Example. (i) PRS is a calendar-year partnership with two equal partners, individuals A and B. PRS is engaged in an activity described in section 465(c) (Activity). PRS has a $500 recourse applicable debt instrument outstanding. Each partner's amount at risk on January 1, 2009 is $50. On June 1, 2009, the creditor agrees to cancel the $500 indebtedness. PRS realizes $500 of COD income as a result of the reacquisition. The partners' share of the liabilities of PRS decreases by $500 under section 752(b), and each partner's amount at risk is decreased by $250. Other than the $500 of COD income, PRS's income and expenses for 2009 are equal. PRS makes an election under section 108(i) to defer $200 of the $500 COD income realized in connection with the reacquisition. PRS allocates the $500 of COD income equally between its partners, A and B. A and B each have a COD income amount of $250 with respect to the applicable debt instrument. PRS determines that, for both partners A and B, $100 of the $250 COD income amount is the deferred amount, and $150 is the included amount. Beginning in each taxable year 2014 through 2018, A and B each include $20 of the deferred amount in gross income.

(ii) Under paragraph (d)(3)(i) of this section, $50 of the $250 decrease in A's and B's amount at risk in Activity is the deferred section 465 amount for each of A and B and is not taken into account for purposes of determining A's and B's amount at risk in Activity at the close of 2009. In taxable year 2014, A's and B's amount at risk in Activity is decreased by $20 (deferred section 465 amount that equals the deferred amount included in A's and B's gross income in 2014). In taxable year 2015, A's and B's amount at risk in Activity is decreased by $20 for the deferred section 465 amount that equals the deferred amount included in A's and B's gross income in 2015. In taxable year 2016, A's and B's amount at risk in Activity is decreased by $10 (the remaining amount of the deferred section 465 amount).

(e) *Election procedures and reporting requirements*—(1) *Partnerships*—(i) *In general.* A partnership makes an election under section 108(i) by following procedures outlined in guidance and applicable forms and instructions issued by the Commissioner. An electing partnership (or its successor) must provide to its partners certain information as required by guidance and applicable forms and instructions issued by the Commissioner.

(ii) *Tiered passthrough entities.* A partnership that is a direct or indirect partner of an electing partnership (or its successor) or a related partnership or an S corporation partner must provide to its partners or shareholders, as the case may be, certain information as required by guidance and applicable forms and instructions issued by the Commissioner.

(iii) *Related partnerships.* A related partnership must provide to its partners certain information as required by guidance and applicable forms and instructions issued by the Commissioner.

(2) *S corporations*—(i) *In general.* An S corporation makes an election under section 108(i) by following procedures outlined in guidance and applicable forms and instructions issued by the Commissioner. An electing S corporation (or its successor) must provide to its shareholders certain information as required by guidance and applicable forms and instructions issued by the Commissioner.

(ii) *Related S corporations.* A related S corporation must provide to its shareholders certain information as required by guidance and applicable forms and instructions issued by the Commissioner.

(f) *Effective/applicability dates.* For the applicability dates of this section, see § 1.108(i)–0(b).

§ 1.108(i)–2T [Removed]

Par. 3. Section 1.108(i)–2T is removed.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

■ **Par. 4.** The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

■ **Par. 5.** In § 602.101, paragraph (b) is amended as follows:

1. The following entry to the table is removed:

§ 602.101 OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control no.
* * * *	*
1.108(i)–2T	1545–2147
* * * *	*

2. The following entry is added in numerical order to the table to read as follows:

§ 602.101 OMB Control numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control no.
* * * *	*
1.108(i)–2	1545–2147
* * * *	*

Beth Tucker,

Deputy Commissioner for Operations Support.

Approved: June 25, 2013.

Mark J. Mazur,

Assistant Secretary of the Treasury.

[FR Doc. 2013–15885 Filed 7–2–13; 8:45 am]

BILLING CODE 4830–01–P

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 9622]

RIN 1545–BI96

Guidance Regarding Deferred Discharge of Indebtedness Income of Corporations and Deferred Original Issue Discount Deductions

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations under section 108(i) of the Internal Revenue Code (Code). These regulations primarily affect C corporations and provide necessary guidance regarding the accelerated inclusion of deferred discharge of indebtedness (also known as cancellation of debt (COD)) income (deferred COD income) and the accelerated deduction of deferred original issue discount (OID) (deferred OID deductions) under section 108(i)(5)(D) (acceleration rules), and the calculation of earnings and profits as a result of an election under section 108(i). In addition, these regulations provide rules applicable to all taxpayers regarding deferred OID deductions under section 108(i) as a result of a reacquisition of an applicable debt instrument by an issuer or related party.

DATES: *Effective Date:* These regulations are effective on July 2, 2013.

Applicability Dates: For dates of applicability, see § 1.108(i)–0(b).

FOR FURTHER INFORMATION CONTACT: Concerning the acceleration rules for deferred COD income and deferred OID deductions, and the rules for earnings and profits, Robert M. Rhyne (202) 622–7790; concerning the generally applicable rules for deferred OID deductions, William E. Blanchard (202) 622–3950 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these regulations has been

reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507) under control number 1545–2147. The collection of information in these final regulations is in § 1.108(i)–1(b)(3). Under § 1.108(i)–1(b)(3), an electing member (other than the common parent) of a consolidated group may elect to accelerate the inclusion of its remaining deferred COD income with respect to all applicable debt instruments by filing a statement.

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

Books 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, tax returns and return information are confidential, as required by 26 U.S.C. 6103.

Background

Section 108(i) was added to the Code by section 1231 of the American Recovery and Reinvestment Tax Act of 2009 (Pub. L. 111–5, 123 Stat. 338), enacted on February 17, 2009. Section 108(i)(1) provides an election for deferral of the inclusion of COD income arising in connection with the reacquisition after December 31, 2008, and before January 1, 2011, of an applicable debt instrument. If an election is made, a taxpayer's deferred COD income generally is includible in gross income ratably over a 5-taxable-year period, beginning with the taxpayer's fourth or fifth taxable year following the taxable year of the reacquisition (inclusion period).

Section 108(i)(2) provides that if, as part of a reacquisition to which section 108(i)(1) applies, a debt instrument is issued (or is treated as issued) for the applicable debt instrument and there is any OID with respect to the newly issued debt instrument, then the deduction for all or a portion of the OID may be deferred. A debt instrument is treated as issued for an applicable debt instrument if the proceeds of the debt instrument are used directly or indirectly by the issuer to reacquire the applicable debt instrument of the issuer. Section 108(i)(2)(B). In general, the aggregate amount of the deferred OID deductions is allowed ratably over the inclusion period.

Section 108(i)(5)(D) requires a taxpayer to accelerate the inclusion or deduction of any remaining items of deferred COD income or deferred (and otherwise allowable) OID (deferred items) under certain circumstances, including the death of the taxpayer, the liquidation or sale of substantially all the assets of the taxpayer (including in a title 11 or similar case), the cessation of business by the taxpayer, or similar circumstances. Section 108(i)(7) authorizes the Secretary to issue guidance necessary or appropriate for purposes of applying section 108(i), including extending the application of the rules of section 108(i)(5)(D) to other appropriate circumstances.

On August 17, 2009, the IRS and Treasury Department issued Rev. Proc. 2009–37, 2009–36 IRB 309, which outlined the procedures for making a section 108(i) election, and required annual reporting of additional information regarding the amount of deferred COD income included in income in the taxable year, the amount of deferred OID deducted in the taxable year, and the amount of any remaining deferred items. See § 601.601(d)(2)(ii)(*b*). On August 13, 2010, the IRS and Treasury Department published temporary regulations (TD 9497) in the **Federal Register** (75 FR 49394) addressing the acceleration rules for C corporations under section 108(i)(5)(D) and the calculation of a C corporation's earnings and profits as a result of an election under section 108(i). In addition, the temporary regulations addressed the deduction of deferred OID under section 108(i)(2). A notice of proposed rulemaking (REG–142800–09) cross-referencing the temporary regulations was published in the **Federal Register** on the same day (75 FR 49428). Comments responding to the notice of proposed rulemaking were received and are available for public inspection at *http://www.regulations.gov* or upon request. No public hearing was requested or held. After consideration of all comments, the proposed regulations are adopted without substantive change by this Treasury decision, and the corresponding temporary regulations are removed.

Summary of Comments

A. Acceleration Rules for an Electing Corporation in Bankruptcy Proceedings

One commenter requested clarification of the acceleration rules applicable to a C corporation in bankruptcy proceedings. Section 108(i)(5)(D) provides, in relevant part, that in the case of the liquidation or sale of substantially all of the assets of the taxpayer (including in a title 11 or similar case), the taxpayer must accelerate the inclusion or deduction of its remaining deferred items in the taxable year in which such event occurs (or in the case of a title 11 case, the day before the petition is filed). Section 108(i)(7)(A) further authorizes the Secretary to prescribe such regulations, rules, or other guidance as may be necessary or appropriate for purposes of applying section 108(i), including extending the application of the rules of section 108(i)(5)(D) to other circumstances, where appropriate.

The rules provided in the proposed regulations are intended to focus on the underlying purpose of section 108(i)(5)(D) to ensure that the government's ability to collect the tax liability associated with the deferred COD income is not impaired. Consistent with this interpretation, the proposed regulations provide for accelerated inclusion of deferred COD income in circumstances in which a C corporation has impaired its ability to pay the latent tax liability. Under the proposed regulations, any C corporation with deferred COD income by reason of a section 108(i) election (an electing corporation) must accelerate the inclusion of its remaining deferred COD income, whether in bankruptcy proceedings or not, immediately before the occurrence of any one of the following events: The electing corporation (i) changes its tax status, (ii) ceases its corporate existence in a transaction to which section 381(a) does not apply, or (iii) engages in a transaction that impairs its ability to pay the tax liability associated with its deferred COD income (the net value acceleration rule). The acceleration rules under § 1.108(i)–2 also apply to C corporations that are direct or indirect partners of an electing partnership. The proposed regulations do not provide any special acceleration rules for an electing corporation in a title 11 or similar case with regard to either (i) acceleration events or (ii) the time of inclusion of deferred COD income resulting from the occurrence of any acceleration event. Accordingly, all deferred COD income of any electing corporation is required to be taken into account by the electing corporation immediately before the occurrence of any acceleration event enumerated in the proposed regulations.

The IRS and Treasury Department believe that the acceleration rules provided in the proposed regulations, including with respect to the inclusion of deferred COD income immediately before the occurrence of an enumerated acceleration event, are sufficient to protect the collectability of tax relating to deferred COD income in the case of all electing corporations, whether or not in a title 11 or similar case. Accordingly,

consistent with the proposed regulations, these final regulations do not provide special acceleration rules for an electing corporation in bankruptcy proceedings. However, to remove any doubt, the final regulations include non-substantive changes to clearly provide that the acceleration rules contained therein apply with respect to any electing corporation regardless of whether the electing corporation is in a title 11 or similar case at the time a mandatory acceleration event occurs.

B. Guidance on Built-in Items

Commenters made requests for guidance on how the treatment of built-in items under section 382 interacts with section 108(i). The IRS and Treasury Department believe that this issue is better addressed in more general guidance regarding the treatment of built-in items under section 382. Accordingly, no guidance on this issue is provided in these final regulations.

C. Adjustments to Earnings and Profits

The proposed regulations provide that deferred COD income generally increases earnings and profits in the taxable year that it is realized, and deferred OID deductions generally decrease earnings and profits in the taxable year or years in which the deductions would be allowed without regard to the deferral rules of section 108(i). The approach adopted in the proposed regulations reflects the view that an electing corporation has recognized economic income in the year of the discharge, enhancing its dividend paying capacity, and has recognized an economic cost in the year the OID accrues, decreasing its dividend paying capacity. Therefore, earnings and profits are appropriately adjusted. The IRS and Treasury Department also recognized that it was important to provide general guidance regarding the timing for adjustments to earnings and profits so that an electing corporation would understand the consequences of making a section 108(i) election.

A question was raised concerning why the proposed regulations did not provide a rule similar to section 301(e) in conjunction with the general rule for earnings and profits. The IRS and Treasury Department do not believe that such a rule is necessary to achieve the purposes of section 108(i). In addition, because adjustments to earnings and profits for the relevant years have already been made in accordance with the proposed regulations (and Rev. Proc. 2009–37 (2009–36 IRB 309)), the IRS and Treasury Department believe that a change to the earnings and profits rules in these final regulations would be burdensome. Accordingly, these final regulations adopt these rules of the proposed regulations without change.

D. Transitional Rules

The proposed regulations provide that the rules for acceleration of deferred COD income and deferred OID deductions apply prospectively. However, electing corporations were given the option to apply these rules to acceleration events occurring prior to the effective date of the proposed regulations if applied consistently. Because certain provisions of the acceleration rules are time sensitive (for example, the time for restoring value under the net value acceleration rule), the proposed regulations included transitional rules extending the period of time in which an electing corporation needed to comply with the provision's requirements in order to allow electing corporations the ability to use and benefit from these provisions for prior periods.

These transitional rules are no longer necessary because additional time is no longer needed to comply with these provisions. Accordingly, these final regulations amend the proposed regulations by removing these transitional rules.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that these final regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that these regulations merely provide more specific guidance for the timing of the inclusion of deferred COD income and the deduction of deferred original issue discount that is otherwise includible or deductible under the Code. Therefore, a Regulatory Flexibility analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business. No comments were received.

Drafting Information

The principal author of these regulations is Robert M. Rhyne of the Office of Associate Chief Counsel (Corporate). Other personnel from the IRS and Treasury Department participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 and 602 are amended as follows:

PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 is amended by removing the entries for § 1.108(i)–0T, § 1.108(i)–1T, and § 1.108(i)–3T, and adding the entries for § 1.108(i)–0, § 1.108(i)–1, and § 1.108(i)–3, to read, in part, as follows:

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

Section 1.108(i)–0 also issued under 26 U.S.C. 108(i)(7) and 1502. * * *

Section 1.108(i)–1 also issued under 26 U.S.C. 108(i)(7) and 1502. * * *

Section 1.108(i)–3 also issued under 26 U.S.C. 108(i)(7) and 1502. * * *

■ **Par. 2.** Section 1.108(i)–0 is added to read as follows:

§ 1.108(i)–0 Definitions and effective/applicability dates.

(a) *Definitions.* For purposes of regulations under section 108(i)—

(1) *Acquisition.* An *acquisition,* with respect to any applicable debt instrument, includes an acquisition of the debt instrument for cash or other property, the exchange of the debt instrument for another debt instrument (including an exchange resulting from a modification of the debt instrument), the exchange of the debt instrument for corporate stock or a partnership interest, the contribution of the debt instrument to capital, the complete forgiveness of the indebtedness by the holder of the debt instrument, and a direct or an indirect acquisition within the meaning of § 1.108–2.

(2) *Applicable debt instrument.* An *applicable debt instrument* is a debt instrument that was issued by a C corporation or any other person in connection with the conduct of a trade or business by such person. In the case of an intercompany obligation (as defined in § 1.1502–13(g)(2)(ii)),

applicable debt instrument includes only an instrument for which COD income is realized upon the instrument's deemed satisfaction under § 1.1502–13(g)(5).

(3) *C corporation issuer. C corporation issuer* means a C corporation that issues a debt instrument with any deferred OID deduction.

(4) *C corporation partner.* A *C corporation partner* is a C corporation that is a direct or indirect partner of an electing partnership or a related partnership.

(5) *COD income. COD income* means income from the discharge of indebtedness, as determined under sections 61(a)(12) and 108(a) and the regulations under those sections.

(6) *COD income amount.* A *COD income amount* is a partner's distributive share of COD income with respect to an applicable debt instrument of an electing partnership.

(7) *Debt instrument. Debt instrument* means a bond, debenture, note, certificate, or any other instrument or contractual arrangement constituting indebtedness (within the meaning of section 1275(a)(1)).

(8) *Deferral period.* For a reacquisition that occurs in 2009, *deferral period* means the taxable year of the reacquisition and the four taxable years following such taxable year. For a reacquisition that occurs in 2010, *deferral period* means the taxable year of the reacquisition and the three taxable years following such taxable year.

(9) *Deferred amount.* A *deferred amount* is the portion of a partner's COD income amount with respect to an applicable debt instrument that is deferred under section 108(i).

(10) *Deferred COD income. Deferred COD income* means COD income that is deferred under section 108(i).

(11) *Deferred item.* A *deferred item* is any item of deferred COD income or deferred OID deduction that has not been previously taken into account under section 108(i).

(12) *Deferred OID deduction.* A *deferred OID deduction* means an otherwise allowable deduction for OID that is deferred under section 108(i)(2) with respect to a debt instrument issued (or treated as issued under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in § 1.108(i)–3(a).

(13) *Deferred section 465 amount.* A *deferred section 465 amount* is described in paragraph (d)(3) of § 1.108(i)–2.

(14) *Deferred section 752 amount.* A *deferred section 752 amount* is described in paragraph (b)(3) of § 1.108(i)–2.

(15) *Direct partner.* A *direct partner* is a person that owns a direct interest in a partnership.

(16) *Electing corporation.* An *electing corporation* is a C corporation with deferred COD income by reason of a section 108(i) election.

(17) *Electing entity.* An *electing entity* is an entity that is a taxpayer that makes an election under section 108(i).

(18) *Electing member.* An *electing member* is an electing corporation that is a member of an affiliated group that files a consolidated return.

(19) *Electing partnership.* An *electing partnership* is a partnership that makes an election under section 108(i).

(20) *Electing S corporation.* An *electing S corporation* is an S corporation that makes an election under section 108(i).

(21) *Included amount.* An *included amount* is the portion of a partner's COD income amount with respect to an applicable debt instrument that is not deferred under section 108(i) and is included in the partner's distributive share of partnership income for the taxable year of the partnership in which the reacquisition occurs.

(22) *Inclusion period.* The *inclusion period* is the five taxable years following the last taxable year of the deferral period.

(23) *Indirect partner.* An *indirect partner* is a person that owns an interest in a partnership through an S corporation and/or one or more partnerships.

(24) *Issuing entity.* An *issuing entity* is any entity that is—

(i) A related partnership;

(ii) A related S corporation;

(iii) An electing partnership that issues a debt instrument (or is treated as issuing a debt instrument under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in § 1.108(i)–3(a); or

(iv) An electing S corporation that issues a debt instrument (or is treated as issuing a debt instrument under section 108(e)(4)) in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in § 1.108(i)–3(a).

(25) *OID. OID* means original issue discount, as determined under sections 1271 through 1275 (and the regulations under those sections). If the amount of OID with respect to a debt instrument is less than a de minimis amount as determined under § 1.1273–1(d), the OID is treated as zero for purposes of section 108(i)(2).

(26) *Reacquisition.* A *reacquisition,* with respect to any applicable debt instrument, is any event occurring after December 31, 2008 and before January 1, 2011, that causes COD income with respect to such applicable debt instrument, including any acquisition of the debt instrument by the debtor that issued (or is otherwise the obligor under) the debt instrument or a person related to such debtor (within the meaning of section 108(i)(5)(A)).

(27) *Related partnership.* A *related partnership* is a partnership that is related to the electing entity (within the meaning of section 108(i)(5)(A)) and that issues a debt instrument in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in § 1.108(i)–3(a).

(28) *Related S corporation.* A *related S corporation* is an S corporation that is related to the electing entity (within the meaning of section 108(i)(5)(A)) and that issues a debt instrument in a debt-for-debt exchange described in section 108(i)(2)(A) or a deemed debt-for-debt exchange described in § 1.108(i)–3(a).

(29) *Separate interest.* A *separate interest* is a direct interest in an electing partnership or in a partnership or S corporation that is a direct or indirect partner of an electing partnership.

(30) *S corporation partner.* An *S corporation partner* is an S corporation that is a direct or indirect partner of an electing partnership or a related partnership.

(b) *Effective/Applicability dates*—(1) *In general.* The rules of this section, § 1.108(i)–1, and § 1.108(i)–2, apply on or after July 2, 2013 to reacquisitions of applicable debt instruments in taxable years ending after December 31, 2008. In addition, the rules of § 1.108(i)–3 apply on or after July 2, 2013 to debt instruments issued after December 31, 2008, in connection with reacquisitions of applicable debt instruments in taxable years ending after December 31, 2008.

(2) *Prior periods.* For rules applying before July 2, 2013 see § 1.108(i)–0T, § 1.108(i)–1T, § 1.108(i)–2T, and § 1.108(i)–3T, as contained in 26 CFR part 1, revised April 1, 2012.

§ 1.108(i)–0T [Removed]

■ **Par. 3.** Section 1.108(i)–0T is removed.

■ **Par. 4.** Section 1.108(i)–1 is added to read as follows:

§ 1.108(i)–1 Deferred discharge of indebtedness income and deferred original issue discount deductions of C corporations.

(a) *Overview.* Section 108(i)(1) provides an election for the deferral of COD income arising in connection with the reacquisition of an applicable debt

instrument. An electing corporation generally includes deferred COD income ratably over the inclusion period. Paragraph (b) of this section provides rules for the mandatory acceleration of an electing corporation's remaining deferred COD income, the mandatory acceleration of a C corporation issuer's deferred OID deductions, and for the elective acceleration of an electing member's (other than the common parent's) remaining deferred COD income. Paragraph (c) of this section provides examples illustrating the application of the mandatory and elective acceleration rules. Paragraph (d) of this section provides rules for the computation of an electing corporation's earnings and profits. Paragraph (e) of this section refers to the effective/applicability dates.

(b) *Acceleration events*—(1) *Deferred COD income.* Except as otherwise provided in paragraphs (b)(2) and (3) of this section, and § 1.108(i)–2(b)(6) (in the case of a corporate partner), an electing corporation's deferred COD income is taken into account ratably over the inclusion period.

(2) *Mandatory acceleration events.* An electing corporation takes into account all of its remaining deferred COD income, including its share of an electing partnership's deferred COD income, immediately before the occurrence of any one of the events described in this paragraph (b)(2) (mandatory acceleration events), regardless of whether the electing corporation is in a title 11 or similar case at the time the mandatory acceleration event occurs.

(i) *Changes in tax status.* The electing corporation changes its tax status. For purposes of the preceding sentence, an electing corporation is treated as changing its tax status if it becomes one of the following entities:

(A) A tax-exempt entity as defined in § 1.337(d)–4(c)(2).

(B) An S corporation as defined in section 1361(a)(1).

(C) A qualified subchapter S subsidiary as defined in section 1361(b)(3)(B).

(D) An entity operating on a cooperative basis within the meaning of section 1381.

(E) A regulated investment company (RIC) as defined in section 851 or a real estate investment trust (REIT) as defined in section 856.

(F) A qualified REIT subsidiary as defined in section 856(i), but only if the qualified REIT subsidiary was not a REIT immediately before it became a qualified REIT subsidiary.

(ii) *Cessation of corporate existence*—(A) *In general.* The electing corporation ceases to exist for Federal income tax purposes.

(B) *Exception for section 381(a) transactions*—(*1*) *In general.* The electing corporation is not treated as ceasing to exist and is not required to take into account its remaining deferred COD income solely because its assets are acquired in a transaction to which section 381(a) applies. In such a case, the acquiring corporation succeeds to the electing corporation's remaining deferred COD income and becomes subject to section 108(i) and the regulations thereunder, including all reporting requirements, as if the acquiring corporation were the electing corporation. A transaction is not treated as one to which section 381(a) applies for purposes of this paragraph (b)(2)(ii)(B) in the following circumstances—

(*i*) The acquisition of the assets of an electing corporation by an S corporation, if the acquisition is described in section 1374(d)(8);

(*ii*) The acquisition of the assets of an electing corporation by a RIC or REIT, if the acquisition is described in § 1.337(d)–7(a)(2)(ii);

(*iii*) The acquisition of the assets of a domestic electing corporation by a foreign corporation;

(*iv*) The acquisition of the assets of a foreign electing corporation by a domestic corporation, if as a result of the transaction, one or more exchanging shareholders include in income as a deemed dividend the all earnings and profits amount with respect to stock in the foreign electing corporation pursuant to § 1.367(b)–3(b)(3);

(*v*) The acquisition of the assets of an electing corporation by a tax-exempt entity as defined in § 1.337(d)–4(c)(2); or

(*vi*) The acquisition of the assets of an electing corporation by an entity operating on a cooperative basis within the meaning of section 1381.

(*2*) *Special rules for consolidated groups*—(*i*) *Liquidations.* For purposes of paragraph (b)(2)(ii)(B) of this section, the acquisition of assets by distributee members of a consolidated group upon the liquidation of an electing corporation is not treated as a transaction to which section 381(a) applies, unless immediately prior to the liquidation, one of the distributee members owns stock in the electing corporation meeting the requirements of section 1504(a)(2) (without regard to § 1.1502–34). See § 1.1502–80(g).

(*ii*) *Taxable years.* In the case of an intercompany transaction to which section 381(a) applies, the transaction does not cause the transferor or distributor to have a short taxable year for purposes of determining the taxable year of the deferral and inclusion period.

(iii) *Net value acceleration rule*—(A) *In general.* The electing corporation engages in an impairment transaction and, immediately after the transaction, the gross value of the electing corporation's assets (gross asset value) is less than one hundred and ten percent of the sum of its total liabilities and the tax on the net amount of its deferred items (the net value floor) (the net value acceleration rule). Impairment transactions are any transactions, however effected, that impair an electing corporation's ability to pay the amount of Federal income tax liability on its deferred COD income and include, for example, distributions (including section 381(a) transactions), redemptions, below-market sales, charitable contributions, and the incurrence of additional indebtedness without a corresponding increase in asset value. Value-for-value sales or exchanges (for example, an exchange to which section 351 or section 721 applies), or mere declines in the market value of the electing corporation's assets are not impairment transactions. In addition, an electing corporation's investments and expenditures in pursuance of its good faith business judgment are not impairment transactions. For purposes of determining an electing corporation's gross asset value, the amount of any distribution that is not treated as an impairment transaction under paragraph (b)(2)(iii)(D) of this section (distributions and charitable contributions consistent with historical practice) or under paragraph (b)(2)(iii)(E) of this section (special rules for RICs and REITs) is treated as an asset of the electing corporation. Solely for purposes of computing the amount of the net value floor, the tax on the deferred items is determined by applying the highest rate of tax specified in section 11(b) for the taxable year.

(B) *Transactions integrated.* Any transaction that occurs before the reacquisition of an applicable debt instrument, but that occurs pursuant to the same plan as the reacquisition, is taken into account in determining whether the gross asset value of the electing corporation is less than the net value floor.

(C) *Corrective action to restore net value.* An electing corporation is not required to take into account its deferred COD income under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section if, before the due date of the electing corporation's return (including extensions), value is

restored in a transaction in an amount equal to the lesser of—

(*1*) The amount of value that was removed from the electing corporation in one or more impairment transactions (net of amounts previously restored under this paragraph (b)(2)(iii)(C)); or

(*2*) The amount by which the electing corporation's net value floor exceeds its gross asset value.

For example, assume an electing corporation incurs $50 of debt, distributes the $50 of proceeds to its shareholder, and immediately after the distribution, the electing corporation's gross asset value is below the net value floor by $25. The electing corporation may avoid the inclusion of its remaining deferred COD income if value of at least $25 is restored to it before the due date of the electing corporation's tax return (including extensions) for the taxable year that includes the distribution. The value that must be restored is determined at the time of the impairment transaction on a net value basis (for example, additional borrowings by an electing corporation do not restore value).

(D) *Exceptions for distributions and charitable contributions that are consistent with historical practice.* An electing corporation's distributions are not treated as impairment transactions (and are not taken into account as a reduction of the electing corporation's gross asset value when applying the net value acceleration rule to any impairment transaction), to the extent that the distributions are described in section 301(c) and the amount of these distributions, in the aggregate, for the applicable taxable year (applicable distribution amount) does not exceed the annual average amount of section 301(c) distributions over the preceding three taxable years (average distribution amount). If an electing corporation's applicable distribution amount exceeds its average distribution amount (excess amount), then the amount of the impairment transaction equals the excess amount. Appropriate adjustments must be made to take into account any issuances or redemptions of stock, or similar transactions, occurring during the year of distribution or any of the three preceding years. If the electing corporation has a short taxable year for the year of the distribution or for any of the three preceding years, the amounts are determined on an annualized basis. If an electing corporation has been in existence for less than three years, the period during which the electing corporation has been in existence is substituted for the preceding three taxable years. For purposes of determining an electing corporation's average distribution amount, the electing corporation does not take into account the distribution history of a distributor or transferor in a transaction to which section 381(a) applies (other than a transaction described in section 368(a)(1)(F)). Rules similar to those prescribed in this paragraph (b)(2)(iii)(D) also apply to an electing corporation's charitable contributions (within the meaning of section 170(c)) that are consistent with its historical practice.

(E) *Special rules for RICs and REITs*—(*1*) *Distributions.* Notwithstanding paragraph (b)(2)(iii)(D) of this section, in the case of a RIC or REIT, any distribution with respect to stock that is treated as a dividend under section 852 or 857 is not treated as an impairment transaction (and is not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction).

(*2*) *Redemptions by RICs.* Any redemption of a redeemable security, as defined in 15 U.S.C. section 80a-2(a)(32), by a RIC in the ordinary course of business is not treated as an impairment transaction (and is not taken into account as a reduction in gross asset value when applying the net value acceleration rule to any impairment transaction).

(F) *Special rules for consolidated groups*—(*1*) *Impairment transactions and net value acceleration rule.* In the case of an electing member, the determination of whether the member has engaged in an impairment transaction is made on a group-wide basis. An electing member is treated as engaging in an impairment transaction if any member's transaction impairs the group's ability to pay the tax liability associated with all electing members' deferred COD income. Accordingly, intercompany transactions are not impairment transactions. Similarly, the net value acceleration rule is applied by reference to the gross asset value of all members (excluding stock of members whether or not described in section 1504(a)(4)), the liabilities of all members, and the tax on all members' deferred items. For example, assume P is the common parent of the P–S consolidated group, S has a section 108(i) election in effect, and S makes a $100 distribution to P which, on a separate entity basis, would reduce S's gross asset value below the net value floor. S's intercompany distribution to P is not an impairment transaction. However, if P makes a $100 distribution to its shareholder, P's distribution is an impairment transaction (unless the distribution is consistent with its historical practice under paragraph (b)(2)(iii)(D) of this section), and the net value acceleration rule is applied by reference to the assets, liabilities, and deferred items of the P–S group.

(*2*) *Departing member.* If an electing member that previously engaged in one or more impairment transactions on a separate entity basis ceases to be a member of a consolidated group (departing member), the cessation is treated as an impairment transaction and the net value acceleration rule under paragraph (b)(2)(iii)(A) of this section is applied to the departing member on a separate entity basis immediately after ceasing to be a member (and taking into account the impairment transaction(s) that occurred on a separate entity basis). If the departing member's gross asset value is below the net value floor, the departing member's remaining deferred COD income is taken into account immediately before the departing member ceases to be a member (unless value is restored under paragraph (b)(2)(iii)(C) of this section). If the departing member's deferred COD income is not accelerated, the departing member is subject to the reporting requirements of section 108(i) on a separate entity basis. If the departing member becomes a member of another consolidated group, the cessation is treated as an impairment transaction and the net value acceleration rule under paragraph (b)(2)(iii)(A) of this section is applied by reference to the assets, liabilities, and the tax on deferred items of the members of the acquiring group immediately after the transaction. If the acquiring group's gross asset value is below the net value floor, the departing member's remaining deferred COD income is taken into account immediately before the departing member ceases to be a member (unless value is restored under paragraph (b)(2)(iii)(C) of this section). If the departing member's remaining deferred COD income is not accelerated, the common parent of the acquiring group succeeds to the reporting requirements of section 108(i) with respect to the departing member.

(3) *Elective acceleration for certain consolidated group members*—(i) *In general.* An electing member (other than the common parent) of a consolidated group may elect at any time to accelerate in full (and not in part) the inclusion of its remaining deferred COD income with respect to all applicable debt instruments by filing a statement described in paragraph (b)(3)(ii) of this section. Once made, an election to accelerate deferred COD income under this paragraph (b)(3) is irrevocable.

(ii) *Time and manner for making election*—(A) *In general.* The election to accelerate the inclusion of an electing member's remaining deferred COD income with respect to all applicable debt instruments is made on a statement attached to a timely filed tax return (including extensions) for the year in which the deferred COD income is taken into account. The election is made by the common parent on behalf of the electing member. See § 1.1502–77(a).

(B) *Additional information.* The statement must include—

(*1*) *Label.* A label entitled ''SECTION 1.108(i)–1 ELECTION AND INFORMATION STATEMENT BY [INSERT NAME AND EMPLOYER IDENTIFICATION NUMBER OF THE ELECTING MEMBER]''; and

(*2*) *Required Information.* An identification of each applicable debt instrument to which an election under this paragraph (b)(3) applies and the corresponding amount of—

(*i*) Deferred COD income that is accelerated under this paragraph (b)(3); and

(*ii*) Deferred OID deductions that are accelerated under paragraph (b)(4) of this section.

(4) *Deferred OID deductions*—(i) *In general.* Except as otherwise provided in paragraph (b)(4)(ii) of this section and § 1.108(i)–2(b)(6) (in the case of a C corporation partner), a C corporation issuer's deferred OID deductions are taken into account ratably over the inclusion period.

(ii) *OID acceleration events.* A C corporation issuer takes into account all of its remaining deferred OID deductions with respect to a debt instrument immediately before the occurrence of any one of the events described in this paragraph (b)(4)(ii), regardless of whether the C corporation issuer is in a title 11 or similar case.

(A) *Inclusion of deferred COD income.* An electing entity or its owners take into account all of the remaining deferred COD income to which the C corporation issuer's deferred OID deductions relate. If, under § 1.108(i)–2(b) or (c), an electing entity or its owners take into account only a portion of the deferred COD income to which the deferred OID deductions relate, then the C corporation issuer takes into account a proportionate amount of the remaining deferred OID deductions.

(B) *Changes in tax status.* The C corporation issuer changes its tax status within the meaning of paragraph (b)(2)(i) of this section.

(C) *Cessation of corporate existence*—(*1*) *In general.* The C corporation issuer ceases to exist for Federal income tax purposes.

(*2*) *Exception for section 381(a) transactions*—(*i*) *In general.* A C corporation issuer is not treated as ceasing to exist and does not take into account its remaining deferred OID deductions in a transaction to which section 381(a) applies, taking into account the application of § 1.1502–34, as appropriate. See § 1.1502–80(g). This exception does not apply to a transaction that is not treated as one to which section 381(a) applies under paragraph (b)(2)(iii)(B)(*1*) of this section.

(*ii*) *Taxable years.* In the case of an intercompany transaction to which section 381(a) applies, the transaction does not cause the transferor or distributor to have a short taxable year for purposes of determining the taxable year of the deferral and inclusion period.

(c) *Examples.* The application of this section is illustrated by the following examples. Unless otherwise stated, P, S, S1, and X are domestic C corporations, and each files a separate return on a calendar year basis:

Example 1. Net value acceleration rule. (i) *Facts.* On January 1, 2009, S reacquires its own note and realizes $400 of COD income. Pursuant to an election under section 108(i), S defers recognition of the entire $400 of COD income. Therefore, absent a mandatory acceleration event, S will take into account $80 of its deferred COD income in each year of the inclusion period. On December 31, 2010, S makes a $25 distribution to its sole shareholder, P, and this is the only distribution made by S in the past four years. Immediately following the distribution, S's gross asset value is $100, S has no liabilities, and the Federal income tax on S's $400 of deferred COD income is $140. Accordingly, S's net value floor is $154 (110% × $140).

(ii) *Analysis.* Under paragraph (b)(2)(iii)(A) of this section, S's distribution is an impairment transaction. Immediately following the distribution, S's gross asset value of $100 is less than the net value floor of $154. Accordingly, under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section, S takes into account its $400 of deferred COD income immediately before the distribution.

(iii) *Corrective action to restore value.* The facts are the same as in paragraph (i) of this *Example 1,* except that P contributes assets with a value of $25 to S before the due date of S's 2010 return (including extensions). Because P restores $25 of value to S (the lesser of the amount of value removed in the distribution ($25) or the amount by which S's net value floor exceeds its gross asset value ($54)), under paragraph (b)(2)(iii)(C) of this section, S does not take into account its $400 of deferred COD income.

Example 2. Distributions consistent with historical practice. (i) *Facts.* P, a publicly traded corporation, makes a valid section 108(i) election with respect to COD income realized in 2009. On December 31, 2009, P distributes $25 million on its 5 million shares of common stock outstanding. As of January 1, 2006, P has 10 million shares of common stock outstanding, and on March 31, 2006, P distributes $10 million on those 10 million shares. On September 15, 2006, P effects a 2:1 reverse stock split, and on December 31, 2006, P distributes $10 million on its 5 million shares of common stock outstanding. In each of 2007 and 2008, P distributes $5 million on its 5 million shares of common stock outstanding. All of the distributions are described in section 301(c).

(ii) *Amount of impairment transaction.* Under paragraph (b)(2)(iii)(D) of this section, P's 2009 distributions are not treated as impairment transactions (and are not taken into account as a reduction of P's gross asset value when applying the net value acceleration rule to any impairment transaction), to the extent that the aggregate amount distributed in 2009 (the applicable distribution amount) does not exceed the annual average amount of distributions (the average distribution amount) over the preceding three taxable years. Accordingly, P's applicable distribution amount for 2009 is $25 million, and its average distribution amount is $10 million ($20 million (2006) plus $5 million (2007) plus $5 million (2008) divided by 3). The reverse stock split in 2006 is not a transaction requiring an adjustment to the determination of the average distribution amount. Because P's applicable distribution amount of $25 million exceeds its average distribution amount of $10 million, under paragraph (b)(2)(iii)(D) of this section, the amount of P's 2009 distribution that is treated as an impairment transaction is $15 million. The balance of the 2009 distribution, $10 million, is not treated as an impairment transaction (and is not taken into account as a reduction in P's gross asset value when applying the net value acceleration rule to any impairment transaction).

(iii) *Distribution history.* The facts are the same as in paragraph (i) of this *Example 2,* except that in 2010, P merges into X in a transaction to which section 381(a) applies, with X succeeding to P's deferred COD income, and X makes a distribution to its shareholders. For purposes of determining whether X's distribution is consistent with its historical practice, the average distribution amount is determined solely with respect to X's distribution history.

Example 3. Cessation of corporate existence. (i) *Transaction to which section 381(a) applies.* P owns all of the stock of S. In 2009, S reacquires its own note and elects to defer recognition of its $400 of COD income under section 108(i). On December 31, 2010, S liquidates into P in a transaction that qualifies under section 332. Under paragraph (b)(2) of this section, S must take into account all of its remaining deferred COD income upon the occurrence of any one of the mandatory acceleration events. Although S ceases its corporate existence as a result of the liquidation, S is not required to take into account its remaining deferred COD income under the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. However, under paragraph (b)(2)(iii)(A) of this section, S's distribution to P is an impairment

transaction and the net value acceleration rule is applied with respect to the assets, liabilities, and deferred items of P (S's successor) immediately following the distribution. If S's deferred COD income is not taken into account under the net value acceleration rule of (b)(2)(iii) of this section, P succeeds to S's remaining deferred COD income and to S's reporting requirements as if P were the electing corporation.

(ii) *Debt-laden distributee.* The facts are the same as in paragraph (i) of this *Example 3,* except that in the liquidation, S distributes $100 of assets to P, a holding company whose only asset is its stock in S. Assume that immediately following the distribution, P's gross asset value is $100, P has $60 of liabilities, and the Federal income tax on the $400 of deferred COD income is $140. Under paragraph (b)(2) of this section, S must take into account all of its remaining deferred COD income upon the occurrence of any one of the mandatory acceleration events. Although S ceases its corporate existence as a result of the liquidation, S is not required to take into account its remaining deferred COD income under the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. However, under paragraph (b)(2)(iii)(A) of this section, S's distribution to X is an impairment transaction and the net value acceleration rule is applied with respect to the assets, liabilities, and deferred items of P (S's successor). Immediately following the distribution, P's gross asset value of $100 is less than the net value floor of $220 [110% × ($60 + $140)]. Accordingly, under the net value acceleration rule of paragraph (b)(2)(iii)(A) of this section, S is required to take into account its $400 of deferred COD income immediately before the distribution, unless value is restored to P pursuant to (b)(2)(iii)(C) of this section.

(iii) *Foreign acquirer.* The facts are the same as in paragraph (i) of this *Example 3,* except that P is a foreign corporation. Although S's assets are acquired in a transaction to which section 381(a) applies, under paragraph (b)(2)(ii)(B)(*1*)(*iii*) of this section, the exception to accelerated inclusion does not apply and S takes into account its remaining deferred COD income immediately before the liquidation. See also section 367(e)(2) and the regulations thereunder.

(iv) *Section 338 transaction.* P, the common parent of a consolidated group (P group), owns all the stock of S1, one of the members of the P group. In 2009, S1 reacquires its own indebtedness and realizes $30 of COD income. Pursuant to an election under section 108(i), S1 defers recognition of the entire $30 of COD income. In 2010, P sells all the stock of S1 to X, an unrelated corporation, for $300, and P and X make a timely section 338(h)(10) election with respect to the sale. Under paragraph (b)(2)(ii)(A) of this section, an electing corporation takes into account its remaining deferred COD income when it ceases its existence for Federal income tax purposes unless the exception in paragraph (b)(2)(ii)(B) of this section applies. Pursuant to section 338(h)(10) and the regulations, S1 is treated as transferring all of its assets to an unrelated person in exchange for consideration that includes the discharge of its liabilities. This deemed value-for-value exchange is not an impairment transaction. Following the deemed sale, while S1 is still a member of the P group, S1 is treated as distributing all of its assets to P and as ceasing its existence. Under these facts, the distribution of all of S1's assets constitutes a deemed liquidation, and is a transaction to which sections 332 and 381(a) apply. Although S1 ceases its corporate existence as a result of the liquidation, S1 is not required to take into account its remaining deferred COD income under the exception in paragraph (b)(2)(ii)(B) of this section because its assets are acquired in a transaction to which section 381(a) applies. P succeeds to S1's remaining deferred COD income and to S1's reporting requirements as if P were the electing corporation. Under paragraph (b)(2)(iii)(F)(*1*) of this section, the intercompany distribution from S1 to P is not an impairment transaction.

(d) *Earnings and profits*—(1) *In general.* Deferred COD income increases earnings and profits in the taxable year that it is realized and not in the taxable year or years that the deferred COD income is includible in gross income. Deferred OID deductions decrease earnings and profits in the taxable year or years in which the deduction would be allowed without regard to section 108(i).

(2) *Exceptions*—(i) *RICs and REITs.* Notwithstanding paragraph (d)(1) of this section, deferred COD income increases earnings and profits of a RIC or REIT in the taxable year or years in which the deferred COD income is includible in gross income and not in the year that the deferred COD income is realized. Deferred OID deductions decrease earnings and profits of a RIC or REIT in the taxable year or years that the deferred OID deductions are deductible.

(ii) *Alternative minimum tax.* For purposes of calculating alternative minimum taxable income, any items of deferred COD income or deferred OID deduction increase or decrease, respectively, adjusted current earnings under section 56(g)(4) in the taxable year or years that the item is includible or deductible.

(e) *Effective/applicability dates.* For *effective/applicability dates,* see § 1.108(i)–0(b).

§ 1.108(i)–1T [Removed].

■ **Par. 5.** Section 1.108(i)–1T is removed.

■ **Par. 6.** Section 1.108(i)–3 is added to read as follows:

§ 1.108(i)–3 Rules for the deduction of OID.

(a) *Deemed debt-for-debt exchanges*—(1) *In general.* For purposes of section 108(i)(2) (relating to deferred OID deductions that arise in certain debt-for-debt exchanges involving the reacquisition of an applicable debt instrument), if the proceeds of any debt instrument are used directly or indirectly by the issuer or a person related to the issuer (within the meaning of section 108(i)(5)(A)) to reacquire an applicable debt instrument, the debt instrument shall be treated as issued for the applicable debt instrument being reacquired. Therefore, section 108(i)(2) may apply, for example, to a debt instrument issued by a corporation for cash in which some or all of the proceeds are used directly or indirectly by the corporation's related subsidiary in the reacquisition of the subsidiary's applicable debt instrument.

(2) *Directly or indirectly.* Whether the proceeds of an issuance of a debt instrument are used directly or indirectly to reacquire an applicable debt instrument depends upon all of the facts and circumstances surrounding the issuance and the reacquisition. The proceeds of an issuance of a debt instrument will be treated as being used indirectly to reacquire an applicable debt instrument if—

(i) At the time of the issuance of the debt instrument, the issuer of the debt instrument anticipated that an applicable debt instrument of the issuer or a person related to the issuer would be reacquired by the issuer, and the debt instrument would not have been issued if the issuer had not so anticipated such reacquisition;

(ii) At the time of the issuance of the debt instrument, the issuer of the debt instrument or a person related to the issuer anticipated that an applicable debt instrument would be reacquired by a related person and the related person receives cash or property that it would not have received unless the reacquisition had been so anticipated; or

(iii) At the time of the reacquisition, the issuer or a person related to the issuer foresaw or reasonably should have foreseen that the issuer or a person related to the issuer would be required to issue a debt instrument, which it would not have otherwise been required to issue if the reacquisition had not occurred, in order to meet its future economic needs.

(b) *Proportional rule for accruals of OID.* For purposes of section 108(i)(2), if only a portion of the proceeds from the issuance of a debt instrument are used directly or indirectly to reacquire an applicable debt instrument, the rules of section 108(i)(2)(A) will apply to the portion of OID on the debt instrument that is equal to the portion of the proceeds from such instrument used to reacquire the outstanding applicable

debt instrument. Except as provided in the last sentence of section 108(i)(2)(A), the amount of deferred OID deduction that is subject to section 108(i)(2)(A) for a taxable year is equal to the product of the amount of OID that accrues in the taxable year under section 1272 or section 1275 (and the regulations under those sections), whichever section is applicable, and a fraction, the numerator of which is the portion of the total proceeds from the issuance of the debt instrument used directly or indirectly to reacquire the applicable debt instrument and the denominator of which is the total proceeds from the issuance of the debt instrument.

(c) *No acceleration*—(1) *Retirement.* Retirement of a debt instrument subject to section 108(i)(2) does not accelerate deferred OID deductions.

(2) *Cross-reference.* See § 1.108(i)–1 and § 1.108(i)–2 for rules relating to the acceleration of deferred OID deductions.

(d) *Examples.* The application of this section is illustrated by the following examples. Unless otherwise stated, all taxpayers in the following examples are calendar-year taxpayers, and P and S each file separate returns:

Example 1. (i) *Facts.* P, a domestic corporation, owns all of the stock of S, a domestic corporation. S has a debt instrument outstanding that has an adjusted issue price of $100,000. On January 1, 2010, P issues for $160,000 a four-year debt instrument that has an issue price of $160,000 and a stated redemption price at maturity of $200,000, resulting in $40,000 of OID. In P's discussion with potential lenders/holders, and as described in offering materials provided to potential lenders/holders, P disclosed that it planned to use all or a portion of the proceeds from the issuance of the debt instrument to reacquire outstanding debt of P and its affiliates. Following the issuance, P makes a $70,000 capital contribution to S. S then reacquires its debt instrument from X, a person not related to S within the meaning of section 108(i)(5)(A), for $70,000. At the time of the reacquisition, the adjusted issue price of S's debt instrument is $100,000. Under § 1.61–12(c), S realizes $30,000 of COD income. S makes a section 108(i) election for the $30,000 of COD income.

(ii) *Analysis.* Under the facts, at the time of P's issuance of its $160,000 debt instrument, P anticipated that the loan proceeds would be used to reacquire the debt of S, and P's debt instrument would not have been issued for an amount greater than $90,000 if P had not anticipated that S would use the proceeds to reacquire its debt. Pursuant to paragraph (a) of this section, the proceeds from P's issuance of its debt instrument are treated as being used indirectly to reacquire S's applicable debt instrument. Therefore, section 108(i)(2)(B) applies to P's debt instrument and P's OID deductions on its debt instrument are subject to deferral under section 108(i)(2)(A). However, because only a portion of the proceeds from P's debt instrument are used by S to reacquire its applicable debt instrument, only a portion of P's total OID deductions will be deferred under section 108(i)(2)(A). See section 108(i)(2)(B). Accordingly, a maximum of $17,500 ($40,000 × $70,000/$160,000) of P's $40,000 total OID deductions is subject to deferral under section 108(i)(2)(A). Under paragraph (b) of this section, the amount of P's deferred OID deduction each taxable year under section 108(i)(2)(A) is equal to the product of the amount of OID that accrues in the taxable year under section 1272 for the debt instrument and a fraction ($70,000/$160,000). As a result, P's deferred OID deductions are the following amounts: $4,015.99 for 2010 ($9,179.40 × $70,000/$160,000); $4,246.39 for 2011 ($9,706.04 × $70,000/$160,000); $4,490.01 for 2012 ($10,262.88 × $70,000/$160,000); and $4,747.61 for 2013 ($10,851.68 × $70,000/$160,000).

Example 2. (i) *Facts.* The facts are the same as in *Example 1,* except that S makes a section 108(i) election for only $10,000 of the $30,000 of COD income.

(ii) *Analysis.* The maximum amount of P's deferred OID deductions under section 108(i)(2)(A) is $10,000 rather than $17,500 because S made a section 108(i) election for only $10,000 of the $30,000 of COD income. Under section 108(i)(2)(A), because the amount of OID that accrues prior to 2014 attributable to the portion of the debt instrument issued to indirectly reacquire S's applicable debt instrument under paragraph (b) of this section ($17,500) exceeds the amount of deferred COD income under section 108(i) ($10,000), P's deferred OID deductions are the following amounts: $4,015.99 for 2010; $4,246.39 for 2011; $1,737.62 for 2012; and $0 for 2013.

Example 3. (i) *Facts.* The facts are the same as in *Example 1,* except that P pays $200,000 in cash to the lenders/holders on December 31, 2012, to retire the debt instrument. P did not directly or indirectly obtain the funds to retire the debt instrument from the issuance of another debt instrument with OID.

(ii) *Analysis.* Under paragraph (c)(1) of this section, the retirement of P's debt instrument is not an acceleration event for the deferred OID deductions of $4,015.99 for 2010, $4,246.39 for 2011, and $4,490.01 for 2012. Except as provided in § 1.108(i)–1(b)(4), these amounts will be taken into account during the inclusion period. P, however, paid a repurchase premium of $10,851.68 in 2012 ($200,000 minus the adjusted issue price of $189,148.32) to retire the debt instrument. If otherwise allowable, P may deduct this amount in 2012 under § 1.163–7(c).

(e) *Effective/applicability dates.* For *effective/applicability dates,* see § 1.108(i)–0(b).

§ 1.108(i)–3T [Removed]

■ **Par. 7.** Section 1.108(i)–3T is removed.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

■ **Par. 8.** The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

■ **Par. 9.** In § 602.101, paragraph (b) is revised as follows:

■ 1. The following entry to the table is removed:

§ 602.101 OMB Control Numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control no.
* * * * *	
1.108(i)–1T	1545–2147
* * * * *	

* * * * *

■ 2. The following entry is added in numerical order to the table:

§ 602.101 OMB Control Numbers.

* * * * *

(b) * * *

CFR part or section where identified and described	Current OMB control no.
* * * * *	
1.108(i)–1	1545–2147
* * * * *	

Beth Tucker,

Deputy Commissioner for Operations Support.

Approved: June 11, 2013.

Mark J. Mazur,

Assistant Secretary of the Treasury (Tax Policy).

[FR Doc. 2013–15881 Filed 7–2–13; 8:45 am]

BILLING CODE 4830–01–P

DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 165

[Docket No. USCG–2013–0238]

RIN 1625–AA00

Safety Zone; Feast of Lanterns Fireworks Display, Pacific Grove, CA

AGENCY: Coast Guard, DHS.