INTERNAL REVENUE
BULLETIN

IRS

Bulletin No. 2020–53
December 28, 2020

HIGHLIGHTS OF THIS ISSUE

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

ADMINISTRATIVE

REV. PROC. 2020-55, page 1811.

General Rules and Specifications for Substitute Forms and Schedules

This procedure provides guidelines and general requirements for the development, printing, and approval of the 2020 substitute tax forms. This procedure will be reproduced as the next revision of Publication 1167. Rev. Proc. 2019-35 is superseded.

ADMINISTRATIVE, INCOME TAX

NOTICE 2020-88, page 1795.

Round 3 of Section 48A Phase III Program under the Qualifying Advanced Coal Project Program. This notice updates and amplifies the procedures for the allocation of credits under the qualifying advanced coal project program of § 48A of the Internal Revenue Code by announcing the immediate beginning of the 2020-2021 reallocation round ("Round 3") of the § 48A Phase III program.

REV. PROC. 2020-54, page 1806.

This revenue procedure will update Rev. Proc. 2019-42, 2019-49 I.R.B. 1298, and identifies circumstances under which the disclosure on a taxpayer's income tax return with respect to an item or position is adequate for the purpose of reducing the understatement of income tax under section 6662(d) of the Internal Revenue Code (relating to the substantial understatement aspect of the accuracy-related penalty), and for the purpose of avoiding the tax return preparer penalty under section 6694(a) (relating to understatements due to unreasonable positions) with respect to income tax returns.

This revenue procedure will apply to any income tax return filed on 2020 tax forms for a taxable year beginning in 2020, and to any income tax return filed in 2021 on 2020 tax forms for short taxable years beginning in 2021.

EMPLOYEE PLANS

NOTICE 2020-86, page 1786.

This notice provides guidance with respect to sections 102 and 103 of the Setting Every Community Up for Retirement Enhancement Act of 2019.

NOTICE 2020-87, page 1792.

This notice sets forth updates on the corporate bond monthly yield curve, the corresponding spot segment rates for December 2020 used under § 417(e)(3)(D), the 24-month average segment rates applicable for December 2020, and the 30-year Treasury rates, as reflected by the application of § 430(h)(2)(C)(iv).

INCOME TAX

Notice 2020-78, page 1785.

The notice provides transition relief related to the work opportunity credit by giving employers additional time to submit a certification request to a Designated Local Agency for the targeted groups described in section 51(d)(5) and (7) of the Internal Revenue Code.

Finding Lists begin on page ii.

T.D. 9921, page 1767.

These final regulations provide guidance on the sourcing of income from certain sales of personal property, including inventory, under section 863 of the Internal Revenue Code ("Code"), which was amended by the Tax Cuts and Jobs Act, Pub. L. No. 155-97 (2017) and also under section 865 of the Code. The final regulations also modify certain rules for determining whether foreign source income is effectively connected with the conduct of a trade or business within the United States under section 864 of the Code. The final regulations replace previously issued proposed regulations and provide guidance on determining the source of income from sales of inventory produced within the United States and sold without the United States or vice versa and new rules for determining the source of income from sales of personal property by nonresidents that are attributable to an office or other fixed place of business that the nonresident maintains in the United States. Finally, the final regulations provide rules, pursuant to section 1502 of the Code, for the determination of source of income from sales of personal property in a consolidated group.

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 1.863-0, 1.863-0A, 1.863-1, 1.863-2, 1.863-3, 1.863-8, 1.864-5, 1.864-6, 1.865-3, 1.937-2, 1.937-3, 1.1502-13

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Source of Income from Certain Sales of Personal Property

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations modifying the rules for determining the source of income from sales of inventory produced within the United States and sold without the United States or vice versa. These final regulations also contain new rules for determining the source of income from sales of personal property (including inventory) by nonresidents that are attributable to an office or other fixed place of business that the nonresident maintains in the United States. Finally, these final regulations modify certain rules for determining whether foreign source income is effectively connected with the conduct of a trade or business within the United States.

DATES: *Effective Date*: These final regulations are effective on December 11, 2020.

Applicability Dates: For dates of applicability, see §§1.863-1(f), 1.863-2(c), 1.863-3(g), 1.863-8(h), 1.864-5(e), 1.864-6(c)(4), and 1.865-3(g).

FOR FURTHER INFORMATION CONTACT: Brad McCormack at (202) 317-6911 (not a toll free number).

SUPPLEMENTARY INFORMATION:

Background

The Tax Cuts and Jobs Act, Public Law 115-97, 131 Stat. 2054, 2208 (2017) (the "Act"), enacted on December 22, 2017, amended section 863(b) of the Internal Revenue Code ("Code"). On December 30, 2019, the Department of the Treasury ("Treasury Department") and the IRS published proposed regulations (REG-100956-19) under sections 863, 864, 865, 937, and 1502 in the **Federal Register** (84 FR 71836) (the "proposed regulations"). A public hearing on the proposed regulations was held on June 3, 2020. All written comments received in response to the proposed regulations are available at *https://www.regulations.gov* or upon request. Terms used but not defined in this preamble have the meaning provided in these final regulations.

Summary of Comments and Explanation of Revisions

I. *Overview*

The final regulations retain the overall approach of the proposed regulations, with certain revisions. This Summary of Comments and Explanation of Revisions section discusses those revisions as well as comments received in response to the solicitation of comments in the notice of proposed rulemaking. Comments outside the scope of this rulemaking are generally not addressed but may be considered in connection with future guidance projects.

II. *Comments on and Revisions to Proposed §1.863-1 — Allocation of Gross Income Under Section 863(a) and Proposed §1.863-3 — Allocation and Apportionment of Income from Certain Sales of Inventory*

The Act amended section 863 of the Code, which provides special sourcing rules for determining the source of income, including income partly from within and partly from without the United States. Specifically, the Act amended section 863(b) to allocate or apportion income from the sale or exchange of inventory property produced (in whole or in part) by a taxpayer within the United States and sold or exchanged without the United States or produced (in whole or in part) by the taxpayer without the United States and sold or exchanged within the United States (collectively, "Section 863(b)(2) Sales") solely on the basis of production activities with respect to that inventory. Before the Act, section 863(b) provided that income from Section 863(b)(2) Sales would be treated as derived partly from sources within and partly from sources without the United States without providing the basis for such allocation or apportionment. Consistent with the Act's changes to section 863(b), the proposed regulations amended §1.863-3 in order to properly allocate or apportion gross income from Section 863(b)(2) Sales based solely on production activity.

Under §1.863-3(c)(1)(ii)(A) (which has been redesignated in the final regulations as §1.863-3(c)(2)(i)), where the taxpayer's production assets are located both within and without the United States, the amount of income from sources without the United States is determined by multiplying all the income attributable to the taxpayer's production activities by a fraction, the numerator of which is the average adjusted basis of production assets that are located without the United States and the denominator of which is the average adjusted basis of all the production assets located within and without the United States.

For purposes of applying this formula, the adjusted basis of production assets is determined under section 1011, which is adjusted under section 1016 for depreciation deductions allowed. The Act also amended section 168(k) to allow an additional first-year depreciation deduction of 100 percent of the basis of certain property placed in service after September 27, 2017, and before January 1, 2023. Therefore, certain new and used production assets placed in service and used predominantly within the United States during this period may have an adjusted basis of zero. However, production assets either placed in service or used predominantly without the United States, or both, do not qualify for this accelerated depreciation and must be depreciated using the straight-line method under the alternative depreciation system ("ADS") of section 168(g)(2). In light of the Act's change to section 168(k) to allow accelerated depreciation in some

circumstances, the proposed regulations provided a new rule for computing the adjusted basis of production assets for purposes of applying the allocation formula in §1.863-3.

A. *Income attributable to sales activity*

Section 1.863-3, as in effect before this Treasury Decision, provided rules and corresponding methods for allocating or apportioning gross income from Section 863(b)(2) Sales between production activity and sales activity. To implement the changes to section 863(b) under the Act, the proposed regulations proposed removing §1.863-3(c)(2) which allocates and apportions income attributable to sales activity.

One comment argued that removing §1.863-3(c)(2) could lead to double taxation when a foreign jurisdiction imposes taxation on the sales activity. The Act amended section 863(b) to source income from the sale by a taxpayer of inventory produced by that taxpayer based only on production activity. Under the Code, sales activity is no longer a relevant factor for allocating and apportioning such income. Therefore, the final regulations remove §1.863-3(c)(2). But see part V of this Summary of Comments and Explanation of Revisions section for a discussion of the interaction with income tax treaties.

Another comment suggested that two aspects of §1.863-3(c)(2) have continued relevance even after the Act's changes to section 863(b)(2). First, §1.863-3(c)(2) has a special rule modifying the rule in §1.861-7(c) that generally sources income from the sale of personal property based on the place of sale. Under §1.861-7(c), a sale is generally treated as consummated in the place where the rights, title, and interest of the seller in the property are transferred to the buyer. However, if a taxpayer wholly produces inventory in the United States and sells it for use, consumption, or disposition in the United States, §1.863-3(c)(2) presumes that the place of sale is in the United States, even if title passes outside the United States. The comment recommended the final regulations include a similar rule and expand it to inventory wholly or partly produced in the United States that is acquired by a related party and resold for use, consumption, or disposition in the United States with title passing outside the United States. The comment observed that in the absence of such a rule, the sale by the related party would generate foreign source income, notwithstanding the fact that the inventory was produced wholly or partly in the United States and ultimately sold for use, consumption, or disposition in the United States.

The final regulations do not adopt this comment. The place of sale rule of §1.861-7(c) already contains a broad anti-abuse rule that would apply to any sales transactions "arranged in a particular manner for the primary purpose of tax avoidance," which may cover certain related party arrangements about which the comment is concerned. Section 482 also applies to require that compensation paid between related parties is consistent with the arm's length standard and will take into account the business functions and assets of, and risks assumed by, the related party intermediary. The Treasury Department and the IRS continue to study issues related to the distribution among related entities of the business functions, assets, and risks that generate business income, including sales income, and may address these issues in future guidance, particularly with respect to the sourcing of income from certain digital transactions.

Second, the comment observed that §1.863-3(c)(2) treats inventory as wholly produced in the United States for purposes of determining whether the place of sale is presumed to be in the United States if only minor assembly, packaging, repackaging, or labeling occurs outside the United States. The comment recommended including this rule as part of proposed §1.863-3(c)(1)(i). The final regulations adopt this comment in §1.863-3(c)(1)(i) by incorporating the "principles of §1.954-3(a)(4)" (other than §1.954-3(a)(4)(iv)). Section 1.954-3(a)(4) provides rules for determining when a corporation has manufactured, produced, or constructed personal property. Under §1.954-3(a)(4)(iii), packaging, repackaging, labeling, or minor assembly operations do not constitute the manufacture, production, or construction of property. Accordingly, under the final regulations, these principles apply for purposes of determining whether a taxpayer's activities constitute production activity under §1.863-3(c)(1)(i) as well. See part II.B of this Summary of Comments and Explanation of Revisions section.

B. *Definition of production activities*

Proposed §1.863-1(b)(2) provided the rule for sourcing gross receipts from the sale of natural resources where the taxpayer performs production activities in addition to its ownership of a farm, mine, oil or gas well, other natural deposit, or uncut timber. Section 1.863-1(b)(3)(ii) defines such "additional production activities" by reference to the "principles of §1.954-3(a)(4)."

Under section 951(a)(1)(A), a United States shareholder of a controlled foreign corporation ("CFC") includes in gross income its pro rata share of the CFC's subpart F income for the CFC's taxable year which ends with or within the taxable year of the shareholder. Section 952(a)(2) defines the term subpart F income to include foreign base company income. Section 954(a)(2) defines foreign base company income to include foreign base company sales income ("FBCSI") for the taxable year. Section 954(d)(1) defines FBCSI to mean income derived by a CFC in connection with certain related party transactions. Section 1.954-3(a)(4) provides an exception to FBCSI when a CFC manufactures property that it sells. One comment supported defining "additional production activities" by reference to "the principles of §1.954-3(a)(4)," as described in §1.863-1(b)(3)(ii), and requested that §§1.863-3 and 1.865-3 include a similar cross reference.

The final regulations adopt this recommendation, in part. Specifically, under the final regulations, §§1.863-3 and 1.865-3 incorporate the principles of §1.954-3(a)(4), with the exception of the rules regarding a "substantial contribution to the manufacturing of personal property" under §1.954-3(a)(4)(iv). See §§1.863-3(c)(1)(i) and 1.865-3(d)(2). The final regulations also modify §1.863-1(b)(3)(ii) to incorporate the principles of §1.954-3(a)(4), other than the "substantial contribution to the manufacturing of personal property" under §1.954-3(a)(4)(iv). The substantial contribution rules were added to §1.954-3(a)(4) in T.D. 9438 (December 29, 2008) after the adoption of §1.863-1(b)(3)(ii) in T.D. 8687 (November 27, 1996). While the Treasury Department

and the IRS agree with the comment that the principles of §1.954-3(a)(4) may generally be helpful in determining the location of production activity for sourcing purposes, the substantial contribution rules of §1.954-3(a)(4)(iv) are concerned with whether there is production activity and do not address the geographic location of that production activity, which is relevant for sourcing under sections 861, 863, and 865. Additionally, the substantial contribution rules are premised on treating a corporation as engaged in production activities even if it is not engaged in the direct use of production assets (other than oversight assets), while §1.863-3 focuses on sourcing income based on the location of a corporation's production assets that are used for production activities. See §1.863-3(c)(1)(ii) (which has been redesignated in the final regulations as §1.863-3(c)(2)). In this regard, there is not a clear metric for quantifying production arising from substantial contribution activities, even if such activities are properly identified, in order to assign production activities to a particular geographic location for purposes of determining the place of production under sections 861, 863, and 865. Therefore, the final regulations provide that the principles of §1.954-3(a)(4), other than the substantial contribution rules in §1.954-3(a)(4)(iv), apply in determining whether production activities exist.

C. *Measuring adjusted basis of production assets*

For inventory produced both within and without the United States, the proposed regulations continued to allocate or apportion the gross income between U.S. and foreign sources based on the formula in §1.863-3(c)(1)(ii)(A) (redesignated as proposed §1.863-3(c)(2)(i)). This formula determined the amount of foreign source income by multiplying the total gross income by a fraction, the numerator of which is the average adjusted basis of production assets located outside the United States and the denominator of which is the average adjusted basis of all production assets within and without the United States. The remaining gross income is from U.S. sources.

In light of the Act's changes to section 168(k), proposed §1.863-3(c)(2)(ii) measured the adjusted basis of the U.S. production assets for purposes of this formula based on the alternative depreciation system ("ADS") of section 168(g)(2). The preamble to the proposed regulations observed that such rule allows the basis of both U.S. and non-U.S. production assets to be measured consistently on a straight-line method over the same recovery period, and requested comments on using ADS for this purpose or alternatives for measuring relative U.S. and non-U.S. production assets.

One comment suggested that some taxpayers such as partnerships and S corporations would face administrative burdens if they had to maintain separate ADS books that they may not otherwise maintain if section 951A(d)(3) or 250(b)(2)(B) do not apply to them. The comment observed that the Act, in contrast to those other sections, does not mandate the use of ADS in the section 863(b) context. The comment requested that the final regulations maintain the existing rule of §1.863-3(c)(1)(ii)(B) measuring the basis under section 1011 (as adjusted by section 1016), either as the principal rule or, alternatively, at the election of the taxpayer.

The final regulations do not adopt this comment. The Treasury Department and the IRS have determined that the use of ADS for this purpose will prevent the Act's modifications to section 168(k) (resulting in accelerated depreciation) from inappropriately skewing the apportionment formula under §1.863-3(c)(2)(i) in favor of foreign source income. While the Act does not mandate the use of ADS for this purpose, the Treasury Department and the IRS have authority to mandate the use of ADS under sections 863(a) and 7805 and have determined that the use of ADS is necessary to accurately measure the place of production using adjusted basis, as other basis measurements might inappropriately inflate foreign production activities.

III. *Comments on and Revisions to Proposed §1.865-3 — Source of Gross Income from Sales of Personal Property (Including Inventory Property) by a Nonresident Attributable to an Office or Other Fixed Place of Business in the United States*

Section 865 provides rules for sourcing income from sales of personal property. Section 865(e)(2) applies with respect to all sales of personal property (including inventory) by a nonresident, as that term is defined in section 865(g)(1)(B), attributable to an office or other fixed place of business in the United States. Section 865(e)(2)(A) generally provides that income from any sale of personal property attributable to such an office or other fixed place of business is sourced in the United States. An exception is provided in section 865(e)(2)(B) for a sale of inventory for use, disposition, or consumption outside the United States if a foreign office of the nonresident ''materially participated'' in the sale. Section 865(e)(3) provides that the ''principles of section 864(c)(5) shall apply'' to determine whether a nonresident has an office or other fixed place of business and whether a sale is attributable to such office or other fixed place of business. Where applicable, section 865(e)(2) applies ''[n]otwithstanding any other provisions'' of subchapter N, part I, including sections 863(b), 861(a)(6), and 862(a)(6). The proposed regulations under §1.865-3 clarified the application of the principles of section 864(c)(5) in the context of section 865(e)(2) and provided that sales of inventory property produced outside the United States and sold through an office maintained by the nonresident in the United States must be sourced in the United States in part.

Proposed §1.865-3(e) also included a cross-reference to the rules for allocating and apportioning expenses to gross income effectively connected with the conduct of a trade or business in the United States in §§1.882-4 and 1.882-5. Since those regulations apply only to foreign corporations, one comment requested that the final regulations also refer to §1.873-1 to cover nonresident alien taxpayers subject to proposed §1.865-3. In response to this comment, the final regulations broaden the cross-references to include sections 882(c)(1) and 873(a) for purposes of allocating and apportioning expenses. See §1.865-3(e).

The final regulations also reorder and revise parts of §1.865-3 in a non-substantive manner solely for purposes of improving clarity and ease of application. The revision also helps to clarify that §1.865-3 applies only if a nonresident maintains an office or other fixed place of business in

the United States to which a sale of personal property is attributable. Otherwise, the source of the income, gain, or loss from the sale will be determined under other applicable provisions of section 865, such as section 865(b) through (d).

The final regulations also retain, with certain modifications, the rules for determining the portion of gross income from sales and production activities under §1.865-3(d). Under the proposed regulations, the "50/50 method," described in §1.865-3(d)(2)(i), was the default method because it was "an appropriate and administrable way" to apply section 865(e)(2), but the proposed regulations also allowed nonresidents to elect a books and records method that would "more precisely" reflect their gross income from both sales and production activities, if any, in the United States, provided the nonresidents met certain requirements for maintaining their books of account under proposed §1.865-3(d)(2)(ii)(B)(*1*) through (*3*). See 84 FR 71836, 71843. Under the final regulations, the 50/50 method continues to be the default method and taxpayers continue to be permitted to elect the books and records method. However, the Treasury Department and the IRS have determined that, where taxpayers have demonstrated the ability to use their books of account to determine their U.S. source gross income under the books and records method, a limitation is appropriate to prevent a nonresident from returning to the less precise 50/50 method solely to obtain a better tax result. In addition, the Treasury Department and the IRS have determined that revising the election to provide that it remains in effect until revoked would reduce the risk to taxpayers of inadvertently failing to include the election with their Federal income tax return. Accordingly, under the final regulations, an election to apply the books and records method continues until revoked and may not be revoked, without the consent of the Commissioner, for any taxable year beginning within 48 months of the end of the taxable year in which the election was made.

The final regulations also revise §1.864-5 to clarify the interaction with section 865(e)(2) and (3) and the promulgation of §1.865-3. Gross income, gain, or loss from the sale of personal property treated as from sources within the United States under §1.865-3 will generally be effectively connected with the conduct of a trade or business in the United States to the extent provided in section 864(c), other than section 864(c)(4) or (5). Gross income, gain, or loss from the sale of personal property treated as from sources without the United States under §1.865-3 is not described in §1.864-5(b) and thus will generally not be effectively connected with the conduct of a trade or business in the United States.

The rules of §§1.864-5, 1.864-6, and 1.864-7 continue to apply, however, in determining whether foreign source income of nonresident aliens and foreign corporations that does not arise from the sale of personal property described in §1.865-3(c) is effectively connected with the conduct of a trade or business in the United States. The rules of §§1.864-5, 1.864-6, and 1.864-7 also continue to apply in determining whether foreign source income from the sale of inventory by nonresident aliens, who would be residents under section 865(g)(1)(A), is effectively connected with the conduct of a trade or business in the United States.

IV. *Comments on the Rules for Determining the Location or Existence of Production Activity*

The proposed regulations did not modify the rules in §1.863-3 for determining the location or existence of production activity for purposes of determining the sourcing of income derived from the sale of inventory. Section 1.863-3(c)(1)(i)(A) (which has been redesignated in the final regulations as §1.863-3(c)(1)(i)) provides the rule for sourcing of income where production occurs only within the United States or only within foreign countries. That paragraph generally limits the scope of "production activities" to only "those conducted directly by the taxpayer." Similarly, §1.863-3(c)(1)(i)(B) (which has been redesignated in the final regulations as §1.863-3(c)(1)(ii)) provides that production assets are those "owned directly by the taxpayer that are directly used by the taxpayer to produce inventory." Section 1.863-3(c)(1)(ii) (which has been redesignated in the final regulations as §1.863-3(c)(2)) provides the rule for the sourcing of income where production occurs both within and without the United States, and, as discussed in part II.C of this Summary of Comments and Explanation of Revisions section, allocates gross income based on the relative adjusted basis of production assets located within and without the United States, respectively.

The final regulations clarify the determination of the adjusted basis of production assets under §1.863-3(c)(1)(ii)(B) (which has been redesignated in the final regulations as §1.863-3(c)(2)(ii)(A)). Under the final regulations, the adjusted basis of production assets for a taxable year is determined by averaging the basis of the assets at the beginning and end of the year, except in the event that a change during the year would cause the average to "materially distort" the calculation for sourcing of income attributable to production activity under §1.863-3(c)(1)(ii)(A) (which has been redesignated in the final regulations as §1.863-3(c)(2)(i)). This clarification uses certain concepts from §1.861-9(g)(2)(i)(A) to further explain when a change might "materially distort" the calculation. For example, the rule applies when an event such as a late-year disposition of substantially all the U.S. production assets of a corporation would cause a material distortion in the corporation's calculation of the split between U.S. and foreign production activities.

One comment provided a range of suggestions to modify the rules of proposed §§1.863-3(c) and 1.865-3(d). This comment suggested that the rules of proposed §§1.863-3(c) and 1.865-3(d) were adequate, in general, where a taxpayer independently manufactured its own inventory, but inadequate with respect to other business models that rely on limited risk contract manufacturers or where multiple members of a group each perform only limited manufacturing functions in various jurisdictions. The comment observed that apportionment of gross income using the relative adjusted basis of production assets may not reflect high value-adding core production and risk management functions and ownership of production assets by unrelated contract manufacturers.

The comment suggested expanding the scope of covered production activities and ownership of production assets to include activities conducted and assets owned by related parties and unrelated agents of the

taxpayer. The comment also recommended that these rules include any activities that constitute a "substantial contribution" within the meaning of §1.954-3(a)(4)(iv) to better conform to the rules under subpart F. See part II.B of this Summary of Comments and Explanation of Revisions section. In addition, the comment suggested that §1.863-3 should not allocate and apportion gross income using only the relative adjusted basis of production assets located within and without the United States, and recommended allocation and apportionment based on other metrics, such as the location of personnel involved in the production activities or personnel costs. The comment suggested that these modifications could, alternatively, be rebuttable presumptions that a taxpayer could overcome by showing that allocating and apportioning gross income based on adjusted basis or some other approach provides a more appropriate result under the taxpayer's facts.

Another comment suggested that the existing allocation and apportionment rules that rely on the relative adjusted basis of production assets encourage businesses to move (or locate additional) production assets outside the United States. Specifically, the comment expressed concern that treating income from the sale of inventory produced, in whole or in part, in the United States as U.S. source income might result in double taxation if the income is also subject to tax in a foreign jurisdiction, since the U.S. source income would be excluded from the numerator of the section 904 limitation, reducing the section 904 limitation, and potentially limiting the U.S. taxpayer's ability to use its foreign tax credits. The comment requested replacing these rules with a more comprehensive formula, preferably one that minimizes the risk of double taxation. The comment did not suggest an alternative formula and observed that further legislation may be necessary in this regard.

The Treasury Department and the IRS appreciate the various concerns presented by these comments and suggested revisions. The final regulations do not adopt these comments, but the Treasury Department and the IRS may consider these recommendations as part of a more comprehensive review of the sourcing rules for production activity (for purposes of both §1.863-3 and §1.865-3) in a future notice of proposed rulemaking. Additionally, the anti-abuse rule in §1.863-3(c)(1)(iii) (which has been redesignated in the final regulations as §1.863-3(c)(3)) already applies to make appropriate adjustments where taxpayers enter into or structure certain transactions with a principal purpose of reducing U.S. tax liability under §1.863-3, including by using production assets owned by a related party. To clarify the application of this rule, the final regulations provide that the anti-abuse rule applies to transactions inconsistent with the purpose of §1.863-3(b) or (c), and adds as an example that the anti-abuse rule may cover acquisitions of domestic production assets by related partnerships (or subsidiaries thereof) with a principal purpose of reducing the transferor's U.S. tax liability by treating income from the sale of inventory property as subject to section 862(a)(6) rather than section 863(b). The Treasury Department and the IRS continue to request comments regarding potential approaches to determine the location or existence of production activity or other modifications to §1.863-3 that may be appropriate.

V. *Comments on Income Tax Treaties*

The preamble to the proposed regulations included a statement about how proposed §1.865-3 interacted with U.S. income tax treaties under which the business profits of foreign treaty residents may be taxable in the United States only if the profits are attributable to a permanent establishment in the United States. The preamble to the proposed regulations stated, "[w]ith respect to taxpayers entitled to the benefits of an income tax treaty, the amount of profits attributable to a U.S. permanent establishment will not be affected by these regulations." See 84 FR 71836, 71844.

One comment supported the preamble's statement and requested that, consistent with the statement in the preamble, the final regulations not apply to Section 863(b)(2) Sales in a manner that results in double taxation to U.S. taxpayers engaged in business operations through a permanent establishment in a treaty jurisdiction, notwithstanding the Act's change to section 863(b). The comment also requested that competent authority relief be provided in this regard. These regulations do not affect the ability of a taxpayer to rely on treaty provisions to mitigate or relieve double taxation, including treaty provisions that permit a taxpayer to make a request to the competent authority for assistance pursuant to a mutual agreement procedure article of an applicable income tax treaty.

VI. *Comment on Proposed Applicability Date*

The proposed regulations were proposed to apply to taxable years ending on or after December 23, 2019, although taxpayers and their related parties could generally apply the rules in their entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019. One comment requested that the final regulations apply to taxable years ending after December 31, 2019, because some taxpayers have consistently relied on the existing methods of §1.863-3(b) for many years. The final regulations do not adopt this comment. Under section 7805(b)(1)(B), a final regulation can apply to any taxable period ending on or after the date on which the proposed regulation to which such final regulation relates was filed with the **Federal Register**, which for these final regulations was December 23, 2019. The final regulations implement the Act's statutory change to section 863(b), which was effective for taxable years beginning after December 31, 2017. To provide certainty to taxpayers and avoid a multiplicity of different interpretations of the statute, the Treasury Department and the IRS have determined that it is appropriate for the final regulations to apply as closely as possible to the effective date of the statutory change.

Applicability Date

The final regulations generally apply to taxable years ending on or after December 23, 2019. Taxpayers may choose to apply the final regulations for any taxable year beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons that are related to the taxpayer (within the meaning of section 267 or 707) apply the

final regulations in their entirety and, once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply the final regulations in their entirety for all subsequent taxable years. See section 7805(b)(7). Alternatively, taxpayers may rely on the proposed regulations for any taxable year beginning after December 31, 2017, and ending on or before September 29, 2020, provided that the taxpayer and all persons that are related to the taxpayer (within the meaning of section 267 or 707) rely on the proposed regulations in their entirety and provided that the taxpayer and all persons that are related to the taxpayer (within the meaning of section 267 or 707) have not applied the final regulations to any preceding year.

Special Analyses

These regulations are 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.

I. *Paperwork Reduction Act*

The Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) ("PRA") generally requires that a federal agency obtain the approval of OMB before collecting information from the public, whether such collection of information is mandatory, voluntary, or required to obtain or retain a benefit.

The final regulations include a collection of information in §1.865-3(d)(2)(ii)(B). Section 1.865-3(d)(2)(ii)(B) allows a nonresident, as defined in section 865(g)(1)(B), whose inventory sales are described in §1.865-3(d)(2) (relating to inventory produced by the nonresident) to elect to allocate the profit from such sales to its U.S. office using a books and records method under §1.865-3(d)(2)(ii), rather than using a default "50/50 method" under §1.865-3(d)(2)(i). If the collection of information in §1.865-3(d)(2)(ii)(B) applies to a nonresident, the nonresident must maintain detailed records of its receipts and expenditures attributable to its sales and production activities to support the allocation of its income, gain, or loss to its sales activities in the United States under the principles of section 482. See §1.865-3(d)(2)(ii)(B)(*2*). The nonresident must also prepare an explanation of how the allocation was determined. See §1.865-3(d)(2)(ii)(B)(*3*). The nonresident must make an election to apply the books and records method under §1.865-3(d)(2)(ii) by attaching a statement to its original timely filed Federal income tax return (including extensions) that it elects to apply the books and records method under §1.865-3(d)(2)(ii)(A) and has prepared the records described in §1.865-3(d)(2)(ii)(B)(*2*) and (*3*). The nonresident must make available the explanation and records upon request of the Commissioner, within 30 days or some other time period as agreed between the Commissioner and the nonresident. See §1.865-3(d)(2)(ii)(B)(*3*).

The reporting burdens associated with the collection of information in §1.865-3(d)(2)(ii)(B) will be reflected in the Form 14029, Paperwork Reduction Act Submission, that the Treasury Department and the IRS will submit to OMB for tax returns in the Forms 1120-F, U.S. Income Tax Return of a Foreign Corporation, and Forms 1040-NR, U.S. Nonresident Alien Income Tax Return. In particular, the reporting burden associated with the information collection in §1.865-3(d)(2)(ii)(B) will be included in the burden estimate for OMB control numbers 1545-0123 and 1545-0074. OMB control number 1545-0123 represents a total estimated burden time for all forms and schedules for corporations of 3.344 billion hours and total estimated monetized costs of $61.558 billion ($2019). OMB control number 1545-0074 represents a total estimated burden time, including all other related forms and schedules for individuals, of 1.717 billion hours and total estimated monetized costs of $33.267 billion ($2019). Table 1 summarizes the status of the PRA submissions of the Treasury Department and the IRS related to Forms 1120-F and 1040-NR.

The overall burden estimate provided by the Treasury Department and the IRS to OMB in the PRA submissions for OMB control numbers 1545-0123 and 1545-0074 are aggregate amounts related to the U.S. Business Income Tax Return and the U.S. Individual Income Tax Return, along with any associated forms. The burden estimates in these PRA submissions, however, do not account for any burden imposed by §1.865-3(d)(2)(ii)(B). The Treasury Department and the IRS have not identified the estimated burden for the collections of information in §1.865-3(d)(2)(ii)(B) because there are no burden estimates specific to §1.865-3(d)(2)(ii)(B) currently available. The burden estimates in the PRA submissions that the Treasury Department and the IRS will submit to OMB will in the future include, but not isolate, the estimated burden related to the collection of information in §1.865-3(d)(2)(ii)(B).

The Treasury Department and the IRS have included the burdens related to the PRA submissions for OMB control numbers 1545-0123 and 1545-0074 in the PRA analysis for other regulations issued by the Treasury Department and the IRS related to the taxation of cross-border income. The Treasury Department and the IRS encourage users of this information to take measures to avoid overestimating the burden that the collection of information in §1.865-3(d)(2)(ii)(B), together with other international tax provisions, imposes. Moreover, the Treasury Department and the IRS also note that the Treasury Department and the IRS estimate PRA burdens on a taxpayer-type basis rather than a provision-specific basis because an estimate based on the taxpayer-type most accurately reflects taxpayers' interactions with the forms.

The Treasury Department and the IRS request comments on the forms that reflect the information collection burdens related to the final regulations, including estimates for how much time it would take to comply with the paperwork burden described above for each relevant form and ways for the IRS to minimize the paperwork burden. Proposed revisions (if any) to these forms that reflect the information collection contained in §1.865-3(d)(2)(ii)(B) will be made available for public comment at https://apps.irs.gov/app/picklist/list/draftTaxForms.html and will not be finalized until after these forms have been approved by OMB under the PRA.

Table 1. Summary of Information Collection Request Submissions Related to Forms 1120-F and Forms 1040-NR.

Form	Type of Filer	OMB Number(s)	Status
Form 1040-NR	Individual (NEW Model)	1545-0074	Approved by OIRA 1/30/2020 until 1/31/2021.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201909-1545-021		
Form 1120-F	Business (NEW Model)	1545-0123	Approved by OIRA 1/30/2020 until 1/31/2021.
	Link: https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201907-1545-001		

II. *Regulatory Flexibility Act*

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that these final regulations will not have a significant economic impact on a substantial number of small entities. Although data are not readily available to assess the number of small entities potentially affected, any economic impact of these regulations is unlikely to be significant. Specifically, the regulations in §§1.863-1 and 1.863-3 (with conforming changes in cross-referencing regulations) implement the statutory change made to section 863(b) by the Act. This change affects sales of inventory property by any taxpayer where the taxpayer produces the inventory (in whole or in part) within the United States and sells that inventory without the United States, or vice versa. The change in sourcing for those entities is attributable to the change in section 863(b) made by the Act. Sections 1.863-1 and 1.863-3 merely implement the statutory change with limited additional guidance. The Treasury Department and the IRS do not anticipate that any differences between the changes in section 863(b) made by the Act and the changes in §§1.863-1 and 1.863-3 made by these regulations will have a significant economic impact on a substantial number of small entities.

The other regulations in this publication (other than changes to ensure consistency with section 863(b)) are the final regulations in §§1.864-5, 1.864-6, and 1.865-3. These regulations solely affect non-U.S. taxpayers, which are not subject to the Regulatory Flexibility Act.

Pursuant to section 7805(f) of the Code, 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 businesses. 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. These regulations do 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.

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. These regulations do not have federalism implications and do 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 regulations is Brad McCormack of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in the development of the regulations.

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 an entry for §1.865-3 in numerical order.

The addition reads in part as follows:

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

* * * * *

Section 1.865-3 also issued under 26 U.S.C. 865(j).

* * * * *

Par. 2. Section 1.863-0 is revised to read as follows:

§1.863-0 Table of contents.

This section lists captions contained in §§1.863-1 through 1.863-10.

§1.863-1 Allocation of gross income under section 863(a).

(a) In general.
(b) Natural resources.
(1) In general.
(2) Additional production activities.
(3) Definitions.
(i) Production activity.

(ii) Additional production activities.
(4) Determination of fair market value.
(5) Determination of gross income.
(6) Tax return disclosure.
(7) Examples.
(i) Example 1. No additional production, foreign source gross receipts.
(ii) Example 2. No additional production, U.S. source gross receipts.
(iii) Example 3. Production in United States, foreign sales.
(iv) Example 4. Production and sales in United States.
(v) Example 5. Additional production.
(c) Determination of taxable income.
(d) Scholarships, fellowship grants, grants, prizes, and awards.
(1) In general.
(2) Source of income.
(i) United States source income.
(ii) Foreign source income.
(iii) Certain activities conducted outside the United States.
(3) Definitions.
(4) Effective dates.
(i) Scholarships and fellowship grants.
(ii) Grants, prizes and awards.
(e) Residual interest in a REMIC.
(1) REMIC inducement fees.
(2) Excess inclusion income and net losses.
(f) Applicability date.

§1.863-2 Allocation and apportionment of taxable income.

(a) Determination of taxable income.
(b) Determination of source of taxable income.
(c) Applicability date.

§1.863-3 Allocation and apportionment of income from certain sales of inventory.

(a) In general.
(1) Scope.
(2) Cross references.
(b) Sourcing based solely on production activities.
(c) Determination of the source of gross income from production activity.
(1) Production only within the United States or only within foreign countries.
(i) Source of income.
(ii) Definition of production assets.
(iii) Location of production assets.
(2) Production both within and without the United States.
(i) Source of income.
(ii) Adjusted basis of production assets.
(A) In general.
(B) Production assets used to produce other property.
(3) Anti-abuse rule.
(4) Examples.
(i) Example1. Source of gross income.
(ii) Example 2. Location of intangible property.
(iii) Example 3. Anti-abuse rule.
(d) Determination of source of taxable income.
(e) Income partly from sources within a possession of the United States.
(1) In general.
(2) Allocation or apportionment for Possession Production Sales.
(3) Allocation or apportionment for Possession Purchase Sales.
(i) Determination of source of gross income from Possession Purchase Sales.
(ii) Determination of source of gross income from business activity.
(A) Source of gross income.
(B) Business activity.
(C) Location of business activity.
(*1*) Sales activity.
(*2*) Cost of goods sold.
(*3*) Expenses.
(4) Examples.
(i) Example 1: Purchase of goods manufactured in possession.
(ii) Example 2: Purchase of goods manufactured outside possession.
(5) Special rules for partnerships.
(f) Special rules for partnerships.
(1) General rule.
(2) Exceptions.
(i) In general.
(ii) Attribution of production assets to or from a partnership.
(iii) Basis.
(3) Examples.
(i) Example 1. Distributive share of partnership income.
(ii) Example 2. Distribution in kind.
(g) Applicability dates.

§1.863-4 Certain transportation services.

(a) General.
(b) Gross income.
(c) Allocation of costs or expenses.
(d) Items not included as costs or expenses.
(1) Taxes and interest.
(2) Other business activity and general expenses.
(3) Personal exemptions and special deductions.
(e) Property used while within the United States.
(1) General.
(2) Average property.
(3) Current assets.
(f) Taxable income.
(1) General.
(2) Interest and taxes.
(3) General expenses.
(4) Personal exemptions.
(5) Special deductions.
(g) Allocation based on books of account.

§1.863-6 Income from sources within a foreign country.

§1.863-7 Allocation of income attributable to certain notional principal contracts under section 863(a).

(a) Scope.
(1) Introduction.
(2) Effective/applicability date.
(b) Source of notional principal contract income.
(1) General rule.
(2) Qualified business unit exception.
(3) Effectively connected notional principal contract income.
(c) Election.
(1) Eligibility and effect.
(2) Time for making election.
(3) Manner of making election.
(d) Example.
(e) Cross references.

§1.863-8 Source of income derived from space and ocean activity under section 863(d).

(a) In general.
(b) Source of gross income from space and ocean activity.
(1) Space and ocean income derived by a United States person.
(2) Space and ocean income derived by a foreign person.
(i) In general.

(ii) Space and ocean income derived by a controlled foreign corporation.

(iii) Space and ocean income derived by foreign persons engaged in a trade or business within the United States.

(3) Source rules for income from certain sales of property.

(i) Sales of purchased property.

(ii) Sales of property produced by the taxpayer.

(A) General.

(B) Production only in space or international water, or only outside space and international water.

(C) Production both in space or international water and outside space and international water.

(4) Special rule for determining the source of gross income from services.

(5) Special rule for determining source of income from communications activity (other than income from international communications activity).

(c) Taxable income.

(d) Space and ocean activity.

(1) Definition.

(i) Space activity.

(ii) Ocean activity.

(2) Determining a space or ocean activity.

(i) Production of property in space or international water.

(ii) Special rule for performance of services.

(A) General.

(B) Exception to the general rule.

(3) Exceptions to space or ocean activity.

(e) Treatment of partnerships.

(f) Examples.

(1) Example 1. Space activity—activity occurring on land and in space.

(2) Example 2. Space activity.

(3) Example 3. Services as space activity—de minimis value attributable to performance occurring in space.

(4) Example 4. Space activity.

(5) Example 5. Space activity.

(6) Example 6. Space activity—treatment of land activity.

(7) Example 7. Use of intangible property in space.

(8) Example 8. Performance of services.

(9) Example 9. Separate transactions.

(10) Example 10. Sale of property in international water.

(11) Example 11. Sale of property in space.

(12) Example 12. Sale of property in space.

(13) Example 13. Source of income of a foreign person.

(14) Example 14. Source of income of a foreign person.

(g) Reporting and documentation requirements.

(1) In general.

(2) Required documentation.

(3) Access to software.

(4) Use of allocation methodology.

(h) Applicability date.

§1.863-9 Source of income derived from communications activity under section 863(a), (d), and (e).

(a) In general.

(b) Source of international communications income.

(1) International communications income derived by a United States person.

(2) International communications income derived by foreign persons.

(i) In general.

(ii) International communications income derived by a controlled foreign corporation.

(iii) International communications income derived by foreign persons with a fixed place of business in the United States.

(iv) International communications income derived by foreign persons engaged in a trade or business within the United States.

(c) Source of U.S. communications income.

(d) Source of foreign communications income.

(e) Source of space/ocean communications income.

(f) Source of communications income when taxpayer cannot establish the two points between which the taxpayer is paid to transmit the communication.

(g) Taxable income.

(h) Communications activity and income derived from communications activity.

(1) Communications activity.

(i) General rule.

(ii) Separate transaction.

(2) Income derived from communications activity.

(3) Determining the type of communications activity.

(i) In general.

(ii) Income derived from international communications activity.

(iii) Income derived from U.S. communications activity.

(iv) Income derived from foreign communications activity.

(v) Income derived from space/ocean communications activity.

(i) Treatment of partnerships.

(j) Examples.

(k) Reporting and documentation requirements.

(1) In general.

(2) Required documentation.

(3) Access to software.

(4) Use of allocation methodology.

(l) Effective date.

§1.863-10 Source of income from a qualified fails charge.

(a) In general.

(b) Qualified business unit exception.

(c) Effectively connected income exception.

(d) Qualified fails charge.

(e) Designated security.

(g) Effective/applicability date.

Par. 3. Section 1.863-0A is added to read as follows:

§1.863-0A Table of contents.

This section lists captions contained in §§1.863-3A and 1.863-3AT.

§1.863-3A Income from the sale of personal property derived partly from within and partly from without the United States.

(a) General.

(1) Classes of income.

(2) Definition.

(b) Income partly from sources within a foreign country.

(1) General.

(2) Allocation or apportionment.

(c) Income partly from sources within a possession of the United States.

(1) General.

(2) Allocation or apportionment.

(3) Personal property produced and sold.

(4) Personal property purchased and sold.

§1.863-3AT Income from the sale of personal property derived partly from within and partly from without the United States (temporary).

(a) [Reserved].

(b) Income partly from sources within a foreign country.

(1) [Reserved].

(2) Allocation or apportionment.

(c)(1) through (4) [Reserved].

Par. 4. Section 1.863-1 is amended as follows:

a. In paragraph (a):

i. Revising the third sentence.

ii. Removing "§1.863-3(g)" and adding in its place "§1.863-3(f)".

b. Revising paragraph (b)(1).

c. In paragraph (b)(2):

i. Removing "prior to export terminal" from the heading and adding in its place "activities".

ii. Removing "before the relevant product is shipped from the export terminal" from the first sentence.

iii. Adding "oil or gas" before "well" and "other natural" before "deposit" in the second sentence.

d. Removing "§§1.1502-13 or 1.863-3(g)(2)" from paragraph (b)(3)(i) and adding in its place "§1.1502-13 or 1.863-3(f)(2)".

e. In paragraph (b)(3)(ii):

i. Adding "uncut" before "timber" in the first sentence.

ii. Adding "(except for §1.954-3(a)(4)(iv))" at the end of the second sentence.

iii. Removing "to or from the export terminal" from the third sentence.

f. Removing paragraph (b)(3)(iii).

g. In paragraph (b)(6), removing "this paragraph (b)" from the first sentence and adding in its place "paragraph (b)(2) of this section".

h. Designating *Examples 1*, *2*, *3*, *4*, and *5* of paragraph (b)(7) as paragraphs (b)(7)(i) through (v).

i. Revising newly designated paragraphs (b)(7)(i) through (v).

j. In paragraph (f):

i. Revising the heading.

ii. Adding three sentences at the start of the paragraph.

The revisions and additions read as follows:

§1.863-1 Allocation of gross income under section 863(a).

(a) * * * See also section 865(b) for rules for sourcing income from the sale of inventory property, within the meaning of section 865(i)(1) (inventory), generally, and section 865(e)(2) and §1.865-3 for sourcing income from the sale of personal property (including inventory) by a nonresident that is attributable to the nonresident's office or other fixed place of business in the United States. * * *

(b) *Natural resources*—(1) *In general*. Notwithstanding any other provision of this part, except to the extent provided in paragraph (b)(2) of this section or §1.865-3, gross receipts from the sale outside the United States of products derived from the ownership or operation of any farm, mine, oil or gas well, other natural deposit, or uncut timber within the United States shall be treated as from sources within the United States, and gross receipts from the sale within the United States of products derived from the ownership or operation of any farm, mine, oil or gas well, other natural deposit, or uncut timber outside the United States shall be treated as from sources without the United States.

* * * * *

(7) * * *

(i) *Example 1. No additional production, foreign source gross receipts*. U.S. Mines, a domestic corporation, operates a copper mine and mill in Country X. U.S. Mines extracts copper-bearing rocks from the ground and transports the rocks to the mill where the rocks are ground and processed to produce copper-bearing concentrate. The concentrate is transported to a port where it is dried in preparation for export, stored, and then shipped to purchasers in the United States. Because, under the facts and circumstances, none of U.S. Mines' activities constitute additional production activities, within the meaning of paragraph (b)(3)(ii) of this section, paragraph (b)(2) of this section does not apply, and under paragraph (b)(1) of this section, gross receipts from the sale of the concentrate will be treated as from sources without the United States.

(ii) *Example 2. No additional production, U.S. source gross receipts*. U.S. Gas, a domestic corporation, extracts natural gas within the United States, and transports the natural gas to a Country X port where it is liquefied in preparation for shipment. The liquefied natural gas is then transported via freighter and sold without additional production activities in a foreign country. Under paragraph (b)(3)(ii) of this section, liquefaction of natural gas is not an additional production activity because liquefaction prepares the natural gas for transportation. Therefore, under paragraph (b)(1) of this section, gross receipts from the sale of the liquefied natural gas will be treated as from sources within the United States.

(iii) *Example 3. Production in United States, foreign sales*. U.S. Gold, a domestic corporation, mines gold in Country X, produces gold jewelry using production assets located in the United States, and sells the jewelry in Country Y. Assume that the fair market value of the gold before the additional production activities in the United States is $40x and that U.S. Gold ultimately sells the gold jewelry in Country Y for $100x. Under paragraph (b)(2) of this section, $40x of U.S. Gold's gross receipts will be treated as from sources without the United States, and the remaining $60x of gross receipts will be treated as from sources within the United States under §1.863-3.

(iv) *Example 4. Production and sales in United States*. U.S. Oil, a domestic corporation, extracts oil in Country X, transports the oil via a pipeline to the United States, refines the oil using production assets located in the United States, and sells the refined product in the United States to unrelated persons. Assume that the fair market value of the oil before refinement in the United States is $80x and U.S. Oil ultimately sells the refined product for $100x. Under paragraph (b)(2) of this section, $80x of gross receipts will be treated as from sources without the United States, and the remaining $20x of gross receipts will be treated as from sources within the United States under §1.863-3.

(v) *Example 5. Additional production*. The facts are the same as in paragraph (b)(7)(i) of this section (the facts in *Example 1*), except that U.S. Mines also operates a smelter in Country X. The concentrate output from the mill is transported to the smelter where it is transformed into smelted copper. The smelted copper is exported to purchasers in the United States. Under the facts and circumstances, all the processes applied to make copper concentrate are considered mining. Therefore, under paragraph (b)(2) of this section, gross receipts equal to the fair market value of the concentrate at the smelter will be treated as from sources without the United States. Under the facts and circumstances, the conversion of the concentrate into smelted copper is an additional production activity in a foreign country within the meaning of paragraph (b)(3)(ii) of this section. Therefore, the source of U.S. Mines's excess gross receipts will be determined under §1.863-3, pursuant to paragraph (b)(2) of this section.

* * * * *

(f) *Applicability date*. Paragraph (b) of this section applies to taxable years ending on or after December 23, 2019. However, a taxpayer may apply paragraph (b) of this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply paragraph (b) of this section and §§1.863-2(b), 1.863-3, 1.863-8(b)(3)(ii), 1.864-5(a) and (b), 1.864-6(c)(2), and 1.865-3 in their entirety for the taxable year, and once applied,

the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.863-1 as contained in 26 CFR part 1 revised as of April 1, 2020. * * *

Par. 5. Section 1.863-2 is amended as follows:

a. In paragraph (a) introductory text:

i. Removing "(and that is treated as derived partly from sources within and partly from sources without the United States)" from the third sentence.

ii. Adding a colon after the word "income" at the end of the paragraph.

b. Revising paragraph (b).

c. Revising paragraph (c).

The revisions read as follows:

§1.863-2 Allocation and apportionment of taxable income.

* * * * *

(b) *Determination of source of taxable income*. Income treated as derived from sources partly within and partly without the United States under paragraph (a) of this section may be allocated or apportioned to sources within and without the United States pursuant to §§1.863-1, 1.863-3, 1.863-4, 1.863-8, and 1.863-9. To determine the source of certain types of income described in paragraph (a)(1) of this section, see §1.863-4. To determine the source of gross income described in paragraph (a)(2) of this section, see §1.863-1 for natural resources, §1.863-3 for other sales of inventory property, and §1.863-8 for source of gross income from space and ocean activity. Section 1.865-3 may apply instead of the provisions in this section to source gross income from sales of personal property (including inventory property) by nonresidents attributable to an office or other fixed place of business in the United States. To determine the source of income partly from sources within a possession of the United States, including income described in paragraph (a)(3) of this section, see §1.863-3(e).

(c) *Applicability date*. Except as provided in this paragraph (c), this section applies to taxable years beginning after December 30, 1996. Paragraph (b) of this section applies to taxable years ending on or after December 23, 2019. However, a taxpayer may apply paragraph (b) of this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply paragraph (b) of this section and §§1.863-1(b), 1.863-3, 1.863-8(b)(3)(ii), 1.864-5(a) and (b), 1.864-6(c)(2), and 1.865-3 in their entirety for the taxable year, and once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.863-2 as contained in 26 CFR part 1 revised as of April 1, 2020.

Par. 6. Section 1.863-3 is revised as follows:

§1.863-3 Allocation and apportionment of income from certain sales of inventory.

(a) *In general*—(1) *Scope*. Subject to the rules of §1.865-3, paragraphs (a) through (d) of this section apply to determine the source of income derived from the sale of inventory property (inventory) that a taxpayer produces (in whole or in part) within the United States and sells without the United States, or that a taxpayer produces (in whole or in part) without the United States and sells within the United States (collectively, Section 863(b)(2) Sales). See section 865(i)(1) for the definition of inventory. Paragraph (b) of this section provides that the source of gross income from Section 863(b)(2) Sales is based solely on the production activities with respect to the inventory. Paragraph (c) of this section describes how to determine source based on production activity, including when inventory is produced partly within the United States and partly without the United States. Paragraph (d) of this section determines taxable income from Section 863(b)(2) Sales. Paragraph (e) of this section applies to determine the source of certain income derived from a possession of the United States. Paragraph (f) of this section provides special rules for partnerships for all sales subject to §§1.863-1 through 1.863-3. Paragraph (g) of this section provides applicability dates for the rules in this section.

(2) *Cross references*. To determine the source of income derived from the sale of personal property (including inventory) by a nonresident that is attributable to the nonresident's office or other fixed place of business in the United States under section 865(e)(2) and §1.865-3(c), the rules of §1.865-3 apply, and the rules of this section do not apply except to the extent provided in §1.865-3. To determine the source of income from sales of property produced by the taxpayer, when the property is either produced in whole or in part in space, as defined in §1.863-8(d)(1)(i), or international water, as defined in §1.863-8(d)(1)(ii), or is sold in space or international water, the rules of §1.863-8 apply, and the rules of this section do not apply except to the extent provided in §1.863-8.

(b) *Sourcing based solely on production activities*. Subject to the rules of §1.865-3, all income, gain, or loss derived from Section 863(b)(2) Sales is allocated and apportioned solely on the basis of the production activities with respect to the inventory.

(c) *Determination of the source of gross income from production activity*—(1) *Production only within the United States or only within foreign countries*—(i) *Source of income*. For purposes of this section, production activity means an activity that creates, fabricates, manufactures, extracts, processes, cures, or ages inventory. See §1.864-1. Whether a taxpayer's activities constitute production activity is determined under the principles of §1.954-3(a)(4) (except for §1.954-3(a)(4)(iv)). Subject to the provisions in §1.1502-13 or paragraph (f)(2)(ii) of this section, the only production activities that are taken into account for purposes of §§1.863-1, 1.863-2, and this section are those conducted directly by the taxpayer. Where the taxpayer's production assets are located only within the United States or only outside the United States, gross income is sourced where the taxpayer's production assets are located. For rules regarding the source of income when production assets are located both within the United States and without the United States, see para-

graph (c)(2) of this section. For rules regarding the source of income when production takes place, in whole or in part, in space or international water, the rules of §1.863-8 apply, and the rules of this section do not apply except to the extent provided in §1.863-8.

(ii) *Definition of production assets*. Subject to the provisions of §1.1502-13 and paragraph (f)(2)(ii) of this section, production assets include only tangible and intangible assets owned directly by the taxpayer that are directly used by the taxpayer to produce inventory described in paragraph (a) of this section. Production assets do not include assets that are not directly used to produce inventory described in paragraph (a) of this section. Thus, production assets do not include such assets as accounts receivables, intangibles not related to production of inventory (e.g., marketing intangibles, including trademarks and customer lists), transportation assets, warehouses, the inventory itself, raw materials, or work-in-process. In addition, production assets do not include cash or other liquid assets (including working capital), investment assets, prepaid expenses, or stock of a subsidiary.

(iii) *Location of production assets*. For purposes of this section, a tangible production asset will be considered located where the asset is physically located. An intangible production asset will be considered located where the tangible production assets owned by the taxpayer to which it relates are located.

(2) *Production both within and without the United States*—(i) *Source of income*. Where the taxpayer's production assets are located both within and without the United States, income from sources without the United States will be determined by multiplying the gross income by a fraction, the numerator of which is the average adjusted basis of production assets that are located outside the United States and the denominator of which is the average adjusted basis of all production assets within and without the United States. The remaining income is treated as from sources within the United States.

(ii) *Adjusted basis of production assets*—(A) *In general*. For purposes of paragraph (c)(2)(i) of this section, the adjusted basis of an asset is determined by using the alternative depreciation system under section 168(g)(2). The adjusted basis of all production assets for purposes of paragraph (c)(2)(i) of this section is determined as though the production assets were subject to the alternative depreciation system set forth in section 168(g)(2) for the entire period that such property has been in service. The adjusted basis of the production assets is determined without regard to the election to expense certain depreciable assets under section 179 and without regard to any additional first-year depreciation provision (for example, section 168(k), (l), and (m), and former sections 1400L(b) and 1400N(d)). The average adjusted basis of assets is computed by averaging the adjusted basis at the beginning and end of the taxable year, unless by reason of changes during the taxable year, as might be the case in the event of a major acquisition or disposition of assets, the average would materially distort the calculation in paragraph (c)(2)(i) of this section. In this event, the average adjusted basis is determined upon a more appropriate basis that is weighted to reasonably reflect the period for which the assets are held by the taxpayer during the taxable year.

(B) *Production assets used to produce other property*. If a production asset is used to produce inventory sold in Section 863(b)(2) Sales and also used to produce other property during the taxable year, the portion of its adjusted basis that is included in the fraction described in paragraph (c)(2)(i) of this section will be determined under any method that reasonably reflects the portion of the asset that produces inventory sold in Section 863(b)(2) Sales. For example, the portion of such an asset that is included in the formula may be determined by multiplying the asset's average adjusted basis by a fraction, the numerator of which is the gross receipts from sales of inventory from Section 863(b)(2) Sales produced by the asset, and the denominator of which is the gross receipts from all property produced by that asset.

(3) *Anti-abuse rule*. The purpose of paragraph (b) of this section and this paragraph (c) is to attribute the source of the taxpayer's gross income from certain sales of inventory property to the location of the taxpayer's production activity. Therefore, if the taxpayer has entered into or structured one or more transactions with a principal purpose of reducing its U.S. tax liability in a manner inconsistent with the purpose of paragraph (b) of this section or this paragraph (c), the Commissioner may make appropriate adjustments so that the source of the taxpayer's gross income more clearly reflects the location of production activity. For example, a taxpayer may be subject to the rule in this paragraph (c)(3) if domestic production assets are acquired by a related partnership (or a subsidiary of a related partnership) with a principal purpose of reducing its U.S. tax liability by claiming that the taxpayer's income from sales of inventory is subject to section 862(a)(6) rather than section 863(b).

(4) *Examples*. The following examples illustrate the rules of this paragraph (c):

(i) *Example 1. Source of gross income*—(A) *Facts*. A, a U.S. corporation, produces widgets that are sold both within the United States and within a foreign country. The initial manufacture of all widgets occurs in the United States. The second stage of production of widgets that are sold within a foreign country is completed within the country of sale. A's U.S. plant and machinery which is involved in the initial manufacture of the widgets has an average adjusted basis of $200, as determined using the alternative depreciation system under section 168(g)(2). A also owns warehouses used to store work-in-process. A owns foreign equipment with an average adjusted basis of $25. A's gross receipts from all sales of widgets is $100, and its gross receipts from export sales of widgets is $25. Assume that apportioning average adjusted basis using gross receipts is reasonable. Assume A's cost of goods sold from the sale of widgets in the foreign countries is $13 and thus, its gross income from widgets sold in foreign countries is $12.

(B) *Analysis*. A determines its gross income from sources without the United States by multiplying A's $12 of gross income from sales of widgets in foreign countries by a fraction, the numerator of which is all relevant foreign production assets, or $25, and the denominator of which is all relevant production assets, or $75 ($25 foreign assets + ($200 U.S. assets × $25 gross receipts from export sales/$100 gross receipts from all sales)). Therefore, A's gross income from sources without the United States is $4 ($12 × ($25/$75)).

(ii) *Example 2. Location of intangible property*. Assume the same facts as in paragraph (c)(4)(i)(A) of this section (the facts in *Example 1*), except that A employs a patented process that applies only to the initial production of widgets. In computing the formula used to determine the source of gross income, A's patent, if it has an average adjusted basis, would be located in the United States.

(iii) *Example 3. Anti-abuse rule*—(A) *Facts*. Assume the same facts as in paragraph (c)(4)(i)(A) of this section (the facts in *Example 1*). A sells its U.S. assets to B, an unrelated U.S. corporation, with a principal purpose of reducing its U.S. tax liability

by manipulating the property fraction. A then leases these assets from B. After this transaction, under the general rule of paragraph (c)(2) of this section, all of A's gross income would be considered from sources without the United States, because all of A's relevant production assets are located within a foreign country. Since the leased property is not owned by the taxpayer, it is not included in the fraction.

(B) *Analysis*. Because A has entered into a transaction with a principal purpose of reducing its U.S. tax liability by manipulating the formula described in paragraph (c)(2)(i) of this section, A's income must be adjusted to more clearly reflect the source of that income. In this case, the Commissioner may redetermine the source of A's gross income by ignoring the sale-leaseback transactions.

(d) *Determination of source of taxable income*. Once the source of gross income has been determined under paragraph (c) of this section, the taxpayer must properly allocate and apportion its expenses, losses, and other deductions to its respective amounts of gross income from sources within and without the United States from its Section 863(b)(2) Sales. See §§1.861-8 through 1.861-14T and 1.861-17.

(e) *Income partly from sources within a possession of the United States*—(1) *In general*. This paragraph (e) relates to certain sales that give rise to income, gain, or loss that is treated as derived partly from sources within the United States and partly from sources within a possession of the United States (Section 863 Possession Sales). This paragraph (e) applies to determine the source of income derived from the sale of inventory produced (in whole or in part) by a taxpayer within the United States and sold within a possession of the United States, or produced (in whole or in part) by a taxpayer in a possession of the United States and sold within the United States (collectively, Possession Production Sales). It also applies to determine the source of income derived from the purchase of personal property within a possession of the United States and its sale within the United States (Possession Purchase Sales). A taxpayer subject to this paragraph (e) must apportion gross income from Section 863 Possession Sales under paragraph (e)(2) of this section (in the case of Possession Production Sales) or under paragraph (e)(3) of this section (in the case of Possession Purchase Sales). The source of taxable income from Section 863 Possession Sales is determined under paragraph (d) of this section.

(2) *Allocation or apportionment for Possession Production Sales*. The source of gross income from Possession Production Sales is determined under the rules of paragraph (c) of this section, except that the term *possession of the United States* is substituted for *foreign country* wherever it appears.

(3) *Allocation or apportionment for Possession Purchase Sales*—(i) *Determination of source of gross income from Possession Purchase Sales*. Gross income from Possession Purchase Sales is allocated in its entirety to the taxpayer's business activity, and is then apportioned between sources within the United States and sources within a possession of the United States under paragraph (e)(3)(ii) of this section.

(ii) *Determination of source of gross income from business activity*—(A) *Source of gross income*. Gross income from the taxpayer's business activity is sourced in the possession in the same proportion that the amount of the taxpayer's business activity for the taxable year within the possession bears to the amount of the taxpayer's business activity for the taxable year both within the possession and outside the possession, with respect to Possession Purchase Sales. The remaining income is sourced in the United States.

(B) *Business activity*. For purposes of this paragraph (e)(3)(ii), the taxpayer's business activity is equal to the sum of—

(*1*) The amounts for the taxable period paid for wages, salaries, and other compensation of employees, and other expenses attributable to Possession Purchase Sales (other than amounts that are nondeductible under section 263A, interest, and research and development);

(*2*) Cost of goods sold attributable to Possession Purchase Sales during the taxable period; and

(*3*) Possession Purchase Sales for the taxable period.

(C) *Location of business activity*. For purposes of determining the location of the taxpayer's business activity within a possession, the following rules apply:

(*1*) *Sales activity*. Receipts from gross sales will be attributed to a possession in accordance with the principles of §1.861-7(c).

(*2*) *Cost of goods sold*. Payments for cost of goods sold will be properly attributable to gross receipts from sources within the possession only to the extent that the property purchased was manufactured, produced, grown, or extracted in the possession (within the meaning of section 954(d)(1)(A)).

(*3*) *Expenses*. Expenses will be attributed to a possession under the rules of §§1.861-8 through 1.861-14T.

(4) *Examples*. The following examples illustrate the rules of paragraph (e)(3)(ii) of this section relating to the determination of source of gross income from business activity:

(i) *Example 1. Purchase of goods manufactured in possession*—(A) *Facts*. U.S. Co. purchases in a possession product X for $80 from A. A manufactures X in the possession. Without further production, U.S. Co. sells X in the United States for $100. Assume U.S. Co. has sales and administrative expenses in the possession of $10.

(B) *Analysis*. To determine the source of U.S. Co.'s gross income, the $100 gross income from sales of X is allocated entirely to U.S. Co.'s business activity. Forty-seven dollars of U.S. Co.'s gross income is sourced in the possession. [Possession expenses ($10) plus possession purchases (i.e., cost of goods sold) ($80) plus possessions sales ($0), divided by total expenses ($10) plus total purchases ($80) plus total sales ($100).] The remaining $53 is sourced in the United States.

(ii) *Example 2. Purchase of goods manufactured outside possession*—(A) *Facts*. Assume the same facts as in paragraph (e)(4)(i)(A) of this section (the facts in *Example 1*), except that A manufactures X outside the possession.

(B) *Analysis*. To determine the source of U.S. Co.'s gross income, the $100 gross income is allocated entirely to U.S. Co.'s business activity. Five dollars of U.S. Co.'s gross income is sourced in the possession. [Possession expenses ($10) plus possession purchases ($0) plus possession sales ($0), divided by total expenses ($10) plus total purchases ($80) plus total sales ($100).] The $80 purchase is not included in the numerator used to determine U.S. Co.'s business activity in the possession, since product X was not manufactured in the possession. The remaining $95 is sourced in the United States.

(5) *Special rules for partnerships*. In applying the rules of this paragraph (e) to transactions involving partners and partnerships, the rules of paragraph (f) of this section apply.

(f) *Special rules for partnerships*—(1) *General rule*. For purposes of §1.863-1 and this section, a taxpayer's production activity does not include production activities conducted by a partnership of which the taxpayer is a partner either directly or through one or more partnerships, except as otherwise provided in paragraphs (c)(3) or (f)(2) of this section.

(2) *Exceptions*—(i) *In general*. For purposes of determining the source of the partner's distributive share of partnership

income or determining the source of the partner's income from the sale of inventory property which the partnership distributes to the partner in kind, the partner's production activity includes an activity conducted by the partnership. In addition, the production activity of a partnership includes the production activity of a taxpayer that is a partner either directly or through one or more partnerships, to the extent that the partner's production activity is related to inventory that the partner contributes to the partnership in a transaction described under section 721.

(ii) *Attribution of production assets to or from a partnership*. A partner will be treated as owning its proportionate share of the partnership's production assets only to the extent that, under paragraph (f)(2)(i) of this section, the partner's activity includes production activity conducted through a partnership. A partner's share of partnership assets will be determined by reference to the partner's distributive share of partnership income for the year attributable to such production assets. Similarly, to the extent a partnership's activities include the production activities of a partner, the partnership will be treated as owning the partner's production assets related to the inventory that is contributed in kind to the partnership. See paragraph (c)(2)(ii) of this section for rules apportioning the basis of assets to Section 863 Sales.

(iii) *Basis*. For purposes of this section, in those cases where the partner is treated as owning its proportionate share of the partnership's production assets, the partner's basis in production assets held through a partnership shall be determined by reference to the partnership's adjusted basis in its assets (including a partner's special basis adjustment, if any, under section 743). Similarly, a partnership's basis in a partner's production assets is determined with reference to the partner's adjusted basis in its assets.

(3) *Examples*. The following examples illustrate the rules of this paragraph (f):

(i) *Example 1. Distributive share of partnership income*. A, a U.S. corporation, forms a partnership in the United States with B, a country X corporation. A and B each have a 50 percent interest in the income, gains, losses, deductions and credits of the partnership. The partnership is engaged in the manufacture and sale of widgets. The widgets are manufactured in the partnership's plant located in the United States and are sold by the partnership outside the United States. The partnership owns the manufacturing facility and all other production assets used to produce the widgets. A's distributive share of partnership income includes 50 percent of the sales income from these sales. In applying the rules of section 863 to determine the source of its distributive share of partnership income from the export sales of widgets, A is treated as carrying on the activity of the partnership related to production of these widgets and as owning a proportionate share of the partnership's assets related to production of the widgets, based upon its distributive share of partnership income.

(ii) *Example 2. Distribution in kind*. Assume the same facts as in paragraph (f)(3)(i) of this section (the facts in *Example 1*) except that the partnership, instead of selling the widgets, distributes the widgets to A and B. A then further processes the widgets and then sells them outside the United States. In determining the source of the income earned by A on the sales outside the United States, A is treated as conducting the activities of the partnership related to production of the distributed widgets. Thus, the source of gross income on the sale of the widgets is determined under section 863 and this section. In applying paragraph (c) of this section, A is treated as owning its proportionate share of the partnership's production assets based upon its distributive share of partnership income.

(g) *Applicability dates*. This section applies to taxable years ending on or after December 23, 2019. However, a taxpayer may apply this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply this section and §§1.863-1(b), 1.863-2(b), 1.863-8(b)(3)(ii), 1.864-5(a) and (b), 1.864-6(c)(2), and 1.865-3 in their entirety for the taxable year, and once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.863-3 as contained in 26 CFR part 1 revised as of April 1, 2020.

Par. 7. Section 1.863-8 is amended as follows:

a. Revising paragraph (b)(3)(ii)(A).

b. In paragraph (b)(3)(ii)(B):

i. Removing "income allocable to production activity" wherever it appears and adding in its place "gross income".

ii. Removing "§1.863-3(c)(1)" from the second sentence and adding in its place "§1.863-3(c)".

c. In paragraph (b)(3)(ii)(C):

i. Removing "allocable to production activity" wherever it appears.

ii. Removing "allocated to production activity" from the fifth sentence.

iii. Removing "§1.863-3(c)(1)" from the fifth sentence and adding in its place "§1.863-3(c)".

d. Removing paragraph (b)(3)(ii)(D).

e. In paragraph (c), removing "(b)(3)(ii)(C)" from the first sentence and adding in its place "(b)(3)(ii)".

f. Designating *Examples 1* through *14* of paragraph (f) as paragraphs (f)(1) through (14).

g. In newly designated paragraphs (f)(1) through (14), removing the period between the second and third level paragraph headings and adding an em-dash in its place.

h. Removing "this *Example 4*" from newly designated paragraph (f)(4)(i) wherever it appears and adding in its place "paragraph (f)(4)(i) (*Example 4*)".

i. Removing "*Example 4*" from newly designated paragraph (f)(5)(i) and adding in its place "paragraph (f)(4)(i) of this section (the facts in *Example 4*)".

j. Revising newly designated paragraph (f)(6)(ii).

k. Removing "*Example 8*" from newly designated paragraph (f)(9)(i) and adding in its place "in paragraph (f)(8)(i) of this section (the facts in *Example 8*)".

l. Removing "*Example 8*" from newly designated paragraph (f)(9)(ii) and adding in its place "paragraph (f)(8)(ii) of this section (the analysis in *Example 8*)".

m. Revising newly designated paragraph (f)(11)(ii).

n. In paragraph (g)(1), removing "(b)(3)(ii)(C)" from the first sentence and adding in its place "(b)(3)(ii)".

o. In paragraph (g)(4) introductory text, removing "(b)(3)(ii)(C)" from the first sentence and adding in its place "(b)(3)(ii)".

p. In paragraph (h), adding three sentences at the end of the paragraph.

The revisions and additions read as follows:

§1.863-8 Source of income derived from space and ocean activity under section 863(d).

* * * * *

(b) * * *

(3) * * *

(ii) *Sales of property produced by the taxpayer*—(A) *General*. If the taxpayer both produces property and sells such property and either the production (in whole or in part) or the sale takes place in space or international water, the taxpayer must allocate and apportion all income, gain, or loss derived from sales of such property solely on the basis of the production activities with respect to such property, and the source of that income will be determined under paragraph (b)(3)(ii)(B) or (C) of this section. To determine the source of income derived from the sale of personal property (including inventory) by a nonresident that is attributable to the nonresident's office or other fixed place of business in the United States under section 865(e)(2), the rules of §1.865-3 apply, and the rules of this section do not apply.

* * * * *

(f) * * *

(6) * * *

(ii) *Analysis*. The collection of data and creation of images in space is characterized as the creation of property in space. Because S both produces and sells the data, the source of the gross income from the sale of the data is determined under paragraph (b)(3)(ii) of this section solely on the basis of the production activities. The source of S's gross income is determined under paragraph (b)(3)(ii)(C) of this section because production activities occur both in space and on land.

* * * * *

(11) * * *

(ii) *Analysis*. Because S's rights, title, and interest in the satellite pass to the customer in space, the sale takes place in space under §1.861-7(c), and the sale transaction is space activity under paragraph (d)(1)(i) of this section. The source of income derived from the sale of the satellite manufactured in the United States and sold in space is determined under paragraph (b)(3)(ii) of this section solely on the basis of the production activities with respect to the satellite.

* * * * *

(h) * * * Paragraph (b)(3)(ii) of this section applies to taxable years ending on or after December 23, 2019. However, a taxpayer may apply paragraph (b)(3)(ii) of this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply paragraph (b)(3)(ii) of this section and §§1.863-1(b), 1.863-2(b), 1.863-3, 1.864-5(a) and (b), 1.864-6(c)(2), and 1.865-3 in their entirety for the taxable year, and once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.863-8 as contained in 26 CFR part 1 revised as of April 1, 2020.

Par. 8. Section 1.864-5 is amended as follows:

a. Adding a sentence to the end of paragraph (a);

b. Revising the first sentence of paragraph (b) introductory text; and

c. Adding paragraph (e).

The additions read as follows:

§1.864-5 Foreign source income effectively connected with U.S. business.

(a) * * * To determine the source of income, gain or loss from the sale of personal property (including inventory property) attributable to an office or other fixed place of business in the United States by nonresidents, as defined in section 865(g)(1)(B), see §1.865-3.

(b) * * * Income, gain, or loss from sources without the United States other than income described in paragraph (c) of this section or income from section 865(e)(2) sales, as defined in §1.865-3(c), shall be taken into account pursuant to paragraph (a) of this section in applying §§1.864-6 and 1.864-7 only if it consists of—

* * * * *

(e) *Applicability dates*. Paragraphs (a) and (b) of this section apply to taxable years ending on or after December 23, 2019. However, a taxpayer may apply paragraphs (a) and (b) of this section in their entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply paragraphs (a) and (b) of this section and §§1.863-1(b), 1.863-2(b), 1.863-3, 1.863-8(b)(3)(ii), 1.864-6(c)(2), and 1.865-3 in their entirety for the taxable year, and once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.864-5 as contained in 26 CFR part 1 revised as of April 1, 2020.

Par. 9. Section 1.864-6 is amended as follows:

a. Revising paragraph (c)(2).

b. Revising paragraph (c)(3).

c. Adding paragraph (c)(4).

The revisions and additions read as follows:

§1.864-6 Income, gain, or loss attributable to an office or other fixed place of business in the United States.

* * * * *

(c) * * *

(2) *Special limitation in case of sales of goods or merchandise through U.S. office*. Notwithstanding paragraph (c)(1) of this section, the special rules described in this paragraph (c)(2) apply with respect to a sale of goods or merchandise specified in §1.864-5(b)(3), to which paragraph (b)(3)(i) of this section does not apply. In the case of a nonresident alien with a tax home within the United States, as defined in section 911(d)(3), the amount of income from the sale of goods or merchandise that is properly allocable to the individual's U.S. office is determined under §1.865-3(d).

(3) *Examples*. The application of this paragraph (c) may be illustrated by the following examples—

(i) *Example 1. Sales of produced inventory through a U.S. sales office*. Individual A, who is a nonresident alien within the meaning of section 7701(b)(1)(B) and has a tax home in the United States, manufactures machinery in a foreign country and sells the machinery outside the United States through A's sales office in the United States for use in foreign countries. A is not a nonresident within the meaning of section 865(g)(1)(B). Therefore, §1.865-3 does not apply to A's sale of the machinery, except to the extent provided in paragraph (c)(2) of this section. Title to the property sold is transferred to the foreign purchaser outside the United States, but no office or other fixed place of business of A in a foreign country materially participates in the sale made through A's U.S. office. By reason of its

sales activities in the United States, A is engaged in business in the United States during the taxable year. During the taxable year, A derives a total income of $250,000x from these sales. Under paragraph (c)(2) of this section, the amount of income that is allocable to A's U.S. office is determined under §1.865-3(d)(2). The taxpayer does not allocate income from the sale under the books and records method described in §1.865-3(d)(2)(ii). Thus, 50 percent of A's foreign source income of $250,000x, plus any additional income allocable based on the location of production activities under §§1.865-3(d)(2)(i) and 1.863-3 (in this case, $0x), is effectively connected for the taxable year with the conduct of A's U.S. trade or business, or $125,000x.

(ii) *Example 2. Sales of inventory purchased and resold through a U.S. sales office by a nonresident alien with a tax home in the United States*. Individual B, who is a nonresident alien within the meaning of section 7701(b)(1)(B) and has a tax home in the United States, has an office in a foreign country that purchases merchandise and sells it through B's sales office in the United States for use in various foreign countries, with title to the property passing outside the United States. B is not a nonresident within the meaning of section 865(g)(1)(B). Therefore, §1.865-3 does not apply to B's sale of the merchandise, except to the extent provided in paragraph (c)(2) of this section. No other office of B materially participates in these sales made through its U.S. office. By reason of its sales activities in the United States, B is engaged in business in the United States during the taxable year. During the taxable year, B derives income of $300,000x from these sales made through its U.S. sales office. All of B's income from these sales is foreign source as B purchases the merchandise outside the United States and title to the merchandise also passes outside the United States. The amount of income properly allocable to B's U.S. office determined under §1.865-3(d)(3) is $300,000x, and thus $300,000x is effectively connected for the taxable year with the conduct of B's U.S. trade or business.

(iii) *Example 3. Foreign sales office also materially participates in sale*. The facts are the same as in paragraph (c)(3)(ii) of this section (the facts in *Example 2*), except that B also has an office in a foreign country that is a material factor in the realization of income from the sales made through B's U.S. office. No income from the sale of merchandise is allocable to B's U.S. sales office for the taxable year, by reason of paragraph (b)(3)(i) of this section, and thus none of the $300,000x is effectively connected for the taxable year with the conduct of B's U.S. trade or business.

(iv) *Example 4. Sales of inventory purchased and resold through a U.S. sales office by a foreign corporation*. The facts are the same as in paragraph (c)(3)(ii) of this section (the facts in *Example 2*), except that B is a foreign corporation. B is a nonresident within the meaning of section 865(g)(1)(B). The income from such sales will be sourced in accordance with §1.865-3(a) and (d)(3).

(4) *Applicability date*. Paragraph (c)(2) of this section applies to taxable years ending on or after December 23, 2019. However, a taxpayer may apply paragraph (c)(2) of this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) apply paragraph (c)(2) of this section and §§1.863-1(b), 1.863-2(b), 1.863-3, 1.863-8(b)(3)(ii), 1.864-5(a) and (b), and 1.865-3 in their entirety for the taxable year, and once applied, the taxpayer and all persons related to the taxpayer (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years. For regulations generally applicable to taxable years ending before December 23, 2019, see §1.864-6 as contained in 26 CFR part 1 revised as of April 1, 2020.

Par. 10. Section 1.865-3 is added to read as follows:

§1.865-3 Source of gross income from sales of personal property (including inventory property) by a nonresident attributable to an office or other fixed place of business in the United States.

(a) *In general*. Notwithstanding any provision of section 861 through 865 or other regulations in this part, this section provides the sole sourcing rules for gross income, gain, or loss from section 865(e)(2) sales. Gross income, gain, or loss from a section 865(e)(2) sale is U.S. source income to the extent that the gross income, gain, or loss is properly allocable to an office or other fixed place of business in the United States under paragraph (d) of this section.

(b) *Exception for certain inventory sales for use, disposition or consumption outside the United States*. A section 865(e)(2) sale does not include any sale of inventory property that is sold for use, disposition, or consumption outside the United States if an office or other fixed place of business of the nonresident in a foreign country materially participates in the sale. See §1.864-6(b)(3) to determine whether a foreign office materially participates in the sale and whether the property was destined for foreign use.

(c) *Section 865(e)(2) sales*. For purposes of this section, a "section 865(e)(2) sale" is a sale of personal property by a nonresident, including inventory property, other than a sale described in paragraph (b) of this section, that is attributable to an office or other fixed place of business in the United States under the principles of section 864(c)(5)(B) as prescribed in §1.864-6(b)(1) and (2). In determining whether a nonresident maintains an office or other fixed place of business in the United States, the principles of section 864(c)(5)(A) as prescribed in §1.864-7 apply, including the rules of paragraph (d) of that section regarding the office or other fixed place of business of a dependent agent of the nonresident. For purposes of this section, "inventory property" has the meaning provided in section 865(i)(1), and "nonresident" has the meaning provided in section 865(g)(1)(B).

(d) *Amount of gross income, gain, or loss on sale of personal property properly allocable to a U.S. office*—(1) *In general*. Except as otherwise provided in paragraphs (d)(2) through (4) of this section, the amount of gross income, gain, or loss from a section 865(e)(2) sale that is properly allocable to an office or other fixed place of business in the United States is determined under the principles of §1.864-6(c)(1).

(2) *Produced inventory property*. Gross income, gain, or loss from a section 865(e)(2) sale of inventory property that is produced by the nonresident seller is properly allocable to an office or other fixed place of business in the United States or to production activities in accordance with the "50/50 method" described in paragraph (d)(2)(i) of this section. However, in lieu of the 50/50 method, the nonresident seller may elect to allocate the gross income, gain, or loss under the "books and records method" described in paragraph (d)(2)(ii)(A) of this section, provided that the nonresident satisfies all of the requirements described in paragraph (d)(2)(ii)(B) of this section to the satisfaction of the Commissioner. Gross income allocable to production activities under this paragraph (d)(2) is sourced in accordance with §1.863-3. For purposes of this paragraph (d)(2), the term "produced" includes created, fabricated, manufactured, extracted, processed, cured, and aged, as determined under the principles of §1.954-3(a)(4) (except for §1.954-3(a)(4)(iv)). See section 864(a) and §1.864-1.

(i) *The 50/50 method*. Fifty percent of the gross income, gain, or loss from a sec-

tion 865(e)(2) sale of inventory property that is produced by the nonresident seller is properly allocable to an office or other fixed place of business in the United States, and the remaining 50 percent of the gross income, gain, or loss is properly allocable to production activities (the "50/50 method").

(ii) *Books and records method*—(A) *Method*. Subject to paragraph (d)(2)(ii)(B) of this section, a nonresident may elect to determine the amount of its gross income, gain, or loss from the sale of inventory property produced by the nonresident seller that is properly allocable to production activities and sales activities for the taxable year based upon its books of account (the "books and records method"). The gross income, gain, or loss allocable to sales activities under this method is treated as properly allocable to an office or other fixed place of business in the United States and the remaining gross income, gain, or loss is treated as properly allocable to production activities.

(B) *Election and reporting rules*—(*1*) *In general*. A nonresident may not make the election described in paragraph (d)(2)(ii)(A) of this section unless the requirements of paragraphs (d)(2)(ii)(B)(*2*) through (*4*) of this section are satisfied. Once the election is made, the nonresident must continue to satisfy the requirements of paragraphs (d)(2)(ii)(B)(*2*) through (*4*) of this section until the election is revoked. If the nonresident fails to satisfy the requirements in paragraphs (d)(2)(ii)(B)(*2*) through (*4*) of this section to the satisfaction of the Commissioner, the Commissioner may, in its sole discretion, apply the 50/50 method described in paragraph (d)(2)(i) of this section.

(*2*) *Books of account*. The nonresident must establish that it, in good faith and unaffected by considerations of tax liability, regularly employs in its books of account a detailed allocation of receipts and expenditures that, under the principles of section 482, clearly reflects both the amount of the nonresident's gross income, gain, or loss from its inventory sales that are attributable to its sales activities, and the amount of its gross income, gain, or loss from its inventory sales that are attributable to its production activities. For purposes of this paragraph (d)(2)(ii)(B)(*2*), section 482 principles apply as if the office or other fixed place of business in the United States were a separate organization, trade, or business (and, thus, a separate controlled taxpayer) from the nonresident (whether or not payments are made between the United States office or other fixed place of business and the nonresident's other offices, and whether or not the nonresident itself would otherwise constitute an organization, trade, or business).

(*3*) *Required records*. The nonresident must prepare and maintain the records described in paragraph (d)(2)(ii)(B)(*2*) of this section, which must be in existence when its return is filed. The nonresident must also prepare an explanation of how the allocation clearly reflects the nonresident's gross income, gain, or loss from production and sales activities under the principles of section 482. The nonresident must make available the explanation and records of the nonresident (including for the office or other fixed place of business in the United States and the offices or branches that perform the production activities) upon request of the Commissioner, within 30 days, unless some other period is agreed upon between the Commissioner and the nonresident.

(*4*) *Making and revoking the books and records method election; disclosure of election*. Except as otherwise provided in publications, forms, instructions, or other guidance, a nonresident makes or revokes the election to apply the books and records method by attaching a statement to its original timely filed Federal income tax return (including extensions) providing that it elects, or revokes the election, to apply the books and records method described in paragraph (d)(2)(ii)(A) of this section. For nonresidents making the election, the statement must provide that the nonresident has prepared the records described in paragraph (d)(2)(ii)(B)(*2*) and (*3*) of this section.

(*5*) *Limitation on revoking the books and records method election*. Once made, the books and records method election continues until revoked. An election cannot be revoked, without the consent of the Commissioner, for any taxable year beginning within 48 months of the last day of the taxable year for which the election was made.

(3) *Purchased inventory property*. All gross income, gain, or loss from a section 865(e)(2) sale of inventory property that is both purchased and sold by a nonresident is properly allocable to an office or other fixed place of business in the United States.

(4) *Depreciable personal property*. Gain from a section 865(e)(2) sale of depreciable personal property (as defined in section 865(c)(4)) is allocated under paragraphs (d)(4)(i) and (ii) of this section.

(i) The gain not in excess of the depreciation adjustments, if any, is properly allocable to an office or other fixed place of business in the United States to the same extent that the gain would be allocated to sources within the United States under the rules of section 865(c)(1). The remaining gain not in excess of the depreciation adjustments, if any, is allocated to sources without the United States in accordance with section 865(c)(1). However, notwithstanding the preceding sentences, if the property was predominantly used in the United States, within the meaning of section 865(c)(3)(B)(i), for a particular taxable year, all of the gain not in excess of depreciation for that year is properly allocable to the office or other fixed place of business in the United States.

(ii) The gain in excess of the depreciation adjustments, if any, is treated as if such gain was from the sale of inventory and the amount allocable to an office or fixed place of business in the United States is determined under paragraph (d)(2) or (3) of this section, as applicable.

(e) *Determination of source of taxable income*. For rules allocating and apportioning expenses to gross income effectively connected with the conduct of a trade or business of a foreign corporation in the United States (including gross income, gain, or loss sourced under this section), see section 882(c)(1). For rules allocating and apportioning expenses to gross income, gain, or loss effectively connected with the conduct of a trade or business of a nonresident alien in the United States (including gross income, gain, or loss sourced under this section), see section 873(a).

(f) *Export trade corporations*. This section does not apply for purposes of defining an export trade corporation under section 971(a).

(g) *Applicability date*. This section applies to taxable years ending on or after December 23, 2019. However, a nonresident may apply this section in its entirety for taxable years beginning after December 31, 2017, and ending before December 23, 2019, provided that the nonresident and all persons related to the nonresident (within the meaning of section 267 or 707) apply this section and §§1.863-1(b), 1.863-2(b), 1.863-3, 1.863-8(b)(3)(ii), 1.864-5(a) and (b), and 1.864-6(c)(2) in their entirety for the taxable year, and once applied, the nonresident and all persons related to the nonresident (within the meaning of section 267 or 707) continue to apply these regulations in their entirety for all subsequent taxable years.

§1.937-2 [Amended]

Par. 11. In §1.937-2 amend paragraph (d) by removing "§1.863-3(f)" and adding in its place "§1.863-3(e)".

§1.937-3 [Amended]

Par. 12. In §1.937-3 amend paragraph (d) by removing "§1.863-3(f)" and adding in its place "§1.863-3(e)".

Par. 13. Section 1.1502-13 is amended by revising paragraph (c)(7)(ii)(N) to read as follows:

§1.1502-13 Intercompany transactions.

* * * * *

(c) * * *

(7) * * *

(ii) * * *

(N) *Example (14): Source of income under section 863*—(*1*) *Intercompany sale*—(*i*) *Facts*. S manufactures inventory property solely in the United States and recognizes $75x of income on sales to B in Year 1. B conducts further production activity on the inventory property solely in Country Y and then sells the inventory property to X in Country Y and recognizes $25x of income on the sale to X, also in Year 1. Title passes from S to B, and from B to X, in Country Y. Assume that applying §1.863-3 on a single entity basis, including the formula for apportionment of multi-country production activities by reference to the basis of production assets, $10x would be treated as foreign source income and $90x would be treated as U.S. source income (that is, 10 percent of the production occurred outside the United States and 90 percent occurred within the United States, as measured by the basis of assets used in production activities with respect to the property). Assume further that, on a separate entity basis, S would have $0x of foreign source income and $75x of U.S. source income and all of B's $25x of income would be foreign source income.

(*ii*) *Analysis*. Under the matching rule, both S's $75x intercompany item and B's $25x corresponding item are taken into account in Year 1. In determining the source of S and B's income from the inventory property sales, the attributes of S's intercompany item and B's corresponding item are redetermined to the extent necessary to produce the same effect on consolidated taxable income (and consolidated tax liability) as if S and B were divisions of a single corporation. See paragraph (c)(1)(i) of this section. On a single entity basis, S and B would have $10x that would be treated as foreign source income and $90x that would be treated as U.S. source income, but without application of this section (that is, on a separate entity basis), S would have $75x of U.S. source income and B would have $25x of foreign source income. Under paragraph (c)(4)(ii) of this section, a redetermined attribute must be allocated between S and B using a reasonable method. On a separate entity basis B would have only foreign source income and S would have only U.S. source income. Accordingly, under paragraph (c)(1)(i) of this section, $15x of B's $25x sales income that would be treated as foreign source income on a separate entity basis is redetermined to be U.S. source income.

(*2*) *Sale of property reflecting intercompany services or intangibles*—(*i*) *Facts*. S earns $10x of income performing services in the United States for B. B capitalizes S's fees into the basis of inventory property that it manufactures in the United States and sells to an unrelated person in Year 1 at a $90x profit, with title passing in Country Y. Assume that on a single entity basis, $100x is treated as U.S. source income and $0x is treated as foreign source income. Further assume that on a separate entity basis, S would have $10x of U.S. source income, and B would have $90x of U.S. source income, with neither having any foreign source income.

(*ii*) *Analysis*. Under the matching rule, S's $10x income and B's $90x income are taken into account in Year 1. In determining the source of S and B's income, the attributes of S's intercompany item and B's corresponding item are redetermined to the extent necessary to produce the same effect on consolidated taxable income (and consolidated tax liability) as if S and B were divisions of a single corporation. Because the results are the same on a single entity basis and a separate entity basis ($100x of U.S. source income and $0x of foreign source income), the attributes are not redetermined under paragraph (c)(1)(i) of this section.

Sunita Lough,
Deputy Commissioner for Services and Enforcement.

Approved: September 21, 2020

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

(Filed by the Office of the Federal Register on December 10, 2020, 8:45 a.m., and published in the issue of the Federal Register for December 11, 2020, 85 F.R. 79837)

Part III

Work Opportunity Tax Credit (WOTC) Transition Relief under Internal Revenue Code § 51

Notice 2020-78

I. PURPOSE

This notice provides transition relief for certain employers claiming the Work Opportunity Tax Credit (WOTC) under § 51 of the Internal Revenue Code (Code). Specifically, this notice provides transition relief by extending the 28-day deadline for employers described in section IV of this notice to request certification from a designated local agency (DLA)[1] that an individual hired on or after January 1, 2018, and before January 1, 2021, is a member of the designated community resident targeted group or the qualified summer youth employee targeted group.

II. BACKGROUND

Section 51(a) of the Code provides the WOTC to employers based on a percentage of qualified wages paid during the taxable year. Section 51(b) defines "qualified wages" as wages paid or incurred by an employer during the taxable year to an individual who is certified as a member of a targeted group. Section 51(d)(1) lists the targeted groups, which include designated community residents defined in § 51(d)(5) and qualified summer youth employees defined in § 51(d)(7).

Pursuant to § 51(d)(13)(A), an individual is not treated as a member of a targeted group unless (1) on or before the day the individual begins work, the employer obtains certification from the DLA that the individual is a member of a targeted group, or (2) the employer completes a pre-screening notice on or before the day the individual is offered employment and submits such notice to the DLA to request certification not later than 28 days after the individual begins work. The Form 8850 (Pre-Screening Notice and Certification Request for the Work Opportunity Credit) is the pre-screening notice that must be submitted to the DLA to request certification.

Among the requirements for an individual to be certified as a member of a targeted group described in § 51(d)(5) or (7), the individual must be certified by the DLA as having a principal place of residence within an empowerment zone[2] where the individual continuously resides. Any wages paid to or incurred on behalf of the individual for services rendered while the individual is not living at a residence within an empowerment zone do not qualify for the WOTC.

III. TAXPAYER CERTAINTY AND DISASTER TAX RELIEF ACT AMENDMENTS

The WOTC has been subject to several legislative extensions and modifications since its enactment by § 1201 of the Small Business Job Protection Act of 1996, Pub. L. 104-188, 110 Stat. 1755 (August 20, 1996). Most recently, the Taxpayer Certainty and Disaster Tax Relief Act (Act), enacted as Division Q of the Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, 133 Stat. 2534, 3226 (December 19, 2019), amended § 51 of the Code to extend the WOTC through December 31, 2020.

Specifically, § 143 of the Act amended § 51(c)(4) of the Code to extend the WOTC for an employer that hires individuals who are members of a targeted group with respect to wages paid or incurred to such individuals who begin work for the employer after December 31, 2019, but not after December 31, 2020.

In addition, § 118(a) of the Act amended § 1391(d)(1) of the Code to provide that any designation of an empowerment zone ends on the earliest of (1) December 31, 2020, (2) the termination date designated by the State and local governments as provided for in their nomination, or (3) the date the appropriate Secretary[3] revokes the designation. Section 118(b) of the Act provides that where a nomination of an empowerment zone included a termination date of December 31, 2017, § 1391(d)(1)(B) of the Code will not apply with respect to such designation if, after the date of the enactment of the Act, the entity that made such nomination amends the nomination, in such manner as the Secretary of the Treasury may provide, to provide for a new termination date. The amendment made by § 118(a) of the Act applies to taxable years beginning after December 31, 2017.

On June 11, 2020, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) issued Revenue Procedure 2020-16, 2020-27 IRB 10, to explain how a State or local government is deemed to extend the termination date designated in an empowerment zone nomination until December 31, 2020. Revenue Procedure 2020-16 provides that if a State or local government did not submit a written declination to the IRS by August 10, 2020, and if the appropriate Secretary did not revoke the empowerment zone designation, then the termination date provided in that empowerment zone nomination is automatically extended to December 31, 2020.

IV. GRANT OF RELIEF

Because the Act extended the WOTC through December 31, 2020, and retroactively extended the period for which an empowerment zone designation is in effect under § 1391(d)(1) from December 31, 2017, to December 31, 2020, employers need additional time to comply with the DLA certification requirements of § 51(d)(13)(A)(ii).

The Treasury Department and the IRS understand that, due to the expiration of empowerment zone designations at the

[1] Section 51(d)(12) provides that a "DLA" is a State employment security agency (sometimes referred to as a State Workforce Agency) established in accordance with 29 U.S.C. §§ 49-49n.
[2] Section 1393(b) provides that for purposes of the Code, the term "empowerment zone" means an area designated as such under § 1391.
[3] Section 1393(a)(1) of the Code defines the term "appropriate Secretary" as the Secretary of Housing and Urban Development (in the case of any nominated area designated under § 1391 that is located in an urban area as defined in § 1393(a)(3)) or the Secretary of Agriculture (in the case of any nominated area designated under § 1391 that is located in a rural area as defined in § 1393(a)(2)).

end of 2017 and the uncertainty of whether empowerment zone designations would be extended, some employers that hired members of targeted groups described in § 51(d)(5) and (7) may not have submitted Form 8850 to the DLA within 28 days of the individual beginning work. To be eligible for the relief provided by this notice, an employer that did not submit Form 8850 to the DLA within 28 days of an individual beginning work must submit the completed Form 8850 to the DLA by the date set forth in section IV.A of this notice.

In addition, the Treasury Department and the IRS are aware that some employers that hired members of targeted groups described in § 51(d)(5) and (7) may have submitted Form 8850 to the DLA within 28 days of an individual beginning work, regardless of the expiration of the empowerment zone designations. To be eligible for the relief provided by this notice, an employer that submitted Form 8850 to the DLA and subsequently received a denial letter from the DLA by reason of the expiration of the empowerment zone designations must re-submit the completed Form 8850 by the date set forth in section IV.A of this notice. In the event that an employer submitted Form 8850 to the DLA and was not issued a denial letter by the DLA, the employer does not need to re-submit Form 8850 to be eligible for the relief provided in this notice.

For these reasons, the Treasury Department and the IRS are providing employers with additional time to submit Form 8850 with the DLAs in accordance with the following timeframe.

A. Additional time for employers that hired or hire designated community residents or qualified summer youth employees between January 1, 2018, and December 31, 2020, to submit a completed Form 8850 to the DLA.

An employer that hired an individual who is a designated community resident described in § 51(d)(5), or a qualified summer youth employee described in § 51(d)(7), and who began work for that employer on or after January 1, 2018, and before January 1, 2021, will be considered to have satisfied the requirements of § 51(d)(13)(A)(ii), whether or not the employer submitted the completed Form 8850 to the DLA within 28 days of the individual beginning work for the employer, if the employer submits the completed Form 8850 to the DLA to request certification no later than January 28, 2021. In the event that an employer submitted Form 8850 to the DLA and was not issued a denial notification by the DLA, the employer does not need to re-submit Form 8850.

B. Application of 28-day requirement to individuals hired on or after January 1, 2021.

An employer that hires a member of a targeted group described in § 51(d)(5) or (7), who begins work for the employer on or after January 1, 2021, is not eligible for the transition relief described in this notice with respect to that new employee.

V. EFFECTIVE DATE

The effective date of this notice is December 11, 2020.

VI. DRAFTING INFORMATION

The principal author of this notice is Christopher Dellana of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). For further information regarding the WOTC, contact Mr. Dellana at (202) 317-5500 (not a toll-free number).

Guidance on Sections 102 and 103 of the SECURE Act With Respect to Safe Harbor Plans

Notice 2020-86

I. PURPOSE

This notice provides guidance in the form of questions and answers with respect to §§ 102 and 103 of Division O of the Further Consolidated Appropriations Act, 2020, Pub. L. 116-94, 133 Stat. 2534 (2019), known as the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act).[1] Section 102 of the SECURE Act increases the 10 percent cap for automatic enrollment safe harbor plans. Section 103 of the Secure Act eliminates certain safe harbor notice requirements for plans that provide for safe harbor nonelective contributions and adds new provisions for the retroactive adoption of safe harbor status for those plans. This notice is not intended to provide comprehensive guidance as to § 102 or 103 of the SECURE Act, but rather is intended to assist taxpayers by providing guidance on particular issues while the Treasury Department and the IRS develop regulations to fully implement these sections of the SECURE Act. The Treasury Department and the IRS invite comments on the guidance in this notice and any other aspect of § 102 or 103 of the SECURE Act.

II. BACKGROUND

A. Exemptions from Actual Deferral Percentage (ADP) and Actual Contribution Percentage (ACP) Testing for Safe Harbor Plans

Under § 401(a)(4) of the Internal Revenue Code (Code) and § 1.401(a)(4)-1(b)(2), contributions or benefits provided under a qualified retirement plan must not be discriminatory in amount in favor of highly compensated employees (HCEs), as defined in § 414(q). Under § 401(k)(3) and § 1.401(k)-1(a)(4)(iv)(A) and (b)(1)(ii)(A), a § 401(k) plan satisfies this requirement if elective contributions made on behalf of eligible employees for a year satisfy the ADP test described in § 1.401(k)-2. Under § 401(m)(2) and § 1.401(m)-1(a)(1)(i) and (b)(1)(i), a similar test, the ACP test, applies to matching contributions and employee contributions.

As an alternative to satisfying the annual ADP test, a plan may satisfy the ADP safe harbor provisions of § 401(k)(12) (a

[1] On September 2, 2020, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) released Notice 2020-68, 2020-38 IRB 567, which provides guidance with respect to §§ 105, 107, 112, 113, 116, and 601 of the SECURE Act (and § 104 of Division M of the Further Consolidated Appropriations Act, 2020, known as the Bipartisan American Miners Act of 2019).

traditional safe harbor § 401(k) plan) or 401(k)(13) (a qualified automatic contribution arrangement (QACA) safe harbor § 401(k) plan). Similarly, as an alternative to satisfying the annual ACP test with respect to matching contributions, a plan may satisfy the ACP safe harbor provisions of § 401(m)(11) (a traditional safe harbor § 401(m) plan) or 401(m)(12) (a QACA safe harbor § 401(m) plan).

B. Safe Harbor Contributions

Under § 1.401(k)-3(a)(1), a traditional safe harbor § 401(k) plan is required to satisfy the safe harbor contribution requirements of either § 1.401(k)-3(b) (safe harbor nonelective contributions) or 1.401(k)-3(c) (safe harbor matching contributions) for the plan year. Under § 1.401(k)-3(b) and (c), contributions must be made on behalf of each eligible employee who is not an HCE (NHCE). Similarly, under § 1.401(m)-3(a)(1), a traditional safe harbor § 401(m) plan is required to satisfy the safe harbor contribution requirements of either § 1.401(m)-3(b), which cross-references the safe harbor nonelective contribution requirements of § 1.401(k)-3(b), or 1.401(m)-3(c), which cross-references the safe harbor matching contribution requirements of § 1.401(k)-3(c), for the plan year.

Under § 1.401(k)-3(a)(2), a QACA safe harbor § 401(k) plan is required to satisfy the safe harbor contribution requirements of § 1.401(k)-3(k) for the plan year. Under § 1.401(k)-3(k)(1), a QACA safe harbor § 401(k) plan must satisfy either the safe harbor nonelective contribution requirements of § 1.401(k)-3(b) or the safe harbor matching contribution requirements of § 1.401(k)-3(c), as modified by § 1.401(k)-3(k)(2) and (3). Similarly, under § 1.401(m)-3(a)(2), a QACA safe harbor § 401(m) plan is required to satisfy the safe harbor requirements of § 1.401(k)-3, including the safe harbor contribution requirements of § 1.401(k)-3(k).

Subject to certain requirements, a plan that provides for safe harbor contributions also may provide for contributions that are not safe harbor contributions. For example, a traditional safe harbor § 401(k) plan that provides for safe harbor nonelective contributions may also provide for either (1) a discretionary matching contribution of four percent of safe harbor compensation that would not need to satisfy the ACP test because the contribution satisfies the requirements of § 1.401(m)-3(d) (including the limits on matching rate increases, matching contributions, and matching rates on behalf of HCEs as compared to matching rates on behalf of NHCEs), or (2) a discretionary matching contribution in excess of four percent of safe harbor compensation that would need to satisfy the ACP test because the contribution does not satisfy the limit on discretionary matching contributions under § 1.401(m)-3(d)(3)(ii). Under § 1.401(k)-3(a)(3), neither of these types of additional matching contributions are referred to as safe harbor contributions.

C. Safe Harbor Notices

Section 401(k)(12)(D) generally requires a traditional safe harbor § 401(k) plan to provide a safe harbor notice to each eligible employee "within a reasonable period before any year." Section 1.401(k)-3(d)(3)(i) clarifies that a safe harbor notice must be "provided within a reasonable period before the beginning of the plan year (or, in the year an employee becomes eligible, within a reasonable period before the employee becomes eligible)." Section 401(m)(11)(A)(ii) requires a traditional safe harbor § 401(m) plan to satisfy the safe harbor notice requirements of § 401(k)(12)(D).

Section 401(k)(13)(E)(i) similarly requires a QACA safe harbor § 401(k) plan to provide a safe harbor notice to each eligible employee "within a reasonable period before each plan year," and § 1.401(k)-3(a)(2) requires a QACA safe harbor § 401(k) plan to satisfy the safe harbor notice requirements of § 1.401(k)-3(d), as modified by § 1.401(k)-3(k)(4). Section 401(m)(12)(A) requires a QACA safe harbor § 401(m) plan to satisfy the requirements for a QACA safe harbor § 401(k) plan.

D. Mid-Year Changes to Safe Harbor Plans and Notices

Section 1.401(k)-3(e)(1) provides that, in general, a plan will fail to satisfy the requirements of § 401(k)(12) and (13) and § 1.401(k)-3 unless plan provisions that satisfy the safe harbor plan rules of § 1.401(k)-3 are adopted before the first day of the plan year and remain in effect for an entire 12-month plan year. In addition, § 1.401(k)-3(e)(1) provides that, except as provided in § 1.401(k)-3(g) or in guidance of general applicability published in the Internal Revenue Bulletin, a plan that includes provisions that satisfy the safe harbor plan rules of § 1.401(k)-3 will not satisfy the nondiscrimination requirements for § 401(k) plans for a plan year if the plan is amended to change those provisions during the plan year. Section 1.401(m)-3(f) includes similar rules for safe harbor § 401(m) plans.

Under § 1.401(k)-3(g), a plan that provides for safe harbor contributions for a plan year may be amended during the plan year to reduce or suspend future safe harbor matching contributions or safe harbor nonelective contributions if the plan is also amended to provide that the ADP test will be satisfied for the entire plan year in which the reduction or suspension occurs (using the current year testing method) and if certain other requirements are satisfied. Section 1.401(k)-3(g)(1)(i) sets forth the requirements for a mid-year reduction or suspension of safe harbor matching contributions, and § 1.401(k)-3(g)(1)(ii) sets forth the requirements for a mid-year reduction or suspension of safe harbor nonelective contributions.

Under § 1.401(k)-3(g)(1)(i)(A) and (ii)(A), the employer must either (1) be operating at an economic loss (as described in § 412(c)(2)(A)) for the plan year, or (2) have included in the plan's safe harbor notice (as described in § 1.401(k)-3(d)) for the plan year a statement that the plan may be amended during the plan year to reduce or suspend safe harbor contributions and that the reduction or suspension will not apply earlier than 30 days after all eligible employees are provided notice of the reduction or suspension. Under § 1.401(k)-3(g)(1)(i)(C) and (ii)(C), the reduction or suspension of safe harbor contributions may be effective no earlier than the later of the date the amendment is adopted or 30 days after eligible employees are provided the supplemental notice described in § 1.401(k)-3(g)(2). Under § 1.401(k)-3(g)(1)(i)(D) and (ii)(D), eligible employees must be given a reasonable opportunity (including a reasonable period after receipt of the supplemental notice)

prior to the reduction or suspension of safe harbor contributions to change their cash or deferred elections and, if applicable, their employee contribution elections.

Section 1.401(m)-3(h) provides rules similar to those of § 1.401(k)-3(g) for a reduction or suspension of future safe harbor matching contributions or safe harbor nonelective contributions in a safe harbor § 401(m) plan.

Notice 2016-16, 2016-7 IRB 318, provides guidance on mid-year changes to safe harbor plans to the extent that conditions for those mid-year changes are not addressed in the Code or regulations (including conditions for reducing or suspending safe harbor contributions under §§ 1.401(k)-3(g) and 1.401(m)-3(h)). Section III.B of Notice 2016-16 provides that a change made to a safe harbor plan or to a plan's required safe harbor notice content does not fail to satisfy the requirements of §§ 1.401(k)-3 and 1.401(m)-3 merely because the change is a mid-year change, provided that: (1) if it is a mid-year change to a plan's required safe harbor notice content, the notice and election opportunity conditions in section III.C of Notice 2016-16 are satisfied; and (2) the mid-year change is not described in a list of prohibited mid-year changes in section III.D of Notice 2016-16. Section III.A of Notice 2016-16 defines required safe harbor notice content as the information that is required by the safe harbor plan regulations to be provided in a plan's safe harbor notice. For example, a plan's safe harbor notice must describe any other contributions under the plan or matching contributions to another plan on account of elective contributions or employee contributions under the plan (including the potential for discretionary matching contributions) and the conditions under which such contributions are made. See § 1.401(k)-3(d)(2)(ii)(B).

E. Section 102 of the SECURE Act

For a QACA safe harbor § 401(k) plan, § 401(k)(13)(C) generally requires that each employee eligible to participate be treated as having elected to have the employer make elective contributions in an amount equal to a qualified percentage of compensation (subject to certain exceptions for employees who have made or make affirmative participation elections). The qualified percentage of compensation may be any percentage determined under the plan if such percentage is applied uniformly, does not exceed the maximum percentage specified in § 401(k)(13)(C)(iii), and satisfies certain minimum percentage requirements specified in § 401(k)(13)(C)(iii)(I) – (IV). For example, § 401(k)(13)(C)(iii)(I) provides that the qualified percentage must be at least three percent during the initial period ending on the last day of the first plan year that begins after the date on which the first automatic elective contribution is made with respect to an employee. Prior to the enactment of the SECURE Act, § 401(k)(13)(C)(iii) of the Code provided that the qualified percentage could not exceed 10 percent.

Section 102(a) of the SECURE Act amended § 401(k)(13)(C)(iii) of the Code to provide that the qualified percentage may not exceed 15 percent (or 10 percent during the initial period of automatic elective contributions described in § 401(k)(13)(C)(iii)(I)).

Section 102(b) of the SECURE Act provides that the amendments made by § 102 of the SECURE Act apply to plan years beginning after December 31, 2019.

F. Section 103 of the SECURE Act

Prior to the enactment of the SECURE Act, § 401(k)(12) required all traditional safe harbor § 401(k) plans to satisfy the safe harbor notice requirements of § 401(k)(12)(D), and § 401(k)(13) required all QACA safe harbor § 401(k) plans to satisfy the safe harbor notice requirements of § 401(k)(13)(E). In addition, § 401(k)(12) and (13) did not explicitly permit retroactive adoption of the safe harbor nonelective contribution requirements of § 401(k)(12)(C) (traditional) or 401(k)(13)(D)(i)(II) (QACA) for a plan year.[2]

Section 103(a) of the SECURE Act amended § 401(k)(12)(A) of the Code to eliminate the safe harbor notice requirements of § 401(k)(12)(D) for a traditional safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C). Section 103(a) of the SECURE Act also amended § 401(k)(13)(B) of the Code to eliminate the safe harbor notice requirements of § 401(k)(13)(E) for a QACA safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(13)(D)(i)(II).

Section 103(a) of the SECURE Act did not amend § 401(m)(11) or 401(m)(12) of the Code. Thus, § 401(m)(11)(A)(ii) continues to require all traditional safe harbor § 401(m) plans to satisfy the safe harbor notice requirements of § 401(k)(12)(D). Section 401(m)(12)(A) also continues to require all QACA safe harbor § 401(m) plans to satisfy the requirements for a QACA safe harbor § 401(k) plan. However, § 103(a) of the SECURE Act eliminated the safe harbor notice requirements of § 401(k)(13)(E) of the Code for a QACA safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(13)(D)(i)(II).

Section 103(b) of the SECURE Act added new § 401(k)(12)(F) of the Code to permit a plan to be amended after the beginning of a plan year to provide that the safe harbor nonelective contribution requirements of § 401(k)(12)(C) will apply for the plan year, provided that: (1) the amendment is adopted before the 30th day before the close of the plan year (or before the last day under § 401(k)(8)(A) for distributing excess contributions for the plan year if the safe harbor nonelective contribution for the plan year is at least four percent of each employee's compensation); and (2) the plan did not provide, at any time during the plan year, for safe harbor matching contributions under § 401(k)(12)(B) (traditional) or 401(k)(13)(D)(i)(I) (QACA) for the plan year.

Section 103(c) of the SECURE Act likewise amended the QACA safe harbor § 401(k) plan rules of § 401(k)(13) of the

[2] Although § 401(k)(12) and (13) did not explicitly permit retroactive adoption of safe harbor nonelective contribution requirements, §§ 1.401(k)-3(f) and 1.401(m)-3(g) permit a plan that provides for the use of the current year testing method to be retroactively amended to adopt a safe harbor design for the plan year, using safe harbor nonelective contributions, if certain additional requirements are met (including contingent and follow-up notice requirements).

Code to add new § 401(k)(13)(F), which provides rules similar to those of § 401(k)(12)(F).

Section 103(d) of the SECURE Act provides that the amendments made by § 103 of the SECURE Act apply to plan years beginning after December 31, 2019.

III. GUIDANCE REGARDING SECTION 102 OF THE SECURE ACT (INCREASE IN 10 PERCENT CAP FOR AUTO-ENROLLMENT SAFE HARBOR)

Q-1. In order to maintain its status as a QACA safe harbor § 401(k) plan, is a QACA safe harbor § 401(k) plan required, pursuant to § 102(a) of the SECURE Act, to increase the maximum qualified percentage of compensation used to determine automatic elective contributions?

A-1. No. The qualified percentage under a QACA safe harbor § 401(k) plan may be any percentage of compensation determined under the plan, as long as the percentage is applied uniformly, does not exceed the maximum percentage specified in § 401(k)(13)(C)(iii) (15 percent, or 10 percent during the initial period of automatic elective contributions described in § 401(k)(13)(C)(iii)(I)), and satisfies certain minimum percentage requirements specified in § 401(k)(13)(C)(iii)(I) – (IV).

Q-2. If a plan incorporates the maximum qualified percentage of § 401(k)(13)(C)(iii) by reference, will the plan fail to operate in accordance with its terms merely because the plan continues to apply the maximum qualified percentage of 10 percent that applied under § 401(k)(13)(C)(iii) of the Code before that section was amended by § 102(a) of the SECURE Act?

A-2. No. However, the plan would need to be amended on or before the plan amendment deadline determined under § 601(b) of the SECURE Act,[3] as described in Q&A G-1 of Notice 2020-68, to provide explicitly that the plan's maximum qualified percentage is 10 percent, retroactive to the first day of the first plan year beginning after December 31, 2019. If a plan incorporates the maximum qualified percentage of § 401(k)(13)(C)(iii) of the Code by reference and the plan is not amended on or before the plan amendment deadline determined under § 601(b) of the SECURE Act to provide a specific maximum qualified percentage, then the plan will be treated as providing for the maximum qualified percentage specified in § 401(k)(13)(C)(iii) of the Code, as amended by § 102(a) of the SECURE Act, effective as of the first day of the first plan year beginning after December 31, 2019. In this case, the plan will have failed to operate in accordance with its terms by applying the maximum qualified percentage of 10 percent that applied under § 401(k)(13)(C)(iii) of the Code before that section was amended by § 102(a) of the SECURE Act.

Q-3. What plan amendment timing rules apply to a plan amendment that increases the maximum qualified percentage of compensation used to determine automatic elective contributions to a percentage greater than 10 percent (but no greater than 15 percent) after the initial period of automatic elective contributions described in § 401(k)(13)(C)(iii)(I)?

A-3. In general, the plan amendment timing provisions of § 601 of the SECURE Act, as described in Q&A G-1 of Notice 2020-68, apply to a plan amendment adopted under § 102 of the SECURE Act. In addition, a plan may be amended to reflect § 102 of the SECURE Act after the applicable plan amendment deadline under § 601 of the SECURE Act, in accordance with the general discretionary amendment deadlines set forth in Rev. Proc. 2016-37, 2016-29 IRB 136, as most recently modified by Rev. Proc. 2020-40, 2020-38 IRB 575.

IV. GUIDANCE REGARDING SECTION 103 OF THE SECURE ACT (SAFE HARBOR NOTICE REQUIREMENTS AND RETROACTIVE SAFE HARBOR STATUS FOR PLANS THAT PROVIDE SAFE HARBOR NONELECTIVE CONTRIBUTIONS)

Q-4. How does § 103(a) of the SECURE Act affect the safe harbor notice requirements for a traditional safe harbor § 401(k) plan or a traditional safe harbor § 401(m) plan?

A-4. Section 103(a) of the SECURE Act amended the requirements for a traditional safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C) of the Code by eliminating the safe harbor notice requirements of § 401(k)(12)(D) (including the requirement under § 1.401(k)-3(d)(3)(i) to provide a safe harbor notice within a reasonable period before an employee becomes eligible). However, § 103(a) of the SECURE Act did not eliminate the safe harbor notice requirements of § 401(m)(11)(A) of the Code for a traditional safe harbor § 401(m) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C).

Thus, for example, if a traditional safe harbor § 401(k) plan satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C), but also provides non-safe harbor matching contributions that are structured to satisfy the requirements of § 1.401(m)-3(d) (and, therefore, are not required to satisfy the ACP test), then the plan still must satisfy the safe harbor notice requirements of § 401(m)(11)(A). On the other hand, if a traditional safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C) also provides non-safe harbor matching contributions that are not intended to satisfy the requirements of § 1.401(m)-3(d) (and, therefore, are required to satisfy the ACP test), then the plan need not satisfy the safe harbor notice requirements of either § 401(k)(12)(D) or 401(m)(11)(A).

Q-5. How does § 103(a) of the SECURE Act affect the safe harbor notice requirements for a QACA safe harbor § 401(k) plan or QACA safe harbor § 401(m) plan?

A-5. Section 103(a) of the SECURE Act amended the requirements for a QACA safe harbor § 401(k) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(13)(D)(i)(II) of the Code by eliminating the safe

[3] In general, for a qualified retirement plan that is not a governmental plan within the meaning of § 414(d) of the Code, or an applicable collectively bargained plan, the plan amendment deadline determined under § 601 of the SECURE Act is the last day of the first plan year beginning on or after January 1, 2022. The plan amendment deadline for a qualified governmental plan, as defined in § 414(d) of the Code, or for an applicable collectively bargained plan is the last day of the first plan year beginning on or after January 1, 2024.

harbor notice requirements of § 401(k)(13)(E) (including the requirement under § 1.401(k)-3(d)(3)(i) to provide a notice within a reasonable period before an employee becomes eligible). The amendments made by § 103(a) of the SECURE Act also result in the elimination of any safe harbor notice requirement under § 401(m)(12) of the Code for a QACA safe harbor § 401(m) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(13)(D)(i)(II). The result is different for a traditional safe harbor § 401(m) plan, as described in Q&A-4 of this notice, than for a QACA safe harbor § 401(m) plan because § 401(m)(11) specifically requires a traditional safe harbor § 401(m) plan to satisfy the safe harbor notice requirements of § 401(k)(12)(D), but § 401(m)(12)(A) merely requires a QACA safe harbor § 401(m) plan to satisfy the requirements for a QACA safe harbor § 401(k) plan.

Q-6. Does § 103(a) of the SECURE Act change any other requirements?

A-6. No. Section 103(a) of the SECURE Act does not change any other requirements that may apply to a plan that satisfies the safe harbor nonelective contribution requirements applicable to a traditional or QACA safe harbor § 401(k) plan under § 401(k)(12)(C) or 401(k)(13)(D)(i)(II) of the Code. For example, § 103(a) of the SECURE Act did not change the notice requirements under § 414(w)(4) of the Code for a plan that permits, pursuant to the eligible automatic contribution arrangement rules of § 414(w), an employee to elect to withdraw automatic elective contributions (and earnings) no later than 90 days after the date of the first elective contribution with respect to the employee under the eligible automatic contribution arrangement. Accordingly, the § 414(w)(4) notice requirements continue to apply even if the plan satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C) or 401(k)(13)(D)(i)(II).

As another example, § 103(a) of the SECURE Act did not change the requirement under § 1.401(k)-1(e)(2)(ii) that a cash or deferred arrangement (including an arrangement in a plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C) or 401(k)(13)(D)(i)(II) of the Code) provide an employee with an effective opportunity, determined based on all the relevant facts and circumstances, including the adequacy of notice of the availability of a cash or deferred election, to make (or change) a cash or deferred election at least once during each plan year.

Q-7. If a plan does not provide a safe harbor notice for a plan year beginning after December 31, 2019 (because, pursuant to § 103(a) of the SECURE Act and Q&A-4 or Q&A-5 of this notice, safe harbor notice requirements no longer apply to the plan), but the employer nevertheless provides a notice that includes a statement that the plan may be amended mid-year to reduce or suspend safe harbor nonelective contributions, as described in §§ 1.401(k)-3(g)(1)(ii)(A)(2) and 1.401(m)-3(h)(1)(ii)(A)(2), and that otherwise satisfies the requirements for a safe harbor notice, will the plan fail to satisfy the condition in § 1.401(k)-3(g)(1)(ii)(A)(2) or 1.401(m)-3(h)(1)(ii)(A)(2) that the statement regarding the possible mid-year reduction or suspension of safe harbor nonelective contributions be included in a safe harbor notice?

A-7. No. The plan will not fail to satisfy § 1.401(k)-3(g)(1)(ii)(A)(2) or 1.401(m)-3(h)(1)(ii)(A)(2) merely because the employer included the statement described in §§ 1.401(k)-3(g)(1)(ii)(A)(2) and 1.401(m)-3(h)(1)(ii)(A)(2) in a notice that otherwise satisfies the requirements for a safe harbor notice (rather than in an actual safe harbor notice).[4] Further, solely with respect to the first plan year beginning after December 31, 2020, a notice will be treated as satisfying the requirement under §§ 1.401(k)-3(d)(3) and 1.401(m)-3(e) that the notice be provided within a reasonable period before the beginning of the plan year if the notice is given to each eligible employee by the later of (1) 30 days before the beginning of the plan year, or (2) January 31, 2021. However, except as provided in Q&A-8 of this notice, the plan must satisfy all other requirements set forth in § 1.401(k)-3(g)(1)(ii) or 1.401(m)-3(h)(1)(ii), as applicable, in order to reduce or suspend safe harbor nonelective contributions during the plan year.

Q-8. If an employer amends a traditional or QACA safe harbor § 401(k) plan (or a traditional or QACA safe harbor § 401(m) plan) to reduce or suspend the plan's safe harbor nonelective contributions during a plan year, but later amends the plan to readopt the safe harbor nonelective contributions in accordance with § 401(k)(12)(F) or 401(k)(13)(F) for the entirety of the plan year, will the plan be required to satisfy the ADP or ACP test (as applicable) for the plan year or be subject to the top-heavy rules under § 416 for the plan year?

A-8. No. The retroactive plan amendment provisions of §§ 401(k)(12)(F) and 401(k)(13)(F) of the Code, as amended by § 103 of the SECURE Act, are not conditioned on whether a prior plan amendment reduced or suspended safe harbor nonelective contributions during the plan year. Accordingly, the plan will not be required to satisfy either § 1.401(k)-3(g)(1)(ii)(E) (ADP testing) or 1.401(m)-3(h)(1)(ii)(E) (ACP testing) for the plan year and, pursuant to § 416(g)(4)(H) of the Code, the plan will not be subject to the top-heavy rules under § 416 for the plan year.[5]

Q-9. If a plan is amended pursuant to § 401(k)(12)(F)(i)(II) (traditional) or 401(k)(13)(F)(i)(II) (QACA) to adopt safe harbor nonelective contributions of at least four percent of compensation for a plan year, and the safe harbor nonelective contributions are contributed to the plan after the tax filing deadline for the prior taxable year (including extensions) but before the last day under § 401(k)(8)(A) for distributing excess contributions for the plan year, are the safe harbor nonelective contributions deductible for the prior taxable year?

A-9. No. Section 404(a)(6) provides that a taxpayer will be deemed to have made a payment on the last day of the prior taxable year if the payment is on account of that taxable year and is made not later than the time prescribed by law for filing the return for that taxable year

[4] In addition, see section IV.A of Notice 2020-52, 2020-29 IRB 79, for certain temporary relief from the requirements of §§ 1.401(k)-3(g)(1)(ii)(A) and 1.401(m)-3(h)(1)(ii)(A).

[5] However, for a plan that terminates during the plan year and has a final plan year of less than 12 months, the guidance provided in this Q&A-8 does not change the requirements under § 1.401(k)-3(e)(4) or § 1.401(m)-3(f)(4).

(including extensions). Therefore, the safe harbor nonelective contributions are not deductible for the prior taxable year because they are contributed to the plan after the latest date permitted under § 404(a)(6) for a contribution to be deductible for the prior taxable year. However, the safe harbor nonelective contributions are deductible for the taxable year in which they are contributed to the plan, to the extent otherwise deductible under § 404.

Q-10. For plan years beginning after December 31, 2019, do the retroactive plan amendment requirements of § 401(k)(12)(F) or 401(k)(13)(F) of the Code, as amended by § 103 of the SECURE Act, apply to an amendment adopted during a plan year that adds the traditional or QACA safe harbor design set forth in § 401(k)(12) or 401(k)(13) of the Code for the plan year using safe harbor nonelective contributions (rather than the retroactive plan amendment rules in § 1.401(k)-3(f))?

A-10. Yes. Effective for plan years beginning after December 31, 2019, in order for a plan to be amended during a plan year to adopt the safe harbor design set forth in § 401(k)(12) or 401(k)(13) for the plan year using safe harbor nonelective contributions, the plan must satisfy the retroactive plan amendment requirements of § 401(k)(12)(F) or 401(k)(13)(F) of the Code, as amended by § 103 of the SECURE Act. Accordingly, the retroactive plan amendment rules of § 1.401(k)-3(f) no longer apply for those plan years.

Q-11. For plan years beginning after December 31, 2019, do the retroactive plan amendment requirements of § 401(k)(13)(F) of the Code, as amended by § 103 of the SECURE Act, apply to an amendment adopted during a plan year that adds the safe harbor design set forth in § 401(m)(12) of the Code (QACA) for the plan year using safe harbor nonelective contributions (rather than the retroactive plan amendment rules in § 1.401(m)-3(g))?

A-11. Yes. Effective for plan years beginning after December 31, 2019, in order for a plan to be amended during a plan year to adopt the safe harbor design set forth in § 401(m)(12) for the plan year using safe harbor nonelective contributions, the plan must satisfy the retroactive plan amendment requirements of § 401(k)(13)(F) of the Code, as amended by § 103 of the SECURE Act. Accordingly, the retroactive plan amendment rules of § 1.401(m)-3(g) no longer apply for those plan years.

Q-12. For plan years beginning after December 31, 2019, do the retroactive plan amendment requirements of § 401(k)(12)(F) of the Code, as amended by § 103 of the SECURE Act, apply to an amendment adopted during a plan year that adds the safe harbor design set forth in § 401(m)(11) of the Code (traditional) for the plan year using safe harbor nonelective contributions (rather than the retroactive plan amendment rules in § 1.401(m)-3(g))?

A-12. No. As described in Q&A-4 of this notice, § 103(a) of the SECURE Act did not eliminate the safe harbor notice requirements of § 401(m)(11)(A) of the Code for a traditional safe harbor § 401(m) plan that satisfies the safe harbor nonelective contribution requirements of § 401(k)(12)(C). Accordingly, a plan sponsor must comply with the retroactive plan amendment rules of § 1.401(m)-3(g) (including both the contingent and follow-up notice requirements under § 1.401(k)-3(f)) in order for the plan to qualify as a safe harbor design set forth in § 401(m)(11) after the beginning of the plan year using safe harbor nonelective contributions.

Q-13. What plan amendment timing rules apply to a plan amendment that is adopted after the beginning of a plan year to provide that the safe harbor nonelective contribution requirements of § 401(k)(12)(C) (traditional) or 401(k)(13)(D)(i)(II) (QACA) will apply for the plan year, in accordance with § 103(b) or (c) of the SECURE Act?

A-13. In general, the plan amendment timing provisions of § 601 of the SECURE Act, as described in Q&A G-1 of Notice 2020-68, apply to a plan amendment adopted under § 103(b) or (c) of the SECURE Act (even if the applicable plan amendment deadline under § 601 of the SECURE Act is later than the deadline under § 103(b) or (c) of the SECURE Act). In addition, a plan may be amended after the applicable plan amendment deadline under § 601 of the SECURE Act, in accordance with the plan amendment provisions of § 103(b) or (c) of the SECURE Act (which provide an exception to the general discretionary amendment deadlines set forth in Rev. Proc. 2016-37, as most recently modified by Rev. Proc. 2020-40).

V. SECTION 403(b) PLANS

This notice applies on similar terms to § 403(b) plans that apply the § 401(m) safe harbor rules pursuant to § 403(b)(12).

VI. REQUEST FOR COMMENTS

The Treasury Department and the IRS invite comments on the guidance in this notice and any other aspect of § 102 or 103 of the SECURE Act.

Comments should be submitted in writing on or before February 8, 2021, and should include a reference to Notice 2020-86. Comments may be submitted in one of two ways:

(1) Electronically via the Federal eRulemaking Portal at *www.regulations.gov* (type IRS-2020-0045 in the search field on the regulations.gov homepage to find this notice and submit comments).

(2) Alternatively, by mail to: Internal Revenue Service, Attn: CC:PA:LPD:PR (Notice 2020-86), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, D.C. 20044.

All commenters are strongly encouraged to submit public comments electronically. The IRS expects to have limited personnel available to process public comments that are submitted on paper through mail. Until further notice, any comments submitted on paper will be considered to the extent practicable. The Treasury Department and the IRS will publish for public availability any comment submitted electronically, and to the extent practicable on paper, to its public docket.

VII. DRAFTING INFORMATION

The principal author of this notice is Kara M. Soderstrom of the Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the Treasury Department and the IRS participated in the development of this guidance. For further information regarding this notice, contact Ms. Soderstrom at (202) 317-6799 (not a toll-free number).

Update for Weighted Average Interest Rates, Yield Curves, and Segment Rates

Notice 2020-87

This notice provides guidance on the corporate bond monthly yield curve, the corresponding spot segment rates used under § 417(e)(3), and the 24-month average segment rates under § 430(h)(2) of the Internal Revenue Code. In addition, this notice provides guidance as to the interest rate on 30-year Treasury securities under § 417(e)(3)(A)(ii)(II) as in effect for plan years beginning before 2008 and the 30-year Treasury weighted average rate under § 431(c)(6)(E)(ii)(I).

YIELD CURVE AND SEGMENT RATES

Section 430 specifies the minimum funding requirements that apply to single-employer plans (except for CSEC plans under § 414(y)) pursuant to § 412. Section 430(h)(2) specifies the interest rates that must be used to determine a plan's target normal cost and funding target. Under this provision, present value is generally determined using three 24-month average interest rates ("segment rates"), each of which applies to cash flows during specified periods. To the extent provided under § 430(h)(2)(C)(iv), these segment rates are adjusted by the applicable percentage of the 25-year average segment rates for the period ending September 30 of the year preceding the calendar year in which the plan year begins.[1] However, an election may be made under § 430(h)(2)(D)(ii) to use the monthly yield curve in place of the segment rates.

Notice 2007-81, 2007-44 I.R.B. 899, provides guidelines for determining the monthly corporate bond yield curve, and the 24-month average corporate bond segment rates used to compute the target normal cost and the funding target. Consistent with the methodology specified in Notice 2007-81, the monthly corporate bond yield curve derived from November 2020 data is in Table 2020-11 at the end of this notice. The spot first, second, and third segment rates for the month of November 2020 are, respectively, 0.53, 2.31, and 3.09.

The 24-month average segment rates determined under § 430(h)(2)(C)(i) through (iii) must be adjusted pursuant to § 430(h)(2)(C)(iv) to be within the applicable minimum and maximum percentages of the corresponding 25-year average segment rates. For plan years beginning before 2021, the applicable minimum percentage is 90% and the applicable maximum percentage is 110%. For plan years beginning in 2021, the applicable minimum percentage is 85% and the applicable maximum percentage is 115%. The 25-year average segment rates for plan years beginning in 2019, 2020, and 2021 were published in Notice 2018-73, 2018-40 I.R.B. 526, Notice 2019-51, 2019-41 I.R.B. 866, and Notice 2020-72, 2020-40 I.R.B. 789, respectively.

24-MONTH AVERAGE CORPORATE BOND SEGMENT RATES

The three 24-month average corporate bond segment rates applicable for December 2020 without adjustment for the 25-year average segment rate limits are as follows:

24-Month Average Segment Rates Without 25-Year Average Adjustment

Applicable Month	First Segment	Second Segment	Third Segment
December 2020	1.87	3.12	3.72

Based on § 430(h)(2)(C)(iv), the 24-month averages applicable for December 2020, adjusted to be within the applicable minimum and maximum percentages of the corresponding 25-year average segment rates, are as follows:

Adjusted 24-Month Average Segment Rates

For Plan Years Beginning In	Applicable Month	First Segment	Second Segment	Third Segment
2019	December 2020	3.74	5.35	6.11
2020	December 2020	3.64	5.21	5.94
2021	December 2020	3.32	4.79	5.47

30-YEAR TREASURY SECURITIES INTEREST RATES

Section 431 specifies the minimum funding requirements that apply to multiemployer plans pursuant to § 412. Section 431(c)(6)(B) specifies a minimum amount for the full-funding limitation described in § 431(c)(6)(A), based on the plan's current liability. Section 431(c)(6)(E)(ii)(I) provides that the interest rate used to calculate current liability for this purpose must be no more than 5 percent above and no more than 10 percent below the weighted average of the rates of interest on 30-year Treasury securities during the four-year period ending on the last day before the beginning of the plan year.

[1] Pursuant to § 433(h)(3)(A), the 3rd segment rate determined under § 430(h)(2)(C) is used to determine the current liability of a CSEC plan (which is used to calculate the minimum amount of the full funding limitation under § 433(c)(7)(C)).

Notice 88-73, 1988-2 C.B. 383, provides guidelines for determining the weighted average interest rate. The rate of interest on 30-year Treasury securities for November 2020 is 1.62 percent. The Service determined this rate as the average of the daily determinations of yield on the 30-year Treasury bond maturing in August 2050 determined each day through November 10, 2020 and the yield on the 30-year Treasury bond maturing in November 2050 determined each day for the balance of the month. For plan years beginning in December 2020, the weighted average of the rates of interest on 30-year Treasury securities and the permissible range of rates used to calculate current liability are as follows:

Treasury Weighted Average Rates

For Plan Years Beginning In	30-Year Treasury Weighted Average	Permissible Range 90% to 105%
December 2020	2.35	2.11 to 2.47

MINIMUM PRESENT VALUE SEGMENT RATES

In general, the applicable interest rates under § 417(e)(3)(D) are segment rates computed without regard to a 24-month average. Notice 2007-81 provides guidelines for determining the minimum present value segment rates. Pursuant to that notice, the minimum present value segment rates determined for November 2020 are as follows:

Minimum Present Value Segment Rates

Month	First Segment	Second Segment	Third Segment
November 2020	0.53	2.31	3.09

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 Paul Stern at 202-317-8702 (not toll-free numbers).

Table 2020-11
Monthly Yield Curve for November 2020
Derived from November 2020 Data

Maturity	*Yield*	*Maturity*	*Yield*	*Maturity*	*Yield*	*Maturity*	*Yield*	*Maturity*	*Yield*
0.5	0.15	20.5	2.93	40.5	3.11	60.5	3.18	80.5	3.21
1.0	0.27	21.0	2.94	41.0	3.11	61.0	3.18	81.0	3.21
1.5	0.38	21.5	2.94	41.5	3.11	61.5	3.18	81.5	3.21
2.0	0.46	22.0	2.95	42.0	3.11	62.0	3.18	82.0	3.21
2.5	0.53	22.5	2.96	42.5	3.12	62.5	3.18	82.5	3.21
3.0	0.57	23.0	2.96	43.0	3.12	63.0	3.18	83.0	3.21
3.5	0.63	23.5	2.97	43.5	3.12	63.5	3.18	83.5	3.21
4.0	0.69	24.0	2.97	44.0	3.12	64.0	3.18	84.0	3.21
4.5	0.77	24.5	2.98	44.5	3.13	64.5	3.18	84.5	3.21
5.0	0.86	25.0	2.98	45.0	3.13	65.0	3.18	85.0	3.22
5.5	0.97	25.5	2.99	45.5	3.13	65.5	3.19	85.5	3.22
6.0	1.09	26.0	2.99	46.0	3.13	66.0	3.19	86.0	3.22
6.5	1.22	26.5	3.00	46.5	3.13	66.5	3.19	86.5	3.22
7.0	1.36	27.0	3.00	47.0	3.14	67.0	3.19	87.0	3.22
7.5	1.50	27.5	3.01	47.5	3.14	67.5	3.19	87.5	3.22
8.0	1.63	28.0	3.01	48.0	3.14	68.0	3.19	88.0	3.22
8.5	1.76	28.5	3.02	48.5	3.14	68.5	3.19	88.5	3.22
9.0	1.89	29.0	3.02	49.0	3.14	69.0	3.19	89.0	3.22
9.5	2.00	29.5	3.03	49.5	3.14	69.5	3.19	89.5	3.22
10.0	2.11	30.0	3.03	50.0	3.15	70.0	3.19	90.0	3.22
10.5	2.21	30.5	3.04	50.5	3.15	70.5	3.19	90.5	3.22
11.0	2.30	31.0	3.04	51.0	3.15	71.0	3.20	91.0	3.22
11.5	2.39	31.5	3.05	51.5	3.15	71.5	3.20	91.5	3.22
12.0	2.46	32.0	3.05	52.0	3.15	72.0	3.20	92.0	3.22
12.5	2.53	32.5	3.06	52.5	3.15	72.5	3.20	92.5	3.22
13.0	2.59	33.0	3.06	53.0	3.16	73.0	3.20	93.0	3.22
13.5	2.64	33.5	3.06	53.5	3.16	73.5	3.20	93.5	3.22
14.0	2.68	34.0	3.07	54.0	3.16	74.0	3.20	94.0	3.22
14.5	2.72	34.5	3.07	54.5	3.16	74.5	3.20	94.5	3.23
15.0	2.75	35.0	3.07	55.0	3.16	75.0	3.20	95.0	3.23
15.5	2.78	35.5	3.08	55.5	3.16	75.5	3.20	95.5	3.23
16.0	2.81	36.0	3.08	56.0	3.16	76.0	3.20	96.0	3.23
16.5	2.83	36.5	3.08	56.5	3.17	76.5	3.20	96.5	3.23
17.0	2.85	37.0	3.09	57.0	3.17	77.0	3.20	97.0	3.23
17.5	2.87	37.5	3.09	57.5	3.17	77.5	3.21	97.5	3.23
18.0	2.88	38.0	3.09	58.0	3.17	78.0	3.21	98.0	3.23
18.5	2.89	38.5	3.10	58.5	3.17	78.5	3.21	98.5	3.23
19.0	2.90	39.0	3.10	59.0	3.17	79.0	3.21	99.0	3.23
19.5	2.91	39.5	3.10	59.5	3.17	79.5	3.21	99.5	3.23
20.0	2.92	40.0	3.10	60.0	3.17	80.0	3.21	100.0	3.23

Round 3 of Phase III of the § 48A Qualifying Advanced Coal Project Program

Notice 2020-88

SECTION 1. PURPOSE

Section 48A of the Internal Revenue Code (Code), as originally enacted by the Energy Policy Act of 2005, Pub. L. 109-58, 119 Stat. 594 (August 5, 2005), provided for the first phase of the Qualifying Advanced Coal Project Program by authorizing the allocation of $1.3 billion of credits (§ 48A Phase I Program). Section 111 of the Energy Improvement and Extension Act of 2008, Pub. L. 110-343, 122 Stat. 3765 (October 3, 2008), amended § 48A to provide for a second phase of the Qualifying Advanced Coal Project Program by authorizing the allocation of an additional $1.25 billion of credits (§ 48A Phase II Program). Pursuant to § 48A(d)(4), on August 13, 2012, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (Service) published Notice 2012-51, 2012-33 I.R.B. 150, to reallocate § 48A credits available after the conclusion of the § 48A Phase I and Phase II Programs (§ 48A Phase III Program). On March 9, 2015, the Treasury Department and the Service published Notice 2015-14, 2015-10 I.R.B. 722, announcing the 2015 reallocation round (Round 2) of the § 48A Phase III program.

This notice updates and amplifies the procedures for the allocation of § 48A Phase III credits by announcing the beginning of Round 3 of the § 48A Phase III Program.

To be considered in Round 3 of the § 48A Phase III Program, applications must be submitted to the Department of Energy (DOE) (Application for DOE Certification) and to the Service (Application for § 48A Certification) on or before March 28, 2021. See section 3 of this notice for additional rules regarding these applications.

SECTION 2. BACKGROUND

.01 Section 46 of the Code provides that the amount of the investment credit for any taxable year is the sum of the credits listed in § 46. That list includes the Qualifying Advanced Coal Project credit under § 48A.

.02 Section 48A(d)(1) provides that the Secretary of the Treasury or his delegate, in consultation with the Secretary of Energy, "shall establish a [Qualifying Advanced Coal Project Program] for the deployment of advanced coal-based generation technologies." The Treasury Department and the Service established the § 48A Phase I Program in Notice 2006-24, 2006-1 C.B. 595, as modified and updated by Notice 2007-52, 2007-1 C.B. 1456.

.03 Pursuant to § 48A(d)(3)(B)(i) and (ii), the § 48A Phase I Program provided for (i) $800 million of credits to be allocated to integrated gasification combined cycle (IGCC) projects and (ii) $500 million of credits to other advanced coal projects. The Service allocated § 48A Phase I Program credits through annual allocation rounds in 2006, 2007-2008, and 2008-2009, with a special allocation round in 2008.

.04 Pursuant to § 48A(d)(3)(B)(iii), the Treasury Department and the Service established the § 48A Phase II Program by issuing Notice 2009-24, 2009-1 C.B. 817, to allocate an additional $1.25 billion of credits for advanced coal-based generation technology projects. The Service allocated § 48A Phase II Program credits through two allocation rounds in 2009-2010 and 2011-2012.

.05 Pursuant to § 48A(d)(4), the Treasury Department and the Service issued Notice 2012-51 to establish the § 48A Phase III Program to reallocate $658.5 million of available § 48A Phase I Program credits. In Announcement 2013-43, 2013-2 C.B. 524, the Service announced that the total amount of $658.5 million of credits had been allocated, and, accordingly, the 2012-2013 allocation round would be the only allocation round in Phase III.

.06 The Treasury Department and the Service later determined that $1,104,000,000 of § 48A credits were available for reallocation due to forfeitures of previously allocated § 48A Phase I and Phase II Program credits and unallocated § 48A Phase II Program credits. Accordingly, the Treasury Department and the Service issued Notice 2015-14, 2015-10 I.R.B. 722, to establish Round 2 of the § 48A Phase III Program.

.07 After the completion of Round 2 of the § 48A Phase III Program, the Treasury Department and the Service completed another review and determined that $2,041,500,000 of § 48A credits are available for reallocation due to forfeitures of previously allocated § 48A credits. Accordingly, the Treasury Department and the Service have determined that an additional allocation round is appropriate, and this notice announces the beginning of Round 3 of the § 48A Phase III Program.

SECTION 3. SECTION 48A PHASE III PROGRAM

.01 Except as otherwise specifically provided in this notice, Round 3 of the § 48A Phase III Program will be conducted in the same manner and under the same procedures as provided under Notice 2012-51. This notice restates or references certain provisions in Notice 2012-51 as a convenience to taxpayers. The restatement or referencing of these provisions does not diminish the effect of provisions in Notice 2012-51 that are not restated or referenced.

.02 For Round 3 of the § 48A Phase III Program, § 48A Phase III credits in the amount of $2,041,500,000 are available for reallocation. The credits will not be separated into pools based on the type of projects or the type of primary feedstock.

.03 The § 48A Phase III credit for a taxable year is an amount equal to 30 percent of the qualified investment (as defined in § 48A(b)) for that taxable year in a Qualifying Advanced Coal Project (as defined in § 48A(c)(1) and § 48A(e)). This rule applies to both facilities that use an IGCC (as defined in § 48A(c)(7)) and facilities that use other advanced coal-based generation technologies (as defined in § 48A(f)).

.04 For Round 3 of the § 48A Phase III Program, the period to submit an Application for § 48A Certification begins on December 28, 2020, and ends on March 28, 2021. See section 3.07 of this notice for the date by which the Application for DOE Certification must be submitted to DOE. For purposes of determining the timeliness of submission of an Application for § 48A Certification by the Service, the rules of § 7502 apply.

.05 The Service will consider a project under Round 3 of the § 48A Phase III Program only if the Application for § 48A Certification for the project is submitted during the application period and DOE provides the DOE certification and ranking (if any) for the project on or before April 27, 2021.

.06 If an Application for DOE Certification does not include all of the information required by section 5.02 of Notice 2012-51, DOE may decline to accept the application. If an Application for § 48A Certification does not include all of the information listed in section 5.03 of Notice 2012-51, the application will not be accepted by the Service.

.07 For Round 3 of the § 48A Phase III Program, DOE will consider an Application for DOE Certification only if the application is postmarked on or before March 28, 2021. See section 5.02 of Notice 2012-51 and Appendix B to this notice for the information to be submitted to DOE in an Application for DOE Certification. Appendix B to this notice also provides the instructions and address for filing the Application for DOE Certification. DOE will determine the technical and economic feasibility of the project and, if the project is determined to be feasible, will provide a DOE certification for the project to the Service. If DOE certifies two or more projects, DOE also will rank each of the projects it certifies (for example, first, second, third, etc.) relative to other certified projects and credits will be allocated to projects based on DOE ranking. DOE will provide DOE certification for projects determined to be feasible and DOE ranking (if any) to the Service by April 27, 2021.

.08 By May 27, 2021, the Service will accept or reject the taxpayer's Application for § 48A Certification and will notify the taxpayer, by letter, of its decision.

.09 If the taxpayer's Application for § 48A Certification is accepted, the acceptance letter will state the amount of the credit allocated to the project. If a credit is allocated to a taxpayer's project, the taxpayer will be required to execute an agreement in the form set forth in Appendix A to this notice. By June 26, 2021, the taxpayer must return the executed agreement to the Service at the appropriate address listed in section 3.11 of this notice.

.10 By August 25, 2021, the Service will execute and return the agreement to the taxpayer. The executed agreement applies only to the accepted taxpayer.

.11 *Instructions and Address for Filing § 48A Application*. There is no fee for filing an Application for § 48A Certification. It should be marked: "SECTION 48A APPLICATION FOR CERTIFICATION." A taxpayer may submit the Application for § 48A Certification to the Service by U.S. mail or private delivery service to:

Internal Revenue Service
LB&I: Enterprise Activities Practice Area
N14W24200 Tower Place Suite 202
Waukesha, Wisconsin 53188

SECTION 4. EFFECT ON OTHER DOCUMENTS

Notice 2012-51, 2012-2 C.B. 150, and Notice 2015-14, 2015-10 I.R.B. 722, are amplified.

SECTION 5. EFFECTIVE DATE

This notice is effective upon publication in the Internal Revenue Bulletin.

SECTION 6. PAPERWORK REDUCTION ACT

The collection of information contained in this notice has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-2003.

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

The collections of information in this notice are in section 3 and Appendix B. This information is required to obtain an allocation of Qualifying Advanced Coal Project credits. This information will be used by the Service to verify that the taxpayer is eligible for an allocation of the Qualifying Advanced Coal Project credits. The collection of information is required to obtain a benefit. The likely respondents are business or other non-profit institutions.

The estimated total annual reporting burden is 550 hours.

The estimated annual burden per respondent varies from 70 to 150 hours, depending on individual circumstances, with an estimated average of 110 hours. The estimated number of respondents is 5.

The estimated annual frequency of responses is on occasion.

Books or 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, and subject to the disclosure of allocations provisions in § 48A(d)(5), tax returns and tax return information are confidential, as required by 26 U.S.C. § 6103.

SECTION 7. DRAFTING INFORMATION

The principal author of this notice is Brendan P. Coppinger of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice contact Mr. Coppinger on (202) 317-6853 (not a toll-free number).

APPENDIX A
AGREEMENT

[Insert taxpayer's name, address, and identifying number] ("Taxpayer") and the Commissioner of Internal Revenue ("Commissioner") make the following Agreement:

WHEREAS:

1. On or before March 28, 2021, Taxpayer submitted to the Internal Revenue Service ("Service"), an application for certification under Round 3 of the § 48A Phase III Program described in Notice 2020-88 ("Application for § 48A Certification").

2. Taxpayer's Application for § 48A Certification in Round 3 is for the project described below (the "Project"):

(a) The Project will use an advanced coal-based generation technology (as defined in § 48A(c)(2) and (f)).

(b) The Project will be located at [insert address or other identifying designation].

(c) The Project site in subsection (b) above may be changed only if the change is consistent with the objectives of the Qualifying Advanced Coal Project program, is requested by the taxpayer that received the credit allocation, and involves moving the Project site to improve the potential to capture and sequester CO_2 emissions, reduce costs of transporting feedstock, and serve a broader customer base. The Service will not agree to a project site change if the dollar amount of tax credits available to the taxpayer under § 48A would increase as a result of the site change or if the Project would not have been originally certified had such modification been included in the taxpayer's application.

(d) The Project is [insert either: "a new electric generation unit (as defined in § 48A(c)(6))"; "a retrofit of an existing electric generation unit (as defined in § 48A(c)(6))"; or "a repower of an existing electric generation unit (as defined in § 48A(c)(6))."]

(e) The Project will have a total nameplate generating capacity (as defined in section 3.02 of Notice 2012-51) of at least [insert number] megawatts.

(f) At all times at least 75 percent of the cumulative total fuel input (as defined in section 3.03(1) of Notice 2012-51) used during normal plant operations (as defined in section 3.03(2) of Notice 2012-51) for the Project will be coal (as defined in section 3.01 of Notice 2012-51).

3. On [insert date of acceptance letter issued under Notice 2020-88], the Service accepted Taxpayer's Application for § 48A Certification for the Project and allocated Qualifying Advanced Coal Project credit under § 48A in the amount of $[insert number] to the Project.

4. Taxpayer understands that if Taxpayer fails to satisfy any of the certification requirements in § 48A(e)(2) within the time specified in § 48A(d)(2)(D) (2 years from the date specified in WHEREAS clause #3), or if the Service does not issue a certification for the Project under Notice 2020-88**,** the § 48A Phase III credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 of § 48A Phase III is fully forfeited.

5. Taxpayer understands that if the Project fails to attain or maintain the separation and sequestration of CO_2 emissions required by § 48A(e)(1)(G), the § 48A Phase III Program credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 will be recaptured pursuant to § 50(a).

6. Taxpayer understands that if the Project is not placed in service by Taxpayer within 5 years of the date of issuance of the certification as determined under section 6.03 of Notice 2012-51, the § 48A Phase III credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 is fully forfeited. Taxpayer must provide evidence to the Service that the Project has been timely placed in service.

7. Taxpayer understands that if the plans for the Project change in any significant respect from the plans set forth in the Application for DOE Certification (as defined in section 5.02 of Notice 2012-51) and the Application for § 48A Certification (as defined in section 5.03 of Notice 2012-51) and, under section 7.01 of Notice 2012-51, the acceptance of Taxpayer's Application for § 48A Certification on the date specified in WHEREAS clause #3 is void, the § 48A Phase III credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 is fully forfeited.

8. Taxpayer understands that if the Project fails to satisfy any of the requirements in § 48A(e)(1)(A), (C), (D), (E), (F), and § 48A(i) for a Qualifying Advanced Coal Project or, during normal plant operations (as defined in section 3.03(2) of Notice 2012-51), fails to satisfy the requirement in § 48A(e)(1)(B) for a Qualifying Advanced Coal Project—

(a) at the time the Project is placed in service, § 48A Phase III credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 is fully forfeited; and

(b) after the Project is placed in service (and after satisfying all such requirements at the time the Project is placed in service), the Project ceases to be investment credit property and the recapture rules of § 50(a) apply.

9. Taxpayer understands that if at any time more than 25 percent of the cumulative total fuel input (as defined in section 3.03(1) of Notice 2012-51) used during normal plant operations (as defined in section 3.03(2) of Notice 2012-51) is not coal (as defined in section 3.01 of Notice 2012-51), the Project ceases to be investment credit property and the recapture rules of § 50(a) apply.

10. Taxpayer cannot claim the qualifying gasification project credit under § 48B for any qualified investment for which the Qualifying Advanced Coal Project credit is allowed under § 48A.

11. Taxpayer understands that if Taxpayer elects to claim the Qualifying Advanced Coal Project Credit on the qualified progress expenditures paid or incurred by Taxpayer during the taxable year(s) during which the Project is under construction and the Project ceases to be a Qualifying Advanced Coal Project (whether before, at the time, or after the Project is placed in service), rules similar to the recapture rules in § 50(a)(2)(A) through (D) apply.

12. This Agreement applies only to Taxpayer. Taxpayer must notify the Service within 90 days of the acquisition of the Project by any other person (a successor in interest). A successor in interest that plans to claim the § 48A credit allocated to the Project must request permission to execute a new agreement with the Service. If the request is granted, the new agreement must be executed no later than the due date (including extensions) of the successor in interest's Federal income tax return for the taxable year in which the transfer occurs. If the interest is acquired at or before the time the Project is placed in service and the successor in interest fails to execute a new agreement, the § 48A Phase III credit in the amount specified in WHEREAS clause #3 allocated to the Project in Round 3 is fully forfeited. If the interest is acquired after the time the Project is placed in service and the successor in interest fails to execute a new agreement, the Project ceases to be investment credit property and the recapture rules of § 50(a) apply.

NOW IT IS HEREBY DETERMINED AND AGREED FOR FEDERAL INCOME TAX PURPOSES THAT:

1. The total amount of the § 48A Phase III credit that Taxpayer will claim for the Project under this Agreement on account of the acceptance of Taxpayer's Application for § 48A Certification in Round 3 cannot exceed the amount specified in WHEREAS clause #3.

2. This Agreement does not express whether the Taxpayer has met the certification requirements under § 48A(e)(2) or other future requirements to receive tax credits under § 48A.

3. This Agreement is limited and applies only to Taxpayer. A successor in interest that plans to claim the § 48A credit allocated to the Project must request permission to execute a new agreement with the Service.

THIS AGREEMENT IS FINAL AND CONCLUSIVE EXCEPT:

1. The matter it relates to may be reopened in the event of fraud, malfeasance, or misrepresentation of a material fact;

2. It is subject to the Internal Revenue Code sections that expressly provide that effect be given to their provisions (including any stated exception for § 7122) notwithstanding any law or rule of law; and

3. If it relates to a tax period ending after the date of this Agreement, it is subject to any law enacted after such date, which applies to the tax period.

By signing, the parties certify that they have read and agreed to the terms of this Agreement.

Taxpayer: [insert name and identifying number]

By: _____ **Date Signed:** _____
[insert name]

Title: [insert title]
[insert taxpayer's name]

Commissioner of Internal Revenue

By: _____ **Date Signed:** _____

Title:

APPENDIX B
APPLICATION FOR DOE CERTIFICATION
REQUEST FOR SUPPLEMENTAL APPLICATION INFORMATION FOR DOE

The Internal Revenue Service ("Service") and the Department of Energy ("DOE") seek to certify Applications for DOE Certification and Applications for § 48A Certification that demonstrate a high likelihood of being successfully implemented by the applicants. To qualify, projects must be technically and economically feasible and use an appropriate clean coal technology.

This request for supplemental information:

- Describes the information to be provided by the applicant seeking a certification of feasibility from DOE, and
- Lists the evaluation criteria and Program Policy Factors to be used by DOE in the evaluation of an Application for DOE Certification. (For purposes of Appendix B, an Application for DOE Certification will be referred to as an "Application".)

If, after review by DOE, a project is determined to be feasible, DOE will provide a DOE certification of feasibility to the Service. The Service will then accept or reject the taxpayer's Application for § 48A Certification.

In conducting this evaluation DOE may utilize assistance and advice from qualified personnel from other Federal agencies and/or non-conflicted contractors. DOE will obtain assurances in advance from all evaluators that Application information shall be kept confidential and used only for evaluation purposes. DOE reserves the right to request clarifications and/or supplemental information from some or all applicants through written submissions and/or oral presentations, but is not required to do so.

Notice is given that DOE may determine whether or not to provide a certification of feasibility to the Service at any time after the Application has been received, without further exchanges or discussions. Therefore, all applicants are advised to submit their most complete and responsive Application.

Applications will not be returned.

A. General

This request, together with the information in relevant sections of Notice 2020-88 includes all the information needed to complete an Application. All Applications shall be prepared in accordance with this request in order to provide a standard basis for evaluation and to ensure that each Application will be uniform as to format and sequence.

Each Application should clearly demonstrate the applicant's capability, knowledge, and experience regarding the requirements described herein.

Applicants should fully address the requirements of Notice 2020-88, including Appendix B, and *not* rely on the presumed background knowledge of reviewers. DOE may eliminate without further consideration an Application that does not follow the instructions regarding the organization and content of the Application when the nature of the deviation and/or omission precludes meaningful review of the Application.

B. Unnecessarily Elaborate Applications

Unnecessarily elaborate brochures or other presentations beyond those sufficient to present a complete and effective Application are not desired. Elaborate artwork, graphics and pictures are neither required nor encouraged.

C. Procedures to Submit an Application for DOE Certification

An Application must include the information and documentation required by relevant sections of Notice 2020-88.

An Application will not be considered for Round 3 of the § 48A Phase III Program unless it is postmarked by March 28, 2021. One electronic version on a USB flash drive of the Application must be submitted to:

ATTN: 48A DOE Application
Stephanie Kennedy
M/S:922-204(D)
National Energy Technology Laboratory
626 Cochrans Mill Road
Pittsburgh, PA 15236

One electronic version of the Application must also be sent to the Service as part of the Application for § 48A Certification. The Application for § 48A Certification will not be considered in Round 3 unless it is submitted to the Service on or before March 28, 2021.

THE INFORMATION REQUIRED BY THIS REQUEST MUST BE SUBMITTED USING THE FORMAT AND THE HEADINGS OF THE "PROJECT INFORMATION MEMORANDUM" AS DESCRIBED BELOW.

To aid in evaluation, an Application shall be clearly and concisely written and logically assembled. All pages of each part shall be appropriately numbered and identified with the name of the applicant and the date.

The Application, including the Project Information Memorandum, MUST be formatted in one of the following software applications:

- Microsoft Word™ 2010 or later edition
- Microsoft Excel™ 2010 or later edition
- Adobe Acrobat™ PDF 7.0 or later edition

Financial models should be submitted using the Excel™ spreadsheet software product and must include working calculation formulas and assumptions.

The applicant is responsible for the integrity and structure of the electronic files. DOE will not be responsible for reformatting, restructuring or converting any files submitted in response to this request.

The Project Information Memorandum, *excluding Appendices*, shall not exceed seventy-five (75) pages. Pages in excess of the page limitation will not be considered for evaluation. All text shall be typed, single spaced, using 12-point font, 1-inch margins, and unreduced 8-1/2-inch by 11-inch pages. Illustrations and charts shall be legible with all text in legible font. Pages shall be sequentially numbered. Except as otherwise noted herein the page guidelines previously set forth constitute a limitation on the total amount of material that may be submitted for evaluation. No material may be incorporated in any Application by reference as a means to circumvent the page limitation.

D. Project Information Memorandum

1. Summary and Introduction

a. Description of the Project
b. Financing and ownership structure
c. Description of the main parties to the project, including background, ownership and related experience
d. Current project status and schedule to beginning of construction

2. Technology and Technical Information

Provide a description of the proposed technology, including sufficient supporting information (such as vendor guarantees, process flow diagrams, equipment descriptions, information on each major process unit and the total plant, compositions of major streams, and the technical plan for achieving the goals proposed for the project) as would be needed to allow DOE to confirm that the technical requirements of § 48A are met. Specifically, the applicant should:

- Provide evidence sufficient to demonstrate that the proposed technology meets the definition of "Advanced Coal-Based Generation Technology," either as integrated gasification combined cycle ("IGCC") technology, or other advanced coal-based electric generation technology meeting the heat rate requirement of 8530 Btu/kWh.
- For advanced coal-based electric generation:
  - The applicant must provide evidence sufficient to justify the actual heat rate and heat rate corrected to conditions specified in § 48A(f)(2).
  - For projects including existing units, the applicant must provide evidence sufficient to justify that the proposed technology meets heat rate requirements specified in § 48A(f)(3).
- Provide evidence sufficient to justify that the proposed project is designed to meet the following performance requirements:
  - SO_2 (subbituminous coal is 80% or more of fuel input): 99% removal or emissions not more than 0.04 lbs/MMBTU
  - SO_2 (subbituminous coal is not more than 80% of fuel input): 99% removal
  - SO_2 (for all projects other than subbituminous coal projects): 99% removal
    - NOx emissions……0.07 lbs / MMBTU
    - PM emissions……..0.015 lbs / MMBTU
    - Hg percent removal……90%
- Provide evidence sufficient to demonstrate that the project meets the requirements for Qualifying Advanced Coal Projects as specified under § 48A(e)(1) including:
  - The project will power a new electric generation unit or retrofit/repower an existing electric generation unit. At least 50% of the useful output of the project is electrical power.
  - The fuel for the project is at least 75% coal (as defined in § 48A(c)(4) and section 3.01 of Notice 2012-51), on an energy input basis.

- The project is located at one site and has a total nameplate electric power generating capacity (as defined in section 3.02 of Notice 2012-51) of at least 400 MW.
- The project includes equipment that separates and sequesters at least 70% of such project's total carbon dioxide ("CO_2") emissions. The CO_2 separation, capture, sequestration, and emission values shall be reported on metric tons per hour and metric tons per year basis under normal plant operating conditions. The CO_2 separation, capture and sequestration percentages shall be calculated based on the total CO_2 that would otherwise be released into the atmosphere as industrial emission of greenhouse gas ("CO_2 emissions").

3. Applicant's Capability to Accomplish the Technical Objectives

Provide a narrative supporting the applicant's capability to accomplish the technical objectives of the proposed project, including supporting documentation demonstrating that the applicant has assembled a team that is formally committed to participate in the proposed project. Provide information to support that the applicant has assembled a team with the skills and resources needed to implement the project as proposed. Provide signed agreements or letters from team members demonstrating that the proposed team members are fully committed to the project.

Provide information, including examples of prior similar projects completed by applicant, engineering-procurement-construction ("EPC") contractor, and suppliers of major subsystems or equipment, which support the capabilities of the applicant and its team members to design, construct, permit, and operate the facility. The applicant should demonstrate that the team members have a corporate history of successful completion of similar projects.

Provide information to support that key personnel of the applicant and its team members have knowledge, experience, and adequate degree of involvement to successfully implement the project.

Include the project status and relevant information from ongoing engineering activities. Also include in an appendix any engineering report or reports used by the applicant to develop the project and to estimate costs and operating performance. Include copies of any signed agreements to support project status claims regarding preliminary design studies, front-end engineering design ("FEED"), and EPC-type agreements.

4. Priority for Qualifying Advanced Coal Projects

The applicant must submit information sufficient for categorization and prioritization of projects for certification, including documentation pertaining to the following:

- High priority project factors:
  - Increased by-product utilization, if applicable.
  - Research partnership with an eligible educational institution as defined in § 48A(e)(3)(B)(iii), if applicable.
- Highest priority factor: Separation and sequestration percentage of total CO_2 emissions.

5. Site Control and Ownership

Provide evidence that demonstrates the overall feasibility of implementing the project at the proposed site.

Provide evidence that the applicant owns or controls a site in the United States of sufficient size to allow the proposed project to be constructed and operated on a long-term basis. Documentation such as a deed demonstrating the applicant owns the project site, a signed option to purchase the site from the site owner, or a letter of intent signed by the site owner and stating the site owner's intent to sell the site to the applicant should be provided.

Describe the current infrastructure at the site available to meet the needs of the project. Provide documentation supporting applicant's conclusion that the proposed site can fully meet all environmental, coal supply, water supply, transmission interconnect, and public policy requirements. Such documentation may include signed agreements, letters of intent, or term sheets relating to coal supply, water supply, and product (*e.g.* CO_2) transportation etc., and regulatory approvals supporting the key claims.

Provide detailed plans, schedules and status updates, particularly for sites with pre-existing conditions that could impact the proposed project. Pre-existing conditions may include, but are not limited to, sites with mandated environmental remediation efforts; brown-field sites that will require building demolition; or sites requiring substantial rerouting of existing roads, railroads, transmission lines or pipelines prior to the start of the project.

Applicants must select one "proposed site." However, projects with key physical or logistical elements that require close integration with another system for the project to succeed should provide information on all integrated systems regardless of where they are located.

Example 1: A power plant designed to operate exclusively on coal from a to-be-opened mine should provide supporting documentation for the new mine.

Example 2: An oxygen-blown IGCC plant planning to purchase oxygen from a third party who will construct a plant exclusively for this project should provide documentation for the oxygen supplier.

Example 3: An IGCC plant planning to sell CO_2 for enhanced oil recovery ("EOR") should provide an agreement for such a transaction indicating the annual CO_2 purchase quantity, expected project lifetime sales, CO_2 capacity of the site for EOR, and EOR site ownership.

This is not a comprehensive set of example projects or situations.

6. Utilization of Project Output

Provide a projection of the anticipated costs of electricity and other marketable by-products produced by the plant.

Provide documentation establishing that a majority of the output of the plant is reasonably expected to be acquired or utilized. Such documentation should be signed by authorizing officials of both the buyer and seller, and may include: Sales Agreements, Letters of Intent, Memoranda of Understanding, Option Agreements, and Power Purchase Agreements.

Describe any energy sales arrangements that exist or that may be contemplated (*e.g.,* a Power Purchase Agreement or Energy Sales Agreement) and summarize their key terms and conditions.

Include as an appendix any independent Energy Price Market Study that has been done in connection with this project, or if no independent market study has been completed, provide a copy of the applicant-prepared market study.

Identify and describe any firm arrangements to sell non-power output, such as CO_2, and provide any evidence of such arrangements. If the project produces a product in addition to power, include as an appendix any related market study of price and volume of sales expected for that product.

7. Project Economics

Describe the project economics and provide satisfactory evidence of economic feasibility as demonstrated through the financial forecast and the underlying project assumptions. The project economic and financial assumptions should be clearly stated and explained.

Show calculation of the amount of tax credit applied for based on allowable cost.

8. Project Development and Financial Plan

Provide the total project budget and major plant costs (*e.g.,* development, operating, capital, construction, and financing costs). Provide the estimated annual budget for and source of project development costs from the time of the Application until the beginning of construction, including legal, engineering, financial, environmental, overhead, and other development costs. Describe the overall approach to project development and financing sufficient to demonstrate project viability. Provide a complete explanation of the source and amount of project equity. Provide a complete explanation of the source and amount of project debt. Provide the audited financial statements for the most recently ended three fiscal years and quarterly interim financial statements for the current fiscal year (a) for the applicant, (b) for any of the project parties providing funding, and (c) for any third-party funding source. If the applicant or another party does not have audited financial statements, the applicant or the party should provide equivalent financial statements prepared by the applicant or the party, in accordance with Generally Accepted Accounting Principles, and certified as to accuracy and completeness by the Chief Financial Officer of the party providing the statements.

For internally financed projects, provide evidence that the applicant has sufficient assets to fund the project with its own resources. Identify any internal approvals required to commit such assets. Include in an appendix copies of any board resolution or other approval authorizing the applicant to commit funds and proceed with the project.

For projects financed through debt instruments either unsecured or secured by assets other than the project, provide evidence that the applicant has sufficient creditworthiness to obtain such financing along with a discussion of the status of such instruments. Identify any internal approvals required to commit the applicant to pursue such financing. Include in an appendix copies of any board resolution or other approval authorizing the applicant to commit to such financing.

For projects financed through investor equity contributions, describe the source and status of each contribution. Discuss each investor's financial capability to meet its commitments. Include in an appendix, copies of any executed investment agreements.

If financing through a public offering or private placement of either debt or equity is planned for the project, provide the expected debt rating for the issue and an explanation of applicant's justification for the rating. Describe the status of any discussions with prospective investment bankers or other financial advisors.

Include as an appendix copies of any existing funding commitments or expressions of interest from funding sources for the project.

For projects employing nonrecourse or limited recourse debt financing, provide a complete discussion of the approach to, and status of, such financing.

In an appendix: (1) provide an Excel™-based financial model of the project, with working formulas, so that review of the model calculations and assumptions may be facilitated; and (2) provide pro-forma project financial, economic, capital cost, and operating assumptions, including detail of all project capital costs, development costs, interest during construction, transmission interconnection costs, other operating expenses, and all other costs and expenses.

9. Project Contract Structure

Describe the current status of each of the agreements set forth below. Include as an appendix copies of the contracts or summaries of the key provisions of each of the following agreements:

- Power Purchase Agreement (if not fully explained in section 6 above).
- Coal Supply: describe the source and price of coal supply for the project. Include as an appendix any studies of coal supply price and amount that have been prepared. Include a summary of the coal supply contract and a signed copy of the contract.
- Coal Transportation: explain the arrangements for transporting coal, including costs.
- Operations & Maintenance Agreement: include a summary of the terms and conditions of the contract and a copy of the contract.
- Shareholders Agreement: summarize key terms and include the agreement as an appendix.
- Engineering, Procurement and Construction Agreement: describe the key terms of the existing or expected EPC contract arrangement, including firm price, liquidated damages, hold-backs, performance guarantees, etc.
- Water Supply Agreement: confirm the amount, source, and cost of water supply.
- Transmission Interconnection Agreement: explain the requirements to connect to the system and the current status of negotiations in this respect.
- If CO_2 is to be sold to a third party for sequestration, provide a Sales Agreement and provide specifics, such as CO_2 sales (metric tons per year), expected project lifetime sales (metric tons), potential CO_2 capacity of the site for sequestration (metric tons), technology and site suitability for sequestration, and sequestration site ownership and operation.

10. Permits Including Environmental Authorizations

Provide a complete list of all Federal, State, and local permits, including environmental authorizations or reviews, necessary to commence construction of the project.

Explain what actions have been taken to date to satisfy the required authorizations and reviews, and the status of each.

Provide a description of the applicant's plan to obtain and complete all necessary permits, and environmental authorizations and reviews.

11. Steam Turbine Purchase

If applicant plans to purchase a steam turbine or turbines for the project, indicate the prospective vendors for the turbine and explain the current status of purchase negotiations, and provide a timeline for negotiation and purchase with expected purchase date.

12. Project Schedule

Provide an overall project schedule which includes technical, business, financial, permitting and other factors to substantiate that the project will meet the 2-year project certification and 5-year placed-in-service requirement.

The project schedule should be comprehensive and provide sufficient detail to demonstrate how applicant will meet the certification and placed-in-service requirements. The schedule should demonstrate that the applicant understands the required tasks and has allowed realistic times for accomplishing the technical and financial tasks. The schedule should include the milestone accomplishments needed to obtain the financing for the project.

Applicants should document their progress toward meeting any completion of permitting deadline. Existing permits and permit applications must be specific to the project proposed. If existing permits are not specific for the proposed coal-based project (e.g. the permits are for oil-fired or natural-gas-based units), specific plans, procedures and schedules for reapplying, modifying and/or renegotiating permits should be provided. Any local, State or Federal permitting schedules that may impact the overall project schedule should be included.

Applicant should document their progress toward obtaining engineering design information (i.e., FEED) to initiate permitting activities and to finalize the turbine generator purchase specification within the 2-year window. Most often, this requires final site, technology, and process selection. Signed FEED and/or EPC-type agreements, if available, should be provided.

13. Appendices

a. Copy of internal or external engineering reports.

b. Copy of site plan, together with evidence that applicant owns or controls a site. Examples of evidence would include a deed, or an executed contract to purchase or lease the site.

c. Information supporting applicant's conclusion that the site is fully acceptable as the project site with respect to environment, coal supply, water supply, transmission interconnect, and public policy reasons.

d. Power Purchase or Energy Sales Agreement.

e. Energy Market Study.

f. Market Study for non-power output.

g. Financial Model of project.

h. Audited financial statements for the applicant and other project funding sources for the most recently ended three fiscal years, and the unaudited quarterly interim financial statements for the current fiscal year.

i. Expressions of interest or commitment letters from funding sources.

j. For each project contract, if no contract currently exists, provide a summary of the expected terms and conditions.

k. List of all Federal, State, and local permits, including environmental authorizations or reviews, necessary to commence construction.

E. Evaluation Criteria

Advanced coal projects will be evaluated on whether they meet all the requirements of § 48A and this notice.

Technical: will be evaluated on whether the applicant has demonstrated the capability to accomplish the technical objectives.

Site: will be evaluated on the basis that the site requirement for ownership or control has been met, and that the site is suitable for the proposed project.

Economic: will be evaluated on whether the project has demonstrated economic feasibility, taking into consideration the submitted financial and project development and structural information and financial plan.

Schedule: will be evaluated on the applicant's ability to meet the 2-year project certification and the 5-year placed-in-service requirement.

F. Program Policy Factors to Be Used by DOE in the Evaluation of Applications

Section 48A identifies minimum requirements for consideration for the Qualifying Advanced Coal Project credit, including the project's technical feasibility, cost, and applicant's ability. In the event that there are more qualified (certifiable) Applications than there are available amount of tax credit, DOE will apply Program Policy Factors to rank eligible Advanced Coal Projects based on their ability to advance coal technology beyond its current state.

In ranking certified projects, highest priority will be given to the Primary Ranking Factor. Secondary and Tertiary Ranking Factors will be taken into account to rank projects that are not clearly differentiated on the basis of the Primary Ranking Factor, with higher priority given to Secondary Ranking Factors than to Tertiary Ranking Factors.

Primary Ranking Factor:

- Capture and sequestration of more than 70% CO_2 emissions. Only projects that capture and sequester 70% or more of the plant's CO_2 emissions will be considered for DOE certification. Among the certified projects, highest rankings will be given to projects with the greatest sequestration percentage of total separated CO_2 emissions.

Secondary Ranking Factors:

- Increased by-product utilization.
- Research partnership with an eligible educational institution as defined in § 48A(e)(3)(B)(iii).

Tertiary Ranking Factors:

- Presentation of other environmental, economic, or performance benefits.
- Higher plant efficiency.
- Geographic distribution of potential markets.
- The ratio of total nameplate generating capacity (as defined in section 3.02 of Notice 2012-51) to requested tax credit.
- Diversity of technology approaches and methods.

G. Supplemental Technical and Financial Guidance for Project Information Memorandum

Technology and Technical Information

It is important that the applicant select a specific advanced coal system for the project. Without that decision, it is difficult to provide the necessary specific design information needed for DOE to evaluate the project feasibility with respect to performance, emissions, outputs of major streams as well as capital and operating costs.

The applicant's capability to meet the legislated heat rate and/or environmental targets should be supported with design information, and/or vendor guarantees that are project, site and coal specific.

Project Economics

Applicants should demonstrate the project's economic feasibility and financial viability by providing a clear statement and explanation of the economic and financial assumptions made by the applicant, and a financial forecast for the project. The financial forecast should flow logically from the applicant's assumptions and be consistent with them. Applicants should include assumptions regarding financial and economic issues that may not be included in the project costs but have a direct impact on the project. The examples given in the "Site Control and Ownership" section are relevant here and their impact on the project economics should be discussed here.

Project Development and Financial Plan

The information provided by the applicant in this section should demonstrate that the applicant's financial plan for developing the project is feasible and that the applicant will have access to necessary financing. The applicant should explain the source and timing for obtaining all financing, including the project development costs. It is important that the applicant explain and provide evidence that it has the capacity to fund the pre-construction project development costs, together with a budget for and description of those costs. Note that financial information is required for the applicant and for any other funding source.

Project Contract Structure

This section requires that the applicant demonstrate an understanding of the commercial contracting process and show progress in establishing the framework of contracts and agreements that a project typically requires. Applicants should show that their intended contract structure is reasonable and that their assumptions relative to price, terms, and conditions are consistent with current market conditions. Evidence of final agreements, agreements in principle, or summaries of terms and conditions between the applicant and contract counterparties should be provided, if available.

26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.
(Also: Part 1, §§ 6662, 6694, 1.6662-4, 1.6694-2)

Rev. Proc. 2020-54

SECTION 1. PURPOSE

This revenue procedure updates Rev. Proc. 2019-42, 2019-49 I.R.B. 1298, and identifies circumstances under which the disclosure on a taxpayer's income tax return with respect to an item or position is adequate for the purpose of reducing the understatement of income tax under section 6662(d) of the Internal Revenue Code (relating to the substantial understatement aspect of the accuracy-related penalty), and for the purpose of avoiding the tax return preparer penalty under section 6694(a) (relating to understatements due to unreasonable positions) with respect to income tax returns. This revenue procedure does not apply with respect to any other penalty provisions (including but not limited to the disregard provisions of the section 6662(b)(1) accuracy-related penalty, the section 6662(i) increased accuracy-related penalty in the case of nondisclosed noneconomic substance transactions, and the section 6662(b)(7) and (j) increased accuracy-related penalty in the case of undisclosed foreign financial asset understatements). If this revenue procedure does not include an item or position, disclosure is adequate with respect to that item or position only if made on a properly completed Form 8275 or 8275-R, as appropriate, attached to the return for the year or to a qualified amended return. *See* Treas. Reg. § 1.6664-2(c) for information about qualified amended returns.

This revenue procedure applies to any income tax return filed on 2020 tax forms for a taxable year beginning in 2020, and to any income tax return filed in 2021 on 2020 tax forms for short taxable years beginning in 2021.

SECTION 2. CHANGES FROM REV. PROC. 2019-42

Editorial changes have been made throughout this revenue procedure. In addition, minor changes have been made in order to update the taxable years and tax forms to which this revenue procedure applies. No additional substantive changes have been made.

SECTION 3. BACKGROUND

.01 If section 6662 applies to any portion of an underpayment of tax required to be shown on a return, an amount equal to 20 percent of the portion of the underpayment is added to the tax. Under section 6662(b)(2), the penalty applies to the portion of any underpayment of tax that is attributable to a substantial understatement of income tax. The penalty rate increases to 40 percent in the case of gross valuation misstatements under section 6662(h), nondisclosed noneconomic substance transactions under section 6662(i), or undisclosed foreign financial asset understatements under section 6662(j).

.02 Generally, there is a substantial understatement of income tax if the amount of the understatement exceeds the greater of (i) 10 percent of the amount of tax required to be shown on the return for the taxable year or (ii) $5,000. Section 6662(d)(1). Section 6662(d)(1)(C) provides a special rule for taxpayers claiming a section 199A deduction. In the case of any taxpayer who claims any deduction allowed under section 199A for the taxable year, there is a substantial understatement of income tax if the amount of the understatement exceeds the greater of (i) 5 percent of the amount of tax required to be shown on the return for the taxable year or (ii) $5,000. Section 6662(d)(1)(B) provides a special rule for corporations. A corporation (other than an S corporation or a personal holding company) has a substantial understatement of income tax if the amount of the understatement exceeds the lesser of (i) 10 percent of the tax required to be shown on the return for a taxable year (or, if greater, $10,000) or (ii) $10,000,000. Generally, an understatement is the excess of the amount of tax required to be shown on the return for the taxable year over the amount of the tax that is shown on the return reduced by any rebate, where the excess is determined without regard to items to which the reportable transaction understatement penalty under section 6662A applies. Section 6662(d)(2)(A). For purposes of determining whether an understatement is substantial, the understatement determined under the general rule is increased by the aggregate amount of any reportable transaction understatements relating to the return. Section 6662A(e)(1)(A).

.03 In the case of an item not attributable to a tax shelter, if the taxpayer has a reasonable basis for the tax treatment of the item, the amount of the understatement is reduced by the portion of the understatement attributable to the item with respect to which the relevant facts affecting the item's tax treatment are adequately disclosed in the return or in a statement attached to the return. Section 6662(d)(2)(B)(ii).

.04 Section 6694(a) imposes a penalty on a tax return preparer who prepares a return or claim for refund reflecting an understatement of liability due to an "unreasonable position" if the tax return preparer knew (or reasonably should have known) of the position. A position (other than a position with respect to a tax shelter or a reportable transaction to which section 6662A applies) is generally treated as unreasonable unless (i) there is or was substantial authority for the position, or (ii) the position was properly disclosed in accordance with section 6662(d)(2)(B)(ii)(I) and had a reasonable basis. If the position is with respect to a tax shelter (as defined in section 6662(d)(2)(C)(ii)) or a reportable transaction to which section 6662A applies, the position is treated as unreasonable unless it is reasonable to believe that the position would more likely than not be sustained on the merits. *See* Notice 2009-5, 2009-3 I.R.B. 309, for interim penalty compliance rules for tax shelter transactions.

.05 In general, this revenue procedure provides guidance for determining when disclosure by return is adequate for purposes of section 6662(d)(2)(B)(ii) and section 6694(a)(2)(B). For purposes of this revenue procedure, the taxpayer must furnish all required information in accordance with the applicable forms and instructions, and the money amounts entered on these forms must be verifiable.

.06 This revenue procedure may apply to a return for a fiscal tax year that begins in 2020 and ends in 2021. This revenue procedure may also apply to a short year return for a period beginning in 2021 if the return is to be filed before the 2021 forms are available. (Note that individuals are generally not put in this position. The most frequent situation in which a short year arises is when filing a decedent's final return for a fractional part of a year. In that situation, the 2021 form will be available because the final return is due the fifteenth day of the fourth month following the close of the 12-month period that began with the first day of such fractional part of the year (meaning the due date is not accelerated). *See* Treas. Reg. § 1.6072-1(b). In the case of fiscal year and short year returns, the taxpayer must take into account any tax law changes that are effective for tax years beginning after December 31, 2020, even though these changes are not reflected on the form or instructions.

.07 This document does not take into account the effect of tax law changes effective for tax years beginning after December 31, 2020. If a line referenced in this revenue procedure is affected by such a change and requires additional reporting, a taxpayer may have to file Form 8275, *Disclosure Statement*, or Form 8275-R, *Regulation Disclosure Statement*, until the Service prescribes criteria for complying with the requirement.

.08 A complete and accurate disclosure of a tax position on the appropriate year's Schedule UTP, *Uncertain Tax Position Statement*, will be treated as if the corporation filed a Form 8275 or Form 8275-R regarding the tax position. The filing of a Form 8275 or Form 8275-R, however, will not be treated as if the corporation filed a Schedule UTP.

SECTION 4. PROCEDURE

.01 General

(1) Additional disclosure of facts relevant to, or positions taken with respect to, issues involving any of the items set forth below is unnecessary for purposes of reducing any understatement of income tax under section 6662(d) (except as otherwise provided in section 4.02(3) concerning Schedules M-1 and M-3), provided that the forms and attachments are completed in a clear manner and in accordance with their instructions.

(2) The money amounts entered on the forms must be verifiable, and the information on the return must be disclosed in the manner described below. For purposes of this revenue procedure, a number is verifiable if, on audit, the taxpayer can prove the origin of the amount (even if that number is not ultimately accepted by the Service) and the taxpayer can show good faith in entering that number on the applicable form.

(3) The disclosure of an amount as provided in section 4.02 below is not adequate when the understatement arises from a transaction between parties who are related within the meaning of section 267(b). If an entry may present a legal issue or controversy because of a related-party transaction, then that transaction and the relationship must be disclosed on a Form 8275 or Form 8275-R.

(4) When the amount of an item is shown on a line that does not have a preprinted description identifying that item (such as on an unnamed line under an "Other Expense" category), the taxpayer must clearly identify the item by including the description on that line. For example, to disclose a bad debt for a sole proprietorship, the words "bad debt" must be written or typed on the line of Schedule C (Form 1040 or 1040SR) that shows the amount of the bad debt. Also, for Schedule M-3 (Form 1120), Part II, line 25, Other income (loss) items with differences, or Part III, line 38, Other expense/deduction items with differences, the entry must provide descriptive language; for example, "Cost of non-compete agreement deductible not capitalizable," and the description must be provided on an attachment. Similarly, for other forms, if space limitations on a form do not allow for an adequate description, the description must be continued on an attachment.

(5) Although a taxpayer may literally meet the disclosure requirements of this revenue procedure, the disclosure will have no effect for purposes of the section 6662 accuracy-related penalty if the item or position on the return (1) does not have a reasonable basis as defined in Treas. Reg. § 1.6662-3(b)(3); (2) is attributable to a tax shelter item as defined in section 6662(d)(2)(C)(ii); or (3) is not properly substantiated or the taxpayer failed to keep adequate books and records with respect to the item or position.

(6) Disclosure also will have no effect for purposes of the section 6694(a) penalty as applicable to tax return preparers if the position is with respect to a tax shelter (as defined in section 6662(d)(2)(C)(ii)) or a reportable transaction to which section 6662A applies.

.02 Items

(1) Form 1040, Schedule A, *Itemized Deductions*:

(a) Medical and Dental Expenses: Complete lines 1 through 4, supplying all required information.

(b) Taxes: Complete lines 5 through 7, supplying all required information. Line 6 must list each type of tax and the amount paid.

(c) Interest Expenses: Complete lines 8 through 10, supplying all required information. This section 4.02(1)(c) does not apply to (i) amounts disallowed under section 163(d) unless Form 4952, *Investment Interest Expense Deduction*, is completed, or (ii) amounts disallowed under section 265.

(d) Charitable Contributions: Complete lines 11 through 14, supplying all required information and attaching all related forms required pursuant to statute or regulation.

(e) Casualty and Theft Losses: Complete Form 4684, *Casualties and Thefts*, and attach to the return. Each item or article for which a casualty or theft loss is claimed must be listed on Form 4684.

(2) Certain Trade or Business Expenses (including, for purposes of this section, the following six expenses as they relate to the rental of property):

(a) Casualty and Theft Losses: The procedure outlined in section 4.02(1)(e) must be followed.

(b) Legal Expenses: The amount claimed must be stated. This section does not apply, however, to amounts properly characterized as capital expenditures, personal expenses, or non-deductible lobbying or political expenditures, including amounts that are required to be (or that are) amortized over a period of years.

(c) Specific Bad Debt Charge-off: The amount written off must be stated.

(d) Officers' Compensation: Complete Form 1125-E, *Compensation of Officers*, when its instructions require completion. You must express the "percent of time devoted to business" as a numerical percentage, rather than as a non-numerical description such as "part" or "as needed." This section does not apply to "excess parachute payments," as defined in section 280G. This section does not apply to the extent that remuneration paid or incurred exceeds an applicable employee-remuneration deduction limitation under section 162(m).

(e) Repair Expenses: The amount claimed must be stated. This section does not apply, however, to any amount properly characterized as capital expenditures or personal expenses.

(f) Taxes (other than foreign taxes): The amount claimed must be stated.

(3) Differences in book and income tax reporting:

For Schedule M-1 and all Schedules M-3, including those listed in (a)-(f) below, the information provided must reasonably apprise the Service of the potential controversy concerning the tax treatment of the item. If the information provided does not so apprise the Service, a Form 8275 or Form 8275-R must be used to adequately disclose the item (*see* Part II of the instructions for those forms).

Note: An item reported on a line with a pre-printed description, shown on an attached schedule or "itemized" on Schedule M-1, may represent the aggregate amount of several transactions producing that item (*i.e.*, a group of similar items, such as amounts paid or incurred for supplies by a taxpayer engaged in business). In some instances, a potentially controversial item may involve a portion of the aggregate amount disclosed on the schedule. The Service will not be reasonably apprised of a potential controversy by the aggregate amount disclosed. In these instances, the taxpayer must use Form 8275 or Form 8275-R regarding that portion of the item.

Combining unlike items, whether on Schedule M-1 or Schedule M-3 (or on an attachment when directed by the instructions), will not constitute an adequate disclosure.

Additionally, taxpayers that file the Schedule M-3 (Form 1120), *Net Income (Loss) Reconciliation for Corporations With Total Assets of $10 Million or More*, may be required to complete Schedule B (Form 1120), *Additional Information for Schedule M-3 Filers*. For further information, see Who Must File in the General Instructions for Schedule B (Form 1120). Taxpayers that file the Schedule M-3 (Form 1065), *Net Income (Loss) Reconciliation for Certain Partnerships*, may be required to complete Schedule C (Form 1065), *Additional Information for Schedule M-3 Filers*. For further information, see Who Must File in the General Instructions for Schedule C (Form 1065). When required, these schedules are necessary to constitute adequate disclosure:

(a) Form 1065. Schedule M-3 (Form 1065), *Net Income (Loss) Reconciliation for Certain Partnerships*:

Part II (reconciliation of income (loss) items)	Column (a), *Income (Loss) per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference*; and Column (d), *Income (Loss) per Tax Return*
Part III (reconciliation of expense/deduction items)	Column (a), *Expense per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference;* and Column (d), *Deduction per Tax Return*

(b) Form 1120. (i) Schedule M-1, *Reconciliation of Income (Loss) per Books With Income per Return*.

(ii) Schedule M-3 (Form 1120), *Net Income (Loss) Reconciliation for Corporations With Total Assets of $10 Million or More*:

Part II (reconciliation of income (loss) items)	Column (a), *Income (Loss) per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference*; and Column (d), *Income (Loss) per Tax Return*
Part III (reconciliation of expense/deduction items)	Column (a), *Expense per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference;* and Column (d), *Deduction per Tax Return*

(c) Form 1120-L. Schedule M-3 (Form 1120-L), *Net Income (Loss) Reconciliation for U.S. Life Insurance Companies With Total Assets of $10 Million or More*:

Part II (reconciliation of income (loss) items)	Column (a), *Income (Loss) per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference*; and Column (d), *Income (Loss) per Tax Return*
Part III (reconciliation of expense/deduction items)	Column (a), *Expense per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference;* and Column (d), *Deduction per Tax Return*

(d) Form 1120-PC. Schedule M-3 (Form 1120-PC), *Net Income (Loss) Reconciliation for U.S. Property and Casualty Insurance Companies With Total Assets of $10 Million or More*:

Part II (reconciliation of income (loss) items)	Column (a), *Income (Loss) per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference*; and Column (d), *Income (Loss) per Tax Return*
Part III (reconciliation of expense/deduction items)	Column (a), *Expense per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference;* and Column (d), *Deduction per Tax Return*

(e) Form 1120-S. Schedule M-3 (Form 1120-S), *Net Income (Loss) Reconciliation for S Corporations With Total Assets of $10 Million or More*:

Part II (reconciliation of income (loss) items)	Column (a), *Income (Loss) per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference*; and Column (d), *Income (Loss) per Tax Return*
Part III (reconciliation of expense/deduction items)	Column (a), *Expense per Income Statement*; Column (b), *Temporary Difference*; Column (c), *Permanent Difference;* and Column (d), *Deduction per Tax Return*

(f) Form 1120-F. Schedule M-3 (Form 1120-F), *Net Income (Loss) Reconciliation for Foreign Corporations With Reportable Assets of $10 Million or More*:

Part II (reconciliation of income (loss) items)	Column (b), *Temporary Differences*; Column (c), *Permanent Differences*; and Column (d), *Other Permanent Differences for Allocations to Non-ECI and ECI*
Part III (reconciliation of expense/deduction items)	Column (b), *Temporary Differences*; Column (c), *Permanent Differences*; and Column (d), *Other Permanent Differences for Allocations to Non-ECI and ECI*

(4) Foreign Tax Items:

(a) International Boycott Transactions: Transactions disclosed on Form 5713, *International Boycott Report*; Schedule A, *International Boycott Factor (Section 999(c)(1))*; Schedule B, *Specifically Attributable Taxes and Income (Section 999(c)(2))*; and Schedule C, *Tax Effect of the International Boycott Provisions*, must be completed when required by their instructions.

(b) Treaty-Based Return Position: Transactions and amounts under section 6114 or section 7701(b) as disclosed on Form 8833, *Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)*, must be completed when required by its instructions.

(5) Other:

(a) Moving Expenses: Complete Form 3903, *Moving Expenses*, and attach to the return.

(b) Employee Business Expenses: Complete Form 2106, *Employee Business*

Expenses (for use only by Armed Forces reservists, qualified performing artists, fee-basis state or local government officials, and employees with impairment-related work expenses), and attach to the return. This section does not apply to club dues or to travel expenses for any non-employee accompanying the taxpayer on the trip.

(c) Fuels Credit: Complete Form 4136, *Credit for Federal Tax Paid on Fuels*, and attach to the return.

(d) Investment Credit: Complete Form 3468, *Investment Credit*, and attach to the return.

SECTION 5. EFFECTIVE DATE

This revenue procedure applies to any income tax return filed on a 2020 tax form for a taxable year beginning in 2020 and to any income tax return filed on a 2020 tax form in 2021 for a short taxable year beginning in 2021.

SECTION 6. DRAFTING INFORMATION

The principal author of this revenue procedure is Han Huang of the Office of the Associate Chief Counsel (Procedure & Administration). For further information regarding this revenue procedure, contact Branch 2 of Procedure and Administration at (202) 317-6844 (not a toll free number).

NOTE. This revenue procedure will be reproduced as the next revision of IRS Publication 1167, General Rules and Specifications for Substitute Forms and Schedules.

Rev. Proc. 2020-55

TABLE OF CONTENTS

Part 1
Introduction to Substitute Forms

Section 1.1 – Overview of Revenue Procedure 2020-55

1.1.1 Purpose

The purpose of this revenue procedure is to provide guidelines and general requirements for the development, printing, and approval of the 2020 substitute tax forms. Approval will be based on these guidelines. After review and approval, submitted forms will be accepted as substitutes for official IRS forms.

1.1.2 Unique Forms

Certain unique specialized forms require the use of other additional publications to supplement this publication. See *Part 4*.

1.1.3 Scope

The IRS accepts quality substitute tax forms that are consistent with the official forms and have no adverse impact on processing. The IRS Substitute Forms Program (the Program) administers the formal acceptance and processing of these forms nationwide. While this Program deals with paper documents, it also reviews for approval other processing and filing forms used in electronic filing.

Only those substitute forms that comply fully with these requirements are acceptable. This revenue procedure is updated as required to reflect pertinent tax year form changes and to meet processing and/or legislative requirements.

1.1.4 Forms Covered by This Revenue Procedure

The following types of forms are covered by this revenue procedure.

- IRS tax forms and their related schedules.
- Worksheets as they appear in the instructions.
- Applications for permission to file returns electronically and forms used as required documentation for electronically filed returns.
- Powers of Attorney.
- Over-the-counter estimated tax payment vouchers.
- Forms and schedules relating to partnerships, exempt organizations, and employee plans.

1.1.5 Forms Not Covered by This Revenue Procedure

The following types of forms are not covered by this revenue procedure.

- W-2 and W-3 (see Pub. 1141 for information on these forms).
- W-2c and W-3c (see Pub. 1223 for information on these forms).
- 941, Schedule B (Form 941), Schedule D (Form 941), Schedule R (Form 941), and 8974 (see Pub. 4436 for information on these forms).
- 1096, 1097-BTC, 1098 series, 1099 series, 3921, 3922, 5498 series, W-2G, and 1042-S (see Pub. 1179 for information on these forms).
- 1095-A, 1094-B, 1095-B, 1094-C, and 1095-C (see Pub. 5223 for information on these forms).

- 8027 (see Pub. 1239 for information on this form).
- Forms 1040-ES (OCR) and 1041-ES (OCR), which may not be reproduced.
- Forms 5500 (for more information on these forms, see the Department of Labor website at www.efast.dol.*gov*).
- Forms 5300, 5307, 8717, and 8905, bar-coded forms requiring separate approval.
- Forms used internally by the IRS.
- State tax forms.
- Forms developed outside the IRS.

1.1.6 Other Information Not Covered by This Revenue Procedure

The following information is not covered by this revenue procedure.

- Requests for information or documentation initiated by the IRS.
- General Instructions and Specific Instructions (these are not reviewed by the Program).

Section 1.2 – IRS Contacts

1.2.1 Where To Send Substitute Forms

Send your substitute forms for **approval** to the following offices (do not send forms with taxpayer data).

Form	Office and Address
5500	Check EFAST2 information at the Department of Labor website at *www.efast.dol.gov*
5300, 5307, 8717, and 8905	*Sandra.K.Barnes@irs.gov*
Software developer vouchers (see *Sections 2.3.7–2.3.9*)	Internal Revenue Service Attn: Doris Bethea 5000 Ellin Road, C5-226 Lanham, MD 20706 *Doris.E.Bethea@irs.gov*
ACA Forms 1094-B, 1095-B, 1094-C, and 1095-C (for more information, see Pub. 5223), and Schedule K-1 forms must be emailed for scannability testing	*scrips@irs.gov*
Schedule K-1 2-D bar-coded forms	For mailing addresses for sending Schedule K-1 2-D bar-coded forms for testing, see *Section 7.1.6*
All others covered by this publication (see *Section 1.1.4*)	Internal Revenue Service Attn: Substitute Forms Program SE:W:CAR:MP:P:TP 1111 Constitution Ave. NW, Room 6554 Washington, DC 20224 *substituteforms@irs.gov*

For questions about:

- Forms W-2 and W-3, refer to Pub. 1141, General Rules and Specifications for Substitute Forms W-2 and W-3;
- Forms W-2c and W-3c, refer to Pub. 1223, General Rules and Specifications for Substitute Forms W-2c and W-3c;
- Form 941 and Schedules B, D, and R, as well as Form 8974, refer to Pub. 4436, General Rules and Specifications for Substitute Form 941, Schedule B (Form 941), Schedule D (Form 941), Schedule R (Form 941), and Form 8974;
- Forms 1096, 1097-BTC, 1098, 1099, 3921, 3922, 5498, W-2G, and 1042-S, refer to Pub. 1179, General Rules and Specifications for Substitute Forms 1096, 1098, 1099, 5498, and Certain Other Information Returns;
- Forms 1095-A, 1094-B, 1095-B, 1094-C, and 1095-C, refer to Pub. 5223, General Rules and Specifications for Affordable Care Act Substitute Forms 1095-A, 1094-B, 1095-B, 1094-C, and 1095-C; and
- Form 8027, refer to Pub. 1239, Specifications for Electronic Filing of Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips.

Section 1.3 – What's New

1.3.1 What's New

The following changes have been made to this year's revenue procedure.

- **.01 Editorial changes.** We made editorial changes throughout and redundancies were eliminated as much as possible.
- **.02 Form 1099-NEC.** Beginning in tax year 2020, use Form 1099-NEC to report nonemployee compensation. Previously, nonemployee compensation was reported on Form 1099-MISC.
- **.03 Employment tax credits related to coronavirus (COVID-19).** The credits for qualified sick and family leave are reported on the quarterly payroll tax return, Form 941. In addition, the employee retention credit is a payroll tax credit reported on Form 941.

Section 1.4 – Definitions

1.4.1 Substitute Form

A tax form (or related schedule) that differs in any way from the official version and is intended to replace the form that is printed and distributed by the IRS. This term also covers those approved substitute forms exhibited in this revenue procedure.

1.4.2 Printed/ Preprinted Form

A form produced using conventional printing processes or a printed form which has been reproduced by photocopying or a similar process.

1.4.3 Preprinted Pin- Fed Form	A printed form that has marginal perforations for use with automated and high-speed printing equipment.
1.4.4 Computer- Prepared Substitute Form	A preprinted form in which the taxpayer's tax entry information has been inserted by a computer, computer printer, or other computer-type equipment.
1.4.5 Computer- Generated Substitute Tax Return or Form	A tax return or form that is entirely designed and printed using a computer printer on plain white paper. This return or form must conform to the physical layout of the corresponding IRS form, although the typeface may differ. The text should match the text on the officially printed form as closely as possible. Condensed text and abbreviations will be considered on a case-by-case basis. **Exception.** All jurats (perjury statements) must be reproduced verbatim.
1.4.6 Manually Prepared Form	A preprinted reproduced form in which the taxpayer's tax entry information is entered by an individual using a pen, pencil, typewriter, or other nonautomated equipment.
1.4.7 Graphics	Parts of a printed tax form that are not tax amount entries or required text. Examples of graphics are line numbers, captions, shadings, special indicators, borders, rules, and strokes created by typesetting, photographics, photocomposition, etc.
1.4.8 Acceptable Reproduced Form	A legible photocopy or an exact replica of an original form.
1.4.9 Supporting Statement (Supplemental Schedule)	A document providing detailed information to support a line entry on an official or approved substitute form and filed with (attached to) a tax return. **Note.** A supporting statement is not a tax form and does not take the place of an official form.
1.4.10 Specific Form Terms	The following specific terms are used throughout this revenue procedure in reference to all substitute forms: format, sequence, line reference, item caption, and data entry field.
1.4.11 Format	The overall physical arrangement and general layout of a substitute form.
1.4.12 Sequence	Sequence is an integral part of the total format requirement. The substitute form should show the same numeric and logical placement order of data as shown on the official form.
1.4.13 Line Reference	The line numbers, letters, or alphanumerics used to identify each captioned line on an official form. These line references are printed to the immediate left of each caption and/or data entry field.
1.4.14 Item Caption	The text on each line of a form, which identifies the data required.
1.4.15 Data Entry Field	Designated areas for the entry of data such as dollar amounts, quantities, responses, and checkboxes.
1.4.16 Advance Draft	A draft version of a new or revised form may be posted to the IRS website (*IRS.gov/DraftForms*) for information purposes. Substitute forms may be submitted based on these advance drafts, but any submitter that receives forms approval based on these early drafts is responsible for monitoring and revising forms to mirror any revisions in the final forms provided by the IRS.
1.4.17 Approval	Generally, approval could be in writing or assumed after 20 business days from our receipt for forms that have not been substantially changed by the IRS. This does not apply to newly created

or substantially revised IRS forms. However, the Program reserves the right to notify vendors of any inaccuracies even after 20 business days have lapsed.

1.4.18 National Association of Computerized Tax Processors (NACTP)

The National Association of Computerized Tax Processors (NACTP) is a nonprofit association that represents tax processing software and hardware developers, electronic filing processors, tax form publishers, tax processing service bureaus, and payroll processors. The association promotes standards in tax processing to advance efficient and effective tax filing. For more information, see *NACTP.org*.

Section 1.5 – Agreement

1.5.1 Important Stipulation of This Revenue Procedure

Any person or company who uses substitute forms and makes all or part of the changes specified in this revenue procedure agrees to the following stipulations.

- The IRS presumes that any required changes are made in accordance with these procedures and will not be disruptive to the processing of the tax return.
- Should any of the changes be disruptive to the IRS's processing of the tax return, the person or company agrees to accept the determination of the IRS as to whether the form may continue to be filed.
- The person or company agrees to work with the IRS in correcting noted deficiencies. Notification of deficiencies may be made by any combination of letter, email, or phone contact and may include the request for the resubmission of unacceptable forms.

1.5.2 Response Policy and Stipulations

The Program will email confirmation of receipt of your forms submission, if possible. Even if you do not receive emailed confirmation of receipt, you will receive an emailed "submission receipt," which will provide feedback on your submission. If the Program anticipates problems in completing the review of your submission within the 20-business-day period, the Program will send an interim email notifying you of the extended period for review.

Once the substitute forms have been approved by the Program, you can release them after the final versions of the forms have been issued by the IRS. Before releasing the forms, you are responsible for updating forms approved as draft and for making form changes we requested.

The policy has the following stipulations.

- This 20-business-day policy applies to electronic submissions only. It does not apply to substitute submissions mailed to the Program.
- The policy applies to submissions of 15 (optimal) or fewer items and submissions containing 75 pages or less. Submissions of more than 15 items may require additional review time.
- If you send a large number of submissions within a short period of time, processing may be delayed.
- Delays in processing could occur if the Program finds significant errors in your submission or has experienced an increase in submissions. The Program will send you an interim email in this case.
- Any anticipated problems in processing your submission within the 20-business-day period will generate an interim email on or about the 15th business day.

- If any significant inaccuracies are discovered after the 20-business-day period, the Program reserves the right to inform you and will require that changes be made to correct the inaccuracies.
- The policy does not apply to substantially revised forms or to new forms created by the IRS for which you have already made an initial submission.

Part 2
General Guidelines for Submissions and Approvals

Section 2.1 – General Specifications for Approval

2.1.1
Overview

If you produce any substitute tax forms that fully comply or follow the changes specifically outlined by the Program, then you can generate your own substitute forms without further approval. Also, if your substitutes have received approval in the past, and there are no substantial formatting or text changes for the tax year, then changes can be made without additional approval. If your changes are more extensive, you must get IRS approval before using substitute forms. More extensive changes include different font style, decreasing or increasing the font size of caption titles, adjusting or omitting format/layout elements, changing page orientation, repositioning line items, tables, and legends.

2.1.2
Email Submissions

The Program accepts submissions of substitute forms for review and approval via email. The email address is *substituteforms@irs.gov*. Please include the term "PDF Submissions" on the subject line.

Follow these guidelines.

- Email submission should include all the forms you wish to submit in one Portable Document Format (PDF) file. Do not email or attach each form individually.
- The emailed submission should include a maximum of 3 PDFs to include: a checksheet, a cover letter or accompanying statement, and a single PDF that includes all of the forms listed on your checksheet, cover letter, or accompanying statement.
- A submission should contain a maximum of 15 forms.
- An approval checksheet listing the forms you are submitting should always be included in the PDF file along with the forms. Excluding the checksheet can slow the reviewing process down, which can result in a delayed response to your submission. See a sample checksheet in *Exhibit B*.
- Optimize PDF files before submitting.
- The maximum allowable email attachment is 2.5 megabytes.
- The Program accepts zip files.
- To alleviate delays during the peak time of September through December, submit advance draft forms as early as possible.

If the guidelines are not followed, you may need to resubmit.

Emailing PDF submissions will not expedite review and approval. Submitting your substitute forms package via email is the preferred and suggested method for submitting forms for review. If, for some reason, you are not able to email your submission(s), you can mail your submission(s) to:

Internal Revenue Service
Attn: Substitute Forms Program
SE:W:CAR:MP:P:TP
1111 Constitution Ave. NW, Room 6554
Washington, DC 20224

2.1.3 Expediting the Process

Follow these basic guidelines for expediting the process.

- Always include a checksheet for the Program's response.
- Include an accompanying statement identifying most, if not all, of the deviations your substitute forms may include which the official IRS version of the form does not.
- Follow the guidance in this publication for general substitute form guidelines. Follow the guidance in specialized publications produced by the Program for other specific forms.
- To spread out the workload, send in draft versions of substitute forms when they are posted. **Note.** Be sure to make any changes to approved drafts before releasing final versions.

2.1.4 Schedules

Schedules are considered to be an integral part of a complete tax return. A schedule may be included as part of a form or printed separately.

2.1.5 Examples of Schedules That Must Be Submitted With the Return

Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, is an example of this situation. Its Schedules A through U have pages numbered as part of the basic return. For Form 706 to be considered for approval, the entire form, including Schedules A through U, as well as Schedule PC, must be submitted.

2.1.6 Examples of Schedules That Can Be Submitted Separately

Schedules C, D, and E for Form 1040 or 1040-SR are examples of schedules that can be submitted separately. Although printed by the IRS as a supplement to Form 1040 or 1040-SR, none of these schedules are required to be filed with Form 1040 or 1040-SR. These schedules may be separated from Form 1040 or 1040-SR and submitted as substitute forms.

2.1.7 Use and Distribution of Unapproved Forms

The IRS is continuing a program to identify and contact tax return preparers, forms developers, and software publishers who use or distribute unapproved forms that do not conform to this revenue procedure. The use of unapproved forms hinders the processing of the returns.

Section 2.2 – Highlights of Permitted Changes and Requirements

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2.2.1 Methods of Reproducing IRS Forms

There are methods of reproducing IRS printed tax forms suitable for use as substitutes without prior approval.

- You can photocopy most tax forms and use them instead of the official ones. The entire substitute form, including entries, must be legible.
- You can reproduce any current tax form as cut sheets, snap sets, and marginally punched, pin-fed forms as long as you use an official IRS version as the master copy.
- You can reproduce a form that requires a signature as a valid substitute form. Many tax forms (including returns) have a taxpayer signature requirement as part of the form layout. The jurat/ perjury statement/ signature line areas must be retained and worded exactly as on the official form. The requirement for a signature, by itself, does not prohibit a tax form from being properly computer generated.

2.3.1
Overview

All payment vouchers (Forms 940-V, 941-V, 943-V, 944-V, 945-V, 1040-ES, 1040-V, 1041-V, and 2290-V) must be reproduced in conjunction with their forms. Substitute vouchers must be the same size as the officially printed vouchers. Vouchers that are prepared for printing on a laser printer may include a scan line.

2.3.2
Scan Line Specifications

	NNNNNNNNN	AA	XXXX	NN	N	NNNNNN	NNN
Item:	A	B	C	D	E	F	G
A.	Social Security Number/Employer Identification Number (SSN/EIN) has 9 numeric (N) spaces.						
B.	Check Digits have 2 alpha (A) spaces.						
C.	Name Control has 4 alphanumeric (X) spaces.						
D.	Master File Tax (MFT) Code has 2 numeric (N) spaces (see *Section 2.3.3*).						
E.	Taxpayer Identification Number (TIN) Type has 1 numeric (N) space (see *Section 2.3.4*).						
F.	Tax Period has 6 numeric (N) spaces in year/month format (YYYYMM).						
G.	Transaction Code has 3 numeric (N) spaces.						

2.3.3
MFT Code

Code Number for Forms:

- 1040 (family) – 30,
- 940 – 10,
- 941 – 01,
- 943 – 11,
- 944 – 14,
- 945 – 16,
- 1041-V – 05,
- 2290 – 60, and
- 4868 – 30.

2.3.4
TIN Type

Type Number for:

- Form 1040 (family), 4868 – 0; and
- Forms 940, 941, 943, 944, 945, 1041-V, and 2290 – 2.

2.3.5
Voucher Size

The voucher size must be exactly 8.0″ x 3.25″ (Forms 1040-ES and 1041-ES must be 7.625″ x 3.0″). The document scan line must be vertically positioned 0.25 inches from the bottom of the scan line to the bottom of the voucher. The last character on the right of the scan line must be placed 3.5 inches from the right leading edge of the document. The minimum required horizontal

clear space between characters is 0.014 inches. The line to be scanned must have a clear band 0.25 inches in height from top to bottom of the scan line, and from border to border of the document. "Clear band" means no printing except for dropout ink.

2.3.6
Print and Paper Weight

Vouchers must be imaged in black ink using OCR A, OCR B, or Courier 10. These fonts may not be mixed in the scan line. The horizontal character pitch is 10 CPI. The preferred paper weight is 20 to 24 pound OCR bond.

2.3.7
Specifications for Software Developers

Certain vouchers may be reproduced for use in the IRS lockbox system. These include the 1040-V, 1040-ES, 1041-V, the 94X family, and 2290 vouchers. Software developers must follow these specific guidelines to produce scannable vouchers strictly for lockbox purposes. Also see *Exhibit A*.

- The total depth must be 3.25 inches.
- The scan line must be 0.5 inches from the bottom edge and 1.75 inches from the left edge of the voucher and left justified.
- Software developers' vouchers must be 8.5 inches wide (instead of 8 inches with a cut line). Therefore, no vertical cut line is required.
- Scan line positioning must be exact.
- Do not use the over-the-counter format voucher and add the scan line to it.
- All scanned data must be in 12-point OCR A font.
- The 4-digit NACTP ID code or IRS source code should be placed under the payment indicator arrow.
- Windowed envelopes must not display the scan line in order to avoid disclosure and privacy issues.

Note. All software developers must ensure that their software uses OCR A font so taxpayers will be able to print the vouchers in the correct font.

2.3.8
Specific Line Positions

Follow these line specifications for entering taxpayer data in the lockbox vouchers.

	Start Row	Start Column	Width	End Column
Line Specifications for Taxpayer Data:				
Taxpayer Name	56	6	36	41
Taxpayer Address, Apt.	57	6	36	41
Taxpayer City, State, ZIP	58	6	36	41
Foreign Country Name	59	6	36	41
Foreign Province/County	60	6	17	22
Foreign Postal Code	60	26	16	41
Line Specifications for Mail To Data:				
Mail Name	56	43	38	80
Mail Address	57	43	38	80
Mail City, State, ZIP	58	43	38	80
Line Specifications for:				
Scan Line	63	26	n/a	n/a

2.3.9
How To Get Approval

To receive approval, the following procedures are in effect due to Covid-19.

Please send an approval sheet with each form type for IRS signature to Doris Bethea at *Doris.E.Bethea@irs.gov*. You should include in the email an example of each type of voucher the site will be testing. **Note.** Do not mail any test vouchers to Doris Bethea.

You are required to send 25 voucher samples of each form in PDF format. You should email the test vouchers to *raul.t.mariduena@jpmorgan.com*. You can also print the vouchers and send them to his mailing address at:

JP Morgan Chase
Attn: Raul Mariduena
830 Tyvola Road, Suite 114
Charlotte, NC 28217

To receive approval under regular circumstances, please send in 25 voucher samples yearly for each form type or scenario, by December 10, 2021, for testing to the following address.

Internal Revenue Service
Attn: Doris Bethea, C5-226
5000 Ellin Road
Lanham, MD 20706

For further information, contact Doris Bethea, *Doris.E.Bethea@irs.gov*, at 240-613-5922 (not toll free), or Kathryn Wheelock, *Kathryn.F.Wheelock@irs.gov*, at 816-499-4443 (not toll free).

Section 2.4 – Restrictions on Changes

2.4.1
What You Cannot Do to Forms Suitable for Substitute Tax Forms

You cannot, without prior IRS approval, change any IRS tax form or use your own (nonapproved) versions including graphics, unless specifically permitted by this revenue procedure. See *Sections 2.5.7* through *2.5.11*.

You cannot adjust any of the graphics on Form 1040 or 1040-SR (except in those areas specified in *Part 5* of this revenue procedure) without prior approval from the Program.

You cannot rearrange or redistribute data entry fields, and/or allow data entry fields to flow from one page onto the next (that is, each page of a substitute form must contain the exact number of data entry fields as there are on the official IRS form). The order of information on the substitute form must be identical to the IRS version of the form. Publications for specific substitute forms will state allowances for those respective forms.

Note. The 20-business-day turnaround policy may not apply to extensive changes.

Section 2.5 – Guidelines for Obtaining IRS Approval

2.5.1
Basic Requirements

Preparers who submit substitute privately designed, privately printed, computer-generated, or computer-prepared tax forms must develop these substitutes using the guidelines established in

this part. These forms, unless there is an exception outlined by the revenue procedure, must be approved by the IRS before being filed.

2.5.2 Conditional Approval Based on Advance Drafts

The IRS cannot grant final approval of your substitute form until the official form has been published. However, the IRS posts advance draft forms on its website at *IRS.gov/DraftForms*.

We encourage submission of proposed substitutes of these advance draft forms and will grant conditional approval based solely on these early drafts. These advance drafts are subject to significant change before forms are finalized. If these advance drafts are used as the basis for your substitute forms, you will be responsible for subsequently updating your final forms to agree with the final official version. These revisions need not be resubmitted for further approval.

Note. Approval of forms based on advance drafts will not be granted after the final version of an official form is published.

2.5.3 Submission Procedures

Follow these general guidelines when submitting substitute forms for approval.

- Any alteration of forms must be within the limits acceptable to the IRS. It is possible that, from one filing period to another, a change in law or a change in internal need (processing, audit, compliance, etc.) may change the allowable limits for the alteration of the official form.

- When approval of any substitute form (other than those exceptions specified in *Part 1*, *Section 1.2 – IRS Contacts*) is requested, a sample of the proposed substitute form should be emailed for consideration to the Program at the address shown in *Section 1.2.1*.

- Schedules and forms (for example, Forms 3468, 4136, etc.) that can be used with more than one type of return (for example, Forms 1040, 1040-SR, 1041, 1120, etc.) should be submitted only once for approval, without regard to the number of different tax returns with which they may be associated. Also, all pages of multi-page forms or returns should be submitted in the same package.

2.5.4 Approving Offices

Because only the Program is authorized to approve substitute forms, unnecessary delays may occur if forms are sent to the wrong office. You may receive an interim letter about the delay. The Program may then coordinate the response with the originator responsible for revising that particular form. Such coordination may include allowing the originator to officially approve the form. No IRS office is authorized to allow deviations from this revenue procedure.

2.5.5 IRS Review of Software Programs, etc.

The IRS does not review or approve the logic of specific software programs, nor does the IRS confirm the calculations on the forms produced by these programs. The accuracy of the program remains the responsibility of the software package developer, distributor, or user.

The Program is primarily concerned with the pre-filing quality review of the final forms that are expected to be processed by IRS field offices. For this purpose, you should submit forms without including any taxpayer information such as names, addresses, monetary amounts, etc.

If the software used is programmed to produce copies with populated fields, then you must use dummy information. This will allow the Program to review and provide feedback or approval. Vendors should use "0" for all number values and "X" for any information that requires alpha characters.

2.5.6 When To Send Proposed Substitutes

Proposed substitutes, which are required to be submitted per this revenue procedure, should be sent as much in advance of the filing period as possible. This is to allow adequate time for analysis and response.

2.5.7 Accompanying Statement

When submitting sample substitutes, you should include an accompanying statement that lists each form number and its changes from the official form (position, arrangement, appearance, line

numbers, additions, deletions, etc.). With each of the items, you should include a detailed reason for the change.

When requesting approval, please include a checksheet. Checksheets expedite the approval process. The checksheet may look like the example in *Exhibit B* displayed in the back of this procedure or may be one of your own design. Please include your email address on the checksheet.

2.5.8
Approval/ Nonapproval Notice

The Program will email the checksheet or an approval letter to the originator, unless:

- The requester has asked for a formal letter, or
- Significant corrections to the submitted forms are required.

Notice of approval may impose qualifications before using the substitutes. Notices of unapproved forms may specify the changes required for approval and require resubmission of the form(s) in question. When appropriate, you will be contacted by telephone.

2.5.9
Duration of Approval

Most signature tax returns and many of their schedules and related forms have the tax (liability) year printed in the upper right corner. Approvals for these annual forms are usually good for 1 calendar year (January through December of the year of filing). Quarterly tax forms in the 94X series and Form 720 require approval for any quarter in which the form has been revised.

Because changes are usually made to an annual form every year, each new filing season generally requires a new submission of a substitute form. Very rarely is updating the preprinted year the only change made to an annual form. However, if no significant content, formatting, or layout changes were made to a tax form, then review and approval received for the prior tax year can be carried over into the current tax year.

2.5.10
Limited Continued Use of an Approved Change

Limited changes approved for one tax year may be allowed for the same form in the following tax year. Examples are the use of abbreviated words, revised form spacing, compressed text lines, and shortened captions, etc., which do not change the integrity of lines or text on the official forms.

If the vendor or filer makes substantial changes to the form, new substitutes must be submitted for approval. If the vendor or filer makes only minor editorial changes to the form, or makes any changes that mirror changes the IRS makes to the form's official version, the new substitute does not need to be submitted for approval. It is the responsibility of each vendor who has been granted permission to produce substitute forms to monitor and revise forms to mirror any revisions to the official forms made by the IRS. If there are any questions, please contact the Program.

2.5.11
When Approval Is Not Required

If you received approval for a specific change on a form last year, you may make the same change this year if the item is still present on the official form.

- The new substitute form does not have to be submitted to the IRS and approval based on that change is not required.
- However, the new substitute form must conform to the official current year IRS form in other respects, such as date, Office of Management and Budget (OMB) approval number, attachment sequence number, Paperwork Reduction Act Notice statement, arrangement, item caption, line number, line reference, data sequence, etc.
- The new substitute form must also comply with changes to the guidelines in this revenue procedure. The procedure may have eliminated, added to, or otherwise changed the guideline(s) that affected the change approved in the prior year.
- An approved change is authorized only for the period from a prior tax year substitute form to a current tax year substitute form.

Exception. Forms with temporary, limited, or interim approvals (or with approvals that state a change is not allowed in any other tax year) are subject to review in subsequent years.

2.5.12
Required Copies

Generally, you must send us one copy of each form being submitted for approval. However, if you are producing forms for different computer platforms (for example, Microsoft vs. Apple), different tax preparation software (for example, TurboTax® vs. TaxSlayer®), or different types of printers (for example, inkjet vs. impact), and these forms differ **significantly** in appearance, submit one copy for each type of platform, tax preparation software, or printer.

2.5.13
Requestor's Responsibility

Following receipt of an initial approval for a substitute forms package or a software output program to print substitute forms, it is the responsibility of the originator (designer or distributor) to provide client firms or individuals with forms that meet the IRS's requirements for continuing acceptability. Examples of this responsibility include:

- Using the prescribed print paper, font size, legibility, state tax data deletion, etc.; and
- Informing all users of substitute forms of the legal requirements of the Paperwork Reduction Act Notice, which is generally found in the instructions for the official IRS forms.

2.5.14
Source Code

The Program will assign a unique source code to each firm that submits substitute forms for approval. This source code will be a permanent identifier that must be used on every submission by a particular firm.

The source code consists of three alpha characters and should generally be printed under or to the left of the "Paperwork Reduction Act" statement. Vendors must ensure that the source code is not printed too close to or within the left or bottom $^1/_2$-inch margin to avoid the source code from being cut off during printing.

Section 2.6 – Office of Management and Budget (OMB) Requirements for All Substitute Forms

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2.6.1
OMB Requirements for All Substitute Forms

There are legal requirements of the Paperwork Reduction Act of 1995 (the Act). Public Law 104-13 requires the following.

- OMB approves all IRS tax forms that are subject to the Act.
- Each IRS form contains (in the upper right corner) the OMB number, if assigned.
- Each IRS form (or its instructions) states why the IRS needs the information, how it will be used, and whether or not the information is required to be furnished to the IRS.

This information must be provided to every user of official or substitute IRS forms or instructions.

2.6.2
Application of the Paperwork Reduction Act

On forms that have been assigned OMB numbers:

- All substitute forms must contain in the upper right corner the OMB number that is on the official form, and
- The required format is: OMB No. 1545-XXXX (preferred) or OMB # 1545-XXXX (acceptable).

2.6.3
Required Explanation to Users

You must inform the users of your substitute forms of the IRS use and collection requirements stated in the instructions for official IRS forms.

- If you provide your users or customers with the official IRS instructions, each form must retain either the Paperwork Reduction Act Notice (or Disclosure, Privacy Act, and Paperwork Reduction Act Notice), or a reference to it as the IRS does on the official forms (usually in the lower left corner of the forms).

- This notice reads, in part, "We ask for tax return information to carry out the tax laws of the United States."

Note. If no IRS instructions are provided to users of your forms, the exact text of the Paperwork Reduction Act Notice (or Disclosure, Privacy Act, and Paperwork Reduction Act Notice) must be furnished separately or on the form.

2.6.4
Finding the OMB Number and Paperwork Reduction Act Notice

The OMB number and the Paperwork Reduction Act Notice, or references to it, may be found printed on an official form (or its instructions). The number and the notice are included on the official paper format and in other formats produced by the IRS.

Part 3
Physical Aspects and Requirements

Section 3.1 – General Guidelines for Substitute Forms

3.1.1
General Information

The official form is the standard. Because a substitute form is a variation from the official form, you should know the requirements of the official form for the year of use before you modify it to meet your needs. To obtain the most frequently used tax forms, visit *IRS.gov/OrderForms*.

3.1.2
Design

Each form must follow the design of the official form as to format arrangement, item caption, line numbers, line references, and sequence.

3.1.3
State Tax Information Prohibited

Generally, state tax information must not appear on the federal tax return, associated form, or schedule that is filed with the IRS. Exceptions occur when amounts are claimed on, or required by, the federal return (for example, state and local income taxes on Schedule A (Form 1040)).

3.1.4
Vertical Alignment of Amount Fields

IF a form is to be...	THEN...
manually prepared and the official IRS form still has a separate cents entry field	1. the entry column must have a vertical line or some type of indicator in the amount field to separate dollars from cents.
	2. the cents column must be at least 3/10″ wide.
computer generated	1. vertically align the amount entry fields where possible.
	2. use one of the following amount formats.
	a) 0,000,000.
	b) 0,000,000.00.
computer prepared	1. you may remove the vertical line in the amount field that separates dollars from cents.
	2. use one of the following amount formats.
	a) 0,000,000.
	b) 0,000,000.00.

3.1.5 Attachment Sequence Number

Many individual income tax forms have a required "attachment sequence number" located just below the year designation in the upper right corner of the form. The IRS uses this number to indicate the order in which forms are to be attached to the tax return for processing. Some of the attachment sequence numbers may change from year to year.

The following applies to computer-prepared forms.

- The sequence number may be printed in no less than 12-point boldface type and centered below the form's year designation.
- The sequence number may also be placed following the year designation for the tax form and separated with an asterisk.
- The actual number may be printed without labeling it the "Attachment Sequence Number."

3.1.6 Assembly of Forms

When developing software or forms for use by others, please inform your customers/clients that the order in which the forms are arranged may affect the processing of the package. A return must be arranged in the order indicated below.

IF the form is...	THEN the sequence is...
1040 or 1040-SR	• Form 1040 or 1040-SR, and schedules and forms in attachment sequence number order.
any other tax return (Form 1120, 1120-S, 1065, 1041, etc.)	• the tax returns, directly associated schedules (Schedule D, etc.), directly associated forms, additional schedules in alphabetical order, and additional forms in numerical order.

Supporting statements should then follow in the same sequence as the forms they support. Additional information required should be attached last.

In this way, the forms are received in the order in which they must be processed. If you do not send returns to the IRS in order, processing may be delayed.

3.1.7 Paid Preparer's Information and Signature Area

On Forms 1040, 1040-SR, 1120, and any other applicable tax forms, the "Paid Preparer Use Only" area may not be rearranged or relocated. You may, however, add three extra lines to the paid preparer's address area, and remove the horizontal rules in that area without prior approval. This applies to other tax forms as well.

3.1.8 Some Common Reasons for Requiring Changes to Substitute Forms

Some reasons that substitute form submissions may require changes include the following.

- Shading areas incorrectly.
- Failing to include a reference to the location of the Paperwork Reduction Act Notice.
- Not including parentheses for losses.
- Not including "Attach Statement" when appropriate.
- Including line references or entry spaces that do not match the official form.
- Printing text that is different from the official form.
- Altering the jurat (perjury statement).
- Having an incorrect OMB number.
- Including the IRS catalog number (Cat. No.) on the form.

- Failing to include preprinted amounts in entry fields.
- Missing IRS source code or NACTP software ID.
- Incorrect dimensions.

Section 3.2 – Paper

3.2.1
Paper Content

The paper must be:

- Chemical wood writing paper that is equal to or better than the quality used for the official form,
- At least 18 pound (17″ x 22″, 500 sheets), or
- At least 50 pound offset book (25″ x 38″, 500 sheets).

3.2.2
Paper With Chemical Transfer Properties

There are several kinds of paper prohibited for substitute forms. These are:

1. Carbon-bonded paper, and
2. Chemical transfer paper except when the following specifications are met.
   a. Each ply within the chemical transfer set of forms must be labeled.
   b. Only the top ply (ply one and white in color), the one that contains chemical on the back only (coated back), may be filed with the IRS.

Example. A set containing three plies would be constructed as follows: ply one (coated back), "Federal Return, File with IRS"; ply two (coated front and back), "Taxpayer's copy"; and ply three (coated front), "Preparer's copy."

The file designation, "Federal Return, File with IRS" for ply one, must be printed in the bottom right margin (just below the last line of the form) in 12-point boldface type.

It is not mandatory, but recommended, that the file designation "Federal Return, File with IRS" be printed in a contrasting ink for visual emphasis.

3.2.3
Paper and Ink Color

It is preferred that the color and opacity of paper substantially duplicates that of the original form. This means that your substitute must be printed in black ink and may be on white or on the colored paper the IRS form is printed on. Form 1040 or 1040-SR substitute reproductions may be in black ink without the colored shading. The only exception to this rule is Form 1041-ES, which should be printed with a PMS 100 yellow shading in the color screened area. This is necessary to assist us in expeditiously separating this form from the very similar Form 1040-ES.

3.2.4
Page Size

Substitute or reproduced forms and computer-prepared/-generated substitutes may be the same size as the official form or they may be the standard commercial size (8.5″ x 11″). The thickness of the stock cannot be less than 0.003 inches.

3.3.1 Printing Medium

The private printing of all substitute tax forms must be by conventional printing processes, photocopying, computer graphics, or similar reproduction processes.

3.3.2 Legibility

All forms must have a high standard of legibility as to printing, reproduction, and fill-in matter. Entries of taxpayer data may be no smaller than 8 points. The IRS reserves the right to reject those with poor legibility. The ink and printing method used must ensure that no part of a form (including text, graphics, data entries, etc.) develops "smears" or similar quality deterioration. This standard must be followed for any subsequent copies or reproductions made from an approved master substitute form, either during preparation or during IRS processing.

3.3.3 Type Font

Many federal tax forms are printed using "Helvetica" as the basic type font. It is preferred that you use this type font when composing substitute forms.

3.3.4 Print Spacing

Substitute forms should be printed using a 6 lines/inch vertical print option. They should also be printed horizontally in 10-pitch pica (that is, 10 print characters per inch) or 12-pitch elite (that is, 12 print positions per inch).

3.3.5 Image Size

The image size of a printed substitute form should be as close as possible to that of the official form. You may omit any text on both computer-prepared and computer-generated forms that is solely instructional.

3.3.6 Title Area Changes

To allow a large top margin for marginal printing and more lines per page, the title line(s) for all substitute forms (not including the form's year designation and sequence number, when present) may be photographically reduced by 40% or reset as one line of type. When reset as one line, the type size may be no smaller than 14-point. You may omit "Department of the Treasury—Internal Revenue Service" and all references to instructions in the form's title area.

3.3.7 Remove Government Printing Office Symbol and IRS Catalog Number

When privately printing substitute tax forms, the Government Printing Office (GPO) symbol and/or jacket number must be removed. In the same place using the same type size, print the Employer Identification Number (EIN) of the printer or designer or the IRS-assigned source code. (We prefer this last number be printed in the lower left area of the first page of each form.) Also, remove the IRS catalog number (Cat. No.) and the recycle symbol if the substitute is not produced on recycled paper.

3.3.8 Printing Single Page Forms

Substitute single page forms should be reproduced the same as IRS single page forms. Other forms or schedules should not be printed on the back or on blank portions of a single page form. However, printing instructions on the back or on blank portions of a single page form is acceptable.

3.3.9 Photocopy Equipment

The IRS does not undertake to approve or disapprove the specific equipment or process used in reproducing official forms. Photocopies of forms must be entirely legible and satisfy the conditions stated in this and other revenue procedures.

3.3.10 Reproductions

Reproductions of official forms and substitute forms that do not meet the requirements of this revenue procedure may not be filed instead of the official forms. Illegible photocopies are subject to being returned to the filer for resubmission of legible copies.

3.3.11 Removal of Instructions

Generally, you may remove references to instructions. No prior approval is needed. However, in some instances, you may be requested to include references to instructions.

Exception. The words "For Paperwork Reduction Act Notice, see instructions" must be retained, or a similar statement indicating the location of the Notice must be provided on each form.

Section 3.4 – Margins

3.4.1 Margin Size

The format of a reproduced tax form when printed on the page must have margins on all sides at least as large as the margins on the official form. This allows room for IRS employees to make necessary entries on the form during processing.

- A 1/2-inch to 1/4-inch margin must be maintained across the top, bottom, and both sides of all substitute forms.
- The marginal, perforated strips containing pin-fed holes must be removed from all forms prior to filing with the IRS.

3.4.2 Marginal Printing

Prior approval is not required for the marginal printing allowed when printed on an official form or on a photocopy of an official form.

- With the exception of the actual tax return forms (for example, Forms 1040, 1040-SR, 1120, 940, 941, etc.), you may print in the left vertical margin and in the left half of the bottom margin.
- Printing is never allowed in the top right margin of the tax return form (for example, Forms 1040, 1040-SR, 1120, 940, 941, etc.). The IRS uses this area to imprint a Document Locator Number for each return. There are no exceptions to this requirement.

Section 3.5 – Miscellaneous Information for Substitute Forms

3.5.1 Filing Substitute Forms

To be acceptable for filing, a substitute form must print out in a format that will allow the filer to follow the same instructions that accompany official forms. The form must be legible, must be on the appropriately sized paper, and must include a jurat (perjury statement) where one appears on the published form.

3.5.2 Caution to Software Publishers

The IRS has received returns produced by software packages with approved output where either the form heading was altered or the lines were spaced irregularly. This produces an illegible or unrecognizable return or a return with the wrong number of pages. We realize that many of these problems are caused by individual printer differences but they may delay input of return data and, in some cases, generate correspondence to the taxpayer. Therefore, in the instructions to the purchasers of your product, both individual and professional, please stress that their returns will be processed more efficiently if they are properly formatted. This includes:

- Having the correct form numbers, six-digit form identifying numbers, and titles at the top of the return; and
- Submitting the same number of pages as if the form were an official IRS form with the line items on the proper pages.

3.5.3
Caution to Producers of Software Packages

If you are producing a software package that generates name and address data onto the tax return, do not, under any circumstances, program either the IRS preprinted check digits or a practitioner-derived name control to appear on any return prepared and filed with the IRS.

3.5.4
Programming to Print Forms

Whenever applicable:

- Use only the following label information format for single filers: JOHN Q. DOE 000 OAK DRIVE HOMETOWN, STATE 00000
- Use only the following information for joint filers: JOHN Q. DOE MARY Q. DOE 000 OAK DRIVE HOMETOWN, STATE 00000
- Use "0" for number values and "X" for alpha characters entered in data entry fields as dummy copy.

Part 4
Additional Resources

Section 4.1 – Guidance From Other Revenue Procedures

4.1.1
General

The IRS publications listed below provide guidance for substitute tax forms not covered in this revenue procedure. These publications are available on the IRS website. Use the publication number listed below to search for the requested document.

- Pub. 1141, General Rules and Specifications for Substitute Forms W-2 and W-3.
- Pub. 1179, General Rules and Specifications for Substitute Forms 1096, 1098, 1099, 5498, and Certain Other Information Returns.
- Pub. 1223, General Rules and Specifications for Substitute Forms W-2c and W-3c.
- Pub. 4436, General Rules and Specifications for Substitute Form 941, Schedule B (Form 941), Schedule D (Form 941), Schedule R (Form 941), and Form 8974.
- Pub. 5223, General Rules and Specifications for Affordable Care Act Substitute Forms 1095-A, 1094-B, 1095-B, 1094-C, and 1095-C.

Section 4.2 – Electronic Tax Products

4.2.1
The IRS Website

Copies of tax forms, their instructions, publications, fillable forms, and prior year forms and publications may be found on the IRS website at *IRS.gov/FormsPubs*.

Draft forms and instructions may be found at *IRS.gov/DraftForms*. Other tax-related information may be found at *IRS.gov*.

4.2.2
System Requirements and Ordering Forms and Instructions

For system requirements, contact the National Technical Information Service (NTIS) at *NTIS.gov*. Prices are subject to change.

You can order IRS forms and other tax material at *IRS.gov/OrderForms*.

Part 5
Requirements for Specific Tax Returns

Section 5.1 – Tax Returns (Forms 1040, 1040-SR, 1120, etc.)

5.1.1
Acceptable Forms

Tax return forms (such as Forms 1040, 1040-SR, and 1120) require a signature and establish tax liability. Computer-generated versions are acceptable under the following conditions.

- These substitute forms must be printed on plain white paper.
- Substitute forms must conform to the physical layout of the corresponding IRS form although the typeface may differ. The text should match the text on the officially published form as closely as possible. Condensed text and abbreviations will be considered on a case-by-case basis. **Caution.** All jurats (perjury statements) must be reproduced verbatim. No text can be added, deleted, or changed in meaning.
- Various computer graphic print media such as laser printing, inkjet printing, etc., may be used to produce the substitute forms.
- The substitute form must be the same number of pages and contain the same line text as the official form.
- All substitute forms must be submitted for approval prior to their original use. You do not need approval for a substitute form if its only change is the preprinted year and you had received a prior year approval letter. **Exception.** If the approval letter specifies a one-time exception for your form, the next year's form must be approved.

5.1.2
Prohibited Forms

The following are prohibited.

- Computer-generated tax forms (for example, Form 1040, 1040-SR, etc.) on lined or color-barred paper.
- Tax forms that differ from the official IRS forms in a manner that makes them nonstandard or unable to process.

5.1.3
Changes Permitted to Form 1040

Certain changes (listed in *Section 5.2*) are permitted to the graphics of the form without prior approval, but these changes apply to only acceptable preprinted forms. Changes not requiring prior approval are good only for the annual filing period, which is the current tax year. Such changes are valid in subsequent years only if the official form does not change.

5.1.4
Other Changes Not Listed

All changes not listed in *Section 5.2* require approval from the IRS before the form can be filed.

Section 5.2 – Changes Permitted to Graphics (Form 1040 or 1040-SR)

5.2.1 Adjustments

You may make minor vertical and horizontal spacing adjustments to allow for computer or word processing printing. This includes widening the amount columns or tax entry areas if the adjustments comply with other provisions stated in revenue procedures. No prior approval is needed for these changes.

Schedules 1–3 cannot be combined for filing purposes. For the client copy of the return, the numbered schedules may be printed two to a page (for example, Schedule 3 below Schedule 2, if both are completed as part of the return). If numbered schedules are combined on the client copy, it must include a statement that it is "Not for Filing."

5.2.2 Name and Address Area

The horizontal rules and instructions within the name and address area may be removed and the entire area left blank. No line or instruction can remain in the area. The heavy-ruled border (when present) that outlines the name, address area, and social security number must not be removed, relocated, expanded, or contracted.

5.2.3 Required Format

When the name and address area is left blank, the following format must be used when printing the taxpayer's name and address.

- 1st name line (35 characters maximum).
- 2nd name line (35 characters maximum).
- In-care-of name line (35 characters maximum).
- City, state (25 characters maximum), one blank character, and ZIP code.

5.2.4 Conventional Name and Address Data

When there is no in-care-of name line, the name and address will consist of only three lines (single filer) or four lines (joint filer). Name and address (joint filer) with no in-care-of name line:

JOHN Q. DOE
MARY Q. DOE
000 ANYWHERE ST., APT. 000
ANYTOWN, STATE 00000

Example of in-care-of name line. Name and address (single filer) with in-care-of name line:

JOHN Q. DOE
C/O JOHN R. DOE
0000 SOMEWHERE AVE.
SAMETOWN, STATE 00000

5.2.5 SSN and Employer Identification Number (EIN) Area

The broken vertical lines separating the format arrangement of the SSN/EIN may be removed. When the vertical lines are removed, the SSN and EIN formats must be 000-00-0000 or 00-0000000, respectively.

5.2.6 Entering Cents

- You may remove the vertical rule that separates the dollars from the cents if it is still included on the official IRS form.

- All entries in the amount column should have a decimal point following the whole dollar amounts whether or not the vertical line that separates the dollars from the cents is present.
- You may omit printing the cents, but all amounts entered on the form must follow a consistent format. You are strongly urged to round off the figures to whole dollar amounts, following the official form instructions.
- When several amounts are added together, the total should be rounded off after addition (that is, individual amounts should not be rounded off for computation purposes).
- When printing money amounts, you must use one of the following formats: (a) 0,000,000; (b) 0,000,000.00.
- When there is no entry for a line, leave the line blank.

5.2.7 Changes to Lines

No prior approval is needed for the following changes (for use with computer-prepared forms only). Specific line numbers in the following headings may have changed due to tax law changes.

5.2.8 Dependents on Form 1040

The vertical lines separating columns (1) through (4) may be removed. The captions may be shortened to allow a one-line caption for each column.

5.2.9 Other Lines

Any other line with text that takes up two or more vertical lines may be compressed to one line by using contractions, etc., and by removing instructional references.

5.2.10 Form 1040 – Tax

You may change the line caption to read "Tax" and computer print the words "Total includes tax from" and either "Form(s) 8814" or "Form 4972" or "962 election." If both forms are used, print both form numbers. This specific line number may have changed.

5.2.11 Color Screening

It is not necessary to duplicate the color screening used on the official form. A substitute Form 1040 or 1040-SR may be printed in black and white only with no color screening.

5.2.12 Other Changes Prohibited

No other changes to the Form 1040 or 1040-SR graphics are permitted without prior approval except for the removal of instructions and references to instructions.

Part 6
Format and Content of Substitute Returns

Section 6.1 – Acceptable Formats for Substitute Forms and Schedules

6.1.1 Exhibits and Use of Acceptable Formats

Exhibit A is an acceptable format for Form 1040-ES.

- If your computer-generated Form 1040-ES appears exactly like *Exhibit A*, no prior authorization is needed.
- You may computer-generate forms not shown here, but you must design them by following the manner and style discussed in *Part 3*.
- Take care to observe the other requirements and conditions in this revenue procedure. The IRS encourages the submission of all proposed forms covered by this revenue procedure.

6.1.2 Instructions

The format of each substitute form or schedule must follow the format of the official form or schedule as to item captions, line references, line numbers, sequence, form arrangement and format, etc. Basically, try to make the form look like the official one, with readability and consistency being primary factors. You may use periods and/or other similar special characters to separate the various parts and sections of the form. Do not use alpha or numeric characters for these purposes. All line numbers and items must be printed even though an amount is not entered on the line.

6.1.3 Line Numbers

When a line on an official form is designated by a number or a letter, that designation (reference code) must be used on a substitute form. The reference code must be printed to the left of the text of each line and immediately preceding the data entry field, even if no reference code precedes the data entry field on the official form. If an entry field contains multiple lines and shows the line references once on the left and right side of the form, use the same number of line references on the substitute form.

In addition, the reference code that is immediately before the data field must either be followed by a period or enclosed in parentheses. There must also be at least two blank spaces between the period or the right parenthesis and the first digit of the data field. (See *Section 6.1.4*.)

6.1.4 Decimal Points

A decimal point (a period) should be used for each money amount regardless of whether the amount is reported in dollars and cents or in whole dollars, or whether or not the vertical line that separates the dollars from the cents is present. The decimal points must be vertically aligned when possible.

Example:		
5 State and local taxes		
a State and local income taxes.....	5a.	000.00
b State and local real estate taxes.....	5b.	
c State and local personal property taxes....	5c.	000.00
or		
a State and local income taxes.....	(5a)	000.00
b State and local real estate taxes.....	(5b)	
c State and local personal property taxes....	(5c)	000.00

6.1.5 Multi-Page Forms

When submitting a multi-page form, send all its pages in the same package. If you will not be producing certain pages, please note that in your cover letter.

Section 6.2 – Additional Instructions for All Forms

6.2.1 Use of Your Own Internal Control Numbers and Identifying Symbols

You may show the computer-prepared internal control numbers and identifying symbols on the substitute if using such numbers or symbols is acceptable to the taxpayer and the taxpayer's representative. Such information must not be printed in the top 1/2-inch clear area of any form or schedule requiring a signature.

Except for the actual tax return form (Forms 1040, 1040-SR, 1120, 940, 941, etc.), you may print in the left vertical and bottom left margins. The bottom left margin you may use extends 3 1/2 inches from the left edge of the form. You may print internal control numbers in place of the removed IRS catalog number.

6.2.2 Required Software ID Number (Source Code) on Computer- Prepared Substitutes

In the February 2009 Government Accountability Office (GAO) report, "Many Taxpayers Rely on Tax Software and IRS Needs to Assess Associated Risks" (GAO-09-297), the GAO recommend-

ed that the IRS require a software identification number on all individual returns to specifically identify the software package used to prepare each tax return. The IRS already has this capability for all *e-filed* returns. In addition, many tax preparation software firms already print an IRS-issued 3-letter Source Code on paper returns that are generated by their individual tax software. This Source Code was assigned when the firms were seeking substitute forms approval under this current publication.

In order to respond properly to this GAO recommendation, the IRS will require all tax preparation software firms to include the 3-letter Source Code on all paper tax returns created by their individual tax preparation software. The many firms that currently have and display their Source Code on paper returns generated from their software should continue to do so, and no change is necessary.

We have reviewed all software companies that passed Assurance Testing System (ATS) testing last filing season and have determined that some firms do not currently have a Source Code. To save you the burden of contacting us and for your convenience, we have assigned Source Codes to those firms.

You should program your Source Code to be placed in the bottom left-hand corner of page one of each paper form that will be generated by your individual tax return package. You do not need to apply for a new Source Code annually.

If you already use a 3-letter Source Code and we have issued you one in error, you are unsure if you were ever issued one, or have other questions or concerns, you may contact Tax Forms and Publications Special Services Section at *substituteforms@irs.gov*.

6.2.3
Descriptions for Captions, Lines, etc.

Descriptions for captions, lines, etc., appearing on the substitute forms may be limited to one print line by using abbreviations and contractions, and by omitting articles, prepositions, etc. However, sufficient keywords must be retained to permit ready identification of the caption, line, or item.

6.2.4
Determining Final Totals

Explanatory detail and/or intermediate calculations for determining final line totals may be included on the substitute. We prefer that such calculations be submitted in the form of a supporting statement. If intermediate calculations are included on the substitute, the line on which they appear may not be numbered or lettered. Intermediate calculations may not be printed in the right column.

This column is reserved only for official numbered and lettered lines that correspond to the ones on the official form. Generally, you may choose the format for intermediate calculations or subtotals on supporting statements to be submitted.

6.2.5
Instructional Text on the Official Form

Text on the official form, which is solely instructional (for example, "See instructions," etc.), may generally be omitted from the substitute form.

6.2.6
Intermingling Is Prohibited

Showing more than one form or schedule on the same printout page is prohibited. Both sides of the paper may be used for multi-page forms, but it is unacceptable to intermingle forms.

For instance, Schedule E can be printed on both sides of the paper because the official form is multi-page, with page 2 continued on the back. However, do not print Schedule E on the front page and Schedule SE on the back page, or Schedule A on the front and Form 8615 on the back, etc. Both pages of a substitute form must match the official form. The back page may be left blank if the back page of the official form contains only the instructions.

6.2.7
Identifying Substitutes

Identify all computer-prepared substitutes clearly. Print the form designation 1/2 inch from the top margin and 1 1/2 inches from the left margin. Print the title centered on the first line of print. Print the tax year and, where applicable, the sequence number on the same line 1/2 inch to 1 inch from the right margin.

Include the taxpayer's name and SSN on all forms and attachments. Also, print the OMB number as reflected on the official form.

6.2.8
Negative Amounts

Negative (or loss) amount entries should be enclosed in brackets or parentheses or include a minus sign. This assists in accurate computation and input of form data. The IRS preprints parentheses in negative data fields on many official forms. These parentheses should be retained or inserted on printouts of affected substitute forms.

Part 7
Miscellaneous Forms and Programs

Section 7.1 – Specifications for Substitute Schedules K-1

7.1.1
Requirements for Schedules K-1 That Accompany Forms 1041, 1065, and 1120-S

Because of significant changes to improve processing, prior approval is now required for substitute Schedules K-1 that accompany Form 1041 (for estates and trusts), Form 1065 (for partnerships), or Form 1120-S (for S corporations). Substitute Schedules K-1 should be as close as possible to exact replicas of copies of the official IRS schedules and follow the same process for submitting other substitute forms and schedules. Before releasing their substitute forms, software vendors are responsible for making any subsequent changes that have been made to the final official IRS forms after the draft forms have been posted.

Submit substitute Schedule K-1 forms, in PDF format, to *scrips@irs.gov* for scannability acceptance. Schedule K-1 forms that require testing do not need to be mailed to the Program. You must include information on the substitute that can be tested. This information should be dummy information. Use an "X" for alpha characters and "0" for numbers. The IRS will review and provide feedback of any changes needed so that your forms can be recognized correctly.

Include the 6-digit form ID code in the upper right of Schedules K-1 of Forms 1041, 1065, and 1120-S. Please allow at least 1/4 inch of white space around the 6-digit code.

- 661117 for Form 1041.
- 651119 for Form 1065.
- 671120 for Form 1120-S.

Schedules K-1 that accompany Forms 1041, 1065, or 1120-S must meet all specifications. The specifications include, but are not limited to, the following requirements.

- You will no longer be able to produce Schedules K-1 that contain only those lines or boxes that taxpayers are required to use. All lines must be included.
- The words "*See attached statement for additional information." must be preprinted in the lower right-hand side on Schedules K-1 of Forms 1041, 1065, and 1120-S.
- All Schedules K-1 that are filed with the IRS should be printed on standard 8.5" x 11" paper (the international standard (A4) of 8.27" x 11.69" may be substituted).
- 10-point Helvetica Light Standard is preferred for all entries that are typed or made using a computer.

- Submissions should include IRS source code or NACTP vendor ID code printed on the lower left corner of the form or in place of the IRS catalog number.

- Each recipient's information must be on a separate sheet of paper. Therefore, you must separate all continuously printed substitutes, by recipient, before filing with the IRS.

- No carbon copies or pressure-sensitive copies will be accepted.

- The Schedule K-1 must contain the name, address, and SSN or EIN of both the entity (estate, trust, partnership, or S corporation) and the recipient (beneficiary, partner, or shareholder).

- The Schedule K-1 must contain the tax year, the OMB number, the schedule number (K-1), the related form number (1041, 1065, or 1120-S), and the official schedule name in substantially the same position and format as shown on the official IRS schedule.

- The Schedule K-1 must contain all the line items as shown on the official form, except for the instructions, if any are printed on the back of the official Schedule K-1.

- The line items or boxes must be in the same order and arrangement as those on the official form.

- The amount of each recipient's share of each item must be shown. A partial percent should be reflected as a decimal (for example, 501/2% should be 50.5%). Furnishing a total amount of each item and a percentage (or decimal equivalent) to be applied to such total amount by the recipient does not satisfy the law and the specifications of this revenue procedure.

- State or local tax-related information may not be included on the Schedules K-1 filed with the IRS.

- The entity may have to pay a penalty if substitute Schedules K-1 are filed that do not conform to specifications.

- Additionally, the IRS may consider the Schedules K-1 that do not conform to specifications as not being able to be processed and may return Form 1041, 1065, or 1120-S to the filer to be filed correctly.

Schedules K-1 that are 2-D bar-coded will continue to require prior approval from the IRS (see *Sections 7.1.3* through *7.1.5*).

7.1.2
Special Requirements for Recipient Copies of Schedules K-1

Standardization for reporting information is required for recipient copies of substitute Schedules K-1 of Forms 1041, 1065, and 1120-S. Uniform visual standards are provided to increase compliance by allowing recipients and practitioners to more easily recognize a substitute Schedule K-1. The entity must furnish to each recipient a copy of Schedule K-1 that meets the following requirements.

- Include the 6-digit form ID code in the upper right of Schedules K-1 of Forms 1041, 1065, and 1120-S. Please allow white space around the 6-digit code.

  – 661117 for Form 1041.

  – 651119 for Form 1065.

  – 671120 for Form 1120-S.

- You will no longer be able to produce Schedules K-1 that contain only those lines or boxes that taxpayers are required to use. All lines must be included.

- The words "*See attached statement for additional information." must be preprinted in the lower right-hand side on Schedules K-1 of Forms 1041, 1065, and 1120-S.

- The Schedule K-1 must contain the name, address, and SSN or EIN of both the entity and recipient.

- The Schedule K-1 must contain the tax year, the OMB number, the schedule number (K-1), the related form number (1041, 1065, or 1120-S), and the official schedule name in substantially the same position and format as shown on the official IRS schedule.

- All applicable amounts and information required to be reported must be titled and numbered in the same manner as shown on the official IRS schedule. The line items or boxes must be in the same order and arrangement and must be numbered like those on the official IRS schedule.

- The Schedule K-1 must contain all items required for use by the recipient. The instructions for the schedule must identify the line or box number and code, if any, for each item as shown in the official IRS schedule.

- The amount of each recipient's share of each item must be shown. A partial percent should be reflected as a decimal (for example, 501/2% should be 50.5%). Furnishing a total amount of each line item and a percentage (or decimal equivalent) to be applied to such total amount by the recipient does not satisfy the law and the specifications of this revenue procedure.

- Instructions to the recipient that are substantially similar to those on or accompanying the official IRS schedule must be provided to aid in the proper reporting of the items on the recipient's income tax return. Where items are not reported to a recipient because they do not apply, the related instructions may be omitted.

- The quality of the ink or other material used to generate recipients' schedules must produce clearly legible documents. In general, black chemical transfer inks are preferred.

- In order to assure uniformity of substitute Schedules K-1, the paper size should be standard 8.5" x 11" (the international standard (A4) of 8.27" x 11.69" may be substituted).

- The paper weight, paper color, font type, font size, font color, and page layout must be such that the average recipient can easily decipher the information on each page. The preferred font is "Helvetica" and a minimal of 10-point font.

- State or local tax-related information may be included on recipient copies of substitute Schedules K-1. All non-tax-related information should be separated from the tax information on the substitute schedule to avoid confusion for the recipient.

- The legend "Important Tax Return Document Enclosed" must appear in a bold and conspicuous manner on the outside of the envelope that contains the substitute recipient copy of Schedule K-1.

- The entity may have to pay a penalty if a substitute Schedule K-1 furnished to any recipient does not conform to the specifications of this revenue procedure and results in impeding processing.

7.1.3
Requirements for Schedules K-1 With Two- Dimensional (2- D) Bar Codes

Electronic filing is now and will continue to be the preferred method of filing; however, 2-D bar code is the best alternative method for paper processing.

In an effort to improve efficiency and increase data accuracy, the IRS partnered with the tax software development community on a two-dimensional bar code project in 2003. Certain tax software packages have been modified to generate 2-D bar codes on Schedules K-1. As a result, when Schedules K-1 are printed using these programs, a bar code will print on the page.

Rather than manually transcribe information from the Schedule K-1, the IRS will scan the bar code and electronically upload the information from the Schedule K-1. The results will be more efficient operation within the IRS and fewer transcription errors for your clients.

Note. If software vendors do not want to produce bar-coded Schedules K-1, they may produce the official IRS Schedules K-1 but cannot use the expedited process for approving bar-coded Schedules K-1 and their parent returns as outlined in *Section 7.1.6*.

In addition to the requirements in *Sections 7.1.1* and *7.1.2*, the bar-coded Schedules K-1 must meet the following specifications.

- The bar code should print in the space labeled "For IRS Use Only" on each Schedule K-1. The entire bar code must print within the "For IRS Use Only" box surrounded by a white space of at least 1/4 inch.
- Bar codes must print in PDF 417 format.
- The bar codes must always be in the specified format with every field represented by at least a field delimiter (carriage return). Leaving out a field in a bar code will cause every subsequent field to be misread.
- Be sure to include the 6-digit form ID code in the upper right of Schedules K-1 of Forms 1041, 1065, and 1120-S. Please allow white space around the 6-digit code.
  - 661117 for Form 1041.
  - 651119 for Form 1065.
  - 671120 for Form 1120-S.

7.1.4
2-D Bar Code Specifications for Schedules K-1

Follow these general specifications for preparing all 2-D bar-coded Schedules K-1.

- Numeric fields.
  - Do not include leading zeros (except Taxpayer Identification Numbers, ZIP codes, and percentages).
  - If negative value, the minus sign "–" must be present immediately to the left of the number and part of the 12 position field.
  - Do not use non-numeric characters except that the literal "STMT" can be put in money fields.
  - All money fields should be rounded to the nearest whole dollar amount—if a money amount ends in 00 to 49 cents, drop the cents; if it ends in 50 to 99 cents, truncate the cents and increment the dollar amount by one. Use the same rounding technique for the bar-coded and the printed Schedules K-1.
  - All numeric-only fields are right justified (except Taxpayer Identification Numbers and ZIP codes).
- All field lengths are expressed as maximum lengths. If the value in the field has fewer positions or the software program does not support that many positions, put in the bar code only those positions actually used.
- Alpha fields.
  - Do not include leading blanks (left justified).

  - Do not include trailing blanks.
  - Use uppercase alpha characters only.
- Variable fields.
  - Do not include leading blanks (left justified).
  - Do not include trailing blanks.
  - Use uppercase alpha characters, numerics, and special characters as defined in each field.
- Delimit each field with a carriage return.
- Express percentages as 6-digit numbers without the percent sign. Left justify with leading zero(s) (for percentages less than 100%) and no decimal point (decimal point is assumed between 3rd and 4th positions). Examples: 25.32% expressed as "025320"; 105% expressed as "105000"; 8.275% expressed as "008275"; 10.24674% expressed as "010247."
- It is vital that the print routine reinitialize the bar code prior to printing each succeeding Schedule K-1. Failure to do this will result in each Schedule K-1 for a parent return having the same bar code as the document before it.

7.1.5 Approval Process for Bar-Coded Schedules K-1

Prior to releasing commercially available tax software that creates bar-coded Schedules K-1, the printed schedule and the bar code must both be tested. If your company is creating bar-coded Schedules K-1, you must receive certification for both the printed Schedule K-1, as well as the bar code before offering your product for sale. Bar-code testing must be done using the final official IRS Schedule K-1. Bar-code approval requests must be resubmitted for any subsequent changes to the official IRS form that would affect the bar code. Below are instructions and a sequence of events that will comprise the testing process.

- The IRS has released the final Schedule K-1 bar-code specifications by publishing them on the IRS.gov website (see *IRS.gov/E-file-Providers/ K-1-Bar-Code-Certification-Process*).
- The IRS will publish a set of test documents that will be used to test the ability of tax preparation software to create bar codes in the correct format.
- Software developers will submit two identical copies of the test documents—one to the IRS and one to a contracted testing vendor.
- The IRS will use one set to ensure the printed schedules comply with standard substitute forms specifications.
- If the printed forms fail to meet the substitute form criteria, the IRS will inform the software developer of the reason for noncompliance.
- The software developer must resubmit the Schedule(s) K-1 until they pass the substitute forms criteria.
- The testing vendor will review the bar codes to ensure they meet the published bar-code specifications.
- If the bar code(s) does not meet published specifications, the testing vendor will contact the software developer directly informing them of the reason for noncompliance.
- Software developers must submit new bar-coded schedules until they pass the bar-code test.

- When the bar code passes, the testing vendor will inform the IRS that the developer has passed the bar-code test and the IRS will issue an overall approval for both the substitute form and the bar code.

- After receiving this consolidated response, the software vendor is free to release software for tax preparation as long as any subsequent revisions to the schedules do not change the fields.

- Find the mailing address for the testing vendor below. Separate and simultaneous mailings to the IRS and the vendor will reduce testing time.

7.1.6 Procedures for Reducing Testing Time

In order to help provide incentives to the software development community to participate in the Schedule K-1 2-D project, the IRS has committed to expediting the testing of bar-coded Schedules K-1 and their associated parent returns. To receive this expedited service, follow the instructions below.

- Mail the parent returns (Forms 1065, 1120-S, 1041) and associated bar-coded Schedule(s) K-1 to the appropriate address below in a separate package from all other approval requests.

  Internal Revenue Service
  Attn: Bar-Coded K-1
  SE:W:CAR:MP:T:M:S, IR-6526
  1111 Constitution Ave. NW
  Washington, DC 20224

- Mail one copy of the parent form(s) and Schedule(s) K-1 to the IRS and another copy to the testing vendor at the address below.

  Leidos-IRS Paper and Remittance
  Processing Support (PRPS II)
  Attn: Dana Hawkins
  4701 Forbes Blvd.
  Lanham, MD 20706

- Include multiple email and phone contact points in the packages.

- While the IRS can expedite bar-coded Schedules K-1 and their associated parent returns, it cannot expedite the approval of nonassociated tax returns.

- Vendors are encouraged to visit *NACTP.org* for compliance guidelines in regards to mil size and error-correction level.

- Submissions should include IRS source code or NACTP vendor ID code printed on the lower left corner of the form or in place of the IRS catalog number.

- If a change is made to the bar code after approval, be sure to increment the version number.

Section 7.2 – Guidelines for Substitute Forms 8655

7.2.1 Increased Standardization for Forms 8655

Increased standardization for reporting information on substitute Forms 8655 is now required to aid in processing and for compliance purposes. Please follow the guidelines in *Section 7.2.2*.

7.2.2
Requirements for Substitute Forms 8655

Please follow these specific requirements when producing substitute Forms 8655.

- The first line of the title must be "Reporting Agent Authorization."
- If you want to include a reference to "State Limited Power of Attorney," it can be in parentheses under the title. "State" must be the first word within the parentheses.
- You must include "Form 8655" on the form.
- While the line numbers do not have to match the official form, the sequence of the information must be in the same order.
- The size of any variable data must be printed in a font no smaller than 10-point.
- For adequate disclosure checks, the following must be included for each taxpayer.
  - Name.
  - EIN.
  - Address.
- At this time, Form 944 will not be required if Form 941 is checked. Only those forms that the reporting agent company supports need to be listed.
- The jurat (perjury statement) must be identical with the exception of references to line numbers.
- A contact name and number for the reporting agent is not required.
- Any state information included should be contained in a separate section of the substitute form. Preferably, this information will be in the same area as line 19 of the official form.
- All substitute Forms 8655 must be approved by the Program as outlined in the Form 8655 specifications in this current publication.
- If you have not already been assigned a 3-letter Source Code, you will be given one when your substitute form is submitted for approval. This Source Code should be included in the lower left corner of the form.
- The 20-business-day assumed approval policy does not apply to Form 8655 approvals.

7.2.3
Exception for Form 8655

Because of how Form 8655 is processed and distributed to recipients, vendors are allowed to affix their logo onto the substitute version of the form. **This exception is for Form 8655 only.**

Part 8
Additional Information

Section 8.1 – Forms for Electronically Filed Returns

8.1.1
Electronic Filing Program

Electronic filing is a method by which authorized providers transmit tax return information to an IRS Service Center in the format of the official IRS forms. The IRS accepts both refund and balance due forms that are filed electronically.

8.1.2
Applying To Participate in IRS e-file

Anyone wishing to participate in IRS *e-file* of tax returns must submit an *e-file* application. The application can be completed and submitted electronically on the IRS website at IRS.gov after first registering for e-services on the website.

8.1.3
Obtaining the Taxpayer Signature/ Submission of Required Paper Documents

Taxpayers choosing to electronically prepare and file their return will be required to use the Self-Select PIN method as their signature.

Electronic Return Originators (EROs) can *e-file* individual income tax returns only if the returns are signed electronically using either the Self-Select or Practitioner PIN method.

Taxpayers must use Form 8453, U.S. Individual Income Tax Transmittal for an IRS *e-file* Return, to send supporting documents that are required to be submitted to the IRS.

For specific information about electronic filing, refer to Pub. 1345, Handbook for Authorized IRS *e-file* Providers of Individual Income Tax Returns.

8.1.4
Guidelines for Preparing Substitute Forms in the Electronic Filing Program

A participant in the electronic filing program who wants to develop a substitute form should follow the guidelines throughout this publication and send a sample form for approval to the Program at *substituteforms@irs.gov*. If you do not prepare substitute Form 8453 using a font in which all IRS wording fits on a single page, the form will not be accepted.

Note. Use of unapproved forms could result in suspension of the participant from the electronic filing program.

Section 8.2 – Effect on Other Documents

8.2.1
Effect on Other Documents

This revenue procedure supersedes Revenue Procedure 2019-35, 2019-41 I.R.B. 871.

Section 8.3 – Exhibits

Exhibit A — Form 1040-ES Voucher 2020

Exhibit B — Substitute Form Checksheet

Exhibit A

Form 1040-ES Voucher

Form 1040-ES (OCR)	2020	Estimated Tax	Voucher 1	Calendar year—
Department of the Treasury Internal Revenue Service	OMB No. 1545-0074		Payment	**Due April 15, 2020**

► Make your check or money order payable to **"United States Treasury."**

► Enter your SSN and "2020 Form 1040-ES" on your payment.

► If your name, address, or SSN is incorrect, see instructions.

Amount of estimated tax you are paying by check or money order.	Dollars	Cents
	0,000	

For Privacy Act and Paperwork Reduction Act Notice, see instructions.

Pay online at IRS.gov/epay. Simple. Fast. Secure.

John Q. Doe
000 Someplace Somewhere Blvd.
City, St 00000

PO Box 00000
City, St 00000 - 0000

000000000 XX DOE 00 0 202012 000

Exhibit B

Substitute Forms Checksheet

Checksheet of IRS Substitute Forms 20 :
Submitted on
Company: . . . . . .
Contact: . . . . . .
Phone: . . . . . .
Fax: . . . . . .
Source Code: . . . . . .

Form Number	Approved	Approved With Corrections	Comments

Authorized Name: _____
Title: _____
Reviewer's Name: _____
Telephone: _____
Date: _____

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 2019–27 through 2019–52 is in Internal Revenue Bulletin 2019–52, dated December 27, 2019.

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[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2019–27 through 2019–52 is in Internal Revenue Bulletin 2019–52, dated December 27, 2019.

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We Welcome Comments About the Internal Revenue Bulletin

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