

rule contained an incorrect effective date, contained an error in the Small Business Regulatory Enforcement and Fairness Act statement in the **SUPPLEMENTARY INFORMATION** section, and omitted a sentence.

In rule FR Document E8-11086 published on May 20, 2008 (73 FR 29353), make the following corrections:

1. On page 29354, in the first column, the effective date is listed as June 19, 2008. This is stayed until August 25, 2008.

2. On page 29358, in the second column, under the heading "Section 292.3 When can a tribe conduct gaming activities on trust lands?" a sentence was omitted after the sentence that ends, "concerns whether a specific area of land is a reservation." A new sentence should be added in this location to read, "Regardless of where the tribe sends its request for an Indian lands opinion, the Department will coordinate the completion of the request by the appropriate offices."

3. On page 29374, in the third column, under the heading "Small Business Regulatory Enforcement and Fairness Act (SBREFA)," the first sentence reads, "This rule is not a major rule under 5 U.S.C. 804(2), the Small Business Regulatory Enforcement and Fairness Act." This sentence should be corrected to read, "This rule is a major rule under 5 U.S.C. 804(2), the Small Business Regulatory Enforcement and Fairness Act." In this same location, paragraph (a) incorrectly states that this rule, "Does not have an annual effect on the economy of \$100 million or more." This should be corrected to read, "Has an annual effect on the economy of \$100 million or more."

Dated: June 19, 2008.

George Skibine,

Acting Deputy Assistant Secretary for Policy and Economic Development—Indian Affairs.
[FR Doc. E8-14211 Filed 6-23-08; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9402]

RIN 1545-BH58

Guidance Under Section 956 for Determining the Basis of Property Acquired in Certain Nonrecognition Transactions

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains final and temporary regulations under section 956 of the Internal Revenue Code (Code) regarding the determination of basis in certain United States property (within the meaning of section 956(c) of the Code) acquired by a controlled foreign corporation in certain nonrecognition transactions that are intended to repatriate earnings and profits of the controlled foreign corporation without United States income taxation. The final regulation adds a cross reference to the temporary regulations. These regulations affect United States shareholders of a controlled foreign corporation that acquires United States property in certain nonrecognition transactions. The text of the temporary regulations serves as the text of the proposed regulations (REG-102122-08) set forth in the notice of proposed rulemaking published in the Proposed Rules section in this issue of the **Federal Register**.

DATES: *Effective Date:* These regulations are effective on June 24, 2008.

Applicability Date: These regulations apply to property acquired in exchanges occurring on or after June 24, 2008.

FOR FURTHER INFORMATION CONTACT: John H. Seibert at (202) 622-3860 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 under section 956, which was added to the Code by the Revenue Act of 1962, Public Law 87-834 (76 Stat. 960 (1962)). The temporary regulations in this document are issued under the authority of sections 367(b) and 956(e). Section 367(b) was added to the Code by section 1042(a) of the Tax Reform Act of 1976, Public Law 94-455 (90 Stat. 1520 (1976)). Section 956(e) was added to the Code by section 13232(b) of the Omnibus Budget Reconciliation Act of 1993, Public Law 103-66, (107 Stat 312 (1993)).

The temporary regulations in this document apply to determine the basis of certain United States property (as defined in section 956(c) of the Code) acquired by a controlled foreign corporation in certain nonrecognition transactions that are intended to repatriate earnings and profits of the controlled foreign corporation without an income inclusion by the United States shareholders of the controlled foreign corporation under section 951(a)(1)(B).

Explanation of Provisions

A. Transactions at Issue

The IRS and the Treasury Department are aware that certain taxpayers are engaging in certain nonrecognition transactions in which a controlled foreign corporation (CFC) acquires certain United States property (within the meaning of section 956(c)) without resulting in an income inclusion to the United States shareholders of the CFC under section 951(a)(1)(B).

In one such transaction, for example, USP, a domestic corporation and the common parent of an affiliated group that files a consolidated tax return, owns 100-percent of the outstanding stock of US1 and US2, both domestic corporations that join USP in the filing of a consolidated tax return. US1 owns 100 percent of the stock of CFC, a controlled foreign corporation. US2 issues \$100x of its stock to CFC in exchange for \$10x of CFC stock and \$90x cash.

USP takes the position that: (i) US2's transfer of its stock to CFC in exchange for \$10x of CFC stock and \$90x cash is an exchange to which section 351 applies; (ii) US2 recognizes no gain on the receipt of \$10x of CFC stock and \$90x cash in exchange for its stock pursuant to section 1032(a); (iii) CFC recognizes no gain on the issuance of its stock to US2 under section 1032(a); (iv) CFC's basis in the US2 stock is zero pursuant to section 362(a); and (v) US1 and US2 do not and will not have an income inclusion under section 951(a)(1)(B) as a result of CFC holding the US2 stock (which constitutes United States property under section 956(c)).

The IRS and the Treasury Department believe these transactions raise significant policy concerns because the transactions may have the effect of repatriating earnings and profits of a CFC without a corresponding dividend inclusion, or an income inclusion under section 951(a)(1)(B) by reason of the CFC's investment in United States property.

B. Section 956—In General

Section 956 was enacted to require an income inclusion by United States shareholders of a CFC that invests certain earnings and profits in United States property "on the grounds that [the investment] is substantially the equivalent of a dividend being paid to them." S. Rep. No. 87-1881, 1962-3 CB 703, 794 (1962). (See § 601.601(d)(2)(ii)(b)).

Under Section 951(a)(1)(B) each United States shareholder (as defined in section 951(b)) of a CFC (as defined in section 957(a)) must include in its gross

income for its taxable year in which or with which the taxable year of the CFC ends, the amount determined under section 956 with respect to such shareholder for such year (but only to the extent not excluded from gross income under section 959(a)(2)).

The amount determined under section 956 with respect to a United States shareholder of a CFC for any taxable year is the lesser of: (1) The excess, if any, of the shareholder's pro rata share of the average amounts of United States property held (directly or indirectly) by the CFC as of the close of each quarter of such taxable year, over the amount of earnings and profits of the CFC described in section 959(c)(1)(A) with respect to such shareholder; or (2) the shareholder's pro rata share of the applicable earnings of the CFC. In general, the amount taken into account with respect to any United States property for this purpose is the adjusted basis of such property as determined for purposes of computing earnings and profits, reduced by any liability to which the property is subject. Earnings and profits described in section 959(c)(1)(A) are attributable to amounts previously included in gross income by the United States shareholder under section 951(a)(1)(B) (or which would have been included except for section 959(a)(2)).

Section 956(c)(1) defines United States property to generally include stock of a domestic corporation and an obligation of a United States person. However, section 956(c)(2) excludes from the definition of United States property, the stock or obligations of a domestic corporation which is neither a United States shareholder of the CFC, nor a domestic corporation 25 percent or more of the total combined voting power of which, immediately after the CFC's acquisition of stock in such domestic corporation, is owned (or is considered as being owned) by the United States shareholders of the CFC in the aggregate.

Section 956(e) grants the Secretary authority to prescribe such regulations as may be necessary to carry out the purposes of section 956, including regulations to prevent the avoidance of section 956 through reorganizations or otherwise.

C. Section 367(b)—In General

Section 367(b)(1) provides that in the case of any exchange described in section 332, 351, 354, 355, 356 or 361, in connection with which there is no transfer of property described in section 367(a)(1), a foreign corporation shall be considered to be a corporation except to the extent provided in regulations

prescribed by the Secretary which are necessary or appropriate to prevent the avoidance of Federal income taxes.

Section 367(b)(2) provides that the regulations prescribed pursuant to section 367(b)(1) shall include (but shall not be limited to) regulations dealing with the sale or exchange of stock or securities in a foreign corporation by a United States person, including regulations providing the circumstances under which gain is recognized, amounts are included in gross income as a dividend, adjustments are made to earnings and profits, or adjustments are made to basis of stock or securities, and basis of assets.

Section 367(b) was enacted to ensure that international tax considerations are adequately addressed when the provisions of subchapter C of the Code apply to certain nonrecognition exchanges involving foreign corporations. In adopting section 367(b), Congress noted that "it is essential to protect against tax avoidance * * * upon the repatriation of previously untaxed foreign earnings." H.R. Rep. No. 658, 94th Cong., 1st Sess. 241 (1975).

D. Determination of Basis in Certain Nonrecognition Exchanges

Section 358(a)(1) generally provides that the basis of property received pursuant to an exchange to which section 351, 354, 355, 356, or 361 applies is the same as that of the property exchanged, decreased by the fair market value of any other property (except money) received by the taxpayer, the amount of any money received by the taxpayer, and the amount of loss to the taxpayer which was recognized on such exchange, and increased by the amount which was treated as a dividend, and the amount of gain to the taxpayer which was recognized on such exchange (not including any portion of such gain which was treated as a dividend).

Section 362(a) provides that if property is acquired by a corporation in connection with a transaction to which section 351 applies, or as paid-in surplus or as a contribution to capital, then the basis of such property shall be the same as it would be in the hands of the transferor, increased in the amount of gain recognized to the transferor on such transfer.

Section 1032(a) provides that no gain or loss shall be recognized to a corporation on the receipt of money or other property in exchange for stock (including treasury stock) of such corporation.

E. Determination of Basis for Purposes of Section 956

These temporary regulations apply when a CFC acquires stock or obligations of a domestic issuing corporation, that constitute United States property under section 956(c), from such corporation pursuant to an exchange in which the controlled foreign corporation's basis in such property is determined under section 362(a). If these temporary regulations apply to such an exchange, then, solely for purposes of section 956, the CFC's basis in such United States property shall be no less than the fair market value of the property transferred by the controlled foreign corporation in exchange for such property. For purposes of the temporary regulations, the term property has the meaning set forth in section 317(a), but includes any liability assumed by the CFC in connection with the exchange notwithstanding section 357(a).

These temporary regulations also apply if United States property, the basis of which is determined under these temporary regulations, is transferred to a related person (related person transferee), or by a related person transferee to another related person, pursuant to an exchange in which the related person transferee's basis in such property is determined, in whole or in part, by reference to the transferor's basis in such property. This rule is intended to prevent taxpayers from attempting to avoid the general rule of the temporary regulations by subsequently transferring the United States property to a related person in another nonrecognition transaction.

The basis of United States property determined under the temporary regulations shall apply only for purposes of determining the amount of United States property acquired or held by a CFC under section 956, and accordingly the amount of a United States shareholder's income inclusion under section 951(a)(1)(B) with respect to such CFC.

The temporary regulations apply only to determine the basis of United States property acquired by a CFC pursuant to an exchange that is within the scope of these temporary regulations. All other basis determinations are made under the rules provided under section 956(a) and § 1.956-1(e)(1)(4).

Effective/Applicability Dates

These regulations apply to United States property acquired in exchanges occurring on or after June 24, 2008. No inference is intended as to the basis of United States property acquired by a

controlled foreign corporation pursuant to a transaction described herein under current law, and the IRS may, where appropriate, challenge such transactions under applicable provisions or judicial doctrines.

Special Analyses

These temporary and final regulations are necessary to prevent abusive transactions of the type described in the explanation of provisions in this preamble. Accordingly, good cause is found for dispensing with notice and public procedure pursuant to 5 U.S.C. 553(b) of the Administrative Procedures Act and for dispensing with a delayed effective date pursuant to 5 U.S.C. 553(d)(1) and (3) of such Act. For applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), please refer to the notice of proposed rulemaking published in the Proposed Rules section of this issue of the **Federal Register**. Pursuant to section 7805(f) of the Code, this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small entities.

Drafting Information

The principal author of these regulations is John H. Seibert, Office of Associate Chief Counsel (International). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

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 continues to read in part as follows:

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

■ **Par. 2.** Section 1.956–1 is amended by adding a sentence to the end of paragraph (e)(1) and adding new paragraphs (e)(5), (e)(6) and (f) to read as follows:

§ 1.956–1 Shareholder's pro rata share of a controlled foreign corporation's increase in earnings invested in United States property.

* * * * *

(e) * * * (1) * * * See § 1.956–1T(e)(6) for a special rule for determining amounts attributable to United States property acquired as the

result of certain nonrecognition transactions.

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(e)(5) and (e)(6) [Reserved]. For further guidance, see § 1.956–1T(e)(5) and (e)(6).

(f) *Effective/applicability dates.* (1) Paragraph (e)(5) of this section is effective June 14, 1988, with respect to investments made on or after June 14, 1988. Paragraph (e)(6) of this section applies to nonrecognition property acquired in exchanges occurring on or after June 24, 2008.

■ **Par. 3.** Section 1.956–1T is amended by:

■ 1. Redesignating paragraph (e)(5)(i) as paragraph (e)(5) and revising the paragraph heading for the newly-designated paragraph (e)(5).

■ 2. Adding paragraph (e)(6).

■ 3. Redesignating paragraph (e)(5)(ii) as paragraph (f) and revising newly-designated paragraph (f).

The revisions and additions read as follows:

§ 1.956–1T Shareholder's pro rata share of a controlled foreign corporation's increase in earnings invested in United States property (temporary).

* * * * *

(e)(5) *Exclusion for certain recourse obligations.* * * *

(6) *Adjusted basis of property acquired in certain nonrecognition transactions—(i) Scope and purpose.* This paragraph (e)(6) provides rules for determining, solely for purposes of section 956, the basis of certain United States property acquired by a controlled foreign corporation pursuant to an exchange in which the controlled foreign corporation's basis in such United States property is determined under section 362(a). This paragraph (e)(6) also applies if United States property, the basis in which has been determined under these temporary regulations, is transferred (in one or more subsequent exchanges) to a related person (within the meaning of section 954(d)(3)), pursuant to an exchange in which the related person's basis in such property is determined, in whole or in part, by reference to the transferor's basis in such property. The purpose of this paragraph (e)(6) is to prevent the effective repatriation of earnings and profits of a controlled foreign corporation that acquires United States property in connection with an exchange to which this paragraph (e)(6) applies without a corresponding income inclusion under section 951(a)(1)(B) by claiming a basis in the United States property less than the amount of earnings and profits effectively repatriated.

(ii) *Definition of United States property.* For purposes of this paragraph (e)(6), *United States property* is stock of a domestic corporation described in section 956(c)(1)(B) or an obligation of a domestic corporation described in 956(c)(1)(C) that is acquired by a controlled foreign corporation from the domestic issuing corporation. The exceptions provided under section 956(c)(2) shall apply for this purpose.

(iii) *Basis of United States property.* Solely for purposes of section 956, the basis of United States property acquired by a controlled foreign corporation in connection with an exchange to which this paragraph (e)(6) applies shall be no less than the fair market value of the property transferred by the controlled foreign corporation in exchange for such United States property. For purposes of this paragraph (e)(6), the term *property* has the meaning set forth in section 317(a), but also includes any liability assumed by the controlled foreign corporation in connection with the exchange notwithstanding the application of section 357(a). The fair market value of the property transferred by the controlled foreign corporation in exchange for the United States property shall be determined at the time of the exchange.

(iv) *Timing.* For purposes of § 1.956–2(d)(1)(i)(a), a controlled foreign corporation that acquires United States property in an exchange to which this paragraph (e)(6) applies acquires an adjusted basis in such property at the time of the controlled foreign corporation's exchange of property for such United States property.

(v) *Transfers to related persons.* If a controlled foreign corporation transfers United States property, the basis in which has been determined under this paragraph (e)(6), to a related person (within the meaning of section 954(d)(3)) (related person transferee) in an exchange pursuant to which the related person transferee's basis in such United States property is determined, in whole or in part, by reference to the controlled foreign corporation's basis in such United States property, then, solely for purposes of section 956, the related person transferee's basis in such United States property shall be no less than the basis of such United States property in the hands of the controlled foreign corporation immediately before the exchange as determined under paragraph (e)(6)(iii) of this section. This paragraph (e)(6)(v) shall also apply in the case of one or more successive transfers of the United States property by a related person transferee to one or more persons related to the controlled foreign corporation (within the meaning

of section 954(d)(3)). This paragraph (e)(6)(v) shall apply regardless of whether a subsequent transfer was part of a plan (or series of related transactions) that includes the controlled foreign corporation's acquisition of the United States property.

(vi) *Examples.* The rules of this paragraph (e)(6) are illustrated by the following examples:

Example 1. (i) *Facts.* USP, a domestic corporation, is the common parent of an affiliated group that joins in the filing of a consolidated return. USP owns 100 percent of the stock of US1 and US2, both domestic corporations and members of the USP consolidated group. US1 owns 100 percent of the stock of CFC, a controlled foreign corporation. US2 issues \$100x of its stock to CFC in exchange for \$10x of CFC stock and \$90x cash. US2's transfer of its stock to CFC is described in section 351, US2 recognizes no gain in the exchange under section 1032(a), and CFC's basis in the US2 stock acquired in the exchange is determined under section 362(a).

(ii) *Analysis.* The US2 stock acquired by CFC in the exchange constitutes United States property under paragraph (e)(6)(ii) of this section because CFC acquires the US2 stock from US2, the issuing corporation. Therefore, because CFC's basis in the US2 stock is determined under section 362(a), then for purposes of section 956, CFC's basis in the US2 stock shall, under paragraph (e)(6)(iii) of this section, be no less than \$90x, the fair market value of the property exchanged by CFC for the US2 stock (the \$10x of CFC stock issued in the exchange does not constitute property for purposes of paragraph (e)(6)(iii) of this section). Pursuant to paragraph (e)(6)(iv) of this section, for purposes of § 1.956-2(d)(1)(i)(a) CFC shall be treated as acquiring its basis of no less than \$90x in the US2 stock at the time of its transfer of property to US2 in exchange for the US2 stock. The result would be the same if, instead of CFC transferring \$90x of cash to US2 in the exchange, CFC assumes a \$90x liability of US2.

Example 2. (i) *Facts.* USP, a domestic corporation owns 100 percent of the stock of USS, a domestic corporation. USP also owns 100 percent of the stock of CFC, a controlled foreign corporation. USP's basis in its USS stock equals the fair market value of the USS stock, or \$100x. USP transfers its USS stock to CFC in exchange for \$100x of CFC stock. USP's transfer of its USS stock to CFC is described in section 351, USP recognizes no gain in the exchange under section 351(a), and CFC's basis in the USS stock acquired in the exchange, determined under section 362(a), equals \$100x.

(ii) *Analysis.* The USS stock acquired by CFC in the exchange does not constitute United States property under paragraph (e)(6)(ii) of this section because CFC acquires the USS stock from USP. Therefore, CFC's basis in the US2 stock, for purposes of section 956, is not determined under this paragraph (e)(6). Instead, CFC's basis in the USS stock is determined under the general rule of section 956(a) and under § 1.956-

1(e)(1)-(4). As determined under section 362(a), CFC's basis in the USS stock is \$100x.

Example 3. (i) *Facts.* USP, a domestic corporation, owns 100 percent of the stock of CFC1, a controlled foreign corporation. CFC1 holds United States property (within the meaning of paragraph (e)(6)(ii) of this section) with a basis of \$30x for purposes of section 956 that was determined under paragraph (e)(6)(iii) of this section. CFC1 owns 100 percent of the stock of CFC2, a controlled foreign corporation. CFC1 transfers the United States property to CFC2 in an exchange described in section 351. CFC2's basis in the United States property is determined under section 362(a).

(ii) *Analysis.* In the section 351 exchange, CFC1 transferred United States property to CFC2 with a basis that was determined under paragraph (e)(6)(iii) of this section. Further, CFC2's basis in the United States property is determined under section 362(a) by reference, in whole or in part, to CFC's basis in such property. Therefore, for purposes of section 956, pursuant to paragraph (e)(6)(v) of this section CFC2's basis in the United States property shall be no less than \$30x. Paragraph (e)(6)(v) of this section would also apply if CFC2 subsequently transfers the United States property to another person related to CFC1 (within the meaning of section 954(d)(3)) if such related person's basis in the United States property is determined by reference, in whole or in part, to CFC2's basis in such property.

(f) *Effective/applicability date.* (1) Paragraph (e)(5) of this section is effective June 14, 1988, with respect to investments made on or after June 14, 1988. Paragraph (e)(6) of this section applies to nonrecognition property acquired in exchanges occurring on or after June 24, 2008.

(2) The applicability of paragraph (e)(6) of this section will expire on June 23, 2011.

Steven T. Miller,

Acting Deputy Commissioner for Services and Enforcement.

Approved: June 6, 2008.

Eric Solomon,

Assistant Secretary of the Treasury (Tax Policy).

[FR Doc. E8-14171 Filed 6-23-08; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 9403]

RIN 1545-BH02

Guidance Under Section 664 Regarding the Effect of Unrelated Business Taxable Income on Charitable Remainder Trusts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide guidance under Internal Revenue Code (Code) section 664 on the tax effect of unrelated business taxable income (UBTI) on charitable remainder trusts. The regulations reflect the changes made to section 664(c) by section 424(a) and (b) of the Tax Relief and Health Care Act of 2006. The regulations affect charitable remainder trusts that have UBTI in taxable years beginning after December 31, 2006.

DATES: *Effective Date:* The regulations are effective on June 24, 2008.

Applicability Date: For dates of applicability, see § 1.664-1(c)(3).

FOR FURTHER INFORMATION CONTACT: Cynthia Morton at (202) 622-3060 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in these final regulations have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545-2101. The collection of information in these final regulations is in § 1.664-1(c)(1). This information is required to enable a charitable remainder trust to report and pay the excise tax due on any UBTI of the trust.

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

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