposed regulations. Two of these commenters requested that the Treasury Department and the IRS clarify that the rules issued with respect to section 101(a)(3) apply to all transfers of life insurance contracts, or interests therein, made after December 31, 2017, or alternatively, that the Treasury Department and the IRS allow taxpayers to rely upon the rules in §1.101-1 of the proposed regulations for transactions undertaken after December 31, 2017, and before the date that the Treasury Department adopts final rules. Another commenter recommended that application of the rules under section 101 (as well as the reporting obligations under section 6050Y) be delayed until 60 days after the date the final regulations are published in the **Federal Register**, but suggested that language should be included in the preamble to the final regulations to provide that taxpayers may rely on the proposed regulations for the period prior to the effective date of the final regulations.

Because the final regulations provide that the reporting obligations under section 6050Y apply to reportable policy sales and payments of reportable death benefits occurring after December 31, 2018, for purposes of determining whether a transfer of an interest in a life insurance contract is a reportable policy sale or a payment of death benefits is a payment of reportable death benefits subject to the reporting requirements of section 6050Y and §§1.6050Y-1 through 1.6050Y-4 of the final regulations, the definitions and rules set forth in §1.101-1(b) through (g) of the final regulations apply to reportable policy sales made after December 31, 2018, and to reportable death benefits paid after December 31, 2018. *See* §§1.101-6(b) and 1.6050Y-1(b) of the final regulations.

The final regulations provide that, for other purposes, specifically for purposes of determining the amount of the proceeds of life insurance contracts payable by reason of death excluded from gross income under section 101, §1.101-1(b) through (g) of the final regulations apply to amounts paid by reason of the death of the insured under a life insurance contract, or interest therein, transferred after October 31, 2019. However, under section 7805(b)(7), a taxpayer may apply the rules set forth in §1.101-1(b) through (g) of the final regulations, in their entirety, with respect to all amounts paid by reason of the death of the insured under a life insurance contract, or interest therein, transferred after December 31, 2017, and on or before October 31, 2019.

2. *Comments and Changes Relating to §1.101-1(b) of the Proposed Regulations*

Generally, amounts received under a life insurance contract that are paid by reason of the death of the insured are excluded from gross income for Federal income tax purposes under section 101(a)(1). However, if a life insurance contract or interest therein is sold or otherwise transferred for valuable consideration, the "transfer for value rule" set forth in section 101(a)(2) limits the excludable portion of the amount received by reason of the death of the insured to the sum of the consideration paid for the contract or interest therein and any premiums and other amounts subsequently paid by the transferee with respect to the contract or interest therein. Section 101(a)(2)(A) and (B) provide two exceptions to this transfer for value rule. One exception (the "certain person exception") applies to transfers to the insured, a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder or officer ("certain persons"). *See* section 101(a)(2)(B). The other exception (the "carryover basis exception") applies if the transferee's basis for determining gain or loss in the life insurance contract or interest therein is determined in whole or in part by reference to the transferor's basis in the contract or interest therein. *See* section 101(a)(2)(A). Under section 101(a)(3), which was added by section 13522 of the TCJA, neither of these exceptions to the transfer for value rule applies in the case of a transfer of a life insurance contract, or any interest therein, that is a reportable policy sale.

Section 1.101-1(b)(1)(i) of the proposed regulations provides the general transfer for value rule set forth in section 101(a)(2). Section 1.101-1(b)(1)(ii) of the proposed regulations sets forth the exceptions from this general rule for transfers for valuable consideration that are not reportable policy sales (the certain person exception and carryover basis exception provided in section 101(a)(2)). Section 1.101-1(b)(2) of the proposed regulations provides rules regarding gratuitous transfers of interests in life insurance contracts, as well as transfers of only a part of an interest in a life insurance contract and bargain sales of an interest in a life insurance contract (that is, transfers that are in part gratuitous and in part transfers for valuable consideration). This section of this Summary of Comments and Explanation of Revisions discusses comments received on §1.101-1(b) of the proposed regulations.

A. *Transfers to certain persons*

One commenter on the proposed regulations described a life insurance policy subject to the section 101(a)(2) transfer for value rule as "tainted," in that death benefits paid under the policy are no longer fully excluded from income under section 101(a)(1). The commenter asked that the final regulations provide for removal of the "taint" by a transfer to the insured, as was permitted before the TCJA, and asked for clarification regarding whether a transfer of a policy to the insured must be a sale for fair market value to remove the "taint" of a transfer for valuable consideration. The commenter suggested that mistakes happen, including the mistake of not seeking tax advice from a professional who knows the section 101 rules, and that taxpayers should be able to take corrective measures to remove this "taint." The commenter noted that the insured may no longer have a business or other need for the current transferee to own the policy and may wish to hold the policy to protect the insured's family, or the insured may regret selling the policy and wish to buy the policy back after the policy was transferred in a reportable policy sale. The commenter pointed out that §1.101-1(b)(3)(ii) of the existing regulations (not yet revised to reflect TCJA changes to section 101) currently provides such a corrective measure, allowing the "taint" to be removed by a transfer of the policy to certain persons. However, §1.101-1(b)(1)(ii)(B)(*2*) of the proposed regulations makes this corrective measure unavailable to the extent that the transfer to those certain persons was preceded by a transfer of the policy for valuable consideration in a reportable policy sale. The commenter also noted that §1.101-1(b)(3)(ii) of the existing regulations does not require the corrective transfer to be a sale for fair market value, and that §1.101-1(b)(1)(ii)(B)(*1*) of the proposed regulations does not impose such a requirement. The commenter suggested that *Example 1*, *Example 2*, and *Example 3* in §1.101-1(g)(1), (2), and (3) of the proposed regulations, read together, however, appear to require that the transfer to the insured be a sale for fair market value to clear the "taint" of a prior transfer for valuable consideration. The commenter asked for clarification on this point. The commenter suggested that the transfer to the insured be available as a corrective measure even if that transfer was preceded by a reportable policy sale, and, to prevent any possible abuse, that the insured be required to pay fair market value if the policy previously had been transferred in a reportable policy sale.

Section 1.101-1(b)(1)(ii)(B)(*1*) of the proposed regulations does not explicitly require that the valuable consideration for a transfer of an interest in a life insurance contract be equal to the interest's fair market value, but, in the case of a bargain sale, the rules implementing the provisions of section 101 are applied separately to the sale and gift portions of the transferred interest. Under §1.101-1(b)

(2)(iii) of the proposed regulations, part of the transfer in a bargain sale is treated as a gratuitous transfer subject to §1.101-1(b)(2)(i) of the proposed regulations. *Example 1*, *Example 2*, and *Example 3* in §1.101-1(g)(1), (2), and (3) of the proposed regulations are intended to illustrate the application of the rules implementing the changes made by the TCJA. For the sake of simplicity, the consideration in these examples equals fair market value, so the bargain sale rules do not apply. The final regulations include an example that illustrates the application of the bargain sale rules. *See Example 7* in §1.101-1(g)(7) of the final regulations.

In response to the comments received, the final regulations provide for a fresh start with respect to an interest gratuitously transferred to the insured, provided the interest has not previously been transferred for value in a reportable policy sale. *See* §1.101-1(b)(2)(i) of the final regulations. *Example 2* in §1.101-1(g)(2) of the final regulations illustrates the application of this rule. The final regulations also provide for a fresh start with respect to an interest (or portion thereof) that is transferred to the insured following a reportable policy sale of the interest for valuable consideration, but only to the extent that the insured pays fair market value for the interest and only with respect to the interest (or relevant portion thereof) transferred to the insured that is not subsequently transferred in a transfer for valuable consideration or in a reportable policy sale. *See* §1.101-1(b)(1)(ii)(B)(*3*) of the final regulations. The application of this rule is illustrated in revised *Example 6*, new *Example 7*, new *Example 8*, and new *Example 9* in §1.101-1(g)(6), (g)(7), (g)(8), and (g)(9) of the final regulations.

B. *Gratuitous transfers*

Under §1.101-1(b)(2)(i) of the proposed regulations, the amount of the policy proceeds attributable to a gratuitously transferred interest in a life insurance policy that is excludable from gross income under section 101(a)(1) is limited to the sum of the amount attributable to the gratuitously transferred interest that would have been excludable by the transferor if the transfer had not occurred, and the premiums and other amounts subsequently paid by the transferee with respect to the interest. Unlike the existing regulations, the proposed regulations do not provide a special rule for a gratuitous transfer made by or to certain persons.[1] As explained in the preamble to the proposed regulations, such a rule is not required by section 101(a), and a special rule for these transfers could be subject to abuse. *See* 84 FR 11009, 11017.

Section 1.101-1(b)(2)(i) of the proposed regulations applies to any gratuitous transfer of an interest in a life insurance contract, "including a reportable policy sale that is not for valuable consideration." One commenter requested that this language be deleted, asserting that including gratuitous transfers within the definition of reportable policy sales is not consistent with section 101.[2] The commenter noted that the title of section 101(a)(3) is "Exception to valuable consideration rules for commercial transactions," which the commenter asserted makes clear that a reportable policy sale can occur only if there has been a transfer for valuable consideration. The commenter further asserted that the provisions of section 101(a)(3)(A) and (B) limit the relevance of reportable policy sales to those situations in which a taxpayer needs to determine whether one of the section 101(a)(2) exceptions applies and, because those exceptions are never relevant for gratuitous transfers, reportable policy sales are never relevant for gratuitous transfers.

The TCJA added section 101(a)(3)(A) to provide that the two pre-existing exceptions to the transfer for value rules no longer apply if the transfer is a reportable policy sale. Section 101(a)(3)(B) defines a reportable policy sale as any acquisition of an interest in a life insurance contract in the absence of the described relationship between the acquirer and insured. Although the availability of exceptions from the transfer for value rules is not directly relevant to a gratuitous transfer standing alone, the acquisition of an interest in a contract by an acquirer that does not have the described relationship with the insured, including a gratuitous transfer, may affect the exclusion of the policy proceeds from gross income under section 101(a) and the regulations thereunder if there are subsequent transfers. Consistent with the statutory language, the definition of a reportable policy sale in the final regulations does not exclude gratuitous transfers.

3. *Comments and Changes Relating to §1.101-1(c) of the Proposed Regulations*

Under section 101(a)(3)(B) and §1.101-1(c)(1) of the proposed regulations, a reportable policy sale is, as a general matter, any direct or indirect acquisition of an interest in a life insurance contract if the acquirer has, at the time of the acquisition, no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in the life insurance contract. Exceptions to the definition of reportable policy sale for transfers between certain related entities are provided in §1.101-1(c)(2)(i) and (ii) of the proposed regulations. Section 1.101-1(c)(2)(iii) of the proposed regulations sets forth exceptions from the definition of reportable policy sales for certain indirect acquisitions. This section of this Summary of Comments and Explanation of Revisions discusses comments received on §1.101-1(c) of the proposed regulations.

[1] Under §1.101-1(b)(2) of the existing regulations, in the case of a gratuitous transfer, by assignment or otherwise, of a life insurance policy or any interest therein, the amount of the proceeds attributable to such policy or interest that is excludable from the transferee's gross income under section 101(a) is, as a general rule, limited to the sum of the amount which would have been excludable by the transferor if no such transfer had taken place and any premiums and other amounts subsequently paid by the transferee with respect to the interest. However, if the gratuitous transfer in question is made by or to the insured, a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder or officer, the entire amount of the proceeds attributable to the policy or interest transferred is excludable from the transferee's gross income.

[2] The commenter also asserted that this language creates unnecessary and confusing reporting requirements under section 6050Y for gift transfers and is inconsistent with the statutory language, which, according to the commenter, indicates that a reportable policy sale must be a transfer for value. The commenter's concerns about reporting are discussed in section 10.A of this Summary of Comments and Explanation of Revisions.

A. *Pre-TCJA acquisitions*

Two commenters on the proposed regulations requested clarification regarding the application of §1.101-1(c)(2)(iii)(A) with respect to the indirect acquisition of an interest in a life insurance contract if the entity that directly holds the interest acquired the interest before January 1, 2018 (that is, before the existence of any reporting requirements under section 6050Y(a)). Both commenters recommended that an exception from the definition of reportable policy sale be provided with respect to the indirect acquisition of an interest in a life insurance contract by a person if the partnership, trust, or other entity that directly holds the interest in the life insurance contract acquired the interest before January 1, 2018. One commenter recommended that, if the requested exception is not provided, the partnership, trust, or other entity in which the investment interest is purchased should be permitted to undertake the applicable reporting, instead of requiring the investor to navigate the complexities of the reporting requirements. This commenter also suggested that, if the requested exception is provided, the partnership, trust, or other entity could file an information return with the IRS for its portfolio of policies acquired prior to January 1, 2018, as a transition solution. However, the other commenter suggested that the partnership, trust, or other entity may not have tracked or retained information sufficient to satisfy the reporting requirements under section 6050Y with respect to interests acquired before January 1, 2018.

In response to these comments, §1.101-1(c)(2)(iii)(A) of the final regulations provides an exception from the definition of reportable policy sale with respect to the indirect acquisition of an interest in a life insurance contract by a person if a partnership, trust, or other entity in which an ownership interest is being acquired directly or indirectly holds the interest in the life insurance contract and acquired that interest before January 1, 2019, or acquired that interest in a reportable policy sale reported in compliance with section 6050Y(a) and §1.6050Y-2.[3]

B. *Additional requests for expanded indirect acquisition exceptions*

One commenter on the proposed regulations identified the existence of a possible technical issue with §1.101-1(c)(2)(iii)(A) of the proposed regulations, which provides an exception from reportable policy sale status for certain indirect acquisitions. The commenter noted that, under this provision, the indirect acquisition of an interest in a life insurance contract is not a reportable policy sale if the partnership, trust, or other entity that directly holds the interest in the life insurance contract acquired the interest in a reportable policy sale that was reported in compliance with section 6050Y(a) and the regulations thereunder. The commenter described a fact pattern in which legal title to a life insurance contract is held by a nominee (for example, a securities intermediary) on behalf of a partnership, trust, or other entity (for example, an investment fund). The commenter concluded that, in this fact pattern, the exception in §1.101-1(c)(2)(iii)(A) of the proposed regulations cannot apply to an investor in the partnership, trust, or other entity because the investor's ownership interest is in the partnership, trust, or other entity (which does not hold a direct interest in the life insurance contract), not in the nominee (which directly holds the legal interest in the life insurance contract). The commenter also recommended that §1.101-1(c)(2)(iii)(A) be revised to clarify that the exception applies if reporting under section 6050Y is done by either the legal owner of the life insurance contract (such as a securities intermediary holding legal title as a nominee) or the beneficial owner of the life insurance policy that controls the life insurance contract under a securities account agreement (such as an investment fund).

In the fact pattern described in the comment letter, the partnership, trust, or other entity in which the investor acquires an ownership interest holds an interest in the life insurance contract. An interest in a life insurance contract is not limited to legal ownership of the contract. Instead, any person that acquires an enforceable right to receive all or a part of the proceeds of the life insurance contract or acquires the right to any other economic benefits of the policy as described in §20.2042-1(c)(2) acquires an interest in the life insurance contract under §1.101-1(e)(1) of the proposed regulations.

The partnership, trust, or other entity described by the commenter presumably would hold such an interest directly, even though legal title to the life insurance contract is held by a nominee or other intermediary. By acquiring an interest in the partnership, trust, or other entity, the investor indirectly would acquire a beneficial interest in the life insurance contract. The exception in §1.101-1(c)(2)(iii)(A) of the proposed regulations would apply to this indirect acquisition if the partnership, trust, or other entity reported its acquisition of the beneficial interest in the contract in compliance with section 6050Y(a). The commenter's recommended revision to §1.101-1(c)(2)(iii)(A) of the proposed regulations therefore is not adopted in the final regulations.

The commenter also proposed that §1.101-1(c)(2)(iii)(A) of the proposed regulations be modified to apply if "the partnership, trust, or other entity that directly *or indirectly* holds the interest in the life insurance contract acquired that interest in a reportable policy sale reported in compliance with section 6050Y(a) and §1.6050Y-2." This change is adopted in the final regulations, which also clarify that the partnership, trust, or other entity must be a partnership, trust, or other entity in which an ownership interest is being acquired. As modified, the exception applies to the indirect acquisition of an interest in a life insurance contract by a person acquiring an ownership interest in a partnership, trust, or other entity that holds the interest in the life insurance contract, regardless of whether the person's ownership interest in the partnership, trust, or other entity that reported its acquisition of the interest in the life insurance contract is direct or in-

[3] As discussed in section 1.A of this Summary of Comments and Explanation of Revisions, the final regulations provide that the reporting obligations under section 6050Y apply to reportable policy sales and payments of reportable death benefits occurring after December 31, 2018. *See* §1.6050Y-1(b) of the final regulations. Section 3.B of this Summary of Comments and Explanation of Revisions describes changes adopted in §1.101-1(c)(2)(iii)(A) of the final regulations in response to other comments requesting expanded indirect acquisition exceptions.

direct and regardless of whether that partnership, trust, or other entity acquired its interest in a direct or indirect acquisition, provided the partnership, trust, or other entity acquired its interest in a reportable policy sale reported in compliance with section 6050Y(a) and §1.6050Y-2 or, as discussed in section 3.A of this Summary of Comments and Explanation, acquired its interest before January 1, 2019.

One commenter on the proposed regulations reiterated its previous request, made in comments on Notice 2018-41, that an exception from the reporting requirements of section 6050Y be provided with respect to an indirect acquisition of an interest in a life insurance contract by any investor that acquires a 5 percent or less economic and voting interest in an investment vehicle that holds, directly or indirectly, life insurance policies, with the added proviso that the investor must not be an officer or director of the investment vehicle. Section 1.101-1(c)(2)(iii)(B) of the proposed regulations provides that the indirect acquisition of an interest in a life insurance contract is not a reportable policy sale if the acquirer and his or her family members own, in the aggregate, 5 percent or less of the partnership, trust, or other entity that directly holds the interest in the life insurance contract, but this exception applies only if, immediately before the acquisition, no more than 50 percent of the gross value of the assets of the partnership, trust, or other entity that directly holds the interest in the life insurance contract consists of life insurance contracts.

The final regulations do not adopt the proposed change because, if more than 50 percent of an entity's asset value is life insurance contracts, investment in life insurance contracts is likely the entity's primary business activity, and it is reasonable to expect even small investors to be able to determine the primary activity of the business they are investing in, regardless of whether they are also officers or directors of the entity. In addition, any investor that does not qualify for the exception set forth in §1.101-1(c)(2)(iii)(B) of the final regulations because more than 50 percent of the gross value of the assets of the partnership, trust, or other entity that directly holds the interest in the life insurance contract consists of life insurance contracts may still qualify for the exception set forth in §1.101-1(c)(2)(iii)(A) of the final regulations if a partnership, trust, or other entity that directly or indirectly holds the interest in the life insurance contract acquired the interest before January 1, 2019, or acquired that interest in a reportable policy sale reported in compliance with section 6050Y(a) and §1.6050Y-2.

Separately, §1.101-1(c)(2)(iii)(B) of the final regulations clarifies that, if the partnership, trust, or other entity in which the acquirer is directly acquiring an ownership interest indirectly holds an interest in one or more life insurance contracts, (i) the assets of the partnership, trust, or other entity in which the ownership interest is being acquired are tested to determine whether more than 50 percent of the gross value of the assets of that partnership, trust, or other entity consists of life insurance contracts, and (ii) the ownership interest in that partnership, trust, or other entity held by the acquirer and his or her family members after the acquisition is tested to determine whether they hold more than a 5 percent ownership interest in the entity. The assets of the partnership, trust, or other entity that directly holds the interest in the life insurance contract and the interest in that partnership, trust, or other entity held by the acquirer and his or her family member are tested only if the acquirer is directly acquiring an ownership interest in that partnership, trust, or other entity.

4. *Comments and Changes Relating to §1.101-1(e) of the Proposed Regulations*

Section 1.101-1(e) of the proposed regulations defines the terms used to determine whether there has been an acquisition of an interest in a life insurance contract. This section of this Summary of Comments and Explanation of Revisions discusses comments that generally relate to the definitions in §1.101-1(e) of the proposed regulations.

A. *Interest in a life insurance contract*

Under §1.101-1(e)(1) of the proposed regulations, an "interest in a life insurance contract" is generally defined as the interest held by any person that has taken title to or possession of the life insurance contract, in whole or part, for state law purposes, and the interest held by any person that has an enforceable right to receive all or a part of the proceeds of the life insurance contract or to any other economic benefits of the policy as described in §20.2042-1(c)(2). Section 1.101-1(e)(2) of the proposed regulations provides that the term "transfer of an interest in a life insurance contract" means the transfer of any interest in the life insurance contract, including any transfer of title to, possession of, or legal or beneficial ownership of the life insurance contract itself. Under §1.101-1(e)(3) of the proposed regulations, the acquisition of an interest in a life insurance contract may be direct or indirect, as described in §1.101-1(e)(3)(i) (defining "direct acquisition of an interest in a life insurance contract") and (ii) (defining "indirect acquisition of an interest in a life insurance contract").

One commenter on the proposed regulations suggested that, in a life settlement transaction in which a securities intermediary holds legal title to the acquired life insurance contract as nominee for the new beneficial owner of the life insurance contract pursuant to a securities account agreement, the new beneficial owner does not acquire an interest in the life insurance contract under §1.101-1(e)(3) of the proposed regulations, even though the new beneficial owner controls and enjoys all of the benefits of the life insurance policy, because the new beneficial owner neither acquires legal title to the life insurance policy nor holds an ownership interest in the securities intermediary holding legal title. However, under the proposed regulations, the new beneficial owner acquires an interest in the life insurance contract because it acquires control of all of the benefits of the life insurance policy. Any person that acquires an enforceable right to receive all or a part of the proceeds of the life insurance contract or to any other economic benefits of the policy as described in §20.2042-1(c)(2) acquires an interest in the life insurance contract under §1.101-1(e)(1) of the proposed regulations. In the situation described in the comment, after the life settlement transaction, there are two persons who have an interest in the life insurance contract at issue: the legal title holder and the new beneficial owner. *Example 16* of §1.101-1(g)(16) of the final regulations illustrates a reportable policy sale in which one acquirer acquires legal title and another acquires beneficial ownership.

B. *Section 1035 exchanges*

Section 1.101-1(e)(2) of the proposed regulations provides that the issuance of a life insurance contract to a policyholder, other than the issuance of a policy in an exchange pursuant to section 1035, is not a transfer of an interest in a life insurance contract. The preamble to the proposed regulations requests comments on whether the proposed regulations should include additional provisions regarding the treatment of section 1035 exchanges of life insurance contracts. *See* 84 FR 11009, 11019.

One commenter on the proposed regulations recommended that no additional provisions be added to the proposed regulations for this circumstance. The commenter stated that the acquirer of a life insurance contract in a reportable policy sale would be unlikely to meet the requirements for an insurable interest in the insured and, consequently, would not be able to make a section 1035 exchange. In support of this position, the commenter explained that, in order for an exchange of policies to qualify as a section 1035 exchange, the owner of the new contract must be the same person who owned the old contract at the time of the exchange. The commenter also stated that an insurer can issue a new policy only when that new policy will meet state insurance laws requiring an insurable interest in the insured, and an insurable interest is generally based on a close familial relationship with the insured or a lawful and substantial financial interest in the continued life of the insured.

Another commenter recommended that the statement in §1.101-1(e)(2) of the proposed regulations regarding section 1035 exchanges be deleted or amended to eliminate any suggestion that such transactions, by themselves, can lead to reportable policy sales. The commenter indicated that the statement suggests that the mere issuance of a new life insurance policy in a section 1035 exchange could (or perhaps would) give rise to a reportable policy sale and asserted that such treatment is unnecessary and would be inappropriate.

In support of this position, the commenter explained that, mechanically, a section 1035 exchange typically involves the assignment by the policyholder of the existing policy to the carrier, followed by the surrender of the policy and the application of the cash proceeds as a premium under a new policy issued to the same owner on the same insured's life. The commenter remarked that, although the new carrier acquires an interest in the old policy, that interest is immediately extinguished. The commenter also remarked that treating the exchange as a reportable policy sale is not necessary to serve any information collection purpose in the case of an exchange involving a new, different carrier, because the exchange must be reported to the IRS and the policyholder on a Form 1099-R. Additionally, the commenter suggested that, even if an exchange were viewed as potentially meeting the definition of a reportable policy sale, the new carrier should be viewed as having a substantial business or financial relationship with the insured, considering that the carrier just issued a new policy on that individual's life.

The commenter suggested that, if there are specific transactions involving section 1035 exchanges that fall outside the normal situation described by the commenter, and the Treasury Department and the IRS determine that such atypical scenarios might give rise to reportable policy sales, the scope of any provision addressing those transactions should be limited to those particular transactions, so that doubt will not be cast on everyday policy exchanges.

The reference in §1.101-1(e)(2) of the proposed regulations to section 1035 exchanges was not intended to imply that the transfer of a policy to an insurance company in a section 1035 exchange would be a reportable policy sale. In response to the comments received on section 1035 exchanges, §1.101-1(c)(2)(iv) of the final regulations provides that the acquisition of a life insurance contract by an insurance company in an exchange pursuant to section 1035 (such as the acquisition that would result from the assignment by the policyholder of the existing policy to the insurance company in exchange for the issuance of a new life insurance contract) is not a reportable policy sale.

The concern prompting the reference in §1.101-1(e)(2) of the proposed regulations to section 1035 exchanges related to the possibility that a policy transferred in a reportable policy sale subsequently could be exchanged for a new policy in an exchange pursuant to section 1035 and that, absent the reference in §1.101-1(e)(2), the death benefits paid under the new policy might not be reported under section 6050Y(c). Under the final regulations, which adopt §1.101-1(e)(2) of the proposed regulations as proposed, the issuance of a new life insurance contract to a policyholder in an exchange pursuant to section 1035 is a transfer of an interest in a life insurance contract (the newly issued life insurance contract) to the policyholder, which results in a direct acquisition of an interest in a life insurance contract (the newly issued life insurance contract) by the policyholder. *See* §1.101-1(e)(2) and (3)(i) of the final regulations. The tax treatment of the newly issued life insurance contract under section 101 is not affected by the tax treatment of the policy for which it was exchanged. However, if the policyholder's acquisition of the newly issued contract constitutes a reportable policy sale, the rules generally applicable to reportable policy sales under section 101 and the regulations thereunder apply to determine the effect of the reportable policy sale on the tax treatment of the newly issued policy under section 101, and the rules generally applicable to reportable policy sales under section 6050Y and the regulations thereunder apply to determine whether section 6050Y reporting is required with respect to the reportable policy sale. The final regulations provide that the acquisition of a newly issued life insurance contract by a policyholder in an exchange pursuant to section 1035 is not a reportable policy sale, if the policyholder has a substantial family, business, or financial relationship with the insured, apart from its interest in the life insurance contract, at the time of the exchange. *See* §1.101-1(c)(2)(v) of the final regulations. If no such relationship exists at the time of the section 1035 exchange, the exchange is a reportable policy sale under §1.101-1(c)(1) of the final regulations. The Treasury Department and the IRS have determined that no exception from the definition of reportable policy sale should apply in this situation. Based on comments received, this situation should rarely arise due to state law insurable interest requirements.

Should this situation arise, however, the policyholder, as an acquirer, must furnish the statement to the issuer required by section 6050Y(a)(2) and §1.6050Y-2(d)(2) of the final regulations (the reportable policy sale statement or "RPSS"). *See* §1.6050Y-2(f)(3) of the final regulations. In this case, the statement must be furnished to the issuer that issues the new life insurance contract. *See* §1.6050Y-1(8)(ii) of the final regulations. However, the policyholder is not required to file the information return required by section 6050Y(a)(1) and §1.6050Y-2(a) of the final regulations. *See* §1.6050Y-2(f)(3). Also, because the policyholder is not only the acquirer, but is also the reportable policy sale payment recipient and the seller with respect to the reportable policy sale, the policyholder is not required to furnish the statement generally required to be furnished to the reportable policy sale payment recipient under §1.6050Y-2(d)(1) of the final regulations. *See* §1.6050Y-1(a)(15), (16), and (18) of the final regulations; §1.6050Y-2(f)(3) of the final regulations. Additionally, although the issuer that issues the new life insurance contract receives an RPSS, it is not required to file a return or furnish a statement to the seller under section 6050Y(b) and §1.6050Y-3 because the seller does not need the information that would be provided on the statement to properly report a section 1035 exchange. *See* §1.6050Y-3(f)(3) of the final regulations. However, if the issuer makes a payment of reportable death benefits under the newly issued life insurance contract, the issuer must report that payment under section 6050Y(c) and §1.6050Y-4 of the final regulations, unless an exception under §1.6050Y-4 applies.

C. *Ordinary course trade or business acquisitions*

Several commenters on Notice 2018-41 suggested that acquisitions of life insurance contracts, or interests therein, in ordinary course business transactions in which one trade or business acquires another trade or business that owns life insurance on the lives of former employees or directors should not be reportable policy sales. The proposed regulations include provisions that exclude certain of these transactions from the definition of reportable policy sales. These provisions include the definition of substantial business relationship in §1.101-1(d)(2) of the proposed regulations, the special rule for indirect acquisitions in §1.101-1(d)(4)(i) of the proposed regulations, and the definition of the term "indirect acquisition of an interest in a life insurance contract" in §1.101-1(e)(3)(ii) of the proposed regulations.

Two commenters on the proposed regulations suggested that ordinary course business transactions (such as mergers or acquisitions) involving businesses that own life insurance contracts were not intended by Congress to fall within the meaning of a reportable policy sale and noted that the rules describing a reportable policy sale in the proposed regulations are very helpful in confirming that narrow intent. Another commenter stated that, although the legislative history does not elaborate on the intent of section 101(a)(3)(A) (which limits the carryover basis exception to transfers for value that fall outside the definition of reportable policy sale in section 101(a)(3)(B)), it is widely understood to be aimed at ensuring enforcement of the transfer for value rule with respect to newer forms of speculative transfers involving life insurance policies, rather than imposing new restrictions on legitimate business uses of life insurance. The commenter asserted that the preamble to the proposed regulations implicitly acknowledges this by stating that some provisions are meant to ensure that "certain ordinary course business transactions" will not be treated as reportable policy sales. In response to these comments supporting the ordinary course exclusions from the definition of reportable policy sales in the proposed regulations, those provisions are retained in the final regulations.

One commenter on the proposed regulations requested that the proposed regulations be revised to provide that any transfer of an interest in a life insurance contract as part of a tax-free reorganization conducted in the ordinary course of business is eligible for an exception to being treated as a reportable policy sale under section 101(a)(3)(B), regardless of whether the target survives the reorganization transaction. In this regard, the commenter recommended revising §1.101-1(e)(3)(ii) of the proposed regulations, which defines the term "indirect acquisition of an interest in a life insurance contract," to specifically cover all transactions involving the acquisition of a C corporation that qualify for tax-free reorganization treatment unless, immediately prior to the acquisition, more than 50 percent of the gross value of the assets of the C corporation consists of life insurance contracts. The commenter also recommended adding an example to illustrate this point. The commenter concluded that §1.101-1(e)(3)(ii) of the proposed regulations applies in the case of acquisition transactions in which the corporate existence of the target survives the acquisition (for instance, a taxable stock sale with no section 338 election, a reverse subsidiary merger structured to qualify as a tax-free reorganization under section 368(a)(2)(E), or a tax-free reorganization under section 368(a)(1)(B)) and appears not to apply in the case of acquisition transactions in which the target corporation is merged with and into the acquiring corporation and the target's separate corporate existence is terminated as of the merger date (for instance, a tax-free reorganization under section 368(a)(1)(A), (C), or (D) or section 368(a)(2)(D)).

Under §1.101-1(e)(3)(ii) of the proposed regulations, an indirect acquisition of an interest in a life insurance contract occurs when a person (acquirer) becomes a beneficial owner of a partnership, trust, or other entity that holds (whether directly or indirectly) the interest in the life insurance contract. However, for this purpose, the term "other entity" does not include a C corporation, unless more than 50 percent of the gross value of the assets of the C corporation consists of life insurance contracts immediately before the indirect acquisition. Accordingly, the acquisition of ownership of a C corporation that owns an interest in a life insurance contract is not an indirect acquisition of such an interest, and therefore is not a reportable policy sale, if no more than 50 percent of the gross value of the assets of the C corporation consists of life insurance contracts. The commenter thus is correct that §1.101-1(e)(3)(ii) of the proposed regulations applies only in the case of indirect acquisitions of life insurance contracts (which include a tax-free reorganization in which the corporate existence of the target that holds an interest in a life insurance contract survives the acquisition), and not direct acquisitions of life insurance contracts (which include a tax-free reorganization in which the separate corporate existence of a target that holds an interest in a life insurance contract is terminated).

The commenter asserted that this disparate treatment (between policies transferred directly in tax-free asset reorganizations and indirectly in stock reorganizations) is inappropriate and not warranted as a matter of good tax policy. The commenter further asserted that all tax-free reorganizations should be eligible for an exception similar to the exception provided in §1.101-1(e)(3)(ii) of the proposed regulations. The commenter noted that the proposed regulations provide certain exceptions that could apply to tax-free mergers in which the target goes out of existence and the surviving corporation continues to hold the life insurance contract, but asserted that having to determine in these types of tax-free mergers whether a particular exception applies on a contract-by-contract basis is unduly complex and a trap for the unwary. The commenter further asserted that this burdensome exercise does not appear to serve the purpose of the change in the statute, which is to address abusive transactions and a failure to report income when appropriate.

The final regulations do not adopt the commenter's recommendation regarding amendments to §1.101-1(e)(3)(ii). The exception in §1.101-1(e)(3)(ii) of the proposed regulations is not targeted to acquisitions of C corporation stock in tax-free reorganizations, but instead is a relatively broad exception that applies to the acquisition of any interest in a C corporation, provided that no more than 50 percent of the C corporation's gross asset value consists of life insurance contracts. This exception is one of a number of exceptions in the proposed regulations intended to provide relief for indirect acquisitions in which acquisition of the underlying life insurance contract interest likely was not a significant motivating factor for the acquisition. The final regulations preserve the different results for stock and asset reorganizations because there are significant differences between these two types of reorganizations, and the Treasury Department and the IRS have concluded that those distinctions justify different treatment for purposes of sections 101 and 6050Y. In addition, no exception is provided in the final regulations that excludes reorganizations from the definition of a reportable policy sale. Rather, there are exclusions based on the application of the definitions of substantial relationships as mandated by the statute and exceptions for certain indirect acquisitions that may produce different results in different types of reorganizations.

One reason for treating indirect and direct acquisitions of life insurance contract interests differently is that an acquirer of an interest in an entity may have limited ability to determine what types of assets an entity owns, or to obtain from the entity information necessary to report on the entity's assets. Thus, for example, the proposed regulations provide a reportable policy sale exception for the acquisition of a small (five percent or less) interest in any entity, unless more than 50 percent of the entity's gross asset value consists of life insurance contracts. *See* §1.101-1(c)(2)(iii)(B) of the proposed regulations. In addition, in the case of a C corporation, a corporate level income tax applies to corporate earnings in addition to income tax on distributions at the shareholder level. As a result, C corporations are not frequently used as vehicles for investing in life insurance contracts covering insureds with respect to which the corporation does not have a substantial business, financial, or family relationship at the time the contract is issued. For this reason, the proposed regulations provide a more generous exception for acquisitions of interests in a C corporation, provided that no more than 50 percent of the C corporation's gross asset value consists of life insurance contracts, as determined under §1.101-1(f)(4) of the proposed regulations. *See* §1.101-1(e)(3)(ii) of the proposed regulations.[4]

After the TCJA amendments to section 101, the fact that the transfer of a life insurance contract occurs in a carryover basis transaction qualifying under section 101(a)(2)(A) (such as a tax-free reorganization) is no longer sufficient to avoid the limit on the amount of life insurance policy proceeds that are excludable from gross income under the section 101(a)(1) transfer for value rule. Rather, Congress provided that the carryover basis exception in section 101(a)(2)(A) does not apply unless the transferee also has a substantial family, business, or financial relationship with the insured. Under the proposed regulations, in the case of life insurance contracts transferred in an asset reorganization, the surviving corporation could, for example, establish that a substantial business relationship exists by determining that the life insurance policies transferred in the reorganization cover insureds who are key persons of, or materially participate in, an active trade or business of the acquirer as owners, employees, or contractors. *See* §1.101-1(d)(2)(i) of the proposed regulations. The surviving corporation could also establish that a substantial business relationship exists by determining that the life insurance contracts cover insureds who either (i) are officers, directors or employees of the business being acquired immediately before the acquisition or (ii) previously were directors, highly compensated employees or highly compensated individuals within the meaning of section 101(j)(2)(A)(ii) and the surviving corporation will have ongoing financial obligations with respect to these individuals after the acquisition (such as retirement obligations). *See* §1.101-1(d)(2)(ii) of the proposed regulations. Corporations must track this data annually for purposes of section 101(j) corporate owned life insurance (COLI) reporting obligations and related recordkeeping, so it should not be overly burdensome to obtain this information. Additionally, in an asset reorganization, it would in any case be necessary to

[4] Section 1.101-1(f)(4) of the final regulations clarifies that the gross value of assets means, with respect to any entity, the fair market value of the entity's assets, including assets beneficially owned by the entity under §1.101-1(f)(1) of the final regulations as a beneficial owner of a partnership, trust, or other entity. Accordingly, the 50 percent test in §1.101-1(e)(3)(ii) of the final regulations applies to a C corporation's assets and the assets held by any partnership, trust, or other entity beneficially owned by the C corporation.

review the life insurance contracts directly acquired on a contract-by-contract basis in order to update insurance contract ownership and beneficiary information with the relevant insurance company.

It is possible that an asset acquisition could result in the loss of the complete exclusion of death benefits from income with respect to some COLI policies that cover insureds who are not employed by the target immediately before the acquisition or employed by the acquirer after the acquisition and with respect to whom the acquirer has no ongoing obligations to pay retirement or other benefits. However, the Treasury Department and the IRS have not identified any clear policy reason why that tax benefit should carry over when ownership of the insurance policy is transferred. The indirect transfer exceptions in the proposed regulations that could permit COLI benefits to be retained with respect to some policies covering no-longer-connected officers, directors, and employees apply only when ownership of the insurance policy is not transferred, such as in a stock reorganization. These exceptions reflect a weighing by the Treasury Department and the IRS of information collection burdens versus potential for abuse in indirect acquisition scenarios.

The commenter also recommended modifying the language in *Example 8* of §1.101-1(g)(8) of the proposed regulations to clarify that the example is intended only to illustrate application of the rule under §1.101-1(d) of the proposed regulations and is not intended to imply that, without the insured's current employment by the acquired corporation, the transaction would be treated as a reportable policy sale. *Example 8* of §1.101-1(g)(8) of the proposed regulations describes a tax-free reorganization in which a corporation transfers to an acquiring corporation its active trade or business and a life insurance policy on the life of a current employee that was acquired from the employee. The example concludes that, because the insured was an employee of the target corporation at the time of the tax-free reorganization, and the acquiring corporation carries on the acquired trade or business, the transfer in the tax-free reorganization is not a reportable policy sale because the acquirer has a substantial business relationship with the insured under §1.101-1(d)(2)(ii) of the proposed regulations. The commenter observed that the example suggests that the transfer of the policy as part of the tax-free reorganization described in the example would not have qualified for an exception from being treated as a reportable policy sale under the proposed regulations absent the existence of the substantial business relationship. The commenter's understanding of the example is correct. The substantial business relationship is necessary for the tax-free reorganization in the example to avoid being treated as a reportable policy sale. As discussed in this section of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have not adopted the commenter's recommendation regarding amendments to §1.101-1(e)(3)(ii), and therefore have not revised the example in the final regulations.

This commenter also recommended a related change to §1.101-1(d)(4)(i) of the proposed regulations. Under §1.101-1(d)(4)(i) of the proposed regulations, an indirect acquirer is deemed to have a substantial business or financial relationship with the insured if the direct holder of the interest in the life insurance contract has a substantial business or financial relationship with the insured immediately before and after the date the indirect acquirer acquires its interest. Section 1.101-1(d)(4)(i) of the proposed regulations provides relief for acquirers who do not hold their interest in the relevant life insurance contracts directly, when the direct holder of those interests has a substantial business or financial relationship with the insured before and after the acquisition. The Department of Treasury and the IRS have determined that it is not appropriate to treat an indirect acquisition of an interest in a life insurance contract as a reportable policy sale when the direct owner of the interest in the life insurance contract does not change and the direct owner has a substantial family, business, or financial relationship with the insured. The commenter recommended modification of §1.101-1(d)(4)(i) of the proposed regulations to eliminate what the commenter describes as disparate treatment that arises depending on the type of merger transaction the acquirer undertakes or whether after the merger the insured remains with the company or retains the right to retirement or other post-employment benefits.

First, the commenter observed that, in a tax-free merger in which the target goes out of existence, the direct holder of the life insurance contract no longer exists, and therefore would no longer have any relationship with the insured. Accordingly, the acquirer cannot be deemed to have a substantial business or financial relationship with the insured under §1.101-1(d)(4)(i) of the proposed regulations. However, in a tax-free merger in which the target does not survive, §1.101-1(d)(4)(i) of the proposed regulations would not apply because the acquirer would own the insurance contract directly. An acquirer that holds its interest in the relevant life insurance contract directly must determine whether it has a substantial family, business, or financial relationship with the insured under §1.101-1(d) of the proposed regulations at the time of the acquisition.

Second, the commenter suggested that there are situations in which the insured's employment with the target company is terminated as a result of a merger or acquisition, and the insured has no continuing relationship with the surviving company that retains the life insurance contract. The commenter observed that, in such cases, the "after the date of the acquisition" prong of §1.101-1(d)(4)(i) of the proposed regulations cannot be satisfied. The commenter recommended modifying §1.101-1(d)(4)(i) of the proposed regulations to provide that the acquirer of an interest in a life insurance contract in a tax-free merger is deemed to have a substantial business or financial relationship with the insured if the target has a substantial business or financial relationship with the insured immediately prior to the merger, provided the acquirer does not otherwise transfer any interest in the life insurance contract in a transaction treated as a reportable policy sale. The commenter also recommended that the rule specifically state that the fact that the surviving company continues to hold, after the merger, the contract on the life of an individual with whom the target had a substantial financial or business relationship is the determinative factor under this modified rule.

The proposed modification is not adopted because, although §1.101-1(d)(4)(i) of the proposed regulations generally would not apply to the situations referenced by the commenter, the proposed regulations already include exceptions that may apply in the situations referenced by the commenter. In a tax-free merger in which the target does not survive, §1.101-1(d)(4)(i) of the proposed regulations would not apply because the acquirer would have a direct acquisition of any interest in a life insurance contract acquired from the target. However, the acquirer does not have a reportable policy sale if the acquirer has a substantial family, business, or financial relationship with the insured. Under §1.101-1(d)(2)(ii) of the proposed regulations, the surviving company has a substantial business relationship with the insured, and therefore has not acquired its interest in the life insurance contract on the insured's life in a reportable policy sale, if: (1) the insured is an employee within the meaning of section 101(j)(5)(A) of the acquired trade or business immediately preceding the acquisition, and (2) the surviving company either carries on the acquired trade or business or uses a significant portion of the acquired business assets in an active trade or business that does not include investing in interests in life insurance contracts. Accordingly, the proposed regulations already include a rule similar to the one requested by the commenter that is applicable to direct acquisitions of interests in life insurance contracts (such as acquisitions resulting from tax-free mergers in which the target does not survive).

5. *Comments and Changes Relating to §1.101-1(d) of the Proposed Regulations*

Section 1.101-1(d) of the proposed regulations defines the terms substantial family relationship, substantial business relationship, and substantial financial relationship, and provides special rules for applying these definitions. This section of this Summary of Comments and Explanation of Revisions discusses comments that generally relate to the definitions and special rules in §1.101-1(d) of the proposed regulations.

A. *Beneficial owners with a combination of substantial relationships*

Under §1.101-1(d)(1) of the proposed regulations, a substantial family relationship exists between the insured and a partnership, trust, or other entity if all of the beneficial owners of that partnership, trust, or other entity have a substantial family relationship with the insured. A partnership, trust, or other entity may itself have a substantial business or financial relationship with the insured under §1.101-1(d)(2) or (3) of the proposed regulations.

One commenter on the proposed regulations recommended that a transfer to a trust, partnership, or other entity not be a reportable policy sale within the meaning of section 101(a)(3) if all of the beneficial owners of the trust, partnership, or other entity have a substantial family, business, or financial relationship with the insured. The Treasury Department and the IRS have determined it would be appropriate to expand the definition of substantial family, business, or financial relationship to include the relationship between the insured and a trust, partnership, or other entity, every beneficial owner of which has a substantial family, business, or financial relationship with the insured. Accordingly, §1.101-1(d)(4)(iii) of the final regulations provides this expanded definition.

The commenter also suggested that the definition of "family member" under §1.101-1(f)(3) should include charities to which the insured has given substantial financial support or significant volunteer support. Another commenter suggested that a trust with beneficiaries that include both individual family members and a charity with a substantial financial relationship to the insured should qualify as a "family member." Under §1.101-1(d)(3)(iii) of the proposed regulations, a substantial financial relationship exists between the insured and acquirer if the acquirer is an organization described in sections 170(c), 2055(a), and 2522(a) that previously received financial support in a substantial amount or significant volunteer support from the insured. Under either of the approaches suggested by the commenters, the acquisition of an interest in a life insurance contract by a trust with beneficiaries that include both individuals who are family members of the insured and a charity described in §1.101-1(d)(3)(iii) of the proposed regulations would not be a reportable policy sale. The Treasury Department and the IRS agree that the existence of a trust beneficiary that is a charity described in §1.101-1(d)(3)(iii) of the proposed regulations should not cause a transfer to that trust to be a reportable policy sale. However, rather than expanding the definition of "family member" under §1.101-1(f)(3) of the proposed regulations as suggested by the commenters, the Treasury Department and the IRS have adopted a more direct and expansive approach to address the commenters' concerns by adding a new rule in the final regulations providing that any combination of the described substantial relationships between a trust's beneficiaries and the insured is sufficient to qualify the transfer to that trust for the reportable policy sale exclusion. *See* §1.101-1(d)(4)(iii) of the final regulations. As a result, under the final regulations, there is no need to also expressly treat a trust established and maintained for the primary benefit of the insured or one or more of the insured's family members as a family member of the insured. Therefore, the final regulations do not include such a trust in the definition of family member.

B. *Substantial financial relationships with charities*

Under §1.101-1(d)(3)(iii) of the proposed regulations, the acquirer of an interest in a life insurance contract has a substantial financial relationship with the insured if the acquirer is an organization described in sections 170(c), 2055(a), and 2522(a) that previously received financial support in a substantial amount or significant volunteer support from the insured. One commenter on the proposed regulations suggested that this provision be expanded to include any other such organization with which the insured has substantial personal ties, such as the donor or a family member having benefitted from the charitable organization's services in some manner. The commenter stated that it is not uncommon for a donor to both (i) contribute very modestly, if at all, to a charity during life because the donor is concerned about having sufficient retirement income, and (ii) want to benefit the charity when the donor no longer needs to preserve retirement income sources. The commenter also stated that donors often benefit charities through either a split interest trust described in section 170(f)(2) or a bargain sale described in §1.1011-2.

The Treasury Department and IRS have not adopted this suggestion in the final regulations because it would be challenging to determine when personal ties with a charity are substantial enough to constitute a substantial financial relationship with the insured, in the absence of a significant donation of time or property. Also, there generally will be little detriment to a charity as a result of an acquisition (whether gratuitous or for value) of an interest in a life insurance contract in a reportable policy sale. Nevertheless, as discussed later in this section, the final regulations provide that the category of charities considered to have a substantial financial relationship with an insured may be expanded in the future in guidance published in the Internal Revenue Bulletin.

Treating a gratuitous transfer of an interest in a life insurance contract (or the part of the transfer that is gratuitous, in the case of a bargain sale) as a reportable policy sale does not affect the amount of proceeds excludable by the gratuitous transferee. Section 1.101-1(b)(2)(i) of the final regulations applies to all gratuitous transfers of interests in life insurance contracts and generally provides that the transferee in a gratuitous transfer of an interest in a life insurance contract steps into the shoes of the transferor and may exclude death benefits paid under the contract from gross income to the same extent that the transferor would have been able to exclude the benefits, in addition to the premiums and other amounts paid by the transferee. Furthermore, treatment of a gratuitous transfer as a reportable policy sale does not result in reporting obligations for the gratuitous transferee because the gratuitous transferor is not a reportable policy sale payment recipient. *See* §§1.6050Y-1(a)(16) and 1.6050Y-2(a) of the final regulations.

Even if a charity purchased some or all of its interest in a life insurance contract for valuable consideration, a charity generally is not subject to Federal income tax on its income (including insurance policy proceeds) unless the income arises from an unrelated trade or business. Thus, the charity's obligation in case of a purchase generally would be limited to acquirer reporting under §1.6050Y-2, which merely requires providing on Form 1099-LS information that should be readily available to the charity. This reporting provides important information regarding the sale to reportable policy sale payment recipients and the IRS.

In response to the commenter's concerns, however, the final regulations provide that the IRS may publish guidance in the Internal Revenue Bulletin (see §601.601(d)(2) of this chapter) describing other situations in which a substantial financial relationship exists between the insured and an acquirer that is an organization described in sections 170(c), 2055(a), and 2522(a). *See* §1.101-1(d)(3)(iii) of the final regulations.

C. *Substantial financial relationships and BOLI pooling transactions*

One commenter on the proposed regulations requested confirmation that a reportable policy sale will not arise when a life insurance policy is involved in a transaction that pools bank-owned life insurance (BOLI). The commenter explained that businesses, such as banks, commonly promise certain pre-and post-retirement benefits to their employees, such as retiree health care benefits, which can result in substantial liabilities for the businesses that must be reflected on their financial statements. The commenter described BOLI as permanent, cash value life insurance coverage on the lives of a bank's officers, directors, and employees purchased by the bank to fund such obligations informally and to establish assets on its financial statements to offset liabilities for the promised benefits. The commenter stated that BOLI owners typically hold the policies until the death benefits become payable and use the benefits to fund the costs of the employee benefits or to recover such costs after the fact. The commenter described BOLI pooling transactions as transactions that pool the BOLI policies of multiple banks for the continued purpose of funding each bank's employee benefits, but in a more effective, centralized way. The commenter described the initial step of a BOLI pooling transaction as the transfer by multiple unrelated banks of their pre-existing BOLI policies to a partnership, in return for which each bank receives a partnership interest proportional to the value of its contributed policies. The commenter explained that the partnership holds and manages the contributed policies and distributes death benefits among the bank-partners pro rata based on their respective partnership interests, which is expected to help normalize cash flows from the policies.

The commenter asserted that BOLI pooling transactions are ordinary course business transactions that should not be treated as reportable policy sales because they are not speculative and can be distinguished from sales of policies to third parties because the intent and result is to pool the policies among all the original policyholders for the continued purpose of funding their employee benefit liabilities. The commenter noted that the IRS has issued private letter rulings that confirm, directly or indirectly, that the carryover basis exception to the transfer for value rule in section 101(a)(2) applies to a bank's contribution of BOLI policies to the partnership in a BOLI pooling transaction, thereby preserving the tax-free character of the death benefits when paid to the partnership. These rulings pre-date the addition of section 101(a)(3) to the Code. The reportable policy sale rules of section 101(a)(3) are in addition to the carryover basis exception of section 101(a)(2). As a result, policy transfers are ineligible for the carryover basis exception if no substantial family, business, or financial relationship exists between the acquirer of an interest in a life insurance contract and the insured under that contract at the time of the acquisition.

The commenter asserted that the proposed regulations support the requested treatment of BOLI pooling transactions because a substantial financial relationship exists between the acquirer and insured. A substantial financial relationship exists under §1.101-1(d)(3)(ii) of the proposed regulations if the acquirer maintains the life insurance contract on the life of the insured to provide funds to purchase assets or satisfy liabilities following the death of the insured. The commenter asserted that this provision applies in BOLI pooling transactions with respect to both the bank and the partnership as follows: (1) the partnership has a direct acquisition of life insurance policies, which it maintains to satisfy liabilities following the death of the insured, namely, the employee benefit liabilities of the bank-partners for which they originally purchased the policies; (2) the bank has an indirect acquisition of life insurance policies contributed by other banks to the partnership; and (3) the bank maintains its indirect interest in those policies to continue funding the same employee benefit liabilities. The commenter recommended clarification of the regulations to confirm this treatment, either by adding additional language to the definition of substantial financial relationship, or by adding an example that applies that provision to the BOLI pooling transaction. Alternatively, the commenter suggested a separate exception to the reportable policy sale definition.

The final regulations do not adopt the commenter's requested changes because the changes would be inconsistent with the statute. The proposed regulations do not support, and were not intended to support, the requested treatment of BOLI pooling transactions.

First, the partnership described by the commenter does not have a substantial family, business, or financial relationship with the insureds under the proposed regulations. Specifically, it does not have a substantial financial relationship with any insured under §1.101-1(d)(3)(ii) of the proposed regulations because it does not maintain the life insurance contract on the life of the insured to provide funds for the partnership to purchase assets or satisfy liabilities following the insured's death. As described by the commenter, the partnership maintains the life insurance contracts to provide its partners, the banks, with funds to satisfy the banks' employee benefit liabilities. Accordingly, the partnership's acquisition of the life insurance contracts in the circumstances described is a reportable policy sale that must be reported under section 6050Y and §1.6050Y-2 of the proposed regulations.

Second, the definition of a substantial financial relationship in §1.101-1(d)(3)(ii) of the proposed regulations was not intended to cover relationships as tenuous as those existing between the indirect acquirers (the banks) and the insureds in the BOLI pooling transactions described by the commenter. Section 1.101-1(d)(3)(ii) of the proposed regulations was intended to cover situations in which the life insurance contract is held to provide funds to purchase assets or satisfy liabilities, when the need for the asset purchases or liability payments results from the insured's death. In the situation described by the commenter, a bank does not have this kind of relationship with the insureds under life insurance contracts contributed to the partnership by other banks. However, in the circumstances described, because the partnership acquires the life insurance contracts in a reportable policy sale that must be reported under section 6050Y(a) and §1.6050Y-2 of the proposed regulations, the bank's indirect acquisition of the life insurance contracts is not a reportable policy sale, provided the partnership complies with the reporting requirements. *See* §1.101-1(c)(2)(iii)(A) of the proposed regulations.

D. *Substantial financial relationships under §1.101-1(d)(3)(ii)*

A substantial financial relationship exists under §1.101-1(d)(3)(ii) of the proposed regulations if the acquirer maintains the life insurance contract on the life of the insured to provide funds to purchase assets or satisfy liabilities following the death of the insured. As described in section 5.C of this Summary of Comments and Explanation of Revisions, this definition was intended to apply in situations in which the life insurance contract is held to provide funds to purchase assets or satisfy liabilities following the death of the insured, when the need for the asset purchases or liability payments results from the insured's death. Accordingly, §1.101-1(d)(3)(ii) of the final regulations revises the definition to provide that a substantial financial relationship exists between the acquirer and insured if the acquirer maintains the life insurance contract on the life of the insured to provide funds to purchase assets of or to satisfy liabilities of the insured or the insured's estate, heirs, legatees, or other successors in interest, or to satisfy other liabilities arising upon or by reason of the death of the insured.

6. *Comments and Changes Relating to §1.101-1(a) of the Proposed Regulations*

The proposed regulations would remove the second sentence of §1.101-1(a)(1) of the existing regulations, which states: "Death benefit payments having the characteristics of life insurance proceeds payable by reason of death under contracts, such as workmen's compensation insurance contracts, endowment contracts, or accident and health insurance contracts, are covered by this provision." As noted in the preamble to the proposed regulations, this update reflects the addition of section 7702 to the Code in 1984. *See* 84 FR 11015.

One commenter stated that it is important that no changes be made with respect to the second sentence because the benefits described therein were written into older policies, some of which are still in effect, and changing the rules would negatively impact policyholders who have long relied on the appropriate exclusion of these death benefits from income. The commenter further stated that there is a longstanding and extensive body of court decisions and IRS rulings that establish the conditions under which such benefits qualify for treatment as life insurance proceeds.

In response to these comments, the final regulations revise, rather than remove, the second sentence of §1.101-1(a)(1) of the existing regulations to clarify that the sentence only applies to contracts issued on or before December 31, 1984, the effective date of section 7702.

7. *Comments and Changes Relating to §1.6050Y-1 of the Proposed Regulations*

Section 1.6050Y-1(a) of the proposed regulations provides definitions for terms used in §§1.6050Y-1 through -4 of the proposed regulations. This section of this Summary of Comments and Explanation of Revisions discusses comments received that generally relate to §1.6050Y-1(a) of the proposed regulations.

A. *Definition of issuer*

Section 6050Y(d)(3) defines issuer to mean any life insurance company that bears the risk with respect to a life insurance contract on the date any return or statement is required to be made under section 6050Y. The definition of issuer under the proposed regulations depends on the context in which the term is used. In general, the term "issuer" means, on any date, with respect to any interest in a life insurance contract, any person that bears any part of the risk with respect to the life insurance contract on that date and any person responsible on that date for administering the contract, including collecting premiums and paying death benefits. *See* §1.6050Y-1(a)(8)(i) of the proposed regulations. For instance, if a reinsurer reinsures on an indemnity basis all or a portion of the risks that the original issuer (and continuing contract administrator) might otherwise have incurred with respect to a life insurance contract, both the reinsurer and the original issuer of the contract are issuers of the life insurance contract.

One commenter noted that this definition of issuer in the proposed regulations appears to be a reversal of position from a statement in Notice 2018-41 that, according to the commenter, appropriately proposed to exclude a "reinsurer in an indemnity contract covering all or a portion of the risks that the original issuer (and continuing contract administrator) might otherwise have incurred with respect to a life insurance contract." In Notice 2018-41, the Treasury Department and the IRS announced the intent to limit the information reporting obligations imposed under §6050Y(b) to the life insurance company that is responsible for administering the contract, including paying death benefits under the life insurance contract to reduce the burden on reporting life insurance companies and prevent duplicative reporting. Notice 2018-41 indicated that, under the proposed regulations, the reporting obligations would not apply, for instance, to a reinsurer in an indemnity contract covering all or a portion of the risks that the original issuer (and continuing contract administrator) might otherwise have incurred with respect to a life insurance contract.

Under the proposed regulations, although the definition of issuer is broad enough that information reporting obligations could apply to a reinsurer, reporting obligations in practice will generally be limited to the life insurance company that is responsible for administering the life insurance contract, or its designee. The proposed regulations facilitate this result by providing relief for an issuer that is subject to reporting obligations, but is not responsible for administering the contract. For purposes of information reporting by the acquirer under section 6050Y(a) and §1.6050Y-2 of the proposed regulations, the "6050Y(a) issuer" to which the acquirer must furnish an RPSS is the issuer responsible for administering the life insurance contract, including collecting premiums and paying death benefits under the contract, on the date of the reportable policy sale. *See* §1.6050Y-1(a)(8)(ii) of the proposed regulations. For purposes of information reporting by the issuer under section 6050Y(b) and §1.6050Y-3 of the proposed regulations, reporting is required by any "6050Y(b) issuer" that receives an RPSS or notice of a transfer to a foreign person, or its designee. *See* §1.6050Y-1(a)(8)(iii)(A) and (B) of the proposed regulations. Accordingly, with respect to reportable policy sales, 6050Y(b) issuers responsible for reporting under section 6050Y(b) and §1.6050Y-3 of the proposed regulations will generally be issuers responsible for administering the life insurance contracts. No other issuer should receive an RPSS. Also, with respect to a transfer to a foreign person, if any issuer other than the issuer responsible for administering the life insurance contract receives notice of the transfer, it will not be considered a 6050Y(b) issuer if it provides the 6050Y(b) issuer responsible for administering the life insurance contract with notice of the transfer and any available information necessary to accomplish reporting under section 6050Y(b) and §1.6050Y-3 of the proposed regulations. *See* §1.6050Y-1(a)(8)(iii)(B) of the proposed regulations. The final regulations clarify that an issuer other than the issuer responsible for administering the life insurance contract will not be considered a 6050Y(b) issuer if it received notice of a transfer to a foreign person from the issuer responsible for administering the life insurance contract. *See* §1.6050Y-1(a)(8)(iii)(B) of the final regulations. Additionally, a 6050Y(b) issuer's reporting obligation is deemed satisfied if the information required by section 6050Y(b) and §1.6050Y-3 of the final regulations is timely reported by any other 6050Y(b) issuer. *See* §1.6050Y-3(b) of the final regulations.

The commenter recommended that the definition of issuer expressly exclude a reinsurer in an indemnity contract covering all or a portion of the risks that the original issuer (or its continuing contract administrator) might otherwise have incurred with respect to a life insurance contract. The commenter stated that in most instances of indemnity reinsurance transactions, the original insurer continues to administer the life insurance contracts, some or all of the underlying risks of which the reinsurer may have assumed, or alternatively, the parties select a third-party contract administrator who assumes such a role, which includes managing ownership changes and other functions relating to contract administration and interfacing with policyholders. The commenter asserted that if the approach in the proposed regulations is due to any presumption that a reinsurer in an indemnity reinsurance transaction may be or may become privy to any information relating to transfers to domestic or foreign persons, such presumptions are misplaced.

The final regulations do not adopt the commenter's proposal because a reinsurer in an indemnity contract bears risk with respect to the life insurance contracts reinsured, and is therefore an issuer under section 6050Y(d). It is thus not appropriate to completely exclude an indemnity reinsurer from the possibility of being an issuer for reporting purposes. However, the definition of 6050Y(b) issuer under the proposed and final regulations is narrower than the definition of issuer in section 6050Y(d) and, consistent with the intent expressed in Notice 2018-41 to limit the information reporting obligations imposed under section 6050Y(b) to the life insurance company that is responsible for administering the contract, will generally exclude a reinsurer in an indemnity contract from reporting obligations, as the commenter acknowledges. Furthermore, §1.6050Y-1(a)(8)(iii)(B) of the final regulations provides any reinsurer in an indemnity contract that is not the issuer responsible for administering the life insurance contract, but nonetheless falls within the definition of 6050Y(b) issuer, with a mechanism to avoid that designation (by providing notice and relevant information to the 6050Y(b) issuer responsible for administering the contract).

B. *Definition of notice of a transfer to a foreign person*

Section 6050Y(b) and §1.6050Y-3 of the proposed regulations generally require reporting by an issuer upon notice of a transfer of a life insurance contract to a foreign person. The proposed regulations define "notice of a transfer to a foreign person" to mean any notice of a transfer of a life insurance contract (that is, a transfer of title to, possession of, or legal ownership of the life insurance contract) received by a 6050Y(b) issuer. *See* §1.6050Y-1(a)(10) of the proposed regulations. The proposed regulations further provide that notice of a transfer to a foreign person includes information provided for nontax purposes, such as a change of address notice for purposes of sending statements or for other purposes, and information relating to loans, premiums, or death benefits with respect to the contract, unless the 6050Y(b) issuer knows that no transfer of the contract has occurred or knows the transferee is a United States person. *Id*. For this purpose, a 6050Y(b) issuer may rely on a Form W-9, "Request for Taxpayer Identification Number and Certification" or a valid substitute form that meets the requirements of §1.1441-1(d)(2) (substituting "6050Y(b) issuer" for "withholding agent"), that indicates the transferee is a United States person. *Id*.

One commenter expressed appreciation that the proposed regulations exclude from the definition of notice of a transfer to a foreign person situations in which the issuer knows that no transfer has occurred or that the transferee is a United States person. The commenter requested that the definition be modified so that the obligation for an issuer to report under section 6050Y(b) and §1.6050Y-3 of the proposed regulations is not triggered unless the issuer receives notice of a transfer of a life insurance contract to a foreign person that includes foreign indicia. Such foreign indicia may include information provided for nontax purposes such as a change of address notice to a foreign residence or mailing address for purposes of sending statements or for other purposes. The commenter noted that section 6050Y(b) requires issuers to identify transfers to foreign persons to capture transfers that may escape section 6050Y(a)(2) reporting in the event that a foreign acquirer does not comply with section 6050Y(a)(2) and suggested that the foreign indicia requirement furthers this purpose by allowing an issuer to identify a foreign acquirer as foreign based on information the acquirer provides to the issuer. This recommendation is adopted in §1.6050Y-1(a)(10) of the final regulations.

C. *Definition of estimate of investment in the contract*

Informal comments were received regarding the definition of the term "estimate of investment in the contract" in the proposed regulations. The commenter asked whether the estimate of investment in the contract with respect to a person includes any amount paid by the person for the life insurance contract or interest therein other than premiums (such as, for example, the amount paid for the contract or interest therein in a transfer for value) and whether information about any other payments must be provided to issuers and payors reporting the estimate of investment in the contract. The definition in §1.6050Y-1(a)(7)(ii) of the proposed regulations, which is adopted without modification by the final regulations, provides that the estimate of investment in the contract is the aggregate amount of premiums paid for the contract by that person before that date, less the aggregate amount received under the contract by that person before that date to the extent such information is known to or can reasonably be estimated by the issuer or payor. Accordingly, the only amounts paid by a person that are included in the estimate of investment in the contract with respect to that person are the premiums paid for the contract by that person. Issuers and payors of reportable death benefits do not need information about other amounts paid for a life insurance contract or interest therein to determine the estimate of investment in the contract. Under section 6050Y(a)(2)(B) and §1.6050Y-2(d)(2)(i)(A) of the final regulations, an acquirer is not required to provide an issuer with the amount of any reportable policy sale payment when fulfilling its reporting obligations under section 6050Y(a).

D. *Definition of reportable policy sale payments*

Under section 6050Y(a) and §1.6050Y-2(a) of the proposed regulations, as a general matter, every person that is an acquirer in a reportable policy sale during any calendar year must file a separate information return with the IRS for each reportable policy sale payment recipient, including any seller that is a reportable policy sale payment recipient. A reportable policy sale payment recipient is defined in §1.6050Y-1(a)(16) of the proposed regulations as any person that receives a reportable policy sale payment in a reportable policy sale, as well as any broker or other intermediary that retains a portion of the cash or other consideration transferred in a reportable policy sale. Under section 6050Y(d)(1), the term "payment" means, with respect to any reportable policy sale, the amount of cash and the fair market value of any consideration transferred in the sale. A reportable policy sale payment is defined by §1.6050Y-1(a)(15) of the proposed regulations as the total amount of cash and the fair market value of any other consideration transferred, or to be transferred in a reportable policy sale, including any amount of a reportable policy sale payment recipient's debt assumed by the acquirer in a reportable policy sale. The final regulations clarify that consideration in this case means consideration reducible to a money value, which is the standard used in §1.101-1(f)(5) of the proposed and final regulations for determining whether a transfer of an interest in a life insurance contract is a transfer for valuable consideration. *See* §1.6050Y-1(a)(15) of the final regulations.

The preamble to the proposed regulations requested information about the types and timing of payments made by acquirers in reportable policy sales, including the types of ancillary costs and expenses paid in reportable policy sales, the recipients of those payments, and existing reporting requirements applicable to those payments. *See* 84 FR 11009, 11019. One commenter on the proposed regulations described ancillary payments made by an acquirer in connection with the acquisition of a life insurance policy as including escrow agent fees and expenses, fees and expenses of securities intermediaries, fees paid to companies that assist the acquirer in evaluating a life insurance policy, fees for policy services, origination fees, fees to life expectancy report providers, miscellaneous other administrative costs such as mailing and courier charges, and legal fees. The commenter asserted that these are all normal and customary transaction costs paid by the acquirer in the ordinary course of its business in connection with the routine process of acquiring a life insurance policy and that the aggregate of such costs in each transaction is relatively small in contrast to the aggregate amount of the consideration paid to the seller of the policy and the seller's broker, if any. The commenter stated that these minor costs and expenses are primarily administrative in nature, and the IRS is already receiving information regarding the payment of fees in connection with existing reporting required under section 6041. The commenter recommended that such ancillary costs be specifically excluded from the definition of reportable policy sale payments.

Another commenter also recommended excluding ancillary fees from the definition of reportable policy sale payments. Alternatively, the commenter suggested that recipients of such ancillary fees could be excluded from the definition of reportable policy sale payment recipients. The commenter stated that the sale of a single life insurance contract from the insured individual to a purchaser on the secondary market may involve several transfers and implicate several potential recipients of a reportable policy sale payment, as that term is defined by the proposed regulations. The commenter described the parties that commonly receive ancillary fees in connection with the sale of a life insurance contract as including securities intermediaries, escrow agents (including separate sub-escrow agents), policy servicers, and other service providers. The commenter asserted that these ancillary fees already should be otherwise reported to the IRS under other provisions of the Code and Treasury Regulations and that including these fees as reportable policy sale payments adds a significant administrative burden to acquirers given the multitude of potential reportable policy sale payment recipients.

The definition of "payment" in section 6050Y(d)(4) is broad, and the legislative history does not suggest that this term was intended to exclude any payment made in a reportable policy sale, such as the ancillary fees described by the commenters. Accordingly, the recommendations to exclude ancillary fees from the definition of reportable policy sale payments or exclude recipients of ancillary fees from the definition of reportable policy sale payment recipients are not adopted. However, after consideration of these comments, the Treasury Department and the IRS have determined that an acquirer that reports a reportable policy sale payment made to a person other than the seller under section 6041 or section 6041A will be deemed to have satisfied its reporting requirements under section 6050Y(a) and §1.6050Y-2 of the final regulations with respect to that payment. *See* §1.6050Y-2(f)(2) of the final regulations. The Treasury Department and the IRS have also determined to exclude from the definition of reportable policy sale payment recipient any person, other than the seller, that receives aggregate payments of less than $600 with respect to that reportable policy sale. *See* §1.6050Y-1(a)(16)(ii) of the final regulations.

8. *Comments and Changes Relating to §1.6050Y-2 of the Proposed Regulations*

Section 6050Y(a) requires reporting of payments made by an acquirer in a reportable policy sale. Section 1.6050Y-2(a) of the proposed regulations sets forth the requirement of information reporting applicable to acquirers in reportable policy sales under section 6050Y(a)(1) and describes the information that must be reported. This section of this Summary of Comments and Explanation of Revisions discusses comments that generally relate to §1.6050Y-2 of the proposed regulations.

A. *Requests to limit the definition of acquirer or expand unified reporting option*

Under §1.6050Y-1(a)(1) of the proposed regulations, an "acquirer" is any person that acquires an interest in a life insurance contract (through a direct or indirect acquisition of the interest) in a reportable policy sale. Section 1.6050Y-1(a)(6) of the proposed regulations adopts by cross-reference the definition of "interest in a life insurance contract" set forth in §1.101-1(e) of the proposed regulations. Section 6050Y(a) imposes reporting requirements on an acquirer in a reportable policy sale.

One commenter on Notice 2018-41 recommended that the definition of acquirer be limited to any person who acquires a direct or indirect economic interest in a life insurance contract and not include any person who acquires title to a life insurance contract as an agent or intermediary for another person and whose sole economic interest in the life insurance contract is security for the payment of a fee to act as an agent or intermediary. For this purpose, the commenter noted, a partnership or a trust (other than a grantor trust) would not be treated as an agent or intermediary. The commenter observed that, in many transactions that will be treated as reportable policy sales, title to the life insurance contract is held in the name of a securities intermediary, but beneficial ownership of the policy is held by an investor. The commenter asserted that, although the securities intermediary may, in a given case, have a portion of the information required to be reported by section 6050Y, burdening the securities intermediary with a reporting obligation is beyond the scope of its duties.

Commenting on the proposed regulations, this commenter again recommended that securities intermediaries should not be deemed to be acquirers in life settlement transactions because they are not likely to know, among other things, the purchase price paid to the seller, fees paid to a life settlement broker, or ancillary fees paid in connection with the acquisition of a policy. The commenter suggested that, if securities intermediaries are deemed acquirers, the regulations could instead provide for elective, substitute reporting by the beneficial owner of the life insurance policy under a securities account agreement. In other words, for a transaction in which a securities intermediary is involved, either the securities intermediary as the legal title holder or the beneficial owner of the life insurance policy under the securities account agreement could be responsible for the reporting required by section 6050Y(a) and §1.6050Y-2 of the proposed regulations.

In response to these comments, §1.6050Y-2(b) of the final regulations expands the situations in which acquirers may use unified reporting. Under §1.6050Y-2(b) of the proposed regulations, the reporting requirement in §1.6050Y-2(a) of the proposed regulations applies to each acquirer in a series of prearranged transfers of an interest in a life insurance contract. However, §1.6050Y-2(b) of the proposed regulations provides for "unified reporting." In a series of prearranged transfers, an acquirer's reporting obligation is deemed satisfied if the information required by §1.6050Y-2(a) of the proposed regulations with respect to that acquirer is timely reported on behalf of that acquirer in a manner that is consistent with forms, instructions, and other IRS guidance by one or more other acquirers or by a third party information reporting contractor. One commenter expressed support for the concept set forth in §1.6050Y-2(b) of the proposed regulations that authorizes but does not mandate unified reporting in certain situations. The final regulations retain this approach of authorizing, but not mandating, unified reporting in certain situations. Additionally, in response to comments requesting elective, substitute reporting by the beneficial owner of the life insurance policy under a securities account agreement for a securities intermediary with reporting obligations, the final regulations expand the applicability of this provision to include acquirers in simultaneous transfers, as well as acquirers in a series of prearranged transfers.

Another commenter recommended that the definition of acquirer be narrowed to include only those acquirers that will ultimately hold beneficial ownership of a life insurance contract after a transfer, thus excluding transitory interest holders from the definition of acquirer. The commenter stated that, under a plain reading of §1.101-1(e)(1) of the proposed regulations, beneficial owners as well as nominees and any other person that holds legal title to any part of a beneficial interest in any life insurance contract for any amount of time during the course of the transaction would be subject to the acquirer reporting requirements of the proposed regulations. The commenter suggested that the definition may be over-inclusive given the realities of the life settlement industry including, for instance, the fact that service providers and their respective securities intermediaries may transitorily hold legal title to a life insurance contract during the course of a transaction. Acknowledging that the proposed regulations provide a unified reporting option, the commenter objected to each such transitory legal title holder being subject to the reporting requirements described in §1.6050Y-2 of the proposed regulations, despite likely not having access to all the information required to sufficiently discharge its reporting obligations. This recommendation is not adopted in the final regulations because the option of unified reporting is available in the situations described by the commenter and it should be feasible, as part of the acquisition transaction, to assign section 6050Y reporting responsibilities to a party with the information needed to satisfy the reporting requirements described in §1.6050Y-2 of the final regulations.

B. *Request to reduce or eliminate reporting on tertiary market transactions*

One commenter asked that the Treasury Department and the IRS consider whether reporting requirements imposed under section 6050Y are appropriate to transactions in the tertiary market (that is, with respect to sales of life insurance contract interests between investors, after the contract has been purchased from the original policyholder). The commenter asserted that the parties (that is, the acquirers and sellers) involved in tertiary transactions in the life settlement industry are already highly regulated, and the reporting requirements under section 6050Y are unduly cumbersome given that the tax information sought by the IRS is already included in such parties' audited financial statements. This request to eliminate or reduce reporting obligations under section 6050Y with respect to tertiary market transactions is not adopted in the final regulations. Section 6050Y requires reporting with respect to reportable policy sales. That term is broadly defined by section 101(a)(3) as the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in such life insurance contract. Tertiary market transactions generally fall within this definition, and therefore are required to be reported.

This commenter also suggested that in the tertiary market, beneficial ownership of a life insurance policy may be transferred between different beneficial owners under separate securities account agreements with the same securities intermediary, without any ownership or beneficiary changes on the books and records of the issuer, so the securities intermediary might be both the seller and the acquirer of the policy interest for purposes of section 6050Y reporting. However, even though the securities intermediary does not transfer its interest in the life insurance contract as the legal title holder in the transfer described, the previous beneficial owner transfers its interest to the new beneficial owner. Under the final regulations, as under the proposed regulations, the new beneficial owner is the acquirer of an interest in the life insurance contract under §1.101-1(e)(3)(i) and §1.6050Y-1(a)(1) and (3), and the previous beneficial owner is the seller under §1.6050Y-1(a)(18)(i), which defines "seller" to include any person that holds an interest in a life insurance contract and transfers that interest, or any part of that interest, to an acquirer in a reportable policy sale.

C. *Request to allow good faith effort reporting*

One commenter on the proposed regulations observed that a situation could arise in which a person acquires a non-controlling interest in an entity that holds direct interests in life insurance contracts, and such entity has neither the obligation nor the willingness to provide the indirect acquirer with information necessary for the indirect acquirer to determine whether it is subject to the reporting requirements or to satisfy any reporting obligations. The commenter suggested that this problem is exacerbated when there are tiers of entities between the indirect acquirer and the entity holding direct interests in life insurance contracts. The commenter recommended that an indirect acquirer be considered to have complied with the reporting requirements of section 6050Y(a) and §1.6050Y-2 of the proposed regulations if it demonstrates that it has in good faith requested information required to comply with the reporting requirements from the relevant entity or entities and was unable to obtain such information by providing to the IRS: (i) the information it does have, (ii) a statement of its efforts to collect any missing data, and (iii) the identifying information on the entity through which it acquired an indirect interest in a life insurance contract or contracts.

Sections 1.6050Y-2(g)(1) and (2) cross-reference section 6724(a) and §301.6724-1 for the waiver of a penalty for failure to file timely a correct information return or furnish a correct statement under section 6050Y and §1.6050Y-2 if the failure is due to reasonable cause and is not due to willful neglect. The penalty may be waived if the filer establishes there are significant mitigating factors with respect to the failure (such as the fact that the filer had not previously had this filing obligation, or has a history of complying with information reporting obligations), or that the failure was due to events beyond the filer's control. Events beyond the filer's control may include the actions of a third party who has information needed by the filer. The filer must show that the failure was due to the failure of another person, who is required to provide information to the filer that is necessary for the filer to comply with information reporting requirements, to provide information or to provide correct information. In addition, a filer seeking a waiver based on reasonable cause must establish that it acted in a responsible manner both before and after the failure. The filer must exercise reasonable care in determining its filing obligations, including requesting extensions to prevent failures, preventing impediments to failures, and rectifying failures when discovered. These penalty relief procedures are available to acquirers and may apply to acquirers in the situation described by the commenter. Accordingly, the final regulations do not adopt the change suggested by the commenter.

9. *Comments Relating to §1.6050Y-3 of the Proposed Regulations*

Section 6050Y(b) imposes reporting requirements on an issuer of a life insurance contract upon the receipt of a written statement furnished by an acquirer under section 6050Y(a)(2), or upon any notice of the transfer of a life insurance contract to a foreign person. Section 1.6050Y-3 of the proposed regulations sets forth the requirement of information reporting applicable to issuers under section 6050Y(b) and describes the information that must be reported. This section of this Summary of Comments and Explanation of Revisions discusses comments that generally relate to §1.6050Y-3 of the proposed regulations.

Section 1.6050Y-3(d)(1) of the proposed regulations requires an issuer to furnish a statement to a seller. Section 1.6050Y-3(d)(2) of the proposed regulations provides that such statement generally must be furnished on or before February 15 of the year following the calendar year in which the reportable policy sale or transfer to a foreign person occurred. This due date was adopted in response to comments on Notice 2018-41. The proposed regulations also provide that if a 6050Y(b) issuer does not receive notice of a transfer to a foreign person until after January 31 of the calendar year following the year in which the transfer occurred, the statement generally must be furnished by the date thirty days after the date notice is received. *See* §1.6050Y-3(d)(2) of the proposed regulations.

One commenter expressed appreciation regarding the adoption of the February 15 due date and the relief provided to 6050Y(b) issuers that do not receive notice of a transfer to a foreign person until after January 31 of the calendar year following the year in which the transfer occurred. The commenter asked that a similar thirty-day period be provided if the 6050Y(b) issuer does not receive an RPSS until after January 31 of the calendar year following the year in which the reportable policy sale occurred. If a 6050Y(b) issuer that receives an RPSS after the January 31 due date and before the February 15 due date is unable to furnish the required statement to the seller by the February 15 due date because of this delay, the 6050Y(b) issuer generally may request, before the February 15 due date, an extension of time to furnish the statement, pursuant to IRS procedures. For example, procedures for requesting such an extension are currently described in the "General Instructions for Certain Information Returns." Additionally, the late furnishing of an RPSS by an acquirer to a 6050Y(a) issuer would generally constitute an event beyond the issuer's control for purposes of determining whether the issuer is eligible for penalty relief for failure, as a 6050Y(b) issuer, to timely furnish a statement to the seller named in the RPSS. *See* §§1.6050Y-3(g)(2), 301.6722-1, and 301.6724-1. Therefore, the Treasury Department and the IRS have determined not to adopt this recommendation.

10. *Comments and Changes Relating to §1.6050Y-4 of the Proposed Regulations*

Section 6050Y(c) imposes reporting requirements on every person who makes a payment of reportable death benefits during any taxable year. Section 1.6050Y-4 of the proposed regulations sets forth the requirement of information reporting applicable to payors of reportable death benefits under section 6050Y(c) and describes the information that must be reported. This section of this Summary of Comments and Explanation of Revisions discusses comments that generally relate to §1.6050Y-4 of the proposed regulations.

A. *Gratuitous transfers*

As discussed in section 2.B of this Summary of Comments and Explanation of Revisions, one commenter requested an exception from the definition of reportable policy sale for any gratuitous transfer of an interest in a life insurance contract. The commenter asserted that treating gratuitous transfers as reportable policy sales creates unnecessary and confusing reporting requirements under section 6050Y for gift transfers. The change requested by the commenter is not adopted in the final regulations because the reporting required under section 6050Y for gift transfers is limited under the proposed and final regulations. However, in response to these comments, the reporting required under section 6050Y for gift transfers is further limited by the addition of §1.6050Y-4(e)(3) of the final regulations, which provides that a payor of reportable death benefits is not required to file an information return under §1.6050Y-4(a) of the final regulations with respect to the reportable death benefits if the payor never received, and has no knowledge of any issuer having received, a related RPSS.

The commenter asserted that the reporting requirements under section 6050Y will result in an acquirer having to send a Form 1099-LS for transfers that are mere gifts, and that this will be confusing to the parties involved, making it appear that the transfer will have taxable consequences to both the donor, who will receive a Form 1099-SB, and the gift recipient, who will receive a Form 1099-R (when a death benefit is paid).

However, with respect to a gratuitous transfer, there is no requirement to provide a Form 1099-SB to the donor. Section 1.6050Y-2(a) of the proposed regulations requires the acquirer (the gratuitous transferee in a gratuitous transfer) to undertake reporting with respect to any reportable policy sale payment recipient, including any seller that is a reportable policy sale payment recipient. A gratuitous transferor will not receive any reportable policy sale payment and therefore will not be a reportable policy sale payment recipient. Accordingly, a gratuitous transferee will not be required to file a Form 1099-LS with respect to the gratuitous transferor, to furnish a statement to the gratuitous transferor, or to furnish an RPSS to the issuer. *See* §1.6050Y-2(a) and (d) of the proposed regulations. Because a gratuitous transferee is not required to furnish an RPSS to the issuer, the issuer should not be required to file a Form 1099-SB or furnish a statement to the "seller" (in this case, the gratuitous transferor) as a result of a gratuitous transfer. *See* §1.6050Y-3(a) of the proposed regulations.

Because amounts paid by reason of the death of the insured under a life insurance contract that are attributable to an interest in the contract that was transferred in a reportable policy sale are reportable death benefits under §1.6050Y-1(a)(12) of the proposed regulations, the proposed regulations technically would require reporting under section 6050Y(c) when death benefits are paid with respect to an interest in a life insurance contract that was transferred in a gratuitous reportable policy sale. *See* 1.6050Y-4(a) and (c). The issuer therefore could be required under the proposed regulations to provide the gratuitous transferee with a statement (for instance, a copy of the Form 1099-R) if the gratuitous transferee is the reportable death benefits payment recipient. *See* 1.6050Y-4(c). The commenter asserted that this would confuse the Form 1099-R recipient, who now possesses a Form 1099-R reporting a gross distribution amount that indicates a possible taxable distribution when none exists. The commenter also asserted that inclusion of the estimate of investment in the contract on the Form 1099-R will further confuse the gift recipient because it would indicate to a taxpayer that they have a taxable gain based on the difference between the gross distribution amount and the basis amount reported on the form.

However, the distribution to the gift recipient may be taxable. Under §1.101-1(b)(2)(i) of the proposed regulations, the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1) is limited to the sum of the amount of the proceeds attributable to the gratuitously transferred interest that would have been excludable by the transferor if the transfer had not occurred, and the premiums and other amounts subsequently paid by the transferee with respect to the interest. Thus, for example, if an interest in a life insurance contract was transferred for value in a reportable policy sale, and then transferred again as a gift, the death benefit exclusion would be limited to the consideration paid in the reportable policy sale, plus subsequent premiums paid.

As a practical matter, however, if the only reportable policy sale of an interest in a life insurance contract is a gratuitous reportable policy sale, and the issuer does not receive an RPSS, the issuer would not know that the death benefits are attributable to an interest in a life insurance contract transferred in a reportable policy sale, and thus would not be on notice to do the reporting technically required under §1.6050Y-4(a) and (c) of the proposed regulations. Accordingly, in response to these comments, §1.6050Y-4(e)(3) of the final regulations provides that a payor of reportable death benefits is not required to file an information return under §1.6050Y-4(a) of the final regulations with respect to the reportable death benefits if the payor never received, and has no knowledge of any issuer having received, a related RPSS.

B. *Other comments relating to §1.6050Y-4*

Section 1.6050Y-4(a)(4) of the proposed regulations requires that "the gross amount of payments made to the reportable death benefits payment recipient during the taxable year" be reported by the payor. One commenter requested that "payments made" be replaced by "reportable death benefits paid" to clarify that "gross amount of payments" are death benefit payments. The commenter asserted that the broader term "payments made" could be confused to include items such as interest paid on delayed claims, which is reportable on Form 1099-INT, "Interest Income," or a payment to the policy owner resulting from a partial surrender in the same year as the insured's death. This recommendation is adopted in the final regulations.

Section 1.6050Y-4(d) of the proposed regulations requires a payor of reportable death benefits that files a return or furnishes a statement reporting the payment of the reportable death benefits to file a corrected return or furnish a corrected statement after receiving notice of rescission of the reportable policy sale. The commenter indicated that, if a payor has already paid the death benefit pursuant to the change in ownership, the payor may not be contractually required, or may not attempt to, reclaim such benefit after a rescission. The commenter asserted that payors of death benefits generally do not file corrected Forms 1099-R in similar instances because the payment was, in fact, made to the initial recipient. The commenter recommended that §1.6050Y-4(d) of the proposed regulations be modified to provide that the payor is required to correct the Form 1099-R only if the reportable death benefit payment was returned to the payor. In response to this comment, §1.6050Y-4(d) of the final regulations requires a payor of reportable death benefits that files a return or furnishes a statement reporting the payment of the reportable death benefits to file a corrected return or furnish a corrected statement within 15 days after recovering any portion of the reportable death benefits payment from the reportable death benefits payment recipient as the result of the rescission of a reportable policy sale.

The commenter also requested that the final regulations clarify that the reportable death benefits paid to a foreign person should be reported on Form 1042-S, "Foreign Person's U.S. Source Income Subject to Withholding," instead of on Form 1099-R. Under §1.6050Y-4(e)(1) of the proposed regulations, a payor generally is not required to report reportable death benefits paid to a foreign person on Form 1099-R if the payor obtains documentation in accordance with §1.1441-1(e)(1)(ii) upon which the payor may rely to treat the reportable death benefits payment recipient as a foreign beneficial owner of the reportable death benefits. However, this exception does not apply if a 6050Y(b) issuer obtains a Form W-8ECI, "Certificate of Foreign Person's Claim that Income is Effectively Connected with the Conduct of a Trade or Business in the United States." Accordingly, if the payment of reportable death benefits to a foreign beneficial owner is income effectively connected with the foreign person's trade or business in the United States, the payor may be required to report the payment on both the Form 1042-S in accordance with §1.1461-1(c) and the Form 1099-R in accordance with §1.6050Y-4 of the proposed regulations. In response to this comment, therefore, §1.6050Y-4(e)(1) of the final regulations does not include the limitation on the use of the exception for reportable death benefits that are income effectively connected with the conduct of a trade or business in the United States, but instead references other due diligence or reporting requirements that may apply to a payor that relies on the exception, including reporting requirements under §1.1461-1(c). As a result, the final regulations do not require reportable death benefits paid to a foreign person that must be reported on Form 1042-S to also be reported on Form 1099-R.

11. *Comments and Changes Relating to Penalties*

Sections 1.6050Y-2(g), 1.6050Y-3(g), and 1.6050Y-4(f) of the proposed regulations cross-reference sections 6721 and 6722 and the regulations thereunder for provisions relating to the penalties provided for failure to file timely a correct information return or furnish timely a correct information return required under section 6050Y and §§1.6050Y-2, 1.6050Y-3, or 1.6050Y-4 of the proposed regulations. Sections 1.6050Y-2(g), 1.6050Y-3(g), and 1.6050Y-4(f) of the proposed regulations also cross-reference §301.6724-1 for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

One commenter asked for permanent penalty relief for issuers unable to meet the filing due date for reasons beyond the control of the issuer. The commenter stated that such relief is available under section 6724(a), which allows for waivers for reasonable cause for reporting failures. The commenter suggested that the requested relief could be accomplished through guidance that designates late receipt of a Form 1099-LS (serving as an RPSS) as establishing reasonable cause for purposes of section 6724. To identify reports eligible for such relief, the commenter suggested that a check box could be added to Form 1099-SB for "late receipt of Form 1099-LS," thereby avoiding the inefficiencies and costs associated with waiver and abatement procedures. The commenter did not provide any reason to anticipate that many acquirers will fail to timely furnish statements to 6050Y(a) issuers as required by section 6050Y(a) and §1.6050Y-2(d)(2). Accordingly, the Treasury Department and the IRS have determined that the normal penalty relief procedures, as described in section 9 of this Summary of Comments and Explanation of Revisions, should be sufficient and have not adopted the commenter's recommendation.

Applicability Dates

Section 1 of this Summary of Comments and Explanation of Revisions describes the applicability dates for §1.101-1(b) through (g) of the final regulations and §§1.6050Y-1 through 1.6050Y-4 of the final regulations.

As described in section 1 of this Summary of Comments and Explanation of Revisions, the final regulations provide transition relief as set forth in §1.6050Y-1(b) of the proposed regulations, with some modifications. For reportable policy sales and payments of reportable death benefits occurring after December 31, 2018, and on or before October 31, 2019, §1.6050Y-1(b) of the final regulations provides transition relief as follows:

(1) Statements required to be furnished to issuers under section 6050Y(a)(2) and §1.6050Y-2(d)(2)(i) must be furnished by the later of the applicable deadline set forth in §1.6050Y-2(d)(2)(ii) or December 30, 2019.

(2) Statements required to be furnished to reportable policy sale payment recipients under section 6050Y(a)(2) and §1.6050Y-2(d)(1)(i) must be furnished by the later of the applicable deadline set forth in §1.6050Y-2(d)(1)(ii) or February 28, 2020.

(3) Statements required to be furnished to sellers under section 6050Y(b)(2) and §1.6050Y-3(d)(1) must be furnished by the later of the applicable deadline set forth in §1.6050Y-3(d)(2) or February 28, 2020.

(4) Statements required to be furnished to reportable death benefits payment recipients under section 6050Y(c)(2) and §1.6050Y-4(c)(1) must be furnished by the later of the applicable deadline set forth in §1.6050Y-4(c)(2) or February 28, 2020.

(5) Returns required to be filed under section 6050Y(a)(1) and §1.6050Y-2(a), section 6050Y(b)(1) and §1.6050Y-3(a), and section 6050Y(c)(1) and §1.6050Y-4 must be filed by the later of the applicable deadline set forth in §1.6050Y-2(c), §1.6050Y-3(c), and §1.6050Y-4(b) or February 28, 2020.

Special Analyses

This regulation is not subject to review under section 6(b) of Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding review of tax regulations.

Paperwork Reduction Act

The collection of information contained in the final regulations has 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 OMB Control Numbers 1545-0119, 1545-1621, and 1545-2281. In general, the collection of information in the final regulations is required under section 6050Y of the Code: (1) The requirement under §1.6050Y-2 of the final regulations for an acquirer to report certain information about payments made in reportable policy sales is required under section 6050Y(a); (2) the requirement under §1.6050Y-3 of the final regulations for an issuer to report certain information about transferors of life insurance contracts is required under section 6050Y(b); and (3) the requirement under §1.6050Y-4 of the final regulations for a payor to report certain information about payments of reportable death benefits is required under section 6050Y(c). Section 1.6050Y-3(a)(3) of the final regulations also requires the issuer to report to the seller and the IRS the amount the seller would have received if the seller had surrendered the life insurance contract on the date of the reportable policy sale. This information is necessary to allow the seller and the IRS to determine the character (capital or ordinary) of all or a portion of the seller's taxable income from the sale of the life insurance contract. Section 1.6050Y-3(f)(1) of the final regulations contains reporting exceptions for certain foreign beneficial owners. To determine qualification for these reporting exceptions, §1.6050Y-3(f)(1) of the final regulations requires that certain foreign beneficial owners provide a Form W-8ECI to the 6050Y(b) issuer. This information is necessary to document whether the reporting exception in §1.6050Y-3(f)(1) of the final regulations applies in a particular situation.

For purposes of the Paperwork Reduction Act, the burden associated with the collection of information contained in section 6050Y(a) and §1.6050Y-2 of the final regulations is reflected in the IRS Form 1099-LS (OMB control number 1545-2281). For purposes of the Paperwork Reduction Act, the burden associated with the collection of information contained in section 6050Y(b) and §1.6050Y-3 of the final regulations is reflected in the IRS Form 1099-SB (OMB control number 1545-2281). For purposes of the Paperwork Reduction Act, the burden associated with the collection of information contained in section 6050Y(c) and §1.6050Y-4 of the final regulations is reflected in the IRS Form 1099-R (OMB Control Number 1545-0119). For purposes of the Paperwork Reduction Act, the burden associated with the collection of information contained in §1.6050Y-3(f)(1) of the final regulations will be reflected in the IRS Form W-8ECI (OMB Control Number 1545-1621), when the burden is revised to reflect the additional collection of information in §1.6050Y-3(f)(1) of the final regulations.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget. Books and records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Regulatory Flexibility Act

It is hereby certified that this rule will not have a significant economic impact on a substantial number of small entities pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6). Section 13520 of the TCJA added section 6050Y to chapter 61 (Information and Returns) of the Code. Section 6050Y imposes information reporting obligations related to certain life insurance contract transactions, including reportable policy sales and payments of reportable death benefits. Section 6050Y provides that each of the returns required by section 6050Y is to be made "at such time and in such manner as the Secretary shall prescribe." The final regulations under section 6050Y implement section 6050Y by specifying the manner in which and time at which the information reporting obligations must be satisfied. Because the regulations are limited in scope to time and manner of information reporting and definitional information, the economic impact of the regulations is expected to be minimal. In addition, the IRS and Treasury expect that the reporting burden will fall primarily on financial and insurance firms with annual receipts greater than $38.5 million and, therefore, will not affect a substantial number of small entities. *See* 13 CFR 121.201, sector 52 (finance and insurance).

Although the reporting burden falls primarily on larger entities, some small entities under the size threshold may be subject to a one-time reporting requirement that includes information that is readily available to the entities. This one-time reporting is unlikely to present a significant economic burden on any small entities affected.

Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding the final regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business, and no comments were received.

Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 (UMRA) requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of $100 million in 1995 dollars, updated annually for inflation. In 2018, that threshold is approximately $150 million. This rule does not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

Executive Order 13132: Federalism

Executive Order 13132 (titled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This final rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Drafting Information

The principal author of these regulations is Kathryn M. Sneade, Office of Associate Chief Counsel (Financial Institutions and Products), IRS. However, other personnel from the Treasury Department and the IRS participated in their development.

Availability of IRS Documents

The IRS notice cited in this preamble is published in the Internal Revenue Bulletin and is available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at www.irs.gov.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding entries for §§1.6050Y-2, 1.6050Y-3, and 1.6050Y-4 in numerical order to read in part as follows:

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

* * * * *

Section 1.6050Y-2 also issued under 26 U.S.C. 6050Y(a).

Section 1.6050Y-3 also issued under 26 U.S.C. 6050Y(b).

Section 1.6050Y-4 also issued under 26 U.S.C. 6050Y(c).

* * * * *

Par. 2. Section 1.101-1 is amended by:

1. Revising the second sentence of paragraph (a)(1), removing the third sentence of paragraph (a)(1), and adding a sentence at the end of paragraph (a)(1).
2. Revising paragraphs (b)(1) through (3).
3. Removing paragraphs (b)(4) and (5).
4. Adding paragraphs (c) through (g).

The revisions and additions read as follows:

§1.101-1 Exclusion from gross income of proceeds of life insurance contracts payable by reason of death.

(a)(1) * * * Death benefit payments having the characteristics of life insurance proceeds payable by reason of death under contracts, such as workmen's compensation insurance contracts, endowment contracts, or accident and health insurance contracts, issued on or before December 31, 1984, are covered by this provision. * * * If the life insurance contract is an employer-owned life insurance contract within the definition of section 101(j)(3), the amount to be excluded from gross income may be affected by the provisions of section 101(j).

* * * * *

(b) * * * (1) *Transfer of an interest in a life insurance contract for valuable consideration*—(i) *In general.* In the case of a transfer of an interest in a life insurance contract for valuable consideration, including a reportable policy sale for valuable consideration, the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1) is limited under section 101(a)(2) to the sum of the actual value of the consideration for the transfer paid by the transferee and the premiums and other amounts subsequently paid by the transferee with respect to the interest. For exceptions to this general rule for certain transfers for valuable consideration that are not reportable policy sales, see paragraph (b)(1)(ii) of this section. The application of section 101(d), (f) or (j), which is not addressed in paragraph (b) of this section, may further limit the amount of the proceeds excludable from gross income.

(ii) *Exceptions*—(A) *Exception for carryover basis transfers.* The limitation described in paragraph (b)(1)(i) of this section does not apply to the transfer of an interest in a life insurance contract for valuable consideration if each of the following requirements are satisfied. First, the transfer is not a reportable policy sale. Second, the basis of the interest, for the purpose of determining gain or loss with respect to the transferee, is determinable in whole or in part by reference to the basis of the interest in the hands of the transferor (see section 101(a)(2)(A)). Third, paragraph (b)(1)(ii)(B) of this section does not apply. In the case of a transfer described in this paragraph (b)(1)(ii)(A), the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1) is limited to the sum of the amount that would have been excludable by the transferor if the transfer had not occurred and the premiums and other amounts subsequently paid by the transferee with respect to the interest. The preceding sentence applies without regard to whether the interest previously has been transferred and the nature of any prior transfer of the interest.

(B) *Exception for transfers to certain persons*—(*1*) *In general.* The limitation described in paragraph (b)(1)(i) of this section does not apply to the transfer of an interest in a life insurance contract for valuable consideration if both of the following requirements are satisfied. First, the transfer is not a reportable policy sale and the interest was not previously transferred for valuable consideration in a reportable policy sale. Second, the interest is transferred to the insured, a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder or officer (see section 101(a)(2)(B)).

(*2*) *Transfers to certain persons subsequent to a reportable policy sale.* Except as provided in paragraph (b)(1)(ii)(B)(*3*) of this section, if a transfer of an interest in a life insurance contract would be described in paragraph (b)(1)(ii)(B)(*1*) of this section, but for the fact that the interest previously was transferred for valuable consideration in a reportable policy sale (whether in the immediately preceding transfer or an earlier transfer), then the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1) is limited to the sum of—

(*i*) The higher of the amount that would have been excludable by the transferor if the transfer had not occurred or the actual value of the consideration for the transfer paid by the transferee; and

(*ii*) The premiums and other amounts subsequently paid by the transferee with respect to the interest.

(*3*) *Transfers to the insured subsequent to a reportable policy sale*—(*i*) Except as provided in paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section, to the extent that an interest (or portion of an interest) in a life insurance contract that was transferred for valuable consideration in a reportable policy sale subsequently is transferred to the insured for valuable consideration, the limitations described in paragraph (b)(1)(i) of this section and paragraph (b)(1)(ii)(B)(*2*) of this section do not apply. To the extent that fair market value is not paid by the insured for the transferred interest, the transfer of the portion of the interest with a value in excess of the consideration paid will be treated as a gift under the bargain sale rule in paragraph (b)(2)(iii) of this section.

(*ii*) This paragraph (b)(1)(ii)(B)(*3*)(*ii*) applies with respect to an interest described in paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section (or portion of such an interest) that subsequently is transferred by the insured to any other person. If all subsequent transfers of the interest (or portion of the interest) are gratuitous transfers that are not reportable policy sales, the amount of the proceeds excluded from gross income is determined under paragraph (b)(2)(i) of this section, taking into account the application of paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section to the insured's acquisition of the interest. If any subsequent transfer of the interest (or portion of the interest) is for valuable consideration or is a reportable policy sale, the amount of the policy proceeds excludable from gross income is determined in accordance with paragraph (b) of this section; if the amount that would have been excludable from gross income by the insured following the transaction described in paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section if no subsequent transfer had occurred is relevant, that amount is determined under paragraph (b)(1)(ii)(B)(*2*) of this section. Paragraph (g)(8) (*Example 8*) of this section and paragraph (g)(9) (*Example 9*) of this section illustrate the application of this paragraph (b)(1)(ii)(B)(*3*)(*ii*).

(2) *Other transfers*—(i) *Gratuitous transfer of an interest in a life insurance contract*. To the extent that a transfer of an interest in a life insurance contract is gratuitous, including a reportable policy sale that is not for valuable consideration, the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1) is limited to the sum of the amount of the proceeds attributable to the gratuitously transferred interest that would have been excludable by the transferor if the transfer had not occurred and the premiums and other amounts subsequently paid by the transferee with respect to the interest. However, if an interest in a life insurance contract is transferred gratuitously to the insured, and that interest has not previously been transferred for value in a reportable policy sale, the entire amount of the proceeds attributable to the interest transferred to the insured is excludable from gross income.

(ii) *Partial transfers*. When only part of an interest in a life insurance contract is transferred, the transferor's exclusion is ratably apportioned between or among the several parts. If multiple parts of an interest are transferred, the transfer of each part is treated as a separate transaction, with each transaction subject to the rule under paragraph (b) of this section that is applicable to the type of transfer involved.

(iii) *Bargain sales*. When the transfer of an interest in a life insurance contract is in part a transfer for valuable consideration and in part a gratuitous transfer, the transfer of each part is treated as a separate transaction for purposes of determining the amount of the proceeds attributable to the interest that is excludable from gross income under section 101(a)(1). Each separate transaction is subject to the rule under paragraph (b) of this section that is applicable to the type of transfer involved.

(3) *Determination of amounts paid by the transferee.* For purposes of paragraphs (b)(1) and (2) of this section, in determining the amounts, if any, of consideration paid by the transferee for the transfer of an interest in a life insurance contract and premiums and other amounts subsequently paid by the transferee with respect to that interest, the amounts paid by the transferee are reduced, but not below zero, by amounts received by the transferee under the life insurance contract that are not received as an annuity, to the extent excludable from gross income under section 72(e).

(c) *Reportable policy sale*—(1) *In general.* Except as provided in paragraph (c)(2) of this section, a reportable policy sale for purposes of this section and section 6050Y is any direct or indirect acquisition of an interest in a life insurance contract if the acquirer has, at the time of the acquisition, no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in the life insurance contract.

(2) *Exceptions*. None of the following transactions is a reportable policy sale:

(i) A transfer of an interest in a life insurance contract between entities with the same beneficial owners, if the ownership interest of each beneficial owner in the transferor entity does not vary by more than a 20 percent ownership interest from that beneficial owner's ownership interest in the transferee entity. In a series of transfers, the prior sentence is applied by comparing the beneficial owners' ownership interest in the first transferor entity and the last transferee entity. For purposes of this paragraph (c)(2)(i), each beneficial owner of a trust is deemed to have an ownership interest determined by the broadest possible exercise of a trustee's discretion in that beneficial owner's favor. Paragraph (g)(13) (*Example 13*) of this section provides an illustration of the application of this paragraph (c)(2)(i).

(ii) A transfer between corporations that are members of an affiliated group (as defined in section 1504(a)) that files a consolidated U.S. income tax return for the taxable year in which the transfer occurs.

(iii) The indirect acquisition of an interest in a life insurance contract by a person if—

(A) A partnership, trust, or other entity in which an ownership interest is being acquired directly or indirectly holds the interest in the life insurance contract and acquired that interest before January 1, 2019, or acquired that interest in a reportable policy sale reported in compliance with section 6050Y(a) and §1.6050Y-2; or

(B) Immediately before the acquisition, no more than 50 percent of the gross value of the assets (as determined under paragraph (f)(4) of this section) of the partnership, trust, or other entity that directly or indirectly holds the interest in the life insurance contract, and in which an ownership interest is being directly acquired, consists of life insurance contracts, provided that, after the acquisition, with respect to that partnership, trust, or other entity, the person indirectly acquiring the interest in the life insurance contract and his or her family members own, in the aggregate—

(*1*) With respect to an S corporation, stock possessing 5 percent or less of the total combined voting power of all classes of stock entitled to vote and 5 percent or less of the total value of shares of all classes of stock of the S corporation;

(*2*) With respect to a trust or decedent's estate, 5 percent or less of the corpus and 5 percent or less of the annual income (taking into account, for the purpose of determining any person's ownership interest, the maximum amount of income and corpus that could be distributed to or held for the benefit of that person); or

(*3*) With respect to a partnership or other entity that is not a corporation or a trust, 5 percent or less of the capital interest and 5 percent or less of the profits interest.

(iv) The acquisition of a life insurance contract by an insurance company that issues a life insurance contract in an exchange pursuant to section 1035.

(v) The acquisition of a life insurance contract by a policyholder in an exchange pursuant to section 1035, if the policyholder has a substantial family, business, or financial relationship with the insured, apart from its interest in the life insurance contract, at the time of the exchange.

(d) *Substantial relationship*—(1) *Substantial family relationship*. For purposes of this section, a substantial family relationship means the relationship between an individual and any family member of that individual as defined in paragraph (f)(3) of this section. In addition, a substantial family relationship exists between an individual and his or her former spouse with regard to the transfer of an interest in a life insurance contract to (or in trust for the benefit of) that former spouse incident to divorce.

(2) *Substantial business relationship.* For purposes of this section, a substantial business relationship between the insured and the acquirer exists in each of the following situations:

(i) The insured is a key person (as defined in section 264) of, or materially participates (within the meaning of section 469) in, an active trade or business as an owner, employee, or contractor, and at least 80 percent of that trade or business is owned (directly or indirectly, through one or more partnerships, trusts, or other entities) by the acquirer or the beneficial owners of the acquirer.

(ii) The acquirer acquires an active trade or business and acquires the interest in the life insurance contract either as part of that acquisition or from a person owning significant property leased to the acquired trade or business or life insurance policies held to facilitate the succession of the ownership of the business if—

(A) The insured—

(*1*) Is an employee within the meaning of section 101(j)(5)(A) of the acquired trade or business immediately preceding the acquisition; or

(*2*) Was a director, highly compensated employee, or highly compensated individual within the meaning of section 101(j)(2)(A)(ii) of the acquired trade or business, and the acquirer, immediately after the acquisition, has ongoing financial obligations to the insured with respect to the insured's employment by the trade or business (for example, the life insurance contract is maintained by the acquirer to fund current or future retirement, pension, or survivorship obligations based on the insured's relationship with the entity or to fund a buy-out of the insured's interest in the acquired trade or business); and

(B) The acquirer either carries on the acquired trade or business or uses a significant portion of the acquired business assets in an active trade or business that does not include investing in interests in life insurance contracts.

(3) *Substantial financial relationship.* For purposes of this section, a substantial financial relationship between the insured and the acquirer exists in each of the following situations:

(i) The acquirer (directly or indirectly, through one or more partnerships, trusts, or other entities of which it is a beneficial owner) has, or the beneficial owners of the acquirer have, a common investment (other than the interest in the life insurance contract) with the insured and a buy-out of the insured's interest in the common investment by the co-investor(s) after the insured's death is reasonably foreseeable.

(ii) The acquirer maintains the life insurance contract on the life of the insured to provide funds to purchase assets of or to satisfy liabilities of the insured or the insured's estate, heirs, legatees, or other successors in interest, or to satisfy other liabilities arising upon or by reason of the death of the insured.

(iii) The acquirer is an organization described in sections 170(c), 2055(a), and 2522(a) that previously received from the insured either financial support in a substantial amount or significant volunteer support or that meets other requirements prescribed in guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter) for establishing that a substantial financial relationship exists between the insured and the organization.

(4) *Special rules.* Paragraphs (d)(4)(i), (ii), and (iii) of this section apply for purposes of determining whether a substantial relationship (whether family, business, or financial) exists under paragraph (d)(1), (2), or (3) of this section, respectively.

(i) *Indirect acquisitions.* The acquirer of an interest in a life insurance contract in an indirect acquisition is deemed to have a substantial business or financial relationship with the insured if the direct holder of the interest in the life insurance contract has a substantial business or financial relationship with the insured immediately before and after the date the acquirer acquires its interest.

(ii) *Acquisitions by certain persons.* The sole fact that an acquirer is a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder or officer, is not sufficient to establish a substantial business or financial relationship with the insured. In addition, an acquirer need not be a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder or officer to have a substantial business or financial relationship with the insured.

(iii) *Acquisitions by those with differing types of substantial relationships*. A substantial family, business, or financial relationship exists between the insured and a partnership, trust, or other entity if each beneficial owner of that partnership, trust, or other entity has a substantial family, business, or financial relationship with the insured. For example, a substantial family, business, or financial relationship exists between the insured and a trust if each trust beneficiary is a family member of the insured or an organization described in paragraph (d)(3)(iii) of this section.

(e) *Interest in a life insurance contract*—(1) *Definition.* For purposes of this section and section 6050Y, the term *interest in a life insurance contract* means the interest held by any person that has taken title to or possession of the life insurance contract (also referred to as a life insurance policy), in whole or part, for state law purposes, including any person that has taken title or possession as nominee for another person, and the interest held by any person that has an enforceable right to receive all or a part of the proceeds of a life insurance contract or to any other economic benefits of the policy as described in §20.2042-1(c)(2) of this chapter, such as the enforceable right to designate a contract beneficiary. Any person named as the owner in the life insurance contract generally is the owner (or an owner) of the contract and holds an interest in the contract.

(2) *Transfer of an interest in a life insurance contract.* For purposes of this section and section 6050Y, the term *transfer of an interest in a life insurance contract* means the transfer of any interest in the life insurance contract, including any transfer of title to, possession of, or legal or beneficial ownership of the life insurance contract itself. The creation of an enforceable right to receive all or a part of the proceeds of a life insurance contract constitutes the transfer of an interest in the life insurance contract. The following events are not a transfer of an interest in a life insurance contract: the revocable designation of a beneficiary of the policy proceeds (until the designation becomes irrevocable other than by reason of the death of the insured); the pledging or assignment of a policy as collateral security; and the issuance of a life insurance contract to a policyholder, other than the issuance of a policy in an exchange pursuant to section 1035.

(3) *Acquisition of an interest in a life insurance contract.* For purposes of this section and section 6050Y, the acquisition of an interest in a life insurance contract may be direct or indirect.

(i) *Direct acquisition of an interest in a life insurance contract.* For purposes of this section and section 6050Y, the transfer of an interest in a life insurance contract results in the direct acquisition of the interest by the transferee (acquirer).

(ii) *Indirect acquisition of an interest in a life insurance contract.* For purposes of this section and section 6050Y, an indirect acquisition of an interest in a life insurance contract occurs when a person (acquirer) becomes a beneficial owner of a partnership, trust, or other entity that holds (whether directly or indirectly) the interest (whether legal or beneficial) in the life insurance contract. For purposes of this paragraph (e)(3)(ii), the term *other entity* does not include a C corporation, unless more than 50 percent of the gross value of the assets of the C corporation consists of life insurance contracts (as determined under paragraph (f)(4) of this section) immediately before the indirect acquisition.

(f) *Definitions.* The following definitions apply for purposes of this section:

(1) *Beneficial owner.* A beneficial owner of a partnership, trust, or other entity is an individual or C corporation with an ownership interest in that entity. The interest may be held directly or indirectly, through one or more other partnerships, trusts, or other entities. For instance, an individual that directly owns an interest in a partnership (P1), which directly owns an interest in another partnership (P2), is an indirect beneficial owner of P2 and any assets or other entities owned by P2 directly or indirectly. For purposes of this paragraph (f)(1), the beneficial owners of a trust include those who may receive current distributions of trust income or corpus and those who could receive distributions if the trust were to terminate currently.

(2) *C corporation.* The term *C corporation* has the meaning given to it in section 1361(a)(2).

(3) *Family member*. With respect to any individual, the term *family member* refers to any person described in paragraphs (f)(3)(i) through (vi) of this section. For purposes of this paragraph (f)(3), full effect is given to a legal adoption, and a step-child is deemed to be a descendant. The family members of an individual include:

(i) The individual;

(ii) The individual's spouse or a person with whom the individual is in a registered domestic partnership, civil union, or other similar relationship established under state law;

(iii) Any parent, grandparent, or great-grandparent of the individual or of the person described in paragraph (f)(3)(ii) of this section and any spouse of such parent, grandparent, or great-grandparent, or person with whom the parent, grandparent, or great-grandparent is in a registered domestic partnership, civil union, or other similar relationship established under state law;

(iv) Any lineal descendant of the individual or of any person described in paragraph (f)(3)(ii) or (iii) of this section;

(v) Any spouse of a lineal descendant described in paragraph (f)(3)(iv) of this section and any person with whom such a lineal descendant is in a registered domestic partnership, civil union, or other similar relationship established under state law; and

(vi) Any lineal descendant of a person described in paragraph (f)(3)(v) of this section.

(4) *Gross value of assets*—(i) *Determination of gross value of assets*. Except as provided in paragraph (f)(4)(ii) or (iii) of this section, for purposes of paragraphs (c)(2)(iii)(B) and (e)(3)(ii) of this section, the term *gross value of assets* means, with respect to any entity, the fair market value of the entity's assets, including assets beneficially owned by the entity under paragraph (f)(1) of this section as a beneficial owner of a partnership, trust, or other entity.

(ii) *Determination of gross value of assets of publicly traded entity.* For purposes of determining the gross value of assets of an entity that is publicly traded, if the entity's annual Form 10-K filed with the United States Securities and Exchange Commission (or equivalent annual filing if the entity is publicly traded in a non-U.S. jurisdiction) for the period immediately preceding a person's acquisition of an ownership interest in the entity does not contain information demonstrating that more than 50 percent of the gross value of the entity's assets consists of life insurance contracts, that person may assume that no more than 50 percent of the gross value of the entity's assets consists of life insurance contracts, unless that person has actual knowledge or reason to know that more than 50 percent of the gross value of the entity's assets consists of life insurance contracts.

(iii) *Safe harbor definition of gross value of assets.* An entity may choose to determine the gross value of all the entity's assets for purposes of this section using the following alternative definition of *gross value of assets*:

(A) In the case of assets that are life insurance policies or annuity or endowment contracts that have cash values, the cash surrender value as defined in section 7702(f)(2)(A); and

(B) In the case of assets not described in paragraph (f)(4)(iii)(A) of this section, the adjusted bases (within the meaning of section 1016) of such assets.

(5) *Transfer for valuable consideration.* A transfer for valuable consideration means any transfer of an interest in a life insurance contract for cash or other consideration reducible to a money value.

(g) *Examples.* The application of this section is illustrated by the following examples. Each example assumes that the transferee did not receive any amounts under the life insurance contract other than the amounts described in the examples. With the exception of paragraph (g)(7) (*Example 7*) of this section, the bargain sale rules set forth in paragraph (b)(2)(iii) of this section do not apply in the examples because the consideration paid for the policy transferred is fair market value:

(1) *Example 1.* A is the initial policyholder of a $100,000 insurance policy on A's life. A sells the policy to B, A's child, for $6,000, its fair market value. B is not a partner in a partnership in which A is a partner. B receives the proceeds of $100,000 upon the death of A. Because the transfer to B was for valuable consideration, and none of the exceptions in paragraph (b)(1)(ii) of this section applies, the amount of the proceeds B may exclude from B's gross income under this section is limited under paragraph (b)(1)(i) of this section to $6,000 plus any premiums and other amounts paid by B with respect to the policy subsequent to the transfer.

(2) *Example 2*. The facts are the same as in *Example 1* in paragraph (g)(1) of this section except that, before A's death, B gratuitously transfers the policy back to A. A's estate receives the proceeds of $100,000 on A's death. Because the transfer from B to A is a gratuitous transfer to the insured, and the preceding transfer from A to B was not a reportable policy sale, the amount of the proceeds A's estate may exclude from gross income under this section is not limited by paragraph (b)(2)(i) of this section.

(3) *Example 3*. The facts are the same as in *Example 1* in paragraph (g)(1) of this section except that, before A's death, B sells the policy back to A for its fair market value. A's estate receives the proceeds of $100,000 on A's death. The transfer from A to B is not a reportable policy sale because the acquirer B has a substantial family relationship with the insured, A. The transfer from B to A also is not a reportable policy sale because the acquirer A has a substantial family relationship with the insured, A. Accordingly, paragraph (b)(1)(ii)(B)(*1*) of this section applies to the transfer to A, and the amount of the proceeds A's estate may exclude from gross income is not limited by paragraph (b) of this section.

(4) *Example 4*. A is the initial policyholder of a $100,000 insurance policy on A's life. A transfers the policy for $6,000, its fair market value, to an individual, C, who does not have a substantial family, business, or financial relationship with A. The transfer from A to C is a reportable policy sale. C receives the proceeds of $100,000 on A's death. The amount of the proceeds C may exclude from C's gross income under this section is limited under paragraph (b)(1)(i) of this section to $6,000 plus any premiums and other amounts paid by C with respect to the policy subsequent to the transfer.

(5) *Example 5*. The facts are the same as in *Example 4* in paragraph (g)(4) of this section, except that before A's death, C transfers the policy to D, a partner of A who co-owns real property with A, for $8,000, the policy's fair market value. D receives the proceeds of $100,000 on A's death. The transfer from C to D is not a reportable policy sale because the acquirer D has a substantial financial relationship with the insured, A. However, because that transfer follows a reportable policy sale (the transfer from A to C), the amount of the proceeds that D may exclude from gross income under this section is limited by paragraph (b)(1)(ii)(B)(*2*) of this section to the sum of—

(i) The higher of the amount C could have excluded had the transfer to D not occurred ($6,000 plus any premiums and other amounts paid by C with respect to the policy subsequent to the transfer to C, as described in *Example 4* in paragraph (g)(4) of this section) or the actual value of the consideration for that transfer paid by D ($8,000); and

(ii) Any premiums and other amounts paid by D with respect to the policy subsequent to the transfer to D.

(6) *Example 6*. The facts are the same as in *Example 4* in paragraph (g)(4) of this section, except that before A's death, C transfers the policy back to A for $8,000, its fair market value. A's estate receives the proceeds of $100,000 on A's death. The transfer from C to A is not a reportable policy sale because the acquirer A has a substantial family relationship with the insured, A. Although the transfer follows a reportable policy sale (the initial transfer from A to C), A's estate may exclude all of the policy proceeds from gross income because paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section applies and, therefore, the amount of the proceeds that A may exclude from gross income is not limited by paragraph (b)(1)(i) of this section or (b)(1)(ii)(B)(*2*) of this section.

(7) *Example 7*. The facts are the same as in *Example 6* in paragraph (g)(6) of this section, except that C transfers the policy back to A for $4,000, rather than its fair market value of $8,000. A's estate receives the proceeds of $100,000 on A's death. Because A did not pay fair market value for the policy, the transfer is bifurcated and treated as a bargain sale under paragraph (b)(2)(iii) of this section. A therefore is treated as having purchased 50% of the policy interest for valuable consideration equal to fair market value and as having received 50% of the policy interest in a gratuitous transfer. The transfer from C to A is not a reportable policy sale because the acquirer, A, has a substantial family relationship with the insured, A, but the transfer from C to A follows a reportable policy sale (the transfer from A to C).

(i) *Treatment of policy interest purchased by A*. A's estate may exclude from income all of the policy proceeds related to the 50% policy interest transferred for valuable consideration ($50,000) because, under paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section, the amount of the proceeds that may be excluded from gross income is not limited by paragraph (b)(1)(i) of this section or (b)(1)(ii)(B)(*2*) of this section.

(ii) *Treatment of policy interest gratuitously transferred to A*. The amount of the policy proceeds related to the 50% policy interest transferred gratuitously that A's estate may exclude from income is limited under paragraph (b)(2)(i) of this section to the sum of the amount C could have excluded with respect to 50% of the policy had the transfer back to A not occurred (that is, 50% of the $6,000 that C paid A for the policy, plus 50% of any premiums and other amounts paid by C with respect to the policy subsequent to the transfer to C), plus 50% of any premiums and other amounts paid by A with respect to the policy subsequent to the transfer to A.

(8) *Example 8*. The facts are the same as in *Example 6* in paragraph (g)(6) of this section, except that, before A's death, A gratuitously transfers 50% of the policy interest to B, A's child, and sells 50% of the policy interest for its fair market value to an individual, E, who does not have a substantial family, business, or financial relationship with A. B and E each receive $50,000 of the proceeds on A's death. Paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section applies to determine the amount of the proceeds that B and E may exclude from gross income because the policy interests transferred to B and E were first transferred for valuable consideration in a reportable policy sale (the transfer by A to C) and then transferred to the insured, A, for fair market value.

(i) *Treatment of policy interest transferred to B*. With respect to the portion of the policy interest transferred to B, because the transfer to B was the only transfer subsequent to the transfer to A and the transfer to B was gratuitous and not a reportable policy sale, under paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section, the amount of the policy proceeds excludable from gross income by B is determined under paragraph (b)(2)(i) of this section, taking into account the application of paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section to A's acquisition of the interest. Under paragraph (b)(2)(i) of this section, the amount of the proceeds B may exclude is limited to the sum of the amount A could have excluded had the transfer to B not occurred, and any premiums and other amounts paid by B with respect to the policy subsequent to the transfer to B. As described in *Example 6* in paragraph (g)(6) of this section, under paragraph (b)(1)(ii)(B)(*3*)(*i*) of this section, the amount of the proceeds that A may exclude from gross income is not limited by paragraph (b)(1)(i) of this section or (b)(1)(ii)(B)(*2*) of this section. Accordingly, the amount of the proceeds that B may exclude from gross income is not limited by paragraph (b) of this section.

(ii) *Treatment of policy interest transferred to E*. With respect to the portion of the policy interest transferred to E, because the transfer to E was not gratuitous and was a reportable policy sale, under paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section, the amount of the policy proceeds excludable from gross income by E is determined in accordance with paragraph (b) of this section. Accordingly, because the transfer to E was for valuable consideration, the amount excludable from gross income by E is limited by paragraph (b)(1)(i) of this section unless an exception in paragraph (b)(1)(ii) of this section applies. Because the transfer from A to E is a reportable policy sale, none of the exceptions in paragraph (b)(1)(ii) of this section apply. Therefore, the amount of the proceeds E may exclude from gross income under this section is limited by paragraph (b)(1)(i) of this section to the sum of the consideration paid by E and the premiums and other amounts paid by E with respect to the policy subsequent to the transfer to E.

(9) *Example 9*. The facts are the same as in *Example 8* in paragraph (g)(8) of this section, except that, before A's death, B transfers B's policy interest to Partnership F, whose partners are A and other family members of A, in exchange for a partnership interest in Partnership F. Partnership F receives $50,000 of the proceeds on A's death. With respect to the policy interest transferred to Partnership F, paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section applies to determine the amount of the proceeds that Partnership F may exclude from gross income for the reasons described in *Example 8* in paragraph (g)(8) of this section.

(i) *Treatment of policy interest transferred to Partnership F*. The transfer to Partnership F was not a reportable policy sale. However, because the transfer to Partnership F was not gratuitous, the amount of the policy proceeds excludable from gross income by Partnership F is determined in accordance with paragraph (b) of this section as if the amount that would have been excludable from gross income by A following the transfer to A, if no subsequent transfer had occurred, was determined under paragraph (b)(1)(ii)(B)(*2*) of this section. Because B's transfer to Partnership F was a transfer for valuable consideration to a partnership in which the insured is a partner that was preceded by a reportable policy sale (the transfer to C), the amount of the proceeds Partnership F may exclude from gross income under this section is limited under paragraph (b)(1)(ii)(B)(*2*) of this section to the higher of the amount that would have been excludable by B if the transfer to Partnership F had not occurred or the actual value of the consideration for the policy paid by Partnership F, plus any premiums and other amounts paid by Partnership F with respect to the policy subsequent to the transfer to Partnership F.

(ii) *Amount that B could have excluded.* Because the transfer from A to B was a gratuitous transfer, the amount of the proceeds B could have excluded from gross income under this section if the transfer to Partnership F had not occurred is limited under paragraph (b)(2)(i) of this section to the sum of the amount A could have excluded had the transfer to B not occurred, and any premiums and other amounts paid by B with respect to the policy subsequent to the transfer to B.

(iii) *Amount that A could have excluded.* As described in paragraph (g)(9)(i) of this section, the amount of the proceeds A could have excluded under this section if the transfer to B had not occurred must be determined under paragraph (b)(1)(ii)(B)(*2*) of this section in accordance with paragraph (b)(1)(ii)(B)(*3*)(*ii*) of this section. Under paragraph (b)(1)(ii)(B)(*2*) of this section, the amount that would have been excludable by A is limited to the higher of the amount that would have been excludable by C if the transfer to A had not occurred ($6,000 plus premiums and other amounts subsequently paid by C) or the actual value of the consideration for the policy paid by A ($8,000), plus any premiums and other amounts paid by A with respect to the policy subsequent to the transfer to A.

(10) *Example 10*. A is the initial policyholder of a $100,000 insurance policy on A's life. A contributes the policy to Corporation X in exchange for stock. Corporation X's basis in the policy is determinable in whole or in part by reference to A's basis in the policy. Corporation X conducts an active trade or business that it wholly owns, and A materially participates in that active trade or business as an employee of Corporation X. Corporation X receives the proceeds of $100,000 on A's death. A's contribution of the policy to Corporation X is not a reportable policy sale because Corporation X has a substantial business relationship with A under paragraph (d)(2)(i) of this section. Although Corporation X's basis in the policy is determinable in whole or in part by reference to A's basis in the policy, paragraph (b)(1)(ii)(A) of this section does not apply because the insured, A, is a shareholder of Corporation X and the other requirements under paragraph (b)(1)(ii)(B) of this section are satisfied. Accordingly, paragraph (b)(1)(ii)(B) of this section applies, and paragraph (b)(1)(ii)(A) of this section is inapplicable. Under paragraph (b)(1)(ii)(B)(*1*) of this section, Corporation X's exclusion is not limited by paragraph (b) of this section.

(11) *Example 11*. The facts are the same as in *Example 10* in paragraph (g)(10) of this section, except that Corporation X transfers its active trade or business and the policy on A's life to Corporation Y in a tax-free reorganization at a time when A is still employed by Corporation X, but is no longer a shareholder of Corporation X. Corporation Y's basis in the policy is determinable in whole or in part by reference to Corporation X's basis in the policy, and Corporation Y carries on the trade or business acquired from Corporation X. Corporation Y receives the proceeds of $100,000 on A's death. The transfer from Corporation X to Corporation Y is not a reportable policy sale because Corporation Y has a substantial business relationship with A under paragraph (d)(2)(ii) of this section. The amount of the proceeds that Corporation Y may exclude from gross income is limited under paragraph (b)(1)(ii)(A) of this section to the sum of the amount that would have been excludable by Corporation X had the transfer to Corporation Y not occurred, plus any premiums and other amounts paid by Corporation Y with respect to the policy subsequent to the transfer. Accordingly, because Corporation X's exclusion is not limited by paragraph (b) of this section, as described in *Example 10* in paragraph (g)(10) of this section, Corporation Y's exclusion is not limited by paragraph (b) of this section.

(12) *Example 12*. A is the initial policyholder of a $100,000 insurance policy on A's life. A contributes the policy to a C corporation, Corporation W, in exchange for stock. After the acquisition, A owns less than 20% of the outstanding stock of Corporation W and owns stock possessing less than 20 % of the total combined voting power of all stock of Corporation W and is therefore not a key person with respect to Corporation W under section 264(e)(3). Corporation W's basis in the policy is determinable in whole or in part by reference to A's basis in the policy. However, no substantial family, business, or financial relationship exists between A and Corporation W, so A's contribution of the policy to Corporation W is a reportable policy sale. Corporation W receives the proceeds of $100,000 on A's death. Under paragraph (b)(1)(i) of this section, the amount of the proceeds Corporation W may exclude from gross income is limited to the actual value of the stock exchanged for the policy, plus any premiums and other amounts paid by Corporation W with respect to the policy subsequent to the transfer. The exceptions in paragraph (b)(1)(ii) of this section do not apply because the transfer to Corporation W is a reportable policy sale.

(13) *Example 13*. Partnership X and Partnership Y are owned by individuals A, B, and C. A holds 40% of the capital and profits interest of Partnership X and 20% of the capital and profits interest of Partnership Y. B holds 35% of the capital and profits interest of Partnership X and 40% of the capital and profits interest of Partnership Y. C holds 25% of the capital and profits interest of Partnership X and 40% of the capital and profits interest of Partnership Y. Partnership X is the initial policyholder of a $100,000 insurance policy on the life of A. Partnership Y purchases the policy from Partnership X. Under paragraph (c)(2)(i) of this section, this transfer is not a reportable policy sale because the ownership interest of each beneficial owner in Partnership X does not vary from that owner's interest in Partnership Y by more than a 20% ownership interest. A's ownership varies by a 20% interest, B's ownership varies by a 5% interest, and C's ownership varies by a 15% interest.

(14) *Example 14*. Partnership X conducts an active trade or business and is the initial policyholder of a $100,000 insurance policy on the life of its full-time employee, A. A materially participates in Partnership X's active trade or business in A's capacity as an employee. Individual B acquires a 10% profits interest in Partnership X in exchange for a cash payment of $1,000,000. Under paragraphs (d)(1) through (3) of this section, B does not have a substantial family, business, or financial relationship with A. Under paragraph (d)(4)(i) of this section, however, B is deemed to have a substantial business relationship with A because, under paragraph (d)(2)(i) of this section, Partnership X (the direct policyholder) has a substantial business relationship with A. Accordingly, although the acquisition of the 10% partnership interest by B is an indirect acquisition of a 10% interest in the insurance policy covering A's life, the acquisition is not a reportable policy sale.

(15) *Example 15*. The facts are the same as in *Example 14* in paragraph (g)(14) of this section, except that A is no longer an employee of Partnership X, and Partnership X has no substantial family, business, or financial relationship with A, when B acquires the profits interest in Partnership X. Also, B acquires only a 5% profits interest in exchange for a cash payment of $500,000. Partnership X does not own an interest in any other life insurance policies, and the gross value of its assets is $10 million. Although neither Partnership X nor B has a substantial family, business, or financial relationship with A at the time

of B's indirect acquisition of an interest in the policy covering A's life, because B's profits interest in Partnership X does not exceed 5%, and because no more than 50% of Partnership X's asset value consists of life insurance contracts, the exception in paragraph (c)(2)(iii)(B) of this section applies, and B's indirect acquisition of an interest in the policy covering A's life is not a reportable policy sale.

(16) *Example 16*. A is the initial policyholder of a $100,000 insurance policy on A's life. A sells the policy for its fair market value. As a result of the sale, Bank X holds legal title to the life insurance contract as the nominee of Partnership B, and Partnership B has the enforceable right to designate the contract beneficiary. Under paragraphs (d)(1) through (4) of this section, neither Bank X nor Partnership B has a substantial family, business, or financial relationship with the insured, A, at the time of the sale. Accordingly, the transfer of legal title to the policy to Bank X is a reportable policy sale under paragraph (c)(1) of this section, unless an exception set forth in paragraph (c)(2) of this section applies. The same is true of the transfer of the economic benefits of the policy to Partnership B. At a later date, Partnership B sells its economic interest in the policy to Partnership C for fair market value. Bank X continues to hold legal title to the life insurance contract, but now holds it as Partnership C's nominee. Partnership C has no substantial family, business, or financial relationship with the insured, A, under paragraphs (d)(1) through (4) of this section at the time of the transfer. Accordingly, Partnership C's acquisition of the economic interest in the policy from Partnership B is a reportable policy sale under paragraph (c)(1) of this section, unless an exception set forth in paragraph (c)(2) of this section applies.

Par. 3. Section 1.101-6 is amended by revising paragraph (b) to read as follows:

§1.101-6 Effective date.

* * * * *

(b) Notwithstanding paragraph (a) of this section, for purposes of determining whether a transfer of an interest in a life insurance contract is a reportable policy sale or a payment of death benefits is a payment of reportable death benefits subject to the reporting requirements of section 6050Y and §§1.6050Y-1 through 1.6050Y-4, §1.101-1(b) through (g) apply to reportable policy sales made after December 31, 2018, and to reportable death benefits paid after December 31, 2018. For any other purpose, including for purposes of determining the amount of the proceeds of life insurance contracts payable by reason of death excluded from gross income under section 101, §1.101-1(b) through (g) apply to amounts paid by reason of the death of the insured under a life insurance contract, or interest therein, transferred after October 31, 2019. However, under section 7805(b)(7), a taxpayer may apply the rules set forth in §1.101-1(b) through (g) of the final regulations, in their entirety, with respect to all amounts paid by reason of the death of the insured under a life insurance contract, or interest therein, transferred after December 31, 2017, and on or before October 31, 2019.

Par. 4. Section 1.6050Y-1 is added to read as follows:

§1.6050Y-1 Information reporting for reportable policy sales, transfers of life insurance contracts to foreign persons, and reportable death benefits.

(a) *Definitions*. The following definitions apply for purposes of this section and §§1.6050Y-2 through 1.6050Y-4:

(1) *Acquirer*. The term *acquirer* means any person that acquires an interest in a life insurance contract (through a direct acquisition or indirect acquisition of the interest) in a reportable policy sale.

(2) *Buyer*. The term *buyer* means, with respect to any interest in a life insurance contract that has been transferred in a reportable policy sale, the person that was the most recent acquirer of that interest in a reportable policy sale as of the date reportable death benefits are paid under the contract.

(3) *Direct acquisition of an interest in a life insurance contract*. The term *direct acquisition of an interest in a life insurance contract* has the meaning given to it in §1.101-1(e)(3)(i).

(4) *Foreign person*. The term *foreign person* means a person that is not a United States person, as defined in section 7701(a)(30).

(5) *Indirect acquisition of an interest in a life insurance contract*. The term *indirect acquisition of an interest in a life insurance contract* has the meaning given to it in §1.101-1(e)(3)(ii).

(6) *Interest in a life insurance contract*. The term *interest in a life insurance contract* has the meaning given to it in §1.101-1(e)(1).

(7) *Investment in the contract*—(i) *Definition of investment in the contract*. With respect to the original policyholder of a life insurance contract, the term *investment in the contract* on any date means that person's investment in the contract under section 72(e)(6) on that date. With respect to any other person, the term *investment in the contract* on any date means the *estimate of investment in the contract* on that date.

(ii) *Definition of estimate of investment in the contract*. The term *estimate of investment in the contract* with respect to any person, other than the original policyholder, means, on any date, the aggregate amount of premiums paid for the contract by that person before that date, less the aggregate amount received under the contract by that person before that date to the extent such information is known to or can reasonably be estimated by the issuer or payor.

(8) *Issuer*—(i) *In general*. Except as provided in paragraph (a)(8)(ii) or (iii) of this section, the term *issuer* generally means, on any date, with respect to any interest in a life insurance contract, any person that bears any part of the risk with respect to the contract on that date and any person responsible on that date for administering the contract, including collecting premiums and paying death benefits. For instance, if a reinsurer reinsures on an indemnity basis all or a portion of the risks that the original issuer (and continuing contract administrator) of the contract might otherwise have incurred with respect to the contract, both the reinsurer and the original issuer of the contract are issuers of the contract for purposes of this paragraph (a)(8)(i). Any designee of an issuer of a contract is also considered an issuer of the contract for purposes of this paragraph (a)(8)(i).

(ii) *6050Y(a) issuer*. For purposes of information reporting under section 6050Y(a) and §1.6050Y-2, the 6050Y(a) issuer is the issuer that is responsible for administering the life insurance contract, including collecting premiums and paying death benefits under the contract, on the date of the reportable policy sale. In the case of the issuance of a life insurance contract to a policyholder in an exchange pursuant to section 1035, the 6050Y(a) issuer is the issuer that issues the new contract.

(iii) *6050Y(b) issuer*. For purposes of information reporting under section 6050Y(b) and §1.6050Y-3, a 6050Y(b) issuer is:

(A) Any person that receives an RPSS with respect to a life insurance contract or interest therein (or, in the case of a designee, receives notice that the issuer for whom it serves as designee received an RPSS), and is or was, on or before the date of receipt of the RPSS, an issuer with respect to the contract; or

(B) Any person that receives notice of a transfer to a foreign person of a life insurance contract, provided that the person is or was, on the date of transfer or on the date of receipt of the notice, an issuer with respect to the contract, and provided that the information is not received from the issuer responsible for administering the contract (or its designee), unless:

(*1*) That person (or, in the case of a designee, the issuer for whom it serves as designee) is not responsible for administering the contract, including collecting premiums and paying death benefits under the contract, on the date the notice of a transfer to a foreign person is received; and

(*2*) That person, or its designee, provides the issuer that is responsible on that date for administering the contract, including collecting premiums and paying death benefits under the contract, with such notice and with any available information necessary to accomplish reporting under section 6050Y(b) and §1.6050Y-3.

(iv) *Designee*. A person is treated as the designee of an issuer for purposes of this paragraph (a)(8) only if so designated in writing, including electronically. The designation must be signed and acknowledged, in writing or electronically, by the person named as designee, or that person's representative, and by the issuer making the designation, or its representative.

(9) *Life insurance contract*. The term *life insurance contract* has the meaning given to it in section 7702(a). A life insurance contract may also be referred to as a life insurance policy.

(10) *Notice of a transfer to a foreign person.* The term *notice of a transfer to a foreign person* means any notice of a transfer of title to, possession of, or legal ownership of a life insurance contract received by a 6050Y(b) issuer that includes foreign indicia, including information provided for nontax purposes such as a change of address notice for purposes of sending statements or for other purposes, and information relating to loans, premiums, or death benefits with respect to the contract, unless the 6050Y(b) issuer knows that no transfer of the contract has occurred or knows that the transferee is a United States person. For this purpose, a 6050Y(b) issuer may rely on a Form W-9, Request for Taxpayer Identification Number and Certification, or a valid substitute form that meets the requirements of §1.1441-1(d)(2) (substituting "6050Y(b) issuer" for "withholding agent"), that indicates the transferee is a United States person. For instance, a change of address notice that changes the address to a foreign address or other updates to the information relating to the payment of premiums that includes foreign banking or other foreign financial institution information is notice of a transfer to a foreign person unless the 6050Y(b) issuer knows that no transfer has occurred or the transferee is a United States person.

(11) *Payor*. The term *payor* means any person making a payment of reportable death benefits.

(12) *Reportable death benefits.* The term *reportable death benefits* means amounts paid by reason of the death of the insured under a life insurance contract that are attributable to an interest in the contract that was transferred in a reportable policy sale.

(13) *Reportable death benefits payment recipient*. The term *reportable death benefits payment recipient* means any person that receives reportable death benefits as a beneficiary under a life insurance contract or as the holder of an interest in a life insurance contract.

(14) *Reportable policy sale*. The term *reportable policy sale* has the meaning given to it in §1.101-1(c).

(15) *Reportable policy sale payment*. The term *reportable policy sale payment* generally means the total amount of cash and the fair market value of any other consideration reducible to a money value transferred, or to be transferred, in a reportable policy sale, including any amount of a reportable policy sale payment recipient's debt assumed by the acquirer in a reportable policy sale. In the case of an indirect acquisition of an interest in a life insurance contract that is a reportable policy sale, the reportable policy sale payment is the total amount of cash and the fair market value of any other consideration reducible to a money value transferred, or to be transferred, for the ownership interest in the entity, including the amount of any debt assumed by the acquirer, that is appropriately allocable to the interest in the life insurance contract held by the entity.

(16) *Reportable policy sale payment recipient*—(i) Except as provided in paragraph (a)(16)(ii) of this section, the term *reportable policy sale payment recipient* means any person that receives a reportable policy sale payment in a reportable policy sale. A broker or other intermediary that retains a portion of the cash or other consideration transferred in a reportable policy sale is also a reportable policy sale payment recipient.

(ii) A person other than the seller is not a reportable policy sale payment recipient with respect to a reportable policy sale if that person receives aggregate payments of less than $600 with respect to that reportable policy sale.

(17) *Reportable policy sale statement*. The term *reportable policy sale statement (RPSS)* means a statement furnished by an acquirer to an issuer under section 6050Y(a)(2) and §1.6050Y-2(d)(2)(i).

(18) *Seller*. The term *seller* means any person that—

(i) Holds an interest in a life insurance contract and transfers that interest, or any part of that interest, to an acquirer in a reportable policy sale; or

(ii) Owns a life insurance contract and transfers title to, possession of, or legal ownership of that contract to a foreign person.

(19) *Transfer of an interest in a life insurance contract*. The term *transfer of an interest in a life insurance contract* has the meaning given to it in §1.101-1(e)(2).

(20) *United States person.* The term *United States person* has the meaning given to it in section 7701(a)(30).

(b) *Applicability date*. This section and §§1.6050Y-2 through 1.6050Y-3 apply to reportable policy sales made after December 31, 2018. This section and §1.6050Y-4 apply to reportable death benefits paid after December 31, 2018. However, for reportable policy sales and payments of reportable death benefits occurring after December 31, 2018, and on or before October 31, 2019, transition relief is provided as follows:

(1) Statements required to be furnished to issuers under section 6050Y(a)(2) and

§1.6050Y-2(d)(2)(i) must be furnished by the later of the applicable deadline set forth in §1.6050Y-2(d)(2)(ii) or December 30, 2019.

(2) Statements required to be furnished to reportable policy sale payment recipients under section 6050Y(a)(2) and §1.6050Y-2(d)(1)(i) must be furnished by the later of the applicable deadline set forth in §1.6050Y-2(d)(1)(ii) or February 28, 2020.

(3) Statements required to be furnished to sellers under section 6050Y(b)(2) and §1.6050Y-3(d)(1) must be furnished by the later of the applicable deadline set forth in §1.6050Y-3(d)(2) or February 28, 2020.

(4) Statements required to be furnished to reportable death benefits payment recipients under section 6050Y(c)(2) and §1.6050Y-4(c)(1) must be furnished by the later of the applicable deadline set forth in §1.6050Y-4(c)(2) or February 28, 2020.

(5) Returns required to be filed under section 6050Y(a)(1) and §1.6050Y-2(a), section 6050Y(b)(1) and §1.6050Y-3(a), and section 6050Y(c)(1) and §1.6050Y-4 must be filed by the later of the applicable deadline set forth in §1.6050Y-2(c), §1.6050Y-3(c), and §1.6050Y-4(b) or February 28, 2020.

Par. 5. Section 1.6050Y-2 is added to read as follows:

§1.6050Y-2 Information reporting by acquirers for reportable policy sale payments.

(a) *Requirement of reporting.* Except as provided in paragraph (f) of this section, every person that is an acquirer in a reportable policy sale during any calendar year must file a separate information return with the Internal Revenue Service (IRS) in the form and manner as required by the IRS for each reportable policy sale payment recipient, including any seller that is a reportable policy sale payment recipient. Each return must include the following information with respect to the seller or other reportable policy sale payment recipient to which the return relates:

(1) The name, address, and taxpayer identification number (TIN) of the acquirer;

(2) The name, address, and TIN of the seller or other reportable policy sale payment recipient to which the return relates;

(3) The date of the reportable policy sale;

(4) The name of the 6050Y(a) issuer of the life insurance contract acquired and the policy number of the life insurance contract;

(5) The aggregate amount of reportable policy sale payments made, or to be made, to the seller or other reportable policy sale payment recipient to which the return relates with respect to the reportable policy sale; and

(6) Any other information that is required by the form or its instructions.

(b) *Unified reporting.* The information reporting requirement of paragraph (a) of this section applies to each acquirer in a series of prearranged transfers of an interest in a life insurance contract, as well as each acquirer in a simultaneous transfer of different interests in a single life insurance contract. In either case, an acquirer's reporting obligation is deemed satisfied if the information required by paragraph (a) of this section with respect to that acquirer is timely reported on behalf of that acquirer in a manner that is consistent with forms, instructions, and other IRS guidance by one or more other acquirers or by a third party information reporting contractor.

(c) *Time and place for filing.* Returns required to be made under paragraph (a) of this section must be filed with the Internal Revenue Service Center designated on the prescribed form or in its instructions on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the reportable policy sale occurred. However, see §1.6050Y-1(b)(5) for transition rules.

(d) *Requirement of and time for furnishing statements*—(1) *Statements to reportable policy sale payment recipients*—(i) *Requirement of furnishing statement.* Every person required to file an information return under paragraph (a) of this section with respect to a reportable policy sale payment recipient must furnish in the form and manner prescribed by the IRS to the reportable policy sale payment recipient whose name is set forth in that return a written statement showing the information required by paragraph (a) of this section with respect to the reportable policy sale payment recipient and the name, address, and phone number of the information contact of the person furnishing the written statement. The contact information of the person furnishing the written statement must provide direct access to a person that can answer questions about the statement. The statement is not required to include information with respect to any other reportable policy sale payment recipient in the reportable policy sale or information about reportable policy sale payments to any other reportable policy sale payment recipient.

(ii) *Time for furnishing statement.* Each statement required by paragraph (d)(1)(i) of this section to be furnished to any reportable policy sale payment recipient must be furnished on or before February 15 of the year following the calendar year in which the reportable policy sale occurred. However, see §1.6050Y-1(b)(2) for transition rules.

(2) *Statements to 6050Y(a) issuers*—(i) *Requirement of furnishing RPSS*—(A) *In general.* Except as provided in paragraph (d)(2)(i)(B) of this section, every person required to file a return under paragraph (a) of this section must furnish in the form and manner prescribed by the IRS to the 6050Y(a) issuer whose name is required to be set forth in the return an RPSS with respect to each reportable policy sale payment recipient that is also a seller. Each RPSS must show the information required by paragraph (a) of this section with respect to the seller named therein, except that the RPSS is not required to set forth the amount of any reportable policy sale payment. Each RPSS must also show the name, address, and phone number of the information contact of the person furnishing the RPSS. This contact information must provide direct access to a person that can answer questions about the RPSS.

(B) *Exception from reporting.* An RPSS is not required to be furnished to the 6050Y(a) issuer by an acquirer acquiring an interest in a life insurance contract in an indirect acquisition.

(ii) *Time for furnishing RPSS.* Except as provided in this paragraph (d)(2)(ii), each RPSS required by paragraph (d)(2)(i) of this section to be furnished to a 6050Y(a) issuer must be furnished by the later of 20 calendar days after the reportable policy sale, or 5 calendar days after the end of the applicable state law rescission period. However, if the later date is after January 15 of the year following the calendar year in which the reportable policy sale occurred, the RPSS must be furnished by January 15 of the year following the calendar year in which the reportable policy sale occurred. However, see §1.6050Y-1(b)(1) for transition rules.

(3) *Unified reporting.* The information reporting requirements of paragraphs (d)(1)(i) and (d)(2)(i) of this section apply to each acquirer in a series of prearranged transfers of an interest in a life insurance contract, as well as each acquirer in a simultaneous transfer of different interests in a single life insurance contract, as described in paragraph (b) of this section. In either case, an acquirer's obligation to furnish statements is deemed satisfied if the information required by paragraphs (d)(1)(i) and (d)(2)(i) of this section with respect to that acquirer is timely reported on behalf of that acquirer consistent with forms, instructions, and other IRS guidance by one or more other acquirers or by a third party information reporting contractor.

(e) *Notice of rescission of a reportable policy sale.* Any person that has filed a return required by section 6050Y(a)(1) and this section with respect to a reportable policy sale must file a corrected return within 15 calendar days of the receipt of notice of the rescission of the reportable policy sale. Any person that has furnished a written statement under section 6050Y(a)(2) and this section with respect to the reportable policy sale must furnish the recipient of that statement with a corrected statement within 15 calendar days of the receipt of notice of the rescission of the reportable policy sale.

(f) *Exceptions to requirement to file*—(1) An acquirer that is a foreign person is not required to file an information return under paragraph (a) of this section with respect to a reportable policy sale unless—

(i) The life insurance contract (or interest therein) transferred in the sale is on the life of an insured who is a United States person at the time of the sale; or

(ii) The sale is subject to the laws of one or more States of the United States that pertain to acquisitions or sales of life insurance contracts (or interests therein).

(2) An acquirer is not required to file an information return under paragraph (a) of this section with respect to a reportable policy sale payment to a reportable policy sale payment recipient other than the seller if the reportable policy sale payment is reported by the acquirer under section 6041 or 6041A.

(3) An acquirer is not required to file an information return under paragraph (a) of this section with respect to the issuance of a life insurance contract in an exchange pursuant to section 1035. However, the acquirer is required to furnish the 6050Y(a) issuer with the statement required under paragraph (d)(2) of this section as if the acquirer were required to file an information return under paragraph (a) of this section.

(g) *Cross-reference to penalty provisions*—(1) *Failure to file correct information return.* For provisions relating to the penalty provided for failure to file timely a correct information return required under section 6050Y(a)(1) and this section, see section 6721 and §301.6721-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

(2) *Failure to furnish correct statement.* For provisions relating to the penalty provided for failure to furnish timely a correct statement to identified persons under section 6050Y(a)(2) and this section, see section 6722 and §301.6722-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

Par. 6. Section 1.6050Y-3 is added to read as follows:

§1.6050Y-3 Information reporting by 6050Y(b) issuers for reportable policy sales and transfers of life insurance contracts to foreign persons.

(a) *Requirement of reporting.* Except as provided in paragraph (f) of this section, each 6050Y(b) issuer that receives an RPSS or any notice of a transfer to a foreign person must file an information return with the Internal Revenue Service (IRS) with respect to each seller in the form and manner prescribed by the IRS. The return must include the following information with respect to the seller:

(1) The name, address, and taxpayer identification number (TIN) of the seller;

(2) The investment in the contract with respect to the seller;

(3) The amount the seller would have received if the seller had surrendered the life insurance contract on the date of the reportable policy sale or the transfer of the contract to a foreign person, or if the date of the transfer to a foreign person is not known to the 6050Y(b) issuer, the date the 6050Y(b) issuer received notice of the transfer; and

(4) Any other information that is required by the form or its instructions.

(b) *Unified reporting.* Each 6050Y(b) issuer subject to the information reporting requirement of paragraph (a) of this section must satisfy that requirement, but a 6050Y(b) issuer's reporting obligation is deemed satisfied if the information required by paragraph (a) of this section with respect to that 6050Y(b) issuer is timely reported on behalf of that 6050Y(b) issuer in a manner that is consistent with forms, instructions, and other IRS guidance by one or more other 6050Y(b) issuers or by a third party information reporting contractor.

(c) *Time and place for filing.* Except as provided in this paragraph (c), returns required to be made under paragraph (a) of this section must be filed with the Internal Revenue Service Center designated on the prescribed form or in its instructions on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the reportable policy sale or the transfer to a foreign person occurred. If the 6050Y(b) issuer does not receive notice of a transfer to a foreign person until after January 31 of the calendar year following the year in which the transfer occurred, returns required to be made under paragraph (a) of this section must be filed by the later of February 28 (March 31 if filed electronically) of the calendar year following the year in which the transfer occurred or thirty days after the date notice is received. However, see §1.6050Y-1(b)(5) for transition rules.

(d) *Requirement of and time for furnishing statements*—(1) *Requirement of furnishing statement.* Every 6050Y(b) issuer filing a return required by paragraph

(a) of this section must furnish to each seller that is a reportable policy sale payment recipient or makes a transfer to a foreign person and whose name is required to be set forth in the return a written statement showing the information required by paragraph (a) of this section with respect to that seller and the name, address, and phone number of the information contact of the person filing the return. This contact information must provide direct access to a person that can answer questions about the statement.

(2) *Time for furnishing statement.* Except as provided in this paragraph (d)(2), each statement required by paragraph (d)(1) of this section to be furnished to any seller must be furnished on or before February 15 of the year following the calendar year in which the reportable policy sale or transfer to a foreign person occurred. If a 6050Y(b) issuer does not receive notice of a transfer to a foreign person until after January 31 of the calendar year following the year in which the transfer occurred, each statement required to be made under paragraph (d) of this section must be furnished by the date thirty days after the date notice is received. However, see §1.6050Y-1(b)(3) for transition rules.

(3) *Unified reporting.* Each 6050Y(b) issuer subject to the information reporting requirement of paragraph (d)(1) of this section must satisfy that requirement, but a 6050Y(b) issuer's reporting obligation is deemed satisfied if the information required by paragraph (d)(1) of this section with respect to that 6050Y(b) issuer is timely reported on behalf of that 6050Y(b) issuer consistent with forms, instructions, and other IRS guidance by one or more other 6050Y(b) issuers or by a third party information reporting contractor.

(e) *Notice of rescission of a reportable policy sale or transfer of an insurance contract to a foreign person.* Any 6050Y(b) issuer that has filed a return required by section 6050Y(b)(1) and this section with respect to a reportable policy sale or transfer of an insurance contract to a foreign person must file a corrected return within 15 calendar days of the receipt of notice of the rescission of the reportable policy sale or transfer of the insurance contract to a foreign person. Any 6050Y(b) issuer that has furnished a written statement under section 6050Y(b)(2) and this section with respect to the reportable policy sale or transfer of the insurance contract to a foreign person must furnish the recipient of that statement with a corrected statement within 15 calendar days of the receipt of notice of the rescission of the reportable policy sale or transfer of the insurance contract to a foreign person.

(f) *Exceptions to requirement to file*. A 6050Y(b) issuer is not required to file an information return under paragraph (a) of this section if paragraph (f)(1), (2), or (3) of this section applies.

(1) Except as provided in this paragraph (f)(1), the 6050Y(b) issuer obtains documentation upon which it may rely to treat a seller of a life insurance contract or interest therein as a foreign beneficial owner in accordance with §1.1441-1(e)(1)(ii), applying in such case the provisions of §1.1441-1 by substituting the term "6050Y(b) issuer" for the term "withholding agent" and without regard to the fact that that these provisions apply only to amounts subject to withholding under chapter 3 of subtitle A of the Internal Revenue Code. A 6050Y(b) issuer may also obtain from a seller that is a partnership or trust, in addition to documentation establishing the entity's foreign status, a written certification from the entity that no beneficial owner of any portion of the proceeds of the sale is a United States person. In such a case, the issuer may rely upon the written certification to treat the partnership or trust as a foreign beneficial owner for purposes of this paragraph (f)(1) provided that the seller does not have actual knowledge that a United States person is the beneficial owner of all or a portion of the proceeds of the sale. See §1.1441-1(c)(6)(ii) for the definition of beneficial owner that applies for purposes of this paragraph (f)(1). Additionally, for certifying its status as a foreign beneficial owner (as applicable) for purposes of this paragraph (f)(1), a seller that is required to report any of the income from the sale as effectively connected with the conduct of a trade or business in the United States under section 864(b) is required to provide to the 6050Y(b) issuer a Form W-8ECI, Certificate of Foreign Person's Claim that Income is Effectively Connected with the Conduct of a Trade or Business in the United States. If a 6050Y(b) issuer obtains a Form W-8ECI from a seller with respect to the sale or has reason to know that income from the sale is effectively connected with the conduct of a trade or business in the United States under section 864(b), the exception to reporting described in this paragraph (f)(1) does not apply.

(2) The 6050Y(b) issuer receives notice of a transfer to a foreign person, but does not receive an RPSS with respect to the transfer, provided that, at the time the notice is received—

(i) The 6050Y(b) issuer is not a United States person;

(ii) The life insurance contract (or interest therein) transferred is not on the life of a United States person; and

(iii) The 6050Y(b) issuer has not classified the seller as a United States person in its books and records.

(3) The RPSS received by the 6050Y(b) issuer is with respect to the 6050Y(b) issuer's issuance of a life insurance contract to a policyholder in an exchange pursuant to section 1035.

(g) *Cross-reference to penalty provisions*—(1) *Failure to file correct information return.* For provisions relating to the penalty provided for failure to file timely a correct information return required under section 6050Y(b)(1) and this section, see section 6721 and §301.6721-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

(2) *Failure to furnish correct statement.* For provisions relating to the penalty provided for failure to furnish timely a correct statement to identified persons under section 6050Y(b)(2) and this section, see section 6722 and §301.6722-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

Par. 7. Section 1.6050Y-4 is added to read as follows:

§1.6050Y-4 Information reporting by payors for reportable death benefits.

(a) *Requirement of reporting.* Except as provided in paragraph (e) of this section, every person that is a payor of reportable death benefits during any calendar year must file a separate information return for such calendar year with the Internal Revenue Service (IRS) for each reportable death benefits payment recipient in the form and manner prescribed by the IRS. The return must include the following information with respect to the reportable death benefits payment recipient to which the return relates:

(1) The name, address, and taxpayer identification number (TIN) of the payor;

(2) The name, address, and TIN of the reportable death benefits payment recipient;

(3) The date of the payment;

(4) The gross amount of reportable death benefits paid to the reportable death benefits payment recipient during the taxable year;

(5) The payor's estimate of investment in the contract with respect to the buyer, limited to the payor's estimate of the buyer's investment in the contract with respect to the interest for which the reportable death benefits payment recipient was paid; and

(6) Any other information that is required by the form or its instructions.

(b) *Time and place for filing.* Returns required to be made under this section must be filed with the Internal Revenue Service Center designated in the instructions for the form on or before February 28 (March 31 if filed electronically) of the year following the calendar year in which the payment of reportable death benefits was made. However, see §1.6050Y-1(b)(5) for transition rules.

(c) *Requirement of and time for furnishing statements*—(1) *Requirement of furnishing statement.* Every person required to file an information return under paragraph (a) of this section must furnish to each reportable death benefits payment recipient whose name is required to be set forth in that return a written statement showing the information required by paragraph (a) of this section with respect to that reportable death benefits payment recipient and the name, address, and phone number of the information contact of the payor. This contact information must provide direct access to a person that can answer questions about the statement.

(2) *Time for furnishing statement.* Each statement required by paragraph (c)(1) of this section to be furnished to any reportable death benefits payment recipient must be furnished on or before January 31 of the year following the calendar year in which the payment of reportable death benefits was made. However, see §1.6050Y-1(b)(4) for transition rules.

(d) *Notice of rescission of a reportable policy sale.* Any person that has filed a return required by section 6050Y(c) and this section with respect to a payment of reportable death benefits must file a corrected return within 15 calendar days of recovering any portion of the reportable death benefits payment from the reportable death benefits payment recipient as a result of the rescission of the reportable policy sale. Any person that has furnished a written statement under section 6050Y(c)(2) and this section with respect to a payment of reportable death benefits must furnish the recipient of that statement with a corrected statement within 15 calendar days of recovering any portion of the reportable death benefits payment from the reportable death benefits payment recipient as a result of the rescission of the reportable policy sale.

(e) *Exceptions to requirement to file.* A payor is not required to file an information return under paragraph (a) of this section with respect to a payment of reportable death benefits if paragraph (e)(1), (2), or (3) of this section applies.

(1) Except as provided in this paragraph (e)(1), the payor obtains documentation in accordance with §1.1441-1(e)(1)(ii) upon which it may rely to treat the reportable death benefits payment recipient as a foreign beneficial owner of the reportable death benefits, applying in such case the provisions of §1.1441-1 by substituting the term "payor" for the term "withholding agent" and without regard to the fact that the provisions apply only to amounts subject to withholding under chapter 3 of subtitle A of the Internal Revenue Code. A payor may also obtain from a partnership or trust that is a reportable death benefits recipient, in addition to documentation establishing the entity's foreign status, a written certification from the entity that no beneficial owner of any portion of the reportable death benefits payment is a United States person. In such a case, a payor may rely upon the written certification to treat the partnership or trust as a foreign beneficial owner for purposes of this paragraph (e)(1) provided that the payor does not have actual knowledge that a United States person is the beneficial owner of all or a portion of the reportable death benefits payment. See §1.1441-1(c)(6)(ii) for the definition of beneficial owner that applies for purposes of this paragraph (e)(1). Other due diligence or reporting requirements may, however, apply to a payor that relies on the exception set forth in this paragraph (e)(1). See §1.1441-5(c) and (e) (determination of payees of foreign partnerships and certain foreign trusts for amounts subject to withholding under §1.1441-2(a)) and §1.1461-1(b) and (c) (amounts subject to reporting for chapter 3 purposes).

(2) The buyer obtained the life insurance contract (or interest therein) under which reportable death benefits are paid in a reportable policy sale to which the exception to reporting described in §1.6050Y-3(f)(2) applies.

(3) The payor never received, and has no knowledge of any issuer having received, an RPSS with respect to the interest in a life insurance contract with respect to which the reportable death benefits are paid.

(f) *Cross-reference to penalty provisions*—(1) *Failure to file correct information return.* For provisions relating to the penalty provided for failure to file timely a correct information return required under section 6050Y(c)(1) and this section, see section 6721 and §301.6721-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

(2) *Failure to furnish correct statement.* For provisions relating to the penalty provided for failure to furnish timely a correct statement to identified persons under section 6050Y(c)(2) and this section, see section 6722 and §301.6722-1 of this chapter. See section 6724(a) and §301.6724-1 of this chapter for the waiver of a penalty if the failure is due to reasonable cause and is not due to willful neglect.

Sunita Lough,
Deputy Commissioner for Services and Enforcement.

Approved: October 15, 2019.

David J. Kautter,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on October 25, 2019, 4:15 p.m., and published in the issue of the Federal Register for October 31, 2019, 84 F.R. 58460)

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26 CFR 1.385-2 [Removed]

TD 9880

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Removal of Section 385 Documentation Regulations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document removes final regulations setting forth minimum documentation requirements that ordinarily must be satisfied in order for certain related-party interests in a corporation to be treated as indebtedness for Federal tax purposes. This document also adopts conforming amendments to other final regulations to reflect the removal of the documentation regulations. The final regulations removed or amended by this document generally affect corporations that issue purported indebtedness to related corporations or partnerships.

DATES: These regulations are effective November 4, 2019**.**

FOR FURTHER INFORMATION CONTACT: Austin Diamond-Jones, (202) 317-5363 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act (44 U.S.C. 3501-3521), approval for the information collection included in these regulations had been requested under control number 1545-2267. Because of the removal of the final documentation regulations, the information burden has been removed and control number 1545-2267 is no longer needed.

Background

I. *Overview*

Section 385(a) of the Internal Revenue Code (Code) authorizes the Secretary to "prescribe such regulations as may be necessary or appropriate to determine whether an interest in a corporation is to be treated for purposes of [the Code] as stock or indebtedness (or as in part stock and in part indebtedness)." Section 385(b) requires such regulations to "set forth factors which are to be taken into account in determining with respect to a particular factual situation whether a debtor-creditor relationship exists or a corporation-shareholder relationship exists." Section 385(b) also enumerates a nonexclusive list of factors potentially to be included in those regulations.

On October 21, 2016, the Department of the Treasury (Treasury Department) and the IRS published final and temporary regulations (T.D. 9790) under section 385 in the **Federal Register** (81 FR 72858). The final and temporary regulations under section 385 (Section 385 Regulations) include rules set forth in §1.385-2, which establish minimum documentation requirements that ordinarily must be satisfied in order for purported debt obligations among related parties to be treated as debt for Federal tax purposes (Documentation Regulations). The Section 385 Regulations also include §§1.385-3, 1.385-3T, and 1.385-4T, which treat as stock certain debt that is issued by a corporation to a controlling shareholder in a distribution or in another related-party transaction that achieves an economically similar result (Distribution Regulations).

The Documentation Regulations, as proposed, would have been applicable with respect to interests issued or deemed issued on or after the date of finalization. However, commenters expressed concern that, if the Documentation Regulations were to be applicable as of that date, taxpayers would lack adequate time to prepare for compliance with the requirements set forth in those regulations. To assist taxpayers in their preparation for the Documentation Regulations, the Treasury Department and the IRS made the regulations applicable with respect to interests issued or deemed issued after January 1, 2018. See §§1.385-1(f), 1.385-2(d)(2)(iii), and 1.385-2(i).

II. *Executive Order 13789*

Executive Order 13789 (E.O. 13789), issued on April 21, 2017, instructed the Secretary to review all significant tax regulations issued on or after January 1, 2016, and to take concrete action to alleviate the burdens of regulations that (i) impose an undue financial burden on U.S. taxpayers; (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the IRS. E.O. 13789 further instructed the Secretary to submit to the President within 60 days a report (First Report) that identifies regulations that meet these criteria. Notice 2017-38 (2017-30 I.R.B. 147 (July 24, 2017)) included the Section 385 Regulations in a list of eight regulations identified by the Secretary in the First Report as meeting at least one of the first two criteria specified in E.O. 13789. In addition, E.O. 13789 instructed the Secretary to submit to the President a second report (Second Report) that recommended specific actions to mitigate the burden imposed by regulations identified in the First Report.

III. *Additional Delay in Application of Documentation Regulations*

As noted in Part I of this Background section, the Treasury Department and the IRS had originally delayed the applicability date of the Documentation Regulations to help taxpayers prepare for compliance with those rules. Taxpayers, however, continued to express concern regarding the timing and potential application of the Documentation Regulations. Based on those continued concerns, and in light of the contemplated additional action regarding the Section 385 Regulations that resulted from E.O. 13789 review, the Treasury Department and the IRS determined that a further delay in the application of the Documentation Regulations would be appropriate. Accordingly, in Notice 2017-36 (2017-33 I.R.B. 208 (August 14, 2017)), the Treasury Department and the IRS announced their intent to amend the Documentation Regulations to delay the applicability of the regulations for 12 months, making the regulations applicable only to interests issued or deemed issued on or after January 1, 2019.

IV. *Proposed Removal of Documentation Regulations*

The Second Report announced that the Treasury Department and the IRS were considering a proposal to revoke the finalized Documentation Regulations. See Executive Order 13789—Second Report to the President on Identifying and Reducing Tax Regulatory Burdens, 82 FR 48013, 48016 (October 16, 2017). On September 24, 2018, the Treasury Department and the IRS published a notice of proposed rulemaking (REG-130244-17) in the **Federal Register** (83 FR 48265) that proposed removing the Documentation Regulations and adopting conforming amendments to other final regulations to reflect the removal of the Documentation Regulations (Proposed Regulations). The preamble to the Proposed Regulations provided that "taxpayers may rely on these proposed regulations, in their entirety, until the date a Treasury decision adopting these regulations as final regulations is published in the Federal Register" (Reliance Provision). Proposed Regulations, 83 FR at 48267.

Summary of Comments

The Treasury Department and the IRS received three written comments regarding the Proposed Regulations. Two of the comments supported removal of the Documentation Regulations, while one comment opposed removal. In connection with the Proposed Regulations, the Treasury Department and the IRS also received a written comment addressing solely the Distribution Regulations.

The single commenter that opposed removal of the Documentation Regulations argued that the Proposed Regulations would hamper the ability of the IRS to counter earnings stripping, and result in significant decreases in Federal revenue. In addition, the commenter asserted that the removal likely would reduce the overall perceived legitimacy of the U.S. tax system, and consequently reduce voluntary compliance. The commenter further argued that removal of the Documentation Regulations would prove unnecessary because of (i) the delayed applicability date provided by Notice 2017-36 and (ii) substantial, taxpayer-favorable modifications included in the finalized Documentation Regulations.

The two commenters that supported removal of the Documentation Regulations contended that the regulations fail to balance appropriately (i) the burdens imposed on taxpayers with (ii) the expected benefits to the Federal government described in the preceding paragraph. Both commenters expressed their appreciation for the Reliance Provision, and emphasized that application of the Documentation Regulations would have imposed onerous compliance burdens and costs on taxpayers. One commenter also asserted that the Reliance Provision appropriately reduced administrative burdens on the IRS.

The Treasury Department and the IRS have considered each of the competing arguments and concerns set forth by the commenters and have determined that the burdens imposed on taxpayers by the Documentation Regulations outweigh the regulations' intended benefits. As a result, this document adopts the Proposed Regulations with no change as final regulations. The Treasury Department and the IRS, however, continue to consider the issues addressed by the Documentation Regulations.

After this further review, the Treasury Department and the IRS may propose a modified version of the Documentation Regulations. In any modified version, the Treasury Department and the IRS would substantially simplify and streamline the proposal to minimize taxpayer burdens, while ensuring the collection of sufficient documentation and other information necessary for tax administration purposes. The Treasury Department and the IRS welcome comments regarding approaches that would most effectively achieve that balance. Any modified version of the Documentation Regulations would be proposed with a prospective effective date to allow sufficient lead-time for taxpayers to design and implement systems to comply with those regulations.

Effective Date

The removal of §1.385-2 and the conforming modifications are effective as of November 4, 2019.

Statement of Availability of IRS Documents

IRS Notices cited in this document are published in the Internal Revenue Bulletin and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at *http://www.irs.gov*.

Special Analyses

I. *Regulatory Planning and Review – Economic Analysis*

Executive Order 13777 directs agencies to alleviate unnecessary regulatory burdens placed on the American people by managing the costs associated with the governmental imposition of private expenditures required to comply with Federal regulations. Executive Orders 13771, 13563, and 12866 direct agencies to prudently manage the cost of planned regulations by assessing costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility.

The final regulations have been designated as subject to review under Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget (OMB) regarding review of tax regulations. OMB has determined that the final regulations are not a significant regulatory action. This final rule is an Executive Order 13771 deregulatory action.

A. *Background*

On October 21, 2016, the Treasury Department and the IRS published final and temporary regulations (T.D. 9790) under section 385 in the **Federal Register** (81 FR 72858). The final and temporary regulations under section 385 include rules set forth in §1.385-2, which establish minimum documentation requirements that ordinarily must be satisfied in order for purported debt obligations among related parties to be treated as debt for Federal tax purposes (that is, the Documentation Regulations).

These final regulations withdraw the Documentation Regulations, and thereby remove the requirements set forth in those regulations on taxpayers with respect to certain transactions related to debt issuance. If applicable, the Documentation Regulations would have prescribed the nature of the documentation necessary to substantiate the Federal income tax treatment of related-party interests as indebtedness, including documentation of factors analogous to those found in third-party loan agreements. In general, to comply with the Documentation Regulations, taxpayers would have needed to provide or otherwise establish the following: (*1*) evidence of an unconditional and binding obligation to make interest and principal payments on certain fixed dates; (*2*) that the holder of the loan had the rights of a creditor, including rights superior to shareholders in the case of dissolution; (*3*) a reasonable expectation of the borrower's ability to repay the loan; and (*4*) evidence of conduct consistent with a debtor-creditor relationship. The Documentation Regulations would have applied to relevant intercompany debt issued by U.S. borrowers beginning in 2019, and would have required that the taxpayer's documentation for a given tax year be prepared by the time the borrower's Federal income tax return is filed.

Since the issuance of the Documentation Regulations, Congress enacted the Tax Cuts and Jobs Act, Public Law 115-97, 131 Stat. 2054 (2017) (TCJA). While the final regulations do not implement any provisions of the TCJA, the final regulations would interact with the TCJA. There are several provisions of the TCJA that reduced the tax advantages of conducting activity as part of a foreign controlled domestic corporation (FCDC) rather than in a domestically controlled company (DCC), and thus may affect the economic efficiency of the Documentation Regulations and, analogously, the removal of those regulations. First, for taxable years beginning after December 31, 2017, the TCJA reduced the statutory corporate tax rate from 35 percent to 21 percent, which lowers the effective tax rate for DCCs more than for FCDCs. Second, the ability of FCDCs to strip earnings out of the United States through the use of deductions for interest expense was significantly reduced by the TCJA through amendments to section 163(j) of the Internal Revenue Code. See section 13301(a) of the TCJA, 131 Stat. 2054, 2117-21. Specifically, the TCJA amendments to section 163(j) (*1*) eliminated the debt-equity ratio safe harbor, (*2*) reduced the maximum net interest deductions' share of adjusted taxable income from 50 percent to 30 percent, (*3*) limited all, rather than just related-party, interest deductions, and (*4*) eliminated the carryforward of excess limitation under pre-TCJA section 163(j). The TCJA's Base Erosion Anti-abuse Tax (BEAT) further reduces the tax advantage to deducting interest expense. See section 14401(a) of the TCJA, 131 Stat. 2054, 2226-32. Thus, the benefits of the Documentation Regulations in reducing foreign acquisitions of U.S. assets and interest stripping were reduced by the TCJA.

B. *Need for the final regulations*

These final regulations implement the fifth deregulatory action identified for further consideration in the Second Report issued pursuant to E.O. 13789. Accordingly, the final regulations are needed to remove the Documentation Regulations.

C. *Overview of the final regulations*

These final regulations remove the Documentation Regulations, which set forth minimum documentation requirements that ordinarily must be satisfied in order for certain related-party interests in a corporation to be treated as indebtedness for Federal tax purposes. In addition, the final regulations adopt conforming amendments to other final regulations to reflect the removal of the Documentation Regulations.

D. *Economic analysis*

1. Baseline

The Treasury Department and the IRS have assessed the benefits and costs of these final regulations compared to a no-action baseline that reflects anticipated Federal income tax-related behavior in the absence of these final regulations.

2. Summary of economic effects

These final regulations provide compliance cost savings for some taxpayers by eliminating the need to document relevant transactions in a prescribed manner. The behavior of taxpayers that nevertheless continue to document such transactions would not be changed to any measurable degree. While the removal of the Documentation Regulations may lead to an increase in investment in the United States, this effect is likely to be small given that a body of other regulations continue to cover the terms of that investment. The final regulations may increase costs of the IRS in administering the Distribution Regulations and potentially lead to more noncompliance by some taxpayers.

An analysis discussing the anticipated economic effects of these regulations was included in the preamble to the Proposed Regulations. See Proposed Regulations, 83 FR at 48267-69. The Treasury Department and the IRS received no substantive comments regarding that analysis in response to the Proposed Regulations. The analysis included herein presents the analysis set forth in those Proposed Regulations.

3. Number of affected taxpayers

The Treasury Department and the IRS project that approximately 6,300 large C corporations are likely to be affected by these regulations. This estimate is based on the number of corporations that have sufficient assets ($100 million) or revenue ($50 million) or are publicly traded such that they would have been required to document the relevant transactions.

4. Monetized estimates of compliance burden effects from Documentation Regulations

The Treasury Department and the IRS estimate that removal of the Documentation Regulations will reduce taxpayer compliance costs by $924 million over the period 2019-2028 (undiscounted nominal total). The net present value of the compliance cost savings is $773 million and $685 million ($2018) using real discount rates of 3 percent and 7 percent, respectively. These amounts are $90.6 million and $97.5 million on an annualized basis, again based on 3 percent and 7 percent real rates, respectively. See below the "Change in Annual Compliance Costs" table.

These estimates include an ongoing reduction in compliance costs and a reduction in the start-up cost equal to four times the annual ongoing compliance cost savings. In addition, the analysis includes a sensitivity analysis in which the compliance costs are estimated for a 90-percent interval around our best estimate. First, the distributional characteristics of critical parameters used to produce the estimate are evaluated. Then, Monte Carlo simulations are used to vary the parameter values. Finally, alternative high and low estimates are computed based on parameter values at either end of the 90-percent range.

Table. Change in Annual Compliance Costs

Estimated change in annual compliance costs (annualized value, $2018 million)	**Fiscal Years 2019 to 2028 (3% real discount rate)**	**Fiscal Years 2019 to 2028 (7% real discount rate)**
Central estimate	-$90.6	-$97.5
High estimate	-$113.3	-$121.9
Low estimate	-$68.0	-$73.1
Technical note: In this rulemaking, the Treasury Department made technical adjustments relative to the Documentation Regulations in calculating the annualized compliance cost estimates. The cost stream in this rulemaking is in 2018 dollars, reflects a two-year delay in effective date (relative to the previous estimates), and applies real discount rates of 3 percent and 7 percent. Technical adjustments account for part of the difference in the estimates between the rulemakings.		

5. Higher tax administrative costs for the IRS

The reduced loan documentation required of large corporations as a result of the removal of the Documentation Regulations will reduce the ability of the IRS to more effectively administer the tax laws by making it more difficult for the IRS to evaluate whether purported loans are properly treated as debt for Federal tax purposes. This will raise the cost of auditing and evaluating the tax returns of companies engaged in these transactions.

6. Other economic effects

a. Reduced tax compliance

As a result of the final regulations, taxpayers will not be required to comply with the Documentation Regulations. Therefore, such taxpayers will not need to satisfy the documentation requirements with respect to relevant transactions formerly addressed by the Documentation Regulations. That lack of documentation likely will slightly reduce voluntary compliance by taxpayers to report accurately the Federal income tax consequences of such transactions. The resulting expected revenue reduction is $407 million over the period 2019 to 2028 (undiscounted nominal total). The annualized value of the revenue reduction is $35.4 million and $34.5 million ($2018) using real discount rates of 3 percent and 7 percent, respectively. The revenue effects were estimated using the methodology described in the preamble to the Section 385 Regulations, although the estimate presented herein covers 2019 to 2028 and reflects factors that changed as a result of the TCJA as well as other technical adjustments.

b. Efficiency and growth effects

The removal of the Documentation Regulations will increase, to some extent, the tax advantage some foreign owners have over some domestic owners of U.S. assets, and consequently may increase the propensity for foreign acquisitions and ownership of U.S. assets that are motivated by tax considerations rather than economics. By increasing the ability to undertake tax-motivated acquisitions or ownership structures, removal of the Documentation Regulations may slightly reduce the incentive for assets to be owned or managed by those most capable of putting the assets to their highest-valued use. Moreover, removal of the Documentation Regulations may put purely domestic U.S. firms on less even tax footing than their foreign-owned competitors operating in the United States.

On the other hand, removal of the Documentation Regulations may slightly reduce the effective tax rate and compliance costs on investment in the United States. While the magnitude of this reduction is small, to the extent that the reduction increases new capital investment in the United States its effects would be efficiency enhancing.

II. *Regulatory Flexibility Act*

As described in more detail in this section, pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), the Treasury Department and the IRS hereby certify that these final regulations will not have a significant economic impact on a substantial number of small entities.

The Documentation Regulations, as finalized, were made applicable with respect to interests issued or deemed issued on or after January 1, 2018. See Background section, part I. In Notice 2017-36, the Treasury Department and the IRS further delayed the applicability of the Documentation Regulations by making the regulations applicable only to interests issued or deemed issued on or after January 1, 2019. See Background section, part III. Because of the Reliance Provision, the Documentation Regulations are not applicable to any interests issued by any taxpayer, unless such taxpayer chooses to apply the regulations despite the Reliance Provision. See Background section, part IV.

The Documentation Regulations apply to large corporate groups (specifically, those that are publicly traded, or have assets exceeding $100 million or annual total revenue exceeding $50 million in its expanded group), thus limiting the scope of small entities affected. The Documentation Regulations apply to financial institutions, which are considered small entities under the Regulatory Flexibility Act if they have less than $550 million in assets. See 13 CFR 121.201. The Treasury Department and the IRS believe that the Documentation Regulations do not affect a substantial number of small entities other than small financial institutions. Even if the Documentation Regulations affected a substantial number of small entities in that sector, the economic impact of this rule would be minimal because the final regulations adopt the Proposed Regulations, which remove the Documentation Regulations and permit taxpayers not to apply such regulations until adoption of these final regulations. Accordingly, this final rule will not have a significant economic impact on a substantial number of small entities.

Pursuant to section 7805(f), the proposed regulations preceding these final regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business and no comments were received.

III. *Unfunded Mandates Reform Act*

Section 202 of the Unfunded Mandates Reform Act of 1995 requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of $100 million in 1995 dollars, updated annually for inflation. In 2019, that threshold is approximately $164 million. This final rule does not include any mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

IV. *Executive Order 13132: Federalism*

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This final rule does not have federalism implications and does not impose substantial, direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Drafting Information

The principal author of the final regulations is Austin Diamond-Jones, Office of the Associate Chief Counsel (Corporate). However, other personnel from the Treasury Department and the IRS participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by removing the sectional authority for §1.385-2 to read, in part, as follows:

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

Par. 2. Section 1.385-1 is amended by:

1. Revising paragraph (a), the last sentence of paragraph (c), the last sentence of paragraph (c)(4)(iv), paragraph (d)(1)(i), the first sentence of paragraph (d)(1)(ii), and paragraphs (d)(1)(iii) and (d)(1)(iv)(A); and
2. Removing and reserving paragraph (d)(2)(i).

The revisions read as follows:

§1.385-1 General provisions.

(a) *Overview of section 385 regulations*. This section and §§1.385-3 through 1.385-4T (collectively, the section 385 regulations) provide rules under section 385 to determine the treatment of an interest in a corporation as stock or indebtedness (or as in part stock and in part indebtedness) in particular factual situations. Paragraph (b) of this section provides the general rule for determining the treatment of an interest based on provisions of the Internal Revenue Code and on common law, including the factors prescribed under common law. Paragraphs (c), (d), and (e) of this section provide definitions and rules of general application for purposes of the section 385 regulations. Section 1.385-3 sets forth additional factors that, when present, control the determination of whether an interest in a corporation that is held by a member of the corporation's expanded group is treated (in whole or in part) as stock or indebtedness.

* * * * *

(c) * * * For additional definitions that apply for purposes of their respective sections, see §§1.385-3(g) and 1.385-4T(e).

* * * * *

(4) * * *

(iv) * * * For purposes of the section 385 regulations, a corporation is a member of an expanded group if it is described in this paragraph (c)(4)(iv) immediately before the relevant time for determining membership (for example, immediately before the issuance of a debt instrument (as defined in §1.385-3(g)(4)) or immediately before a distribution or acquisition that may be subject to §1.385-3(b)(2) or (3)).

* * * * *

(d) * * *

(1) * * *

(i) *In general*. If a debt instrument (as defined in §1.385-3(g)(4)) is deemed to be exchanged under the section 385 regulations, in whole or in part, for stock, the holder is treated for all Federal tax purposes as having realized an amount equal to the holder's adjusted basis in that portion of the debt instrument as of the date of the deemed exchange (and as having basis in the stock deemed to be received equal to that amount), and, except as provided in paragraph (d)(1)(iv)(B) of this section, the issuer is treated for all Federal tax purposes as having retired that portion of the debt instrument for an amount equal to its adjusted issue price as of the date of the deemed exchange. In addition, neither party accounts for any accrued but unpaid qualified stated interest on the debt instrument or any foreign exchange gain or loss with respect to that accrued but unpaid qualified stated interest (if any) as of the deemed exchange. This paragraph (d)(1)(i) does not affect any rules in Title 26 of the United States Code that otherwise apply to the debt instrument prior to the date of the deemed exchange (for example, this paragraph (d)(1)(i) does not affect the issuer's deduction of accrued but unpaid qualified stated interest otherwise deductible prior to the date of the deemed exchange). Moreover, the stock issued in the deemed exchange is not treated as a payment of accrued but unpaid original issue discount or qualified stated interest on the debt instrument for Federal tax purposes.

(ii) * * * Notwithstanding the first sentence of paragraph (d)(1)(i) of this section, the rules of §1.988-2(b)(13) apply to require the holder and the issuer of a debt instrument that is deemed to be exchanged under the section 385 regulations, in whole or in part, for stock to recognize any exchange gain or loss, other than any exchange gain or loss with respect to accrued but unpaid qualified stated interest that is not taken into account under paragraph (d)(1)(i) of this section at the time of the deemed exchange. * * *

(iii) *Section 108(e)(8)*. For purposes of section 108(e)(8), if the issuer of a debt instrument is treated as having retired all or a portion of the debt instrument in exchange for stock under paragraph (d)(1)(i) of this section, the stock is treated as having a fair market value equal to the adjusted issue price of that portion of the debt instrument as of the date of the deemed exchange.

(iv) * * *

(A) A debt instrument that is issued by a disregarded entity is deemed to be exchanged for stock of the regarded owner under §1.385-3T(d)(4);

* * * * *

§1.385-2 [Removed]

Par. 3. Section 1.385-2 is removed.

Par. 4. Section 1.385-3 is amended by revising paragraph (g)(4) to read as follows:

§1.385-3 Transactions in which debt proceeds are distributed or that have a similar effect.

* * * * *

(g) * * *

(4) *Debt instrument*. The term debt instrument means an interest that would, but for the application of this section, be treated as a debt instrument as defined in section 1275(a) and §1.1275-1(d).

* * * * *

Par. 5. Section 1.1275-1 is amended by revising the last sentence of paragraph (d) to read as follows:

§1.1275–1 Definitions.

* * * * *

(d) * * * See §1.385–3 for rules that treat certain instruments that otherwise would be treated as indebtedness as stock for Federal tax purposes.

* * * * *

Sunita Lough,
Deputy Commissioner for Services and Enforcement.

Approved: September 30, 2019.

David J. Kautter,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on October 31, 2019, 4:15 p.m., and published in the issue of the Federal Register for November 4, 2019, 84 F.R. 59297)

Part III

2020 Limitations Adjusted As Provided in Section 415(d), etc.

Notice 2019-59

Section 415 of the Internal Revenue Code (the Code) provides for dollar limitations on benefits and contributions under qualified retirement plans. Section 415(d) requires that the Secretary of the Treasury annually adjust these limits for cost-of-living increases. Other limitations applicable to deferred compensation plans are also affected by these adjustments under § 415. Under § 415(d), the adjustments are to be made under adjustment procedures similar to those used to adjust benefit amounts under § 215(i)(2)(A) of the Social Security Act.

Cost-of-Living Adjusted Limits for 2020

Effective January 1, 2020, the limitation on the annual benefit under a defined benefit plan under § 415(b)(1)(A) is increased from $225,000 to $230,000.

For a participant who separated from service before January 1, 2020, the participant's limitation under a defined benefit plan under § 415(b)(1)(B) is computed by multiplying the participant's compensation limitation, as adjusted through 2019, by 1.0176.

The limitation for defined contribution plans under § 415(c)(1)(A) is increased in 2020 from $56,000 to $57,000.

The Code provides that various other dollar amounts are to be adjusted at the same time and in the same manner as the dollar limitation of § 415(b)(1)(A). After taking into account the applicable rounding rules, the amounts for 2020 are as follows:

The limitation under § 402(g)(1) on the exclusion for elective deferrals described in § 402(g)(3) is increased from $19,000 to $19,500.

The annual compensation limit under §§ 401(a)(17), 404(l), 408(k)(3)(C), and 408(k)(6)(D)(ii) is increased from $280,000 to $285,000.

The dollar limitation under § 416(i)(1)(A)(i) concerning the definition of "key employee" in a top-heavy plan is increased from $180,000 to $185,000.

The dollar amount under § 409(o)(1)(C)(ii) for determining the maximum account balance in an employee stock ownership plan subject to a 5-year distribution period is increased from $1,130,000 to $1,150,000, while the dollar amount used to determine the lengthening of the 5-year distribution period is increased from $225,000 to $230,000.

The limitation used in the definition of "highly compensated employee" under § 414(q)(1)(B) is increased from $125,000 to $130,000.

The dollar limitation under § 414(v)(2)(B)(i) for catch-up contributions to an applicable employer plan other than a plan described in § 401(k)(11) or § 408(p) for individuals aged 50 or over is increased from $6,000 to $6,500. The dollar limitation under § 414(v)(2)(B)(ii) for catch-up contributions to an applicable employer plan described in § 401(k)(11) or § 408(p) for individuals aged 50 or over remains unchanged at $3,000.

The annual compensation limitation under § 401(a)(17) for eligible participants in certain governmental plans that, under the plan as in effect on July 1, 1993, allowed cost-of-living adjustments to the compensation limitation under the plan under § 401(a)(17) to be taken into account, is increased from $415,000 to $425,000.

The compensation amount under § 408(k)(2)(C) regarding simplified employee pensions (SEPs) remains unchanged at $600.

The limitation under § 408(p)(2)(E) regarding SIMPLE retirement accounts is increased from $13,000 to $13,500.

The limitation on deferrals under § 457(e)(15) concerning deferred compensation plans of state and local governments and tax-exempt organizations is increased from $19,000 to $19,500.

The limitation under § 664(g)(7) concerning the qualified gratuitous transfer of qualified employer securities to an employee stock ownership plan remains unchanged at $50,000.

The compensation amount under § 1.61-21(f)(5)(i) of the Income Tax Regulations concerning the definition of "control employee" for fringe benefit valuation purposes is increased from $110,000 to $115,000. The compensation amount under § 1.61-21(f)(5)(iii) is increased from $225,000 to $230,000.

The dollar limitation on premiums paid with respect to a qualifying longevity annuity contract under § 1.401(a)(9)-6, A-17(b)(2)(i) of the Income Tax Regulations is increased from $130,000 to $135,000.[1]

The Code provides that the $1,000,000,000 threshold used to determine whether a multiemployer plan is a systemically important plan under § 432(e)(9)(H)(v)(III)(aa) is adjusted using the cost-of-living adjustment provided under § 432(e)(9)(H)(v)(III)(bb). After taking the applicable rounding rule into account, the threshold used to determine whether a multiemployer plan is a systemically important plan under § 432(e)(9)(H)(v)(III)(aa) is increased from $1,097,000,000 to $1,135,000,000.

The Code also provides that several retirement-related amounts are to be adjusted using the cost-of-living adjustment under § 1(f)(3). After taking the applicable rounding rules into account, the amounts for 2020 are as follows:

The adjusted gross income limitation under § 25B(b)(1)(A) for determining the retirement savings contributions credit for married taxpayers

[1] Notice 2017-64, 2017-45 I.R.B. 486, raised this limit from $125,000 to $130,000 although § 1.401(a)(9)6, A-17(d)(2) provides for increases of the $125,000 limitation only in multiples of $10,000. Notice 2018-83, 2018-47 I.R.B. 774, indicated that this limit would remain at $130,000 until it would be adjusted to $135,000 pursuant to § 1.401(a)(9)-6, A-17(d)(2), and would be adjusted only in increments of $10,000 after that adjustment. Accordingly, future adjustments to this limit (which has been raised to $135,000 for 2020) will be made in increments of $10,000.

filing a joint return is increased from $38,500 to $39,000; the limitation under § 25B(b)(1)(B) is increased from $41,500 to $42,500; and the limitation under §§ 25B(b)(1)(C) and 25B(b)(1)(D) is increased from $64,000 to $65,000.

The adjusted gross income limitation under § 25B(b)(1)(A) for determining the retirement savings contributions credit for taxpayers filing as head of household is increased from $28,875 to $29,250; the limitation under § 25B(b)(1)(B) is increased from $31,125 to $31,875; and the limitation under §§ 25B(b)(1)(C) and 25B(b)(1)(D) is increased from $48,000 to $48,750.

The adjusted gross income limitation under § 25B(b)(1)(A) for determining the retirement savings contributions credit for all other taxpayers is increased from $19,250 to $19,500; the limitation under § 25B(b)(1)(B) is increased from $20,750 to $21,250; and the limitation under §§ 25B(b)(1)(C) and 25B(b)(1)(D) is increased from $32,000 to $32,500.

The deductible amount under § 219(b)(5)(A) for an individual making qualified retirement contributions remains unchanged at $6,000.

The applicable dollar amount under § 219(g)(3)(B)(i) for determining the deductible amount of an IRA contribution for taxpayers who are active participants filing a joint return or as a qualifying widow(er) is increased from $103,000 to $104,000. The applicable dollar amount under § 219(g)(3)(B)(ii) for all other taxpayers who are active participants (other than married taxpayers filing separate returns) is increased from $64,000 to $65,000. If an individual or the individual's spouse is an active participant, the applicable dollar amount under § 219(g)(3)(B)(iii) for a married individual filing a separate return is not subject to an annual cost-of-living adjustment and remains $0. The applicable dollar amount under § 219(g)(7)(A) for a taxpayer who is not an active participant but whose spouse is an active participant is increased from $193,000 to $196,000.

Accordingly, under § 219(g)(2)(A), the deduction for taxpayers making contributions to a traditional IRA is phased out for single individuals and heads of household who are active participants in a qualified plan (or another retirement plan specified in § 219(g)(5)) and have adjusted gross incomes (as defined in § 219(g)(3)(A)) between $65,000 and $75,000, increased from between $64,000 and $74,000. For married couples filing jointly, if the spouse who makes the IRA contribution is an active participant, the income phase-out range is between $104,000 and $124,000, increased from between $103,000 and $123,000. For an IRA contributor who is not an active participant and is married to someone who is an active participant, the deduction is phased out if the couple's income is between $196,000 and $206,000, increased from between $193,000 and $203,000. For a married individual filing a separate return who is an active participant, the phase-out range is not subject to an annual cost-of-living adjustment and remains $0 to $10,000.

The adjusted gross income limitation under § 408A(c)(3)(B)(ii)(I) for determining the maximum Roth IRA contribution for married taxpayers filing a joint return or for taxpayers filing as a qualifying widow(er) is increased from $193,000 to $196,000. The adjusted gross income limitation under § 408A(c)(3)(B)(ii)(II) for all other taxpayers (other than married taxpayers filing separate returns) is increased from $122,000 to $124,000. The applicable dollar amount under § 408A(c)(3)(B)(ii)(III) for a married individual filing a separate return is not subject to an annual cost-of-living adjustment and remains $0.

Accordingly, under § 408A(c)(3)(A), the adjusted gross income phase-out range for taxpayers making contributions to a Roth IRA is $196,000 to $206,000 for married couples filing jointly, increased from $193,000 to $203,000. For singles and heads of household, the income phase-out range is $124,000 to $139,000, increased from $122,000 to $137,000. For a married individual filing a separate return, the phase-out range is not subject to an annual cost-of-living adjustment and remains $0 to $10,000.

Drafting Information

The principal author of this notice is Tom Morgan of the Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the IRS participated in the development of this guidance. For further information regarding this notice, contact Mr. Morgan at 202-317-6700 or John Heil at 443-853-5519 (not toll-free numbers).

26 CFR 601.602: Tax forms and instructions.
(Also Part I, §§ 1, 23, 24, 25A, 32, 36B, 42, 45R, 55, 59, 62, 63, 125, 132(f),135, 137, 146, 147, 148, 152, 179, 199A, 213, 220, 221, 448, 461, 512, 513, 642, 831, 877, 877A, 911, 1274A, 2010, 2032A, 2503, 2523, 4161, 4261, 6033, 6039F, 6323, 6334, 6601, 6651, 6652, 6695, 6698, 6699, 6721, 6722, 7345, 7430, 7702B, 9831; 1.148-5.)

Rev. Proc. 2019-44

Table of Contents

SECTION 1. PURPOSE

This revenue procedure sets forth inflation-adjusted items for 2020 for various provisions of the Internal Revenue Code of 1986 (Code) as amended as of November 18, 2019. To the extent amendments to the Code are enacted for 2020 after November 18, 2019, taxpayers should consult additional guidance to determine whether these adjustments remain applicable for 2020.

SECTION 2. CHANGES

.01 Section 3201 of the Taxpayer First Act of 2019, Pub. L. 116-25, increased the amount of the additional tax under § 6651(a) for failure to file a tax return within 60 days of the due date of such return (determined with regard to any extensions of time for filing). For returns required to be filed after December 31, 2019, the amount of the addition to tax shall not be less than the lesser of $330 (increased from $205) or 100 percent of the amount required to be shown as tax on such returns. Accordingly, the $330 is adjusted for inflation in accordance with § 6651.

SECTION 3. 2020 ADJUSTED ITEMS

.01 *Tax Rate Tables*. For taxable years beginning in 2020, the tax rate tables under § 1 are as follows:

TABLE 1 - Section 1(j)(2)(A) - Married Individuals Filing Joint Returns and Surviving Spouses

If Taxable Income Is:	*The Tax Is*:
Not over $19,750	10% of the taxable income
Over $19,750 but not over $80,250	$1,975 plus 12% of the excess over $19,750
Over $80,250 but not over $171,050	$9,235 plus 22% of the excess over $80,250
Over $171,050 but not over $326,600	$29,211 plus 24% of the excess over $171,050
Over $326,600 but not over $414,700	$66,543 plus 32% of the excess over $326,600
Over $414,700 but not over $622,050	$94,735 plus 35% of the excess over $414,700
Over $622,050	$167,307.50 plus 37% of the excess over $622,050

TABLE 2 - Section 1(j)(2)(B) – Heads of Households

If Taxable Income Is:	*The Tax Is*:
Not over $14,100	10% of the taxable income
Over $14,100 but not over $53,700	$1,410 plus 12% of the excess over $14,100
Over $53,700 but not over $85,500	$6,162 plus 22% of the excess over $53,700
Over $85,500 but not over $163,300	$13,158 plus 24% of the excess over $85,500
Over $163,300 but not over $207,350	$31,830 plus 32% of the excess over $163,300
Over $207,350 but not over $518,400	$45,926 plus 35% of the excess over $207,350
Over $518,400	$154,793.50 plus 37% of the excess over $518,400

TABLE 3 - Section 1(j)(2)(C) – Unmarried Individuals (other than Surviving Spouses and Heads of Households)

If Taxable Income Is:	*The Tax Is*:
Not over $9,875	10% of the taxable income
Over $9,875 but not over $40,125	$987.50 plus 12% of the excess over $9,875
Over $40,125 but not over $85,525	$4,617.50 plus 22% of the excess over $40,125
Over $85,525 but not over $163,300	$14,605.50 plus 24% of the excess over $85,525
Over $163,300 but not over $207,350	$33,271.50 plus 32% of the excess over $163,300
Over $207,350 but not over $518,400	$47,367.50 plus 35% of the excess over $207,350
Over $518,400	$156,235 plus 37% of the excess over $518,400

TABLE 4 - Section 1(j)(2)(D) – Married Individuals Filing Separate Returns

If Taxable Income Is:	*The Tax Is*:
Not over $9,875	10% of the taxable income
Over $9,875 but not over $40,125	$987.50 plus 12% of the excess over $9,875
Over $40,125 but not over $85,525	$4,617.50 plus 22% of the excess over $40,125
Over $85,525 but not over $163,300	$14,605.50 plus 24% of the excess over $85,525
Over $163,300 but not over $207,350	$33,271.50 plus 32% of the excess over $163,300
Over $207,350 but not over $311,025	$47,367.50 plus 35% of the excess over $207,350
Over $311,025	$83,653.75 plus 37% of the excess over $311,025

TABLE 5 - Section 1(j)(2)(E) – Estates and Trusts

If Taxable Income Is:	*The Tax Is*:
Not over $2,600	10% of the taxable income
Over $2,600 but not over $9,450	$260 plus 24% of the excess over $2,600
Over $9,450 but not over $12,950	$1,904 plus 35% of the excess over $9,450
Over $12,950	$3,129 plus 37% of the excess over $12,950

.02 *Unearned Income of Minor Children (the "Kiddie Tax")*. For taxable years beginning in 2020, the amount in § 1(g)(4)(A)(ii)(I), which is used to reduce the net unearned income reported on the child's return that is subject to the "kiddie tax," is $1,100. This $1,100 amount is the same as the amount provided in § 63(c)(5)(A), as adjusted for inflation. The same $1,100 amount is used for purposes of § 1(g)(7) (that is, to determine whether a parent may elect to include a child's gross income in the parent's gross income and to calculate the "kiddie tax"). For example, one of the requirements for the parental election is that a child's gross income is more than the amount referenced in § 1(g)(4)(A)(ii)(I) but less than 10 times that amount; thus, a child's gross income for 2020 must be more than $1,100 but less than $11,000.

.03 *Maximum Capital Gains Rate*. For taxable years beginning in 2020, the Maximum Zero Rate Amount under § 1(h)(1)(B)(i) is $80,000 in the case of a joint return or surviving spouse ($40,000 in the case of a married individual filing a separate return), $53,600 in the case of an individual who is a head of household (§ 2(b)), $40,000 in the case of any other individual (other than an estate or trust), and $2,650 in the case of an estate or trust. The Maximum 15-percent Rate Amount under § 1(h)(1)(C)(ii)(l) is $496,600 in the case of a joint return or surviving spouse ($248,300 in the case of a married individual filing a separate return), $469,050 in the case of an individual who is the head of a household (§ 2(b)), $441,450 in the case of any other individual (other than an estate or trust), and $13,150 in the case of an estate or trust.

.04 *Adoption Credit*. For taxable years beginning in 2020, under § 23(a)(3) the credit allowed for an adoption of a child with special needs is $14,300. For taxable years beginning in 2020, under § 23(b)(1) the maximum credit allowed for other adoptions is the amount of qualified adoption expenses up to $14,300. The available adoption credit begins to phase out under § 23(b)(2)(A) for taxpayers with modified adjusted gross income in excess of $214,520 and is completely phased out for taxpayers with modified adjusted gross income of $254,520 or more. (See section 3.20 for the adjusted items relating to adoption assistance programs.)

.05 *Child Tax Credit*. For taxable years beginning in 2020, the value used in § 24(d)(1)(A) to determine the amount of credit under § 24 that may be refundable is $1,400.

.06 *Lifetime Learning Credit*. For taxable years beginning in 2020, a taxpayer's modified adjusted gross income in excess of $59,000 ($118,000 for a joint return) is used to determine the reduction under § 25A(d)(2) in the amount of the Lifetime Learning Credit otherwise allowable under § 25A(a)(2).

.07 *Earned Income Credit*.

(1) *In general*. For taxable years beginning in 2020, the following amounts are used to determine the earned income credit under § 32(b). The "earned income amount" is the amount of earned income at or above which the maximum amount of the earned income credit is allowed. The "threshold phaseout amount" is the amount of adjusted gross income (or, if greater, earned income) above which the maximum amount of the credit begins to phase out. The "completed phaseout amount" is the amount of adjusted gross income (or, if greater, earned income) at or above which no credit is allowed. The threshold phaseout amounts and the completed phaseout amounts shown in the table below for married taxpayers filing a joint return include the increase provided in § 32(b)(2)(B), as adjusted for inflation for taxable years beginning in 2020.

	Number of Qualifying Children			
Item	*One*	*Two*	*Three or More*	*None*
Earned Income Amount	$10,540	$14,800	$14,800	$7,030
Maximum Amount of Credit	$3,584	$5,920	$6,660	$538
Threshold Phaseout Amount (Single, Surviving Spouse, or Head of Household)	$19,330	$19,330	$19,330	$8,790
Completed Phaseout Amount (Single, Surviving Spouse, or Head of Household)	$41,756	$47,440	$50,954	$15,820
Threshold Phaseout Amount (Married Filing Jointly)	$25,220	$25,220	$25,220	$14,680
Completed Phaseout Amount (Married Filing Jointly)	$47,646	$53,330	$56,844	$21,710

The instructions for the Form 1040 series provide tables showing the amount of the earned income credit for each type of taxpayer.

(2) *Excessive Investment Income*. For taxable years beginning in 2020, the earned income tax credit is not allowed under § 32(i) if the aggregate amount of certain investment income exceeds $3,650.

.08 *Refundable Credit for Coverage Under a Qualified Health Plan*. For taxable years beginning in 2020, the limitation on tax imposed under § 36B(f)(2)(B) for excess advance credit payments is determined using the following table:

If the household income (expressed as a percent of poverty line) is:	The limitation amount for unmarried individuals (other than surviving spouses and heads of *household) is:*	The limitation amount for all other taxpayers is:
Less than 200%	$325	$650
At least 200% but less than 300%	$800	$1,600
At least 300% but less than 400%	$1,350	$2,700

.09 *Rehabilitation Expenditures Treated as Separate New Building*. For calendar year 2020, the per low-income unit qualified basis amount under § 42(e)(3)(A)(ii)(II) is $7,100.

.10 *Low-Income Housing Credit*. For calendar year 2020, the amount used under § 42(h)(3)(C)(ii) to calculate the State housing credit ceiling for the low-income housing credit is the greater of (1) $2.8125 multiplied by the State population, or (2) $3,217,500.

.11 *Employee Health Insurance Expense of Small Employers*. For taxable years beginning in 2020, the dollar amount in effect under § 45R(d)(3)(B) is $27,600. This amount is used under § 45R(c) for limiting the small employer health insurance credit and under § 45R(d)(1)(B) for determining who is an eligible small employer for purposes of the credit.

.12 *Exemption Amounts for Alternative Minimum Tax*. For taxable years beginning in 2020, the exemption amounts under § 55(d)(1) are:

Joint Returns or Surviving Spouses	$113,400
Unmarried Individuals (other than Surviving Spouses)	$72,900
Married Individuals Filing Separate Returns	$56,700
Estates and Trusts	$25,400

For taxable years beginning in 2020, under § 55(b)(1), the excess taxable income above which the 28 percent tax rate applies is:

Married Individuals Filing Separate Returns	$98,950
Joint Returns, Unmarried Individuals (other than surviving spouses), and Estates and Trusts	$197,900

For taxable years beginning in 2020, the amounts used under § 55(d)(2) to determine the phaseout of the exemption amounts are:

Joint Returns or Surviving Spouses	$1,036,800
Unmarried Individuals (other than Surviving Spouses)	$518,400
Married Individuals Filing Separate Returns	$518,400
Estates and Trusts	$84,800

.13 *Alternative Minimum Tax Exemption for a Child Subject to the "Kiddie Tax."* For taxable years beginning in 2020, for a child to whom the § 1(g) "kiddie tax" applies, the exemption amount under §§ 55(d) and 59(j) for purposes of the alternative minimum tax under § 55 may not exceed the sum of (1) the child's earned income for the taxable year, plus (2) $7,900.

.14 *Certain Expenses of Elementary and Secondary School Teachers*. For taxable years beginning in 2020, under § 62(a)(2)(D) the amount of the deduction allowed under § 162 that consists of expenses paid or incurred by an eligible educator in connection with books, supplies (other than nonathletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services) and other equipment, and supplementary materials used by the eligible educator in the classroom is $250.

.15 *Transportation Mainline Pipeline Construction Industry Optional Expense Substantiation Rules for Payments to Employees Under Accountable Plans*. For calendar year 2020, an eligible employer may pay certain welders and heavy equipment mechanics an amount up to $18 per hour for rig-related expenses that are deemed substantiated under an accountable plan if paid in accordance with Rev. Proc. 2002-41, 2002-1 C.B. 1098. If the employer provides fuel or otherwise reimburses fuel expenses, an amount up to $11 per hour is deemed substantiated if paid under Rev. Proc. 2002-41.

.16 *Standard Deduction*.

(1) *In general*. For taxable years beginning in 2020, the standard deduction amounts under § 63(c)(2) are as follows:

Filing Status	*Standard Deduction*
Married Individuals Filing Joint Returns and Surviving Spouses (§ 1(j)(2)(A))	$24,800
Heads of Households (§ 1(j)(2)(B))	$18,650
Unmarried Individuals (other than Surviving Spouses and Heads of Households) (§ 1(j)(2)(C))	$12,400
Married Individuals Filing Separate Returns (§ 1(j)(2)(D))	$12,400

(2) *Dependent*. For taxable years beginning in 2020, the standard deduction amount under § 63(c)(5) for an individual who may be claimed as a dependent by another taxpayer cannot exceed the greater of (1) $1,100, or (2) the sum of $350 and the individual's earned income.

(3) *Aged or blind*. For taxable years beginning in 2020, the additional standard deduction amount under § 63(f) for the aged or the blind is $1,300. The additional standard deduction amount is increased to $1,650 if the individual is also unmarried and not a surviving spouse.

.17 *Cafeteria Plans*. For taxable years beginning in 2020, the dollar limitation under § 125(i) on voluntary employee salary reductions for contributions to health flexible spending arrangements is $2,750.

.18 *Qualified Transportation Fringe Benefit*. For taxable years beginning in 2020, the monthly limitation under § 132(f)(2)(A) regarding the aggregate fringe benefit exclusion amount for transportation in a commuter highway vehicle and any transit pass is $270. The monthly limitation under § 132(f)(2)(B) regarding the fringe benefit exclusion amount for qualified parking is $270.

.19 *Income from United States Savings Bonds for Taxpayers Who Pay Qualified Higher Education Expenses*. For taxable years beginning in 2020, the exclusion under § 135, regarding income from United States savings bonds for taxpayers who pay qualified higher education expenses, begins to phase out for modified adjusted gross income above $123,550 for joint returns and $82,350 for all other returns. The exclusion is completely phased out for modified adjusted gross income of $153,550 or more for joint returns and $97,350 or more for all other returns.

.20 *Adoption Assistance Programs*. For taxable years beginning in 2020, under § 137(a)(2), the amount that can be excluded from an employee's gross income for the adoption of a child with special needs is $14,300. For taxable years beginning in 2020, under § 137(b)(1) the maximum amount that can be excluded from an employee's gross income for the amounts paid or expenses incurred by an employer for qualified adoption expenses furnished pursuant to an adoption assistance program for other adoptions by the employee is $14,300. The amount excludable from an employee's gross income begins to phase out under § 137(b)(2)(A) for taxpayers with modified adjusted gross income in excess of $214,520 and is completely phased out for taxpayers with modified adjusted gross income of $254,520 or more. (See section 3.04 of this revenue procedure for the adjusted items relating to the adoption credit.)

.21 *Private Activity Bonds Volume Cap*. For calendar year 2020, the amounts used under § 146(d) to calculate the State ceiling for the volume cap for private activity bonds is the greater of (1) $105 multiplied by the State population, or (2) $321,775,000.

.22 *Loan Limits on Agricultural Bonds*. For calendar year 2020, the loan limit amount on agricultural bonds under § 147(c)(2)(A) for first-time farmers is $552,500.

.23 *General Arbitrage Rebate Rules*. For bond years ending in 2020, the amount of the computation credit determined under § 1.148-3(d)(4) of the Income Tax Regulations is $1,760.

.24 *Safe Harbor Rules for Broker Commissions on Guaranteed Investment Contracts or Investments Purchased for a Yield Restricted Defeasance Escrow*. For calendar year 2020, under § 1.148-5(e)(2)(iii)(B)(1), a broker's commission or similar fee for the acquisition of a guaranteed investment contract or investments purchased for a yield restricted defeasance escrow is reasonable if (1) the amount of the fee that the issuer treats as a qualified administrative cost does not exceed the lesser of (A) $41,000, and (B) 0.2 percent of the computational base (as defined in § 1.148-5(e)(2)(iii)(B)(*2*)) or, if more, $4,000; and (2) for any issue, the issuer does not treat more than $117,000 in brokers' commissions or similar fees as qualified administrative costs for all guaranteed investment contracts and investments for yield restricted defeasance escrows purchased with gross proceeds of the issue.

.25 *Gross Income Limitation for a Qualifying Relative*. For taxable years beginning in 2020, the exemption amount referenced in § 152(d)(1)(B) is $4,300.

.26 *Election to Expense Certain Depreciable Assets*. For taxable years beginning in 2020, under § 179(b)(1), the aggregate cost of any § 179 property that a taxpayer elects to treat as an expense cannot exceed $1,040,000 and under § 179(b)(5)(A), the cost of any sport utility vehicle that may be taken into account under § 179 cannot exceed $25,900. Under § 179(b)(2), the $1,040,000 limitation is reduced (but not below zero) by the amount the cost of § 179 property placed in service during the 2020 taxable year exceeds $2,590,000.

.27 *Qualified Business Income*. For taxable years beginning in 2020, the threshold amount under § 199A(e)(2) is $326,600 for married filing joint returns, $163,300 for married filing separate returns, and $163,300 for all other returns.

.28 *Eligible Long-Term Care Premiums*. For taxable years beginning in 2020, the limitations under § 213(d)(10), regarding eligible long-term care premiums includible in the term "medical care," are as follows:

Attained Age Before the Close of the Taxable Year	*Limitation on Premiums*
40 or less	$430
More than 40 but not more than 50	$810
More than 50 but not more than 60	$1,630
More than 60 but not more than 70	$4,350
More than 70	$5,430

.29 *Medical Savings Accounts*.

(1) *Self-only coverage*. For taxable years beginning in 2020, the term "high deductible health plan" as defined in § 220(c)(2)(A) means, for self-only coverage, a health plan that has an annual deductible that is not less than $2,350 and not more than $3,550, and under which the annual out-of-pocket expenses required to be paid (other than for premiums) for covered benefits do not exceed $4,750.

(2) *Family coverage*. For taxable years beginning in 2020, the term "high deductible health plan" means, for family coverage, a health plan that has an annual deductible that is not less than $4,750 and not more than $7,100, and under which the annual out-of-pocket expenses required to be paid (other than for premiums) for covered benefits do not exceed $8,650.

.30 *Interest on Education Loans*. For taxable years beginning in 2020, the $2,500 maximum deduction for interest paid on qualified education loans under § 221 begins to phase out under § 221(b)(2)(B) for taxpayers with modified adjusted gross income in excess of $70,000 ($140,000 for joint returns), and is completely phased out for taxpayers with modified adjusted gross income of $85,000 or more ($170,000 or more for joint returns).

.31 *Limitation on Use of Cash Method of Accounting*. For taxable years beginning in 2020, a corporation or partnership meets the gross receipts test of § 448(c) for any taxable year if the average annual gross receipts of such entity for the 3-taxable-year period ending with the taxable year which precedes such taxable year does not exceed $26,000,000.

.32 *Threshold for Excess Business Loss*. For taxable years beginning in 2020, in determining a taxpayer's excess business loss, the amount under § 461(l)(3)(A)(ii)(II) is $259,000 ($518,000 for joint returns).

.33 *Treatment of Dues Paid to Agricultural or Horticultural Organizations*. For taxable years beginning in 2020, the limitation under § 512(d)(1), regarding the exemption of annual dues required to be paid by a member to an agricultural or horticultural organization, is $171.

.34 *Insubstantial Benefit Limitations for Contributions Associated with Charitable Fund-Raising Campaigns*.

(1) *Low cost article*. For taxable years beginning in 2020, for purposes of defining the term "unrelated trade or business" for certain exempt organizations under § 513(h)(2), "low cost articles" are articles costing $11.20 or less.

(2) *Other insubstantial benefits*. For taxable years beginning in 2020, under § 170, the $5, $25, and $50 guidelines in section 3 of Rev. Proc. 90-12, 1990-1 C.B. 471 (as amplified by Rev. Proc. 92-49, 1992-1 C.B. 987, and modified by Rev. Proc. 92-102, 1992-2 C.B. 579), for the value of insubstantial benefits that may be received by a donor in return for a contribution, without causing the contribution to fail to be fully deductible, are $11.20, $56 and $112, respectively.

.35 *Special Rules for Credits and Deductions*. For taxable years beginning in 2020, the amount of the deduction under § 642(b)(2)(C)(i) is $4,300.

.36 *Tax on Insurance Companies Other than Life Insurance Companies.* For taxable years beginning in 2020, under § 831(b)(2)(A)(i) the amount of the limit on net written premiums or direct written premiums (whichever is greater) is $2,350,000 to elect the alternative tax for certain small companies under § 831(b)(1) to be taxed only on taxable investment income.

.37 *Expatriation to Avoid Tax*. For calendar year 2020, under § 877A(g)(1)(A), unless an exception under § 877A(g)(1)(B) applies, an individual is a covered expatriate if the individual's "average annual net income tax" under § 877(a)(2)(A) for the five taxable years ending before the expatriation date is more than $171,000.

.38 *Tax Responsibilities of Expatriation*. For taxable years beginning in 2020, the amount that would be includible in the gross income of a covered expatriate by reason of § 877A(a)(1) is reduced (but not below zero) by $737,000.

.39 *Foreign Earned Income Exclusion*. For taxable years beginning in 2020, the foreign earned income exclusion amount under § 911(b)(2)(D)(i) is $107,600.

.40 *Debt Instruments Arising Out of Sales or Exchanges*. For calendar year 2020, a qualified debt instrument under § 1274A(b) has stated principal that does not exceed $6,039,100, and a cash method debt instrument under § 1274A(c)(2) has stated principal that does not exceed $4,313,600.

.41 *Unified Credit Against Estate Tax*. For an estate of any decedent dying in calendar year 2020, the basic exclusion amount is $11,580,000 for determining the amount of the unified credit against estate tax under § 2010.

.42 *Valuation of Qualified Real Property in Decedent's Gross Estate*. For an estate of a decedent dying in calendar year 2020, if the executor elects to use the special use valuation method under § 2032A for qualified real property, the aggregate decrease in the value of qualified real property resulting from electing to use § 2032A for purposes of the estate tax cannot exceed $1,180,000.

.43 *Annual Exclusion for Gifts*.

(1) For calendar year 2020, the first $15,000 of gifts to any person (other than gifts of future interests in property) are not included in the total amount of taxable gifts under § 2503 made during that year.

(2) For calendar year 2020, the first $157,000 of gifts to a spouse who is not a citizen of the United States (other than gifts of future interests in property) are not included in the total amount of taxable gifts under §§ 2503 and 2523(i)(2) made during that year.

.44 *Tax on Arrow Shafts*. For calendar year 2020, the tax imposed under § 4161(b)(2)(A) on the first sale by the manufacturer, producer, or importer of any shaft of a type used in the manufacture of certain arrows is $0.52 per shaft.

.45 *Passenger Air Transportation Excise Tax*. For calendar year 2020, the tax under § 4261(b)(1) on the amount paid for each domestic segment of taxable air transportation is $4.30. For calendar year 2020, the tax under § 4261(c)(1) on any amount paid (whether within or without the United States) for any international air transportation, if the transportation begins or ends in the United States, generally is $18.90. Under § 4261(c)(3), however, a lower amount applies under § 4261(c)(1) to a domestic segment beginning or ending in Alaska or Hawaii, and the tax applies only to departures. For calendar year 2020, the rate is $9.50.

.46 *Reporting Exception for Certain Exempt Organizations with Nondeductible Lobbying Expenditures*. For taxable years beginning in 2020, the annual per person, family, or entity dues limitation to qualify for the reporting exception under § 6033(e)(3) (and section 5.05 of Rev. Proc. 98-19, 1998-1 C.B. 547), regarding certain exempt organizations with nondeductible lobbying expenditures, is $119 or less.

.47 *Notice of Large Gifts Received from Foreign Persons*. For taxable years beginning in 2020, § 6039F authorizes the Treasury Department and the Internal Revenue Service to require recipients of gifts from certain foreign persons to report these gifts if the aggregate value of gifts received in the taxable year exceeds $16,649.

.48 *Persons Against Whom a Federal Tax Lien Is Not Valid*. For calendar year 2020, a federal tax lien is not valid against (1) certain purchasers under § 6323(b)(4) who purchased personal property in a casual sale for less than $1,620, or (2) a mechanic's lien or under § 6323(b)(7) who repaired or improved certain residential property if the contract price with the owner is not more than $8,100.

.49 *Property Exempt from Levy*. For calendar year 2020, the value of property exempt from levy under § 6334(a)(2) (fuel, provisions, furniture, and other household personal effects, as well as arms for personal use, livestock, and poultry) cannot exceed $9,690. The value of property exempt from levy under § 6334(a)(3) (books and tools necessary for the trade, business, or profession of the taxpayer) cannot exceed $4,850.

.50 *Exempt Amount of Wages, Salary, or Other Income*. For taxable years beginning in 2020, the dollar amount used to calculate the amount determined under § 6334(d)(4)(B) is $4,300.

.51 *Interest on a Certain Portion of the Estate Tax Payable in Installments*. For an estate of a decedent dying in calendar year 2020, the dollar amount used to determine the "2-percent portion" (for purposes of calculating interest under § 6601(j)) of the estate tax extended as provided in § 6166 is $1,570,000.

.52 *Failure to File Tax Return*. In the case of any return required to be filed in 2021, the amount of the addition to tax under § 6651(a) for failure to file a tax return within 60 days of the due date of such return (determined with regard to any extensions of time for filing) shall not be less than the lesser of $330 or 100 percent of the amount required to be shown as tax on such returns.

.53 *Failure to File Certain Information Returns, Registration Statements, etc*. For returns required to be filed in 2021, the penalty amounts under § 6652(c) are:

(1) for failure to file a return required under § 6033(a)(1) (relating to returns by exempt organization) or § 6012(a)(6) (relating to returns by political organizations):

Scenario	Daily Penalty	Maximum Penalty
Organization (§ 6652(c)(1)(A))	$20	Lessor of $10,500 or 5% of gross receipts of the organization for the year.
Organization with gross receipts exceeding $1,084,000 (§ 6652(c)(1)(A))	$105	$54,000
Managers (§ 6652(c)(1)(B))	$10	$5,000
Public inspection of annual returns and reports (§ 6652(c)(1)(C))	$20	$10,500
Public inspection of applications for exemption and notice of status (§ 6652(c)(1)(D))	$20	No Limits

(2) for failure to file a return required under § 6034 (relating to returns by certain trust) or § 6043(b) (relating to terminations, etc., of exempt organizations):

Scenario	Daily Penalty	Maximum Penalty
Organization or trust (§ 6652(c)(2)(A))	$10	$5,000
Managers (§ 6652(c)(2)(B))	$10	$5,000
Split-Interest Trust (§ 6652(c)(2)(C)(ii))	$20	$10,500
Any trust with gross income exceeding $271,000 (§ 6652(c)(2)(C)(ii))	$105	$54,000

(3) for failure to file a disclosure required under § 6033(a)(2):

Scenario	Daily Penalty	Maximum Penalty
Tax–exempt entity (§ 6652(c)(3)(A))	$105	$54,000
Failure to comply with written demand (§ 6652(c)(3)(B)(ii))	$105	$10,500

.54 *Other Assessable Penalties With Respect to the Preparation of Tax Returns for Other Persons*. In the case of any failure relating to a return or claim for refund filed in 2021, the penalty amounts under § 6695 are:

Scenario	Per Return or Claim for Refund	Maximum Penalty
Failure to furnish copy to taxpayer (§ 6695(a))	$50	$27,000
Failure to sign return (§ 6695(b))	$50	$27,000
Failure to furnish identifying number (§ 6695(c))	$50	$27,000
Failure to retain copy or list (§ 6695(d))	$50	$27,000
Failure to file correct information returns (§ 6695(e))	$50 per return and item in return	$27,000
Negotiation of check (§ 6695(f))	$540 per check	No limit
Failure to be diligent in determining eligibility for head of household filing status, child tax credit, American opportunity tax credit, and earned income credit (§ 6695(g))	$540 per failure	No limit

.55 *Failure to File Partnership Return*. In the case of any return required to be filed in 2021, the dollar amount used to determine the amount of the penalty under § 6698(b)(1) is $210.

.56 *Failure to File S Corporation Return*. In the case of any return required to be filed in 2021, the dollar amount used to determine the amount of the penalty under § 6699(b)(1) is $210.

.57 *Failure to File Correct Information Returns*. In the case of any failure relating to a return required to be filed in 2021, the penalty amounts under § 6721 are:

(1) for persons with average annual gross receipts for the most recent three taxable years of more than $5,000,000, for failure to file correct information returns:

Scenario	Penalty Per Return	Calendar Year Maximum
General Rule (§ 6721(a)(1))	$280	$3,392,000
Corrected on or before 30 days after required filing date (§ 6721(b)(1))	$50	$565,000
Corrected after 30th day but on or before August 1 (§ 6721(b)(2))	$110	$1,696,000

(2) for persons with average annual gross receipts for the most recent three taxable years of $5,000,000 or less, for failure to file correct information returns:

Scenario	Penalty Per Return	Calendar Year Maximum
General Rule (§ 6721(d)(1)(A))	$280	$1,130,500
Corrected on or before 30 days after required filing date (§ 6721(d)(1)(B))	$50	$197,500
Corrected after 30th day but on or before August 1 (§ 6721(d)(1)(C))	$110	$565,000

(3) for failure to file correct information returns due to intentional disregard of the filing requirement (or the correct information reporting requirement):

Scenario	Penalty Per Return	Calendar Year Maximum
Return other than a return required to be filed under §§ 6045(a), 6041A(b), 6050H, 6050I, 6050J, 6050K, or 6050L (§ 6721(e)(2)(A))	Greater of (i) $560, or (ii) 10% of aggregate amount of items required to be reported correctly	No limit
Return required to be filed under §§ 6045(a), 6050K, or 6050L (§ 6721(e)(2)(B))	Greater of (i) $560, or (ii) 5% of aggregate amount of items required to be reported correctly	No limit
Return required to be filed under § 6050I(a) (§ 6721(e)(2)(C))	Greater of (i) $28,260, or (ii) amount of cash received up to $113,000	No limit
Return required to be filed under § 6050V (§ 6721(e)(2)(D))	Greater of (i) $560, or (ii) 10% of the value of the benefit of any contract with respect to which information is required to be included on the return	No limit

.58 *Failure to Furnish Correct Payee Statements*. In the case of any failure relating to a statement required to be furnished in 2021, the penalty amounts under § 6722 are:

(1) for persons with average annual gross receipts for the most recent three taxable years of more than $5,000,000, for failure to file correct information returns:

Scenario	Penalty Per Return	Calendar Year Maximum
General Rule (§ 6722(a)(1))	$280	$3,392,000
Corrected on or before 30 days after required filing date (§ 6722(b)(1))	$50	$565,000
Corrected after 30th day but on or before August 1 (§ 6722(b)(2))	$110	$1,696,000

(2) for persons with average annual gross receipts for the most recent 3 taxable years of $5,000,000 or less, for failure to file correct information returns:

Scenario	Penalty Per Return	Calendar Year Maximum
General Rule (§ 6722(d)(1)(A))	$280	$1,130,500
Corrected on or before 30 days after required filing date (§ 6722(d)(1)(B))	$50	$197,500
Corrected after 30th day but on or before August 1 (§ 6722(d)(1)(C))	$110	$565,000

(3) for failure to file correct payee statements due to intentional disregard of the requirement to furnish a payee statement (or the correct information reporting requirement):

Scenario	Penalty Per Return	Calendar Year Maximum
Statement other than a statement required under §§ 6045(b), 6041A(e) (in respect of a return required under § 6041A(b)), 6050H(d), 6050J(e), 6050K(b), or 6050L(c) (§ 6722(e)(2)(A))	Greater of (i) $560, or (ii) 10% of aggregate amount of items required to be reported correctly	No limit
Payee statement required under §§ 6045(b), 6050K(b), or 6050L(c) (§ 6722(e)(2)(B))	Greater of (i) $560, or (ii) 5% of aggregate amount of items required to be reported correctly	No limit

.59 *Revocation or Denial of Passport in Case of Certain Tax Delinquencies*. For calendar year 2020, the amount of a serious delinquent tax debt under § 7345 is $53,000.

.60 *Attorney Fee Awards*. For fees incurred in calendar year 2020, the attorney fee award limitation under § 7430(c)(1)(B)(iii) is $210 per hour.

.61 *Periodic Payments Received Under Qualified Long-Term Care Insurance Contracts or Under Certain Life Insurance Contracts*. For calendar year 2020, the stated dollar amount of the per diem limitation under § 7702B(d)(4), regarding periodic payments received under a qualified long-term care insurance contract or periodic payments received under a life insurance contract that are treated as paid by reason of the death of a chronically ill individual, is $380.

.62 *Qualified Small Employer Health Reimbursement Arrangement*. For taxable years beginning in 2020, to qualify as a qualified small employer health reimbursement arrangement under § 9831(d), the arrangement must provide that the total amount of payments and reimbursements for any year cannot exceed $5,250 ($10,600 for family coverage).

SECTION 4. EFFECTIVE DATE

.01 *General Rule*. Except as provided in section 4.02, this revenue procedure applies to taxable years beginning in 2020.

.02 *Calendar Year Rule*. This revenue procedure applies to transactions or events occurring in calendar year 2020 for purposes of sections 3.09 (rehabilitation expenditures treated as separate new building), 3.10 (low-income housing credit), 3.15 (transportation mainline pipeline construction industry optional expense substantiation rules for payments to employees under accountable plans), 3.21 (private activity bonds volume cap), 3.22 (loan limits on agricultural bonds), 3.23 (general arbitrage rebate rules), 3.24 (safe harbor rules for broker commissions on guaranteed investment contracts or investments purchased for a yield restricted defeasance escrow), 3.37 (expatriation to avoid taxes), 3.40 (debt instruments arising out of sales or exchanges), 3.41 (unified credit against estate tax), 3.42 (valuation of qualified real property in decedent's gross estate), 3.43 (annual exclusion for gifts), 3.44 (tax on arrow shafts), 3.45 (passenger air transportation excise tax), 3.48 (persons against whom a federal tax lien is not valid), 3.49 (property exempt from levy), 3.51 (interest on a certain portion of the estate tax payable in installments), 3.59 (revocation or denial of passport in case of certain tax delinquencies), 3.60 (attorney fee awards), and 3.61 (periodic payments received under qualified long-term care insurance contracts or under certain life insurance contracts).

SECTION 5. DRAFTING INFORMATION

The principal author of this revenue procedure is William Ruane of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue procedure, contact Mr. Ruane at (202) 317-4718 (not a toll-free number).

Part IV

Advance Notice of Proposed Rulemaking

REG-123112-19

The Treatment of Certain Interests in Corporations as Stock or Indebtedness

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: This document announces that the Department of the Treasury (Treasury Department) and the IRS intend to issue proposed regulations regarding the treatment of certain interests in corporations as stock or indebtedness and requests comments from the public regarding the contemplated rules. This document also announces that, following the expiration of the 2016 Temporary Regulations (described in the Background section of this advance notice of proposed rulemaking), a taxpayer may rely on the 2016 Proposed Regulations (also described in the Background) until further notice is given in the **Federal Register**, provided that the taxpayer consistently applies the rules in the 2016 Proposed Regulations in their entirety.

DATES: Written or electronic comments must be received by February 3, 2020.

ADDRESSES: Submit electronic submissions via the Federal eRulemaking Portal at *https://www.regulations.gov* (indicate IRS and REG-123112-19) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Treasury Department and the IRS will publish for public availability any comment received to its public docket, whether submitted electronically or in hard copy. Send hard copy submissions to: CC:PA:LPD:PR (REG-123112-19), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

FOR FURTHER INFORMATION CONTACT: Concerning the proposals, Azeka J. Abramoff at (202) 317-6938; concerning submissions of comments, Regina Johnson at (202) 317-6901 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

I. *Overview*

Section 385 authorizes the Secretary of the Treasury or his delegate (Secretary) to prescribe rules to determine whether an interest in a corporation is treated as stock or indebtedness (or as in part stock and in part indebtedness). On October 21, 2016, the Treasury Department and the IRS published T.D. 9790 in the **Federal Register** (81 FR 72858), which included final regulations under section 385 and temporary regulations under section 385 (Temporary Regulations). On the same date, the Treasury Department and the IRS also published a notice of proposed rulemaking (REG-130314-16) in the **Federal Register** (81 FR 72751) (2016 Proposed Regulations) by cross-reference to the Temporary Regulations, which include §§1.385-3T and 1.385-4T. Technical corrections to the final regulations and the Temporary Regulations were published in the **Federal Register** (82 FR 8169) on January 24, 2017.

The final regulations under section 385, the Temporary Regulations, and the 2016 Proposed Regulations address the classification of certain related-party debt as debt or equity for Federal tax purposes. Treasury Decision 9790 included rules set forth in §1.385-2, which establish minimum documentation requirements that ordinarily must be satisfied in order for debt obligations among related parties to be treated as debt for Federal tax purposes (Documentation Regulations). Treasury Decision 9790 also included §§1.385-3, 1.385-3T, and 1.385-4T, which treat as stock certain debt that is issued by a corporation to a controlling shareholder in a distribution or in another related-party transaction that achieves an economically similar result (the Distribution Regulations). The Distribution Regulations are applicable for taxable years ending on or after January 19, 2017.

The Temporary Regulations set forth rules regarding the treatment under the Distribution Regulations of certain qualified short-term debt instruments, transactions involving controlled partnerships, and transactions involving consolidated groups. The Temporary Regulations apply to taxable years ending on or after January 19, 2017. The Temporary Regulations expired on October 13, 2019. See section 7805(e); §1.385-3T(l); §1.385-4T(h).

The 2016 Proposed Regulations cross-referencing the Temporary Regulations are proposed to apply to taxable years ending on or after January 19, 2017; in contrast to the Temporary Regulations, the 2016 Proposed Regulations do not expire.

II. *Executive Order 13789*

Executive Order 13789 (E.O. 13789), issued on April 21, 2017, instructed the Secretary to review all significant tax regulations issued on or after January 1, 2016, and to take concrete action to alleviate the burdens of regulations that (i) impose an undue financial burden on U.S. taxpayers; (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the IRS. E.O. 13789 further instructed the Secretary to submit to the President within 60 days a report (First Report) that identifies regulations that meet these criteria. Notice 2017-38, 2017-30 I.R.B. 147, which was published on July 24, 2017, included the final section 385 regulations in a list of eight regulations identified by the Secretary in the First Report as meeting at least one of the first two criteria specified in E.O. 13789.

E.O. 13789 further instructed the Secretary to submit to the President a report (Second Report) that recommended specific actions to mitigate the burden imposed by regulations identified in the First Report. On October 16, 2017, the Secretary published in the **Federal Register** the Second Report (82 FR 48013), which stated that (i) the Treasury Department and the IRS were considering a proposal to revoke the Documentation Regulations as issued and (ii) the Treasury Department will reassess the distribution regulations in light of impending tax reform and the Treasury Department and the IRS may then propose more streamlined and targeted regulations. On September 24, 2018, the Treasury Department and the IRS issued proposed regulations that, if finalized, would remove the Documentation Regulations from the Code of Federal Regulations. See 83 FR 48265 (September 24, 2018). The Treasury Department and the IRS are publishing in the Rules section of this issue of the **Federal Register** final regulations that remove the Documentation Regulations.

Some taxpayers submitted comments in response to E.O. 13789 and the September 2018 proposed regulations recommending that the Treasury Department and the IRS revoke the Distribution Regulations in addition to the Documentation Regulations, while another comment recommended that the Treasury Department and the IRS issue more streamlined and targeted Distribution Regulations. This advance notice of proposed rulemaking announces that the Treasury Department and the IRS intend to propose more streamlined and targeted Distribution Regulations.

III. *The Distribution Regulations*

Under the Distribution Regulations' general rule, the issuance of a debt instrument by a member of an expanded group to another member of the same expanded group in a distribution, or an economically similar transaction, may result in the treatment of the debt instrument as stock. See §1.385-3(b)(2). The Distribution Regulations include a funding rule that treats as stock a debt instrument that is issued as part of a series of transactions that achieves a result similar to a distribution of a debt instrument. See §1.385-3(b)(3)(i). Specifically, §1.385-3(b) treats as stock a debt instrument that was issued in exchange for property, including cash, to fund a distribution to an expanded group member or another transaction that achieves an economically similar result. Id. Furthermore, the Distribution Regulations include a per se rule, which treats a debt instrument as funding a distribution to an expanded group member or other transaction with a similar economic effect if it was issued in exchange for property during the period beginning 36 months before and ending 36 months after the issuer of the debt instrument made the distribution or undertook a transaction with a similar economic effect. See §1.385-3(b)(3)(iii). The Distribution Regulations also include several exceptions limiting their scope. See, e.g., §1.385-3(c).

The Distribution Regulations address debt instruments that do not finance any new investment in the operations of the borrower and therefore have the potential to create significant Federal tax benefits, including interest deductions that erode the U.S. tax base, without having meaningful non-tax significance. The Treasury Department and the IRS are cognizant that a complete withdrawal of the Distribution Regulations could restore incentives for multinational corporations to generate additional interest deductions without new investment. Accordingly, the Treasury Department and the IRS have determined that the Distribution Regulations continue to be necessary at this time.

Explanation of Contemplated Regulations

Pursuant to E.O. 13789, the Treasury Department and the IRS intend to issue proposed regulations modifying the Distribution Regulations. To make the Distribution Regulations more streamlined and targeted, the Treasury Department and the IRS intend to issue proposed regulations substantially modifying the funding rule, including by withdrawing the per se rule. The Treasury Department and the IRS intend that the proposed regulations would not treat a debt instrument as funding a distribution or economically similar transaction solely because of their temporal proximity; rather, the proposed regulations would apply the funding rule to a debt instrument only if its issuance has a sufficient factual connection to a distribution to a member of the taxpayer's expanded group or an economically similar transaction (for example, when the funding transaction and distribution or economically similar transaction are pursuant to an integrated plan). Thus, under the proposed regulations, a debt instrument issued without such a connection to a distribution or similar transaction would not be treated as stock. As a result, the proposed distribution regulations would be more streamlined and targeted while continuing to deter tax-motivated uneconomic activity. As part of the intended revisions of the funding rule, the Treasury Department and the IRS also are considering substantial revisions to, or removal of, certain exceptions in the regulations, consistent with the revised standard. The proposed distribution regulations would not alter materially the definition of a covered member (defined in §1.385-1(c)(2) as a member of an expanded group that is a domestic corporation).

Proposed Applicability Date

The Treasury Department and the IRS intend to provide that the proposed regulations would apply to taxable years beginning on or after the date of publication of the Treasury decision adopting those rules as final regulations in the **Federal Register**.

Reliance on the 2016 Proposed Regulations

For periods after October 13, 2019 (the expiration date of the Temporary Regulations), a taxpayer may rely on the 2016 Proposed Regulations until further notice is given, provided that the taxpayer consistently applies the rules in the 2016 Proposed Regulations in their entirety.

Request for Comments

The Treasury Department and the IRS request comments on all aspects of the rules described in part III of this advance notice of proposed rulemaking. In particular, the Treasury Department and the IRS request comments on the appropriate standard for determining the existence of a connection between a debt instrument and a distribution or economically similar transaction under the funding rule. For example, the funding rule could apply solely in cases in which a debt instrument is issued as part of an overall plan to fund the distribution or economically similar transaction. The Treasury Department and the IRS also request comments on whether the proposed regulations should include particular factors that indicate when the funding rule applies and factors that indicate when the funding rule does not apply. The Treasury Department and the IRS also request comments on what additional guidance, if any, should be issued (or which provisions should be eliminated from the final regulations) to reduce the compliance burdens associated with the Distribution Regulations. The Treasury Department and the IRS also request comments on how the Distribution Regulations may affect small businesses. All comments will be available at http://www.regulations.gov or upon request.

Effect on Other Documents

Notice 2019-58, 2019-44 I.R.B. 1022 (October 28, 2019), which addresses the status of the 2016 Proposed Regulations after October 13, 2019, is obsoleted.

Statement of Availability

IRS Notices and other guidance cited in this document are published in the Internal Revenue Bulletin and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at *https://www.irs.gov*.

Drafting Information

The principal author of this advance notice of proposed rulemaking is Azeka J. Abramoff of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in its development.

Sunita Lough,
Deputy Commissioner for Services and Enforcement.

(Filed by the Office of the Federal Register on October 31, 2019, 4:15 p.m., and published in the issue of the Federal Register for November 11, 2019, 84 F.R. 59318)

Definition of Terms

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

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

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

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

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

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

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

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

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

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

Abbreviations

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

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

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[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2018–27 through 2018–52 is in Internal Revenue Bulletin 2018–52, dated December 27, 2018.

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Internal Revenue Service
Washington, DC 20224

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INTERNAL REVENUE BULLETIN

The Introduction at the beginning of this issue describes the purpose and content of this publication. The weekly Internal Revenue Bulletins are available at *www.irs.gov/irb/*.

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