

INTERNAL REVENUE BULLETIN



HIGHLIGHTS OF THIS ISSUE

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

EMPLOYEE PLANS

Rev. Proc. 2020-43, page 991.

This revenue procedure provides the inflation-adjusted maximum dollar amount that may be made newly available for excepted benefit health reimbursement arrangements or other account-based group health plans for plan years beginning after December 31, 2020, and before January 1, 2022. Due to indexing methodology requiring rounding down to the nearest \$50 increment, this amount remains \$1,800 for the 2021 plan year.

Rev. Proc. 2020-46, page 995.

This revenue procedure modifies and updates Rev. Proc. 2016-47, 2016-37 I.R.B. 346, which provides a list of permissible reasons for a taxpayer to self-certify eligibility for a waiver of the 60-day rollover requirement under certain eligible retirement plans. This revenue procedure modifies that list by adding a new reason: a distribution was made to a state unclaimed property fund.

EMPLOYMENT PLANS

Notice 2020-77, page 988.

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

Bulletin No. 2020-45 November 2, 2020

INCOME TAX

Announcement 2020-40, page 999.

The United States provided written notification, dated August 18, 2020, to the Government of the Hong Kong Special Administrative Region of its termination of a reciprocal agreement to exempt from income tax certain income from the international operation of ships. The termination of the agreement takes effect on January 1, 2021, and will have effect for taxable years beginning on or after January 1, 2021.

Rev. Proc. 2020-44, page 991.

To facilitate the market's transition away from the London Interbank Offered Rate and other interbank offered rates, this revenue procedure mitigates certain potential tax consequences of adopting fallback language recommended by the Alternative Reference Rates Committee (ARRC) and the International Swaps and Derivatives Association (ISDA). The revenue procedure generally provides that modifying certain contracts to incorporate the ARRC's and ISDA's recommended fallback language will not result in a realization event. In addition, the revenue procedure generally provides that such modifications will not result in legging out of an integrated transaction or in the disposition or termination of either leg of a hedging transaction.

Rev. Rul. 2020-22, page 963.

Federal rates; adjusted federal rates; adjusted federal long-term rate, and the long-term tax exempt rate. For purposes of sections 382, 1274, 1288, 7872 and other sections of the Code, tables set forth the rates for November 2020.

Rev. Rul. 2020-24, page 965.

This revenue ruling clarifies the federal income tax withholding and reporting obligations that apply for the year a payment is made from a qualified plan to a state unclaimed property fund.

T.D. 9911, page 966.

The final regulations provide guidance on determining life insurance reserves and changing the method of computing certain insurance company reserves. The final regulations also authorize changes to insurance company reporting requirements and contain numerous conforming changes to other regulations. The final regulations implement legislative changes made by sections 13513 and 13517 of the Tax Cuts and Jobs Act.

The main regulation citations are: 26 CFR 1.338-11: Effect of section 338 election on insurance company targets; 26 CFR 1.807-1: Computation of life insurance reserves; 26 CFR 1.807-3: Reporting of reserves; 26 CFR 1.807-4: Adjustment for change in computing reserves; 26 CFR 1.816-1: Life insurance reserves; 26 CFR 1.817A-1: Certain modified guaranteed contracts; 26 CFR 1.6012-2: Corporations required to make returns of income; 26 CFR

301.9100-6T: Time and manner of making certain elections under the Deficit Reduction Act of 1984.

T.D. 9913, page 975.

These final regulations clarify the definition of a “qualifying relative” for purposes of various provisions of the Internal Revenue Code for taxable years 2018 through 2025.

T.D. 9918, page 979.

This document contains final regulations clarifying that the following deductions allowed to an estate or non-grantor trust are not miscellaneous itemized deductions subject to the suspension in section 67(g): costs paid or incurred in connection with the administration of an estate or non-grantor trust that would not have been incurred if the property were not held in the estate or trust, the personal exemption of an estate or non-grantor trust, the distribution deduction for trusts distributing current income, and the distribution deduction for estates and trusts accumulating income. The final regulations also provide guidance on determining the character, amount, and allocation of deductions in excess of gross income succeeded to by a beneficiary on the termination of an estate or non-grantor trust.

The IRS Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly.

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

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

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

against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.

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

Part II.—Treaties and Tax Legislation.

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

Part III.—Administrative, Procedural, and Miscellaneous.

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

Part IV.—Items of General Interest.

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

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

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

Part I

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

(Also §§ 42, 280G, 382, 467, 468, 482, 483, 1288, 7520, 7872.)

Rev. Rul. 2020-22

This revenue ruling provides various prescribed rates for federal income tax

purposes for November 2020 (the current month). Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section 1288(b). Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropri-

ate percentages for determining the low-income housing credit described in section 42(b)(1) for buildings placed in service during the current month. However, under section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, shall not be less than 9%. Finally, Table 5 contains the federal rate for determining the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 2020-22 TABLE 1
Applicable Federal Rates (AFR) for November 2020
Period for Compounding

| | <i>Annual</i> | <i>Semiannual</i> | <i>Quarterly</i> | <i>Monthly</i> |
|----------|---------------|-------------------|------------------|----------------|
| | | <i>Short-term</i> | | |
| AFR | 0.13% | 0.13% | 0.13% | 0.13% |
| 110% AFR | 0.14% | 0.14% | 0.14% | 0.14% |
| 120% AFR | 0.16% | 0.16% | 0.16% | 0.16% |
| 130% AFR | 0.17% | 0.17% | 0.17% | 0.17% |
| | | <i>Mid-term</i> | | |
| AFR | 0.39% | 0.39% | 0.39% | 0.39% |
| 110% AFR | 0.43% | 0.43% | 0.43% | 0.43% |
| 120% AFR | 0.47% | 0.47% | 0.47% | 0.47% |
| 130% AFR | 0.51% | 0.51% | 0.51% | 0.51% |
| 150% AFR | 0.59% | 0.59% | 0.59% | 0.59% |
| 175% AFR | 0.68% | 0.68% | 0.68% | 0.68% |
| | | <i>Long-term</i> | | |
| AFR | 1.17% | 1.17% | 1.17% | 1.17% |
| 110% AFR | 1.29% | 1.29% | 1.29% | 1.29% |
| 120% AFR | 1.40% | 1.40% | 1.40% | 1.40% |
| 130% AFR | 1.53% | 1.52% | 1.52% | 1.52% |

REV. RUL. 2020-22 TABLE 2
Adjusted AFR for November 2020
Period for Compounding

| | <i>Annual</i> | <i>Semiannual</i> | <i>Quarterly</i> | <i>Monthly</i> |
|-------------------------|---------------|-------------------|------------------|----------------|
| Short-term adjusted AFR | 0.10% | 0.10% | 0.10% | 0.10% |
| Mid-term adjusted AFR | 0.30% | 0.30% | 0.30% | 0.30% |
| Long-term adjusted AFR | 0.89% | 0.89% | 0.89% | 0.89% |

REV. RUL. 2020-22 TABLE 3

Rates Under Section 382 for November 2020

| | |
|--|------|
| Adjusted federal long-term rate for the current month | .89% |
| Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.) | .89% |

REV. RUL. 2020-22 TABLE 4

Appropriate Percentages Under Section 42(b)(1) for November 2020

Note: Under section 42(b)(2), the applicable percentage for non-federally subsidized new buildings placed in service after July 30, 2008, shall not be less than 9%.

| | |
|--|-------|
| Appropriate percentage for the 70% present value low-income housing credit | 7.18% |
| Appropriate percentage for the 30% present value low-income housing credit | 3.08% |

REV. RUL. 2020-22 TABLE 5

Rate Under Section 7520 for November 2020

| | |
|---|-----|
| Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest | .4% |
|---|-----|

Section 42.—Low-Income Housing Credit

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

Section 483.—Interest on Certain Deferred Payments

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

Section 280G.—Golden Parachute Payments

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

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

The applicable federal short-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

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

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

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

The adjusted applicable federal long-term rate is set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

Section 482.—Allocation of Income and Deductions Among Taxpayers

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

Section 7520.—Valuation Tables

The applicable federal mid-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

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

The applicable federal short-term, mid-term, and long-term rates are set forth for the month of November 2020. See Rev. Rul. 2020-22, page 963.

Section 3405.—Special Rules for Pensions, Annuities, and Certain Other Deferred Income

(Also, § 6047)

Rev. Rul. 2020-24

Withholding and Reporting With Respect to Payments From Qualified Plans to State Unclaimed Property Funds

ISSUES

(1) Under the facts presented, is the payment of Individual C's accrued benefit from Plan X subject to federal income tax withholding under § 3405 of the Internal Revenue Code?

(2) Is the payment from Plan X subject to reporting under § 6047?

FACTS

Employer M is the plan administrator of Plan X, a qualified retirement plan under § 401(a) that does not include designated Roth accounts under § 402A, hold employer securities, or provide benefits described in § 104 (compensation for injuries or sickness) or § 105 (amounts received under accident and health plans). Individual C, a U.S. person under § 7701(a)(30)(A) with a calendar year taxable year, has an accrued benefit in Plan X with a value of \$900, has not made a withholding election under § 3405 with respect to her benefit, and has no investment in the contract within the meaning of § 72 with respect to her benefit. In 2020, Individual C's accrued benefit (net of any applicable withholding) is paid to the State J unclaimed property fund, a fund under which a claim for property may be made by an owner.¹

LAW AND ANALYSIS

(1) Withholding

Section 3405 provides federal income tax withholding rules with respect to designated distributions. Under § 3405(d), the payor or plan administrator shall withhold from a designated distribution, and be liable for, payment of the tax required to be withheld under § 3405. Under § 3405(e)(1)(A), the term "designated distribution" means, except as provided in § 3405(e)(1)(B), any distribution or payment from or under an employer deferred compensation plan, an individual retirement plan under § 7701(a)(37), or a commercial annuity. Under § 3405(e)(5), the term "employer deferred compensation plan" includes any pension, annuity, profit-sharing, or stock bonus plan, or other plan deferring the receipt of compensation. A qualified retirement plan under § 401(a) is an employer deferred compensation plan.

Section 3405(e)(1)(B)(i), (iii), and (iv) provides exceptions to treatment as a designated distribution with respect to amounts that are wages, amounts that are subject to withholding on nonresident aliens and foreign corporations,² and distributions described in § 404(k)(2) relating to dividends on employer securities. None of these exceptions apply under the facts presented. In addition, § 3405(e)(1)(B)(ii) provides that a designated distribution does not include the portion of a distribution or payment it is reasonable to believe is not includible in gross income. Under the facts presented, it is not reasonable for Employer M to believe that the payment of any portion of Individual C's accrued benefit from Plan X is not includible in gross income.

Because none of the statutory exceptions from treatment as a designated distribution in § 3405(e)(1)(B) apply to the payment of Individual C's accrued benefit from Plan X, the payment, including the amount withheld, is a designated distribution. Accordingly, the payment is subject to federal income tax withholding under § 3405(d).

(2) Reporting

Section 6047(d) provides that the Secretary of the Treasury shall, by forms or

regulations, require the employer maintaining a plan from which designated distributions (as defined in § 3405(e)(1)) may be made, or the plan administrator of that plan, to make returns and reports regarding the plan. However, no such return or report may be required with respect to distributions to any person during any year unless the distributions aggregate \$10 or more.

Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, is used to satisfy the reporting obligations under § 6047(d). Under the 2020 instructions to Form 1099-R, a Form 1099-R must be filed for each person to whom a designated distribution of \$10 or more has been made, and the total amount of the distribution (before income tax or other withholding) must be reported in Box 1 of that form. In addition, under those instructions, the federal income tax withheld must be reported in Box 4 of the Form 1099-R.

The Plan X payment of Individual C's accrued benefit, including both the amount sent to the State J unclaimed property fund and the amount withheld, is a designated distribution under § 3405(e)(1) that exceeds the reporting threshold. Accordingly, Employer M is required to report that designated distribution in Box 1, and the federal income tax withheld in Box 4, of the Form 1099-R for 2020.

HOLDINGS

(1) The payment of Individual C's accrued benefit from Plan X is subject to federal income tax withholding under § 3405.

(2) The payment from Plan X is subject to reporting under § 6047.

TRANSITION RELIEF

A person will not be treated as failing to comply with the withholding and reporting requirements described in this revenue ruling with respect to payments made before the earlier of January 1, 2022, or the date it becomes reasonably practicable for the person to comply with those requirements.

¹ This revenue ruling does not address whether the payment to the State J unclaimed property fund otherwise complies with applicable law. For example, it does not address compliance with any search requirements applicable under state law and does not address matters arising under Title I of the Employee Retirement Income Security Act of 1974, Pub. L. 93-406, 88 Stat. 829, as amended, for which the Department of Labor has subject matter jurisdiction under Reorganization Plan No. 4 of 1978, 5 U.S.C. App.

² Under § 3405(e)(1)(B)(iii), a designated distribution does not include a payment that is subject to withholding under the withholding rules applicable to payments to nonresident aliens and foreign corporations. See § 1441 (Withholding of tax on nonresident aliens), § 1442 (Withholding of tax on foreign corporations), and § 1.1441-4(b)(1)(ii).

DRAFTING INFORMATION

The principal author of this revenue ruling is Angelique Carrington of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). Ms. Carrington may be reached at (202) 317-4148 (not a toll-free number).

Section 807 — Rules for certain reserves

26 CFR 1, 301: Computation and Reporting of Reserves for Life Insurance Companies

T.D. 9911

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Parts 1 and 301

Computation and Reporting of Reserves for Life Insurance Companies

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide guidance on the computation of life insurance reserves and the change in basis of computing certain reserves of insurance companies. These final regulations implement recent legislative changes to the Internal Revenue Code. This document affects entities taxable as insurance companies.

DATES: *Effective date:* These regulations are effective October 13, 2020.

Applicability dates: For dates of applicability, see §§ 1.338-11(d)(7)(iii), 1.807-1(c), 1.807-3(b), 1.807-4(e), 1.816-1(b), 1.817A-1(c), and 1.6012-2(l).

FOR FURTHER INFORMATION CONTACT: Ian Follansbee at (202) 317-4453 (not a toll-free number)

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 under sections 807 and 816 of the Internal Revenue Code (Code). Sections 807 and 816 were added to the Code by section 211(a) of the Deficit Reduction Act of 1984, Public Law 98-369, 98 Stat. 494. Section 807 was amended by sections 13513 and 13517 of Public Law No. 115-97, 131 Stat. 2054, 2143, 2144 (2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA). These amendments by the TCJA apply to taxable years beginning after December 31, 2017.

This document also amends or removes the following regulations in 26 CFR: §§ 1.338-11, 1.381(c)(22)-1, 1.801-2, 1.801-5, 1.801-7, 1.801-8, 1.806-4, 1.807-1, 1.809-2, 1.809-5, 1.810-3, 1.817A-0, 1.817A-1, 1.818-2, 1.818-4, 1.848-1, 1.6012-2, and 301.9100-6T. These changes are conforming changes to regulations that (i) relate to repealed or amended law, (ii) reference regulations that are being removed, (iii) have no future application, or (iv) relate to other regulations made final by this document.

The Department of the Treasury (Treasury Department) and the IRS published proposed regulations (REG-132529-17) in the **Federal Register** (85 FR 18496) on April 2, 2020 (proposed regulations). A correction to the proposed regulations was published in the **Federal Register** (85 FR 21129) on April 16, 2020. The Treasury Department and the IRS received six public comments on the proposed regulations. Copies of the comments received are available for public inspection at <https://www.regulations.gov> or upon request. No public hearing was requested, and none was held.

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

Summary of Comments and Explanation of Revisions

This section discusses the public comments received on the proposed regulations, explains the revisions adopted in

the final regulations in response to those comments, and describes guidance the Treasury Department and the IRS are providing contemporaneously with publication of the final regulations in the **Federal Register**.

1. *Comments and Changes Relating to § 1.807-1 of the Proposed Regulations*

Section 807(d) of the Code provides the method of computing life insurance reserves for purposes of determining the income of an insurance company subject to Federal income tax under subchapter L of chapter 1 of the Code (subchapter L). Section 807(d)(1)(A) provides generally that the amount of life insurance reserves for a life insurance contract (other than a variable contract subject to section 807(d)(1)(B)) is the greater of (i) the net surrender value of such contract, or (ii) 92.81 percent of the reserve determined under the tax-reserve method applicable to the contract under section 807(d)(3).

Section 1.807-1(a) of the proposed regulations (proposed § 1.807-1(a)) provides that no asset adequacy reserve may be included in the amount of life insurance reserves under section 807(d). Proposed § 1.807-1(a) describes an asset adequacy reserve as “includ[ing] any reserve that is established as an additional reserve based upon an analysis of the adequacy of reserves that would otherwise be established or any reserve that is not held with respect to a particular contract.” Further, proposed § 1.807-1(a) provides that an asset adequacy reserve is “any reserve or portion of a reserve that would have been established pursuant to an asset adequacy analysis required by the National Association of Insurance Commissioner’s Valuation Manual 30 as it existed on December 22, 2017, the date of enactment of Public Law 115-97”

Two commenters requested that the first quoted provision be changed to provide that asset adequacy reserves are those reserves established pursuant to an analysis of the adequacy of reserves only if that analysis is pursuant to the requirements of the National Association of Insurance Commissioners’ (NAIC) Valuation Manual 30. Both commenters suggested the final regulations state what an asset adequacy reserve “is” as opposed to what it

“includes.” Moreover, both commenters would remove the language that includes within the definition of “asset adequacy reserve” any reserve that is not held with respect to a particular contract.

The final regulations generally incorporate these comments. The final regulations, however, also incorporate in the definition of asset adequacy reserves any reserve that is similar to an asset adequacy reserve that is determined under the NAIC’s requirements as of the date the reserve is determined.

With respect to the second provision previously quoted, one commenter proposed removing the December 22, 2017, fixed date and replacing it with a reference to “the date the reserve is determined.” The commenter believed that such a change would make the provision more consistent with section 807(d)(3), which generally requires using the tax reserve method that is applicable as of the date the reserve is determined.

The final regulations do not adopt this suggestion. Section 807(d)(3) specifically provides that the tax reserve method (for example, the Commissioners’ Reserve Valuation Method (CRVM) or Commissioners’ Annuity Reserve Valuation Method (CARVM)) to be used in determining a reserve is the tax reserve method that is applicable when the reserve is determined. No such rule exists with respect to asset adequacy reserves.

The reserves determined based on the application of those parts of the NAIC Valuation Manual, as it existed when the TCJA was enacted, that implement and define CRVM and CARVM are not asset adequacy reserves. *See* Staff of the Joint Committee on Taxation, 115th Cong., General Explanation of Public Law 115-97, 235 (Comm. Print 2018) (Bluebook) (“Under NAIC-prescribed principle-based reserve methodology in effect at the time of the enactment of the provision, principle-base[d] reserves for any contract do not include any asset adequacy reserve component.”) (citation omitted). On the other hand, any additional reserve required to be set aside under Valuation Manual 30, as it existed when the TCJA was enacted, based on an analysis of the adequacy of the reserves otherwise determined, constitutes an asset adequacy reserve under § 1.807-1 of the final regulations.

One commenter proposed the addition of a general provision explaining the significance and selection of the tax reserve method for a contract. The final regulations include such a provision.

The commenter also proposed the addition of an example illustrating the determination of life insurance reserves under section 807(d)(1) and the exclusion of asset adequacy reserves from life insurance reserves. The Treasury Department and the IRS did not include the example in the final regulations, but the principles illustrated by the example are explained in this preamble.

2. Comments and Changes Relating to § 1.807-4 of the Proposed Regulations

Section 807(f)(1) of the Code provides that if the basis for determining any item referred to in section 807(c) as of the close of any taxable year differs from the basis for such determination as of the close of the preceding taxable year, then so much of the difference between (A) the amount of the item at the close of the taxable year, computed on the new basis, and (B) the amount of the item at the close of the taxable year, computed on the old basis, as is attributable to contracts issued before the taxable year must be taken into account under section 481 as adjustments attributable to a change in method of accounting initiated by the taxpayer and made with the consent of the Secretary.

Section 1.807-4 of the proposed regulations (proposed § 1.807-4) provides guidance relating to both the change in basis of computing reserves of a life insurance company and the change in basis of computing life insurance reserves of an insurance company other than a life insurance company (a nonlife insurance company). Under proposed § 1.807-4(a), a change in basis of computing an item referred to in section 807(c) is a change in method of accounting for purposes of § 1.446-1(e), unless § 1.446-1(e) provides otherwise. Accordingly, under proposed § 1.807-4(a), both a life insurance company changing the basis of computing an item referred to in section 807(c) and a nonlife insurance company changing the basis of computing life insurance reserves must follow the administrative procedures prescribed by the Commissioner of Internal

Revenue or his delegate (Commissioner) to obtain the consent of the Commissioner to such a change.

A. Relationship between section 446 and subchapter L

One commenter suggested that § 1.807-4(a) state at the outset that section 807(f) treats a change in basis of computing reserves as a change in method of accounting. The commenter thought this would better establish why § 1.446-1(e) applies to the change in basis of computing reserves. The final regulations incorporate this suggestion. The amendment of section 807(f) by the TCJA led to the requirement in § 1.807-4(a) that changes in basis of computing an item referred to in section 807(c) must follow the same administrative procedures as other changes in method of accounting. Accordingly, this Treasury decision removes or obsoletes contrary guidance (for example, § 1.806-4 and Rev. Rul. 94-74, 1994-2 C.B. 157).

Another commenter took the position that a change in basis of computing an item referred to in section 807(c) is not a change in method of accounting that should require consent under section 446(e). The commenter believed that the IRS’s consent should be needed under section 481(c) only to reflect a multi-year spread of a section 481(a) adjustment that may result from a change in basis of computing reserves. The Treasury Department and the IRS do not agree with this position. The computation of reserves has always been a method of accounting. *See Am. Gen. Life & Accident Ins. Co. v. United States*, 90-1 USTC (CCH) ¶ 50,010 (M.D. Tenn. 1989) (“[W]hile the government is correct in classifying the change at issue as a change in method of accounting, it is also more specifically a change in the method of computing reserves.”); Rev. Rul. 94-74 (stating that “§ 807(f) is a more specific application of the general tax rules governing a change in method of accounting”). Under the specific provisions of former section 807(f), the general change in method of accounting procedures did not apply to a change in basis of computing reserves. With the TCJA’s amendment to section 807(f), the procedures generally applica-

ble to a change in method of accounting apply to a change in basis of computing reserves under section 807(c). *See* Blue-book at 228 (stating that a company that changes its method of computing reserves must comply with applicable IRS procedures).

The same commenter recommended that if the final regulations do not remove the requirement that a change in basis of computing reserves under section 807(f) requires consent under section 446(e), then the preamble to the final regulations should clarify that section 446(b) does not apply to the determination of insurance reserves. This recommendation is similar to another commenter's recommendation that the preamble should acknowledge that the application of the consent provisions of section 446(e) and § 1.446-1(e) does not affect the role of sections 811(a) and 807(d) with respect to the determination of section 807(c) reserves.

Except in extraordinary circumstances, section 446(b) does not affect the requirement that a life insurance company compute its reserves for Federal income tax purposes as required by subchapter L. Similarly, subchapter L does not affect the requirement under section 446(e) that an insurance company secure the consent of the Commissioner before changing its basis of computing reserves.

B. Examples in § 1.807-4(d)

Proposed § 1.807-4 contains four examples illustrating the principles of proposed § 1.807-4(a) through (c). One commenter suggested several clarifications to Example 1 and Example 2 in proposed § 1.807-4(d). Additionally, the commenter requested additional guidance on how the standard for what constitutes a change in basis of computing reserves applies to frequently-encountered fact patterns involving life insurance reserves, such as under principle-based reserve methodologies.

The final regulations do not include what had been Example 1 and Example 2 in proposed § 1.807-4(d). The principles illustrated in these examples are sufficiently illustrated in the remaining examples. Moreover, the Treasury Department and the IRS are providing additional

guidance on the fact patterns that constitute a change in basis of computing life insurance reserves in Rev. Rul. 2020-19, 2020-40 I.R.B. 611, released contemporaneously with publication of these final regulations in the **Federal Register**.

C. Automatic consent procedures for reserves of nonlife insurance companies

Currently, section 26.04 of Rev. Proc. 2019-43, 2019-48 I.R.B. 1107, provides for automatic consent to a change in method of accounting if that change relates to section 807(c) items (which include life insurance reserves for a nonlife insurance company). One commenter requested that the same treatment be extended to changes in method of accounting for the unearned premium reserves and the unpaid loss reserves of nonlife insurance companies.

The final regulations do not incorporate this request, and the Treasury Department and the IRS do not anticipate that Rev. Proc. 2019-43 will be amended to allow for the requested automatic consent. The automatic consent procedures provided in section 26.04 of Rev. Proc. 2019-43 to life insurance companies for a change in basis of computing reserves and to nonlife insurance companies for a change in basis of computing life insurance reserves were a response to the specific change in section 807(f) made by the TCJA. No such change was made by the TCJA for unearned premium reserves or unpaid loss reserves of nonlife insurance companies.

D. Obsoleting of revenue rulings and notice

The preamble to the proposed regulations proposes obsoleting the following revenue rulings because they are inconsistent with section 807(f), as amended by the TCJA: Rev. Rul. 2002-6, 2002-1 C.B. 460, Rev. Rul. 94-74, 1994-2 C.B. 157, Rev. Rul. 80-117, 1980-1 C.B. 143, Rev. Rul. 80-116, 1980-1 C.B. 141, Rev. Rul. 78-354, 1978-2 C.B. 190, Rev. Rul. 77-198, 1977-1 C.B. 190, Rev. Rul. 75-308, 1975-2 C.B. 264, Rev. Rul. 74-57, 1974-1 C.B. 163, Rev. Rul. 70-568, 1970-2 C.B. 140, Rev. Rul. 70-192, 1970-1 C.B. 153, Rev. Rul. 69-444, 1969-2 C.B. 145, Rev. Rul. 65-240, 1965-2 C.B. 236, Rev. Rul.

65-233, 1965-2 C.B. 228, Rev. Rul. 65-143, 1965-1 C.B. 261.

One commenter believes Rev. Rul. 2002-6, Rev. Rul. 94-74, and Rev. Rul. 69-444 contain principles that provide guidance on what constitutes a change in basis of computing reserves and that additional guidance is needed if these revenue rulings are obsoleted. While this Treasury decision obsoletes those revenue rulings, the Treasury Department and the IRS are providing additional guidance on the fact patterns that constitute a change in basis of computing life insurance reserves contemporaneously with publication of the final regulations in the **Federal Register**. *See* Rev. Rul. 2020-19.

The preamble to the proposed regulations also proposes to obsolete Notice 2010-29, 2010-15 I.R.B. 547, which provided interim guidance relating to variable annuity contracts as a result of the adoption by the NAIC of Actuarial Guideline 43, which describes a principle-based reserve method. No comments were received regarding this proposed obsolescence, and this Treasury decision obsoletes Notice 2010-29.

E. Revising section 26.04 of Rev. Proc. 2019-43

The preamble to the proposed regulations describes revisions that the Treasury Department and the IRS intend to make to section 26.04 of Rev. Proc. 2019-43. First, section 26.04(2)(b)(ii) of Rev. Proc. 2019-43 provides that multiple changes during the same taxable year for the same type of contract are considered a single change in basis and the effects of such changes are netted and treated as a single section 481(a) adjustment. Section 807(f)(1), however, provides that the section 481(a) adjustment is the difference between the amount of any item referred to in section 807(c) computed on the new basis and the amount of such item computed on the old basis. Accordingly, the Treasury Department and the IRS intend to revise section 26.04 of Rev. Proc. 2019-43 to require netting of the section 481(a) adjustments at the level of each item referred to in section 807(c) so there is a single section 481(a) adjustment for each of the items referred to in section 807(c).

Second, section 26.04(1) of Rev. Proc. 2019-43 provides that the automatic change procedures apply to a nonlife insurance company. The Treasury Department and the IRS intend to revise section 26.04 of Rev. Proc. 2019-43 to clarify the manner in which nonlife insurance companies implement changes to the basis of computing life insurance reserves (as defined in section 816(b)) during a taxable year (year of change). Specifically, the clarification would provide that, if a nonlife insurance company changes the basis of computing its life insurance reserves, then for purposes of applying section 832(b)(4), (i) for the year of change, life insurance reserves at the end of the year of change with respect to contracts issued before the year of change are determined on the old basis and (ii) for the year following the year of change, life insurance reserves at the end of the preceding taxable year with respect to contracts issued before the year of change are determined on the new basis. Life insurance reserves attributable to contracts issued during the year of change and thereafter must be computed on the new basis.

One commenter agreed with the intended revisions.

3. Comments and Changes Relating to § 1.807-3 of the Proposed Regulations

Section 13517 of the TCJA added section 807(e)(6) to the Code, which provides that the Secretary of the Treasury or his delegate (Secretary) “shall require reporting (at such time and in such manner as the Secretary shall prescribe) with respect to the opening and closing balance of reserves and with respect to the method of computing reserves for purposes of determining income.” In accordance with section 807(e)(6), § 1.807-3 of the proposed regulations (proposed § 1.807-3) provides that the IRS may require reporting on Form 1120-L with respect to the opening and closing balances of the items described in section 807(c) and with respect to the method of computing such items for the purposes of determining income.

One commenter requested further consultation with the life insurance industry before any additional reserve reporting requirements are implemented. According to the commenter, this consultation will

be necessary to ensure that the information provided is useful to the government and that providing the information is not unduly burdensome to taxpayers relative to the information’s utility.

The IRS understands the importance of obtaining the life insurance industry’s input before changing the reporting requirements. Proposed § 1.807-3 is adopted as final by this Treasury decision, and the IRS expects to consult with the life insurance industry before making any changes to reporting requirements. Further, as discussed in the Special Analysis section of this preamble, any future changes to tax return form requirements stemming from this provision would be subject to burden analysis and public notice and comment under the Paperwork Reduction Act, which requirements the IRS is committed to follow.

4. Comments and Changes Relating to § 1.816-1 of the Proposed Regulations

Section 1.816-1(a) of the proposed regulations (proposed § 1.816-1(a)) provides that a reserve (other than an asset adequacy reserve) that is computed using a tax reserve method as defined in section 807(d)(3) and that meets the requirements of section 816(b)(1) and (b)(2) will not be disqualified as a life insurance reserve solely because the method used to calculate the reserve takes into account factors other than those prescribed by section 816(b)(1) and (b)(2). Thus, for instance, reserves calculated using principle-based reserve methodologies will not fail to qualify as life insurance reserves solely because the reserves might be calculated using certain factors in addition to assumed rates of interest and recognized mortality or morbidity tables.

One commenter requested the preamble for the final regulations state that in some cases the use of additional factors in computing reserves for taxable years prior to the effective date of these final regulations is not prohibited. The commenter did not want any negative inference that proposed § 1.816-1 is making permissible what was before impermissible (namely using certain additional factors in computing reserves).

The Treasury Department and the IRS agree that certain factors other than those

prescribed by section 816(b)(1) and (b)(2) may be taken into account in determining life insurance reserves for taxable years prior to the effective date of these final regulations if the use of such factors would make the calculation of the reserve more accurate. *See, e.g., Mutual Benefit Life Insurance Co. v. Commissioner*, 488 F.2d 1101, 1106 (3d Cir. 1974).

5. Comments and Changes Relating to § 1.6012-2 of the Proposed Regulations

The Conference Report to the TCJA contemplates requiring the electronic filing of annual statements to improve reporting of insurance reserves, as necessary to carry out and enforce section 807. H.R. Rep. No. 115-466, at 478-79 (2017) (Conference Report). In response to the Conference Report, the proposed regulations propose to remove § 1.6012-2(c)(4), which prohibits an insurance company that files its Form 1120-L or Form 1120-PC electronically from attaching its annual statement (or pro forma annual statement) to its return.

One commenter stated that for some of the largest groups of companies, the size limits found in section 2.1.2 of IRS Publication 4164, *Modernized e-File (MeF) Guide to Software Developers and Transmitters, Processing Year 2020*, would likely be exceeded if the annual statement were to be filed electronically, and for other groups of companies, the size limit would likely be exceeded by the return and the annual statement when combined. The commenter suggested retaining the existing rule that electronic filers should not submit their annual statements with their returns, or alternatively, changing the requirement such that electronic filers must only submit limited parts of the annual statement.

The final regulations retain § 1.6012-2(c)(4), but it now provides that electronic filers must file their annual statement or a portion thereof in accordance with the applicable rules in the forms or instructions. The Treasury Department and the IRS anticipate that once the IRS has the capacity to accept the electronic filing of annual statements, the tax return forms and instructions will require electronic filing of all or portions of the annual statement. The IRS, however, expects to consult with

the insurance industry before requiring such electronic filing.

6. Comments and Changes Relating to § 1.817A-1 of the Proposed Regulations

The proposed regulations propose to remove parts of § 1.817A-1 that pertain to sections 807(d)(2)(B) and 812(b)(2) (A). Those sections were removed by the TCJA. The notice of proposed rulemaking requested comments on whether § 1.817A-1 should continue to provide a current market interest rate to be used in computing reserves under section 807(c) (3) during the temporary guarantee period of a modified guaranteed contract (MGC) given that the TCJA modified the flush language of section 807(c) to provide a specific interest rate to be used in making section 807(c)(3) computations.

One commenter recommended that § 1.817A-1 be removed in its entirety. The final regulations remove provisions relating to section 807(c)(3) but retain the provision (and related definitions) that waives section 811(d) for non-equity indexed MGCs during the temporary guarantee period, because these rules continue to remain relevant.

7. Conforming Changes to Regulations

The proposed regulations also propose to remove or amend the following regulatory provisions: §§ 1.338-11, 1.381(c)(22)-1, 1.801-2, 1.801-5, 1.801-7, 1.801-8, 1.806-4, 1.809-2, 1.809-5, 1.810-3, 1.817A-0, 1.818-2, 1.818-4, 1.848-1, and 301.9100-6T. These provisions were proposed to be removed or amended because they related to repealed or amended law or to regulations that were proposed to be removed or amended or they had no future application.

One commenter suggested that parts of paragraph (a) of § 1.801-7, a provision proposed to be removed in its entirety, continue to remain relevant under section 817. By its terms, § 1.801-7 is not applicable to any taxable year beginning after 1962. *See* § 1.801-7(d). Because § 1.801-7 is not applicable to any taxable year after 1962, the commenter's suggestion is not adopted.

More generally, the commenter requested removal of more "deadwood"

provisions than provided for in the notice of proposed rulemaking. The removal of additional "deadwood" provisions is beyond the scope of this rulemaking. No other specific comments were received with respect to these proposed conforming changes.

8. Comments Regarding Foreign-Issued Life Insurance and Annuity Contracts

The Code contains a statutory definition of a life insurance contract under section 7702, rules applicable to certain flexible premium contracts under section 101(f), distribution on death requirements under section 72(s), and diversification requirements under section 817(h). These statutory requirements, which reflect Congress's concern that the tax-favored treatment generally accorded life insurance and annuity contracts was available to contracts that were too investment oriented or provided for undue tax deferral, are relevant to the tax treatment of a policyholder, annuitant, or beneficiary as well as the entity that issues or reinsures a life insurance or annuity contract.

In response to a request to promulgate regulations that exempt certain contracts from the statutory requirements of sections 72(s), 101(f), 817(h), and 7702, the preamble to the proposed regulations asks for comments on whether such regulations should be promulgated. As described in the preamble to the proposed regulations, the requested exemption would apply to contracts issued by a non-U.S. insurance company and reinsured by a U.S. insurance company if (i) no policyholder, insured, annuitant, or beneficiary with respect to the contract is a U.S. person and (ii) such contract is regulated as a life insurance or annuity contract by a foreign regulator. The preamble to the proposed regulations states that the Treasury Department and the IRS are evaluating the request, including whether to address it as part of this rulemaking, and requests comments including in respect of statutory interpretation and implications in various contexts and provisions outside of subchapter L.

Three comments were received. One commenter (whose comment was endorsed by another commenter) generally repeated the original request (but nar-

rowed the requested exemptions to only sections 7702 and 72(s)) and stated that such regulations would assist U.S. reinsurers of exempted contracts to qualify as life insurance companies under section 816. The commenter asserted that the proposal would (i) align with domestic and U.S. international tax policy considerations because they would be applicable only to contracts owned by and benefitting persons not subject to Federal income tax and (ii) support policy goals of the TCJA to bring profitable business operations into the United States. The commenter further asserted that such regulations would not (i) affect the character, source, or separate category basket in which income derived from the reinsurance is included for U.S. withholding tax or foreign tax credit purposes, (ii) alter the application of any applicable U.S. withholding tax on income from sources within the United States paid by a domestic insurance company to any foreign corporation, or (iii) affect the treatment under section 59A of any claims and benefits or any other amounts paid by a domestic insurance company to a foreign related party under a reinsurance contract. The commenter acknowledged that it may not be possible for a U.S. insurance company to know the identity of a contract's underlying beneficial owners unless the beneficial owner and the policyholder were the same person and requested that U.S. insurance companies be able to rely upon the Foreign Account Tax Compliance Act beneficial ownership rules to determine if a contract has a U.S. person as a beneficial owner.

Another commenter stated that tax reserve deductions are already available for failed life insurance contracts under other provisions of section 807(c), just in a different amount than would be the case with life insurance reserve treatment. The commenter stated that there could nevertheless be benefits of conformity and suggested an alternative proposal. The commenter recommended that the Treasury Department and the IRS use their authority under sections 811(a) and 7805(a) to issue regulations that provide that reserves held by a U.S. reinsurer relating to indemnity reinsurance of contracts issued by a foreign insurance company be treated as life insurance reserves for purposes of subchapter L if: (i) the underlying contracts

are issued by a foreign insurer, (ii) such contracts are regulated as life insurance or annuity contracts both under the applicable law in the foreign jurisdiction and by the regulator of the reinsuring domestic insurance company, (iii) the NAIC prescribes reserves for such contracts that are computed as reserves applicable to life insurance or annuity contracts, and (iv) the initial issuance of the insurance contract to the policyholder was not through the conduct of a trade or business within the United States.

The considerations surrounding the issuance of the requested regulations are complex and require further study. Accordingly, the Treasury Department and the IRS have decided not to issue the requested regulations as part of this rulemaking and will continue to carefully consider these comments.

Applicability Dates

The rules in the final regulations apply to taxable years beginning after October 13, 2020.

A taxpayer may rely on § 1.807-4 or 1.816-1 of the proposed regulations for a taxable year beginning after December 31, 2017, and on or before October 13, 2020. Alternatively, a taxpayer may choose to apply § 1.807-4, 1.816-1, or 1.817A-1(b) of the final regulations to a taxable year beginning after December 31, 2017, the effective date of the revision of section 807 made by the TCJA, and on or before October 13, 2020, provided the taxpayer consistently applies the relevant regulation to that taxable year and all subsequent taxable years. See section 7805(b)(7).

Effect on Other Documents

The following revenue rulings are obsolete for taxable years beginning after October 13, 2020: Rev. Rul. 2002-6, 2002-1 C.B. 460, Rev. Rul. 94-74, 1994-2 C.B. 157, Rev. Rul. 80-117, 1980-1 C.B. 143, Rev. Rul. 80-116, 1980-1 C.B. 141, Rev. Rul. 78-354, 1978-2 C.B. 190, Rev. Rul. 77-198, 1977-1 C.B. 190, Rev. Rul. 75-308, 1975-2 C.B. 264, Rev. Rul. 74-57, 1974-1 C.B. 163, Rev. Rul. 70-568, 1970-2 C.B. 140, Rev. Rul. 70-192, 1970-1 C.B. 153, Rev. Rul. 69-444, 1969-2 C.B. 145, Rev. Rul. 65-240, 1965-2 C.B. 236, Rev.

Rul. 65-233, 1965-2 C.B. 228, and Rev. Rul. 65-143, 1965-1 C.B. 261.

Notice 2010-29 is obsolete for taxable years beginning after December 31, 2017.

Special Analyses

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

Paperwork Reduction Act

The collection of information relating to the final regulations was submitted to the Office of Management and Budget for review under OMB Control Number 1545-0123 in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)).

In response to the Conference Report and comments on the proposed regulations, § 1.6012-2(c)(4), as revised by the final regulations, provides that an insurance company should include the insurance company's annual statement (as defined in § 1.6012-2(c)(5)), or a portion thereof, with an electronically filed Federal income tax return (Form 1120-L for a life insurance company and Form 1120-PC for a nonlife insurance company) as required by the applicable forms or instructions. Federal income tax items of an insurance company are determined in part based upon the insurance company's annual statement. Providing the annual statement, or a portion thereof, to the IRS with an electronically filed Federal income tax return will allow the IRS to better and more efficiently examine an insurance company's Federal income tax return. However, until the applicable forms or instructions are revised, the current rules for including the annual statement with an electronically filed Federal income tax return continue to apply.

For purposes of the Paperwork Reduction Act, the burden for the collection of information associated with § 1.6012-2 of the final regulations will be reflected in the burden on the Form 1120-L and in the burden on the Form 1120-PC (OMB Control Number 1545-0123) when the burden for each is revised to reflect the collection of

information associated with § 1.6012-2 of the final regulations. The respondents to the collection of information are life insurance companies that file the Form 1120-L electronically and nonlife insurance companies that file the Form 1120-PC electronically. The Treasury Department and the IRS expect to consult with the life insurance industry before making any changes to these reporting requirements.

In accordance with section 807(e)(6), as added by the TCJA, § 1.807-3 of the final regulations provides that the IRS may require reporting on Form 1120-L of the opening balance and closing balance of items described in section 807(c) (for example, life insurance reserves) and the method of computing such items for purposes of determining income. Providing this information will allow the IRS to better examine an insurance company's Federal income tax return. However, under § 1.807-3 of the final regulations, this information is not required to be provided on any prescribed forms, such as the Form 1120-L, until the relevant prescribed forms or instructions are revised to require the reporting of such information.

For purposes of the Paperwork Reduction Act, the burden for the collection of information associated with § 1.807-3 of the final regulations will be reflected in the burden on the Form 1120-L (OMB Control Number 1545-0123) when the burden is revised to reflect the collection of information associated with § 1.807-3 of the final regulations. The respondents to the collection of information are life insurance companies that file a Form 1120-L. The Treasury Department and the IRS expect to consult with the life insurance industry before making any changes to these reporting requirements.

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.

Regulatory Flexibility Act

It is hereby certified that the final regulations will not have a significant economic impact on a substantial number of small entities pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

Section 13517 of the TCJA added section 807(e)(6) to the Code. Under section 807(e)(6), the Secretary may require reporting (at such time and in such manner as the Secretary shall prescribe) with respect to the opening balances and the closing balances of reserves and with respect to the method of computing reserves for purposes of determining income. Section 1.807-3 of the final regulations allows the IRS to require the reporting of this information on any prescribed forms, such as the Form 1120-L.

The Conference Report provides that, under existing authority, the Secretary may require an insurance company to provide its annual statement via a link, electronic copy, or other similar means. *See* Conference Report at 478-79. Section 1.6012-2(c)(4) of the final regulations provides that an insurance company should include the insurance company's annual statement, or a portion thereof, with an electronically filed Federal income tax return (Form 1120-L for a life insurance company and Form 1120-PC for a nonlife insurance company) as required by the applicable forms or instructions. Under current procedures, an insurance company can only electronically file a Form 1120-L or Form 1120-PC if the insurance company is part of an affiliated group filing a consolidated return, the parent of which files a Form 1120. Although data are not readily available, the Treasury Department and the IRS expect that any reporting burden associated with § 1.6012-2(c) will fall primarily on financial and insurance firms with annual receipts greater than \$41.5 million and, therefore, will not affect a substantial number of small entities. *See* 13 CFR 121.201, sector 52 (finance and insurance).

As stated in the preceding paragraph, the rule is not expected to affect a substantial number of small entities; however, even if a substantial number of small entities were affected, the economic impact of the regulation is not likely to be significant. Section 1.807-3 of the final regulations is limited in scope to time and manner of information reporting, and any economic impact associated with this regulation is expected to be minimal. Further, the information reported to the IRS is information that the insurance company has readily available and the Treasury Department and the IRS expect

to consult with the life insurance industry before making any changes to the reporting requirements. Accordingly, the Secretary certifies that the final regulations will not have a significant economic impact on a substantial number of small entities.

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

Drafting Information

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

Statement of Availability of IRS Documents

The IRS notices, revenue procedures, and revenue rulings cited in this preamble are published in the Internal Revenue Bulletin (or Cumulative Bulletin) and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at <http://www.irs.gov>.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and record-keeping requirements.

26 CFR Part 301

Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Penalties, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 301 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding a sectional authority for § 1.807-3 in numerical order to read in part as follows:

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

Section 1.807-3 also issued under 26 U.S.C. 807(e)(6).

* * * * *

Par. 2. Section 1.338-11 is amended by:

1. Revising paragraph (d)(2).
2. In paragraph (d)(3)(i), removing the language “and (d)(3)(iii)” and adding “through (iv)” in its place.
3. Redesignating paragraph (d)(3)(iii) as paragraph (d)(3)(iv).
4. Adding a new paragraph (d)(3)(iii).
5. Revising newly redesignated paragraph (d)(3)(iv).
6. Adding paragraph (d)(7)(iii).

The revisions and additions read as follows:

§ 1.338-11 Effect of section 338 election on insurance company targets.

* * * * *

(d) * * *

(2) *Exception.* New target is not treated as receiving additional premium under paragraph (d)(1) of this section if it is under state receivership as of the close of the taxable year for which the increase in reserves occurs.

(3) * * *

(iii) *Increases in section 807(c) reserves.* The positive amount with respect to the items referred to in section 807(c) other than discounted unpaid loss reserves is the sum of the net increases in such items that are required to be taken into account under section 807(f).

(iv) *Increases in other reserves.* The positive amount with respect to reserves other than discounted unpaid loss reserves and other items referred to in section 807(c) is the net increase of those reserves due to changes in estimate, methodology, or other assumptions used to compute the reserves (including the adoption by new target of a methodology or assumptions different from those used by old target).

* * * * *

(7) * * *

(iii) *Application of paragraphs (d)(2) and (3) of this section.* Paragraphs (d)(2) and (3) of this section apply to taxable years beginning after October 13, 2020. For taxable years beginning on or before such date, see paragraph (d) of this section as contained in 26 CFR part 1 revised as of April 1, 2020.

* * * * *

§ 1.381(c)(22)-1 [Amended]

Par. 3. In § 1.381(c)(22)-1, paragraph (b)(6) is removed and reserved.

§ 1.801-2 [Amended]

Par. 4. Section 1.801-2 is amended in the second sentence by removing the language “1.801-7” and adding “1.801-6” in its place.

§ 1.801-5 [Amended]

Par. 5. In § 1.801-5, paragraph (c) is removed and reserved.

§ 1.801-7 [Removed and reserved]

Par. 6. Section 1.801-7 is removed and reserved.

§ 1.801-8 [Amended]

Par. 7. In § 1.801-8, paragraph (e) is removed and reserved.

§ 1.806-4 [Removed]

Par. 8. Section 1.806-4 is removed.

Par. 9. Section 1.807-1 is revised to read as follows:

§ 1.807-1 Computation of life insurance reserves.

(a) *Tax reserve method.* For purposes of determining the amount of life insurance reserves for a contract under section 807(d)(1), section 807(d)(2) requires the determination of the amount of the reserve for a contract using the tax reserve method applicable to the contract. Under section 807(d)(3), the tax reserve method applicable to the contract is the Commissioners’ Reserve Valuation Method (CRVM), the Commissioners’ Annuities Reserve

Valuation Method (CARVM), or other reserve method prescribed by the National Association of Insurance Commissioners (NAIC) that applies to the contract as of the date the reserve is determined. If the NAIC has not prescribed a reserve method that covers the contract, a reserve method that is consistent with the CRVM, the CARVM, or other NAIC-prescribed method as of the date the reserve is determined (whichever is most appropriate) must be used.

(b) *No asset adequacy reserve.* The life insurance reserve determined under section 807(d)(1) does not include any asset adequacy reserve.

(1) An asset adequacy reserve is—

(i) Any reserve that is established as an additional reserve based upon an analysis of the adequacy of reserves that would otherwise be established in accordance with the requirements set forth in the NAIC Valuation Manual, such as the CRVM or CARVM as applicable, or

(ii) Any similar reserve.

(2) In determining whether a reserve is a life insurance reserve, the label placed on such reserve is not determinative, provided, however, any reserve or portion of a reserve that would have been established pursuant to an asset adequacy analysis required by the NAIC’s Valuation Manual 30 as it existed on December 22, 2017, the date of enactment of Public Law 115-97, is an asset adequacy reserve.

(c) *Applicability date.* The rules of this section apply to taxable years beginning after October 13, 2020.

Par. 10. Sections 1.807-3 and 1.807-4 are added before the undesignated center heading “Gain and Loss From Operations” to read as follows:

§ 1.807-3 Reporting of reserves.

(a) *Reserve reporting.* A life insurance company subject to tax under section 801 is required to make a return on Form 1120-L, *U.S. Life Insurance Company Income Tax Return*. The Internal Revenue Service may require reporting with respect to the opening balance and closing balance of items described in section 807(c) and with respect to the method of computing such items for purposes of determining income. Such

reporting may provide for the manner in which separate account items are reported. (See section 6011 and § 301.6011-1 of this chapter.)

(b) *Applicability date.* The rules of this section apply to taxable years beginning after October 13, 2020.

§ 1.807-4 Adjustment for change in computing reserves.

(a) *Requirement to follow administrative procedures.* Under section 807(f), a change in basis of computing an item referred to in section 807(c) is a change in method of accounting. Accordingly, except as provided in § 1.446-1(e), a change in basis of computing an item referred to in section 807(c) is a change in method of accounting for purposes of § 1.446-1(e). Before computing such item under a new basis, a life insurance company must obtain the consent of the Commissioner of Internal Revenue or his delegate (Commissioner) pursuant to administrative procedures prescribed by the Commissioner. Similarly, an insurance company other than a life insurance company (a nonlife insurance company) that changes its basis of computing life insurance reserves must obtain the consent of the Commissioner pursuant to administrative procedures prescribed by the Commissioner.

(b) *Section 481 adjustment—(1) In general.* If the basis of computing any item referred to in section 807(c) as of the close of any taxable year (the year of change) differs from the basis of computing such item at the close of the preceding taxable year, then the difference between the amount of the item at the close of the taxable year computed on the new basis and the amount of the item at the close of the taxable year computed on the old basis that is attributable to contracts issued before the taxable year, is taken into account under section 481 and §§ 1.481-1 through 1.481-5 as an adjustment attributable to a change in method of accounting.

(2) *Loss of company status.* If for any taxable year a taxpayer that was an insurance company for the year of change is no longer an insurance company, then the taxpayer must take into account in the preceding taxable year (that is, the last

taxable year it was an insurance company) the balance of any section 481(a) adjustment determined under paragraph (b) (1) of this section. A taxpayer that was an insurance company for the year of change does not accelerate the balance of any section 481(a) adjustment determined under paragraph (b)(1) of this section merely because it changes from a life insurance company to a nonlife insurance company or because it changes from a nonlife insurance company to a life insurance company.

(c) *Effect on determining increase or decrease in reserves*—(1) *Effect under section 807(a) and (b)*. If there is a change in basis of computing any item referred to in section 807(c) for a taxable year, then, for purposes of section 807(a) and (b), the closing balance for such item for the year of change with respect to contracts issued before the year of change is determined on the old basis and the opening balance for such item for the next taxable year for such contracts is computed on the new basis.

(2) *Effect under section 832*. The following rules apply for purposes of section 832(b)(4):

(i) For the year of change, life insurance reserves at the end of the year of change with respect to contracts issued before the year of change are determined on the old basis.

(ii) For the taxable year following the year of change, life insurance reserves at the end of the preceding taxable year (that is, the year of change) with respect to contracts issued before the year of change are determined on the new basis.

(d) *Examples*. The principles of paragraphs (a) through (c) of this section are illustrated by the following examples. For purposes of these examples and except as otherwise provided, IC is a life insurance company within the meaning of section 816(a) that issues life insurance and annuity contracts. IC is required to determine the amount of life insurance reserves under section 807(d) and to take net increases or decreases in the reserves into account in computing life insurance company taxable income. IC's reserve for each insurance contract at issue exceeds the net surrender value for such contract and does not exceed the statutory reserve for such contract. IC is on an

accrual method and uses a calendar year as its taxable year.

(1) *Example 1*—(i) *Facts*. In 2021, IC changed the basis of computing the amount of life insurance reserves for a certain type of life insurance contract as described in section 807(f). Both the basis used for computing the reserves for the relevant contracts at the close of the 2020 taxable year (old basis) and the basis of computing the reserves for the relevant type of contract at the close of the 2021 taxable year (new basis) are consistent with the applicable Commissioners' Reserve Valuation Method. IC followed the administrative procedures prescribed by the Commissioner to obtain consent to change the basis of computing these reserves. IC determined that the life insurance reserves as of December 31, 2021, for the relevant contracts issued prior to 2021 were \$110x if computed using the old method and \$120x if computed using the new method. IC also determined that the life insurance reserves as of December 31, 2021, for the relevant contracts issued during 2021 were \$15x using the new basis.

(ii) *Analysis*. IC must take into account under section 481 and the administrative procedures prescribed by the Commissioner the \$10x difference between the reserves for the relevant contracts issued prior to 2021 computed under the old basis (\$110x) and the reserves for such contracts computed under the new basis (\$120x). For purposes of determining any net increase or net decrease in reserves in taxable year 2021 under section 807(a) or (b), IC's closing balance of life insurance reserves computed under section 807(d) with respect to the relevant contracts is \$110x for contracts issued prior to 2021 (computed on the old basis) and \$15x for contracts issued during 2021 (computed on the new basis). IC's opening balance in 2022 for life insurance reserves for the relevant contracts is \$135x (computed on the new basis).

(2) *Example 2*—(i) *Facts*. The facts are the same as in paragraph (d)(1) of this section (the facts in *Example 1*), except that IC is an insurance company that is not a life insurance company. IC is required to compute taxable income under section 832.

(ii) *Analysis*. IC must take into account under section 481 and the administrative procedures prescribed by the Commissioner the \$10x difference between the reserves for the relevant contracts issued prior to 2021 computed under the old basis (\$110x) and the reserves for such contracts computed under the new basis (\$120x). For purposes of determining the premiums earned on insurance contracts during the taxable year as described in section 832(b)(4) for the year of change, the life insurance reserves at the end of the taxable year are \$110x for contracts issued prior to 2021 (computed on the old basis) and \$15x for contracts issued during 2021 (computed on the new basis). For purposes of determining the premiums earned on insurance contracts during the taxable year as described in section 832(b)(4) for the taxable year following the year of change, the life insurance reserves at the end of the preceding taxable year (the year of change) with respect to relevant contracts are \$135x (computed on the new basis).

(e) *Applicability date*. The rules of this section apply to taxable years beginning

after October 13, 2020. However, a taxpayer may choose to apply the rules of this section for a taxable year beginning after December 31, 2017, the effective date of the revision of section 807 by Public Law 115-97, and on or before October 13, 2020, provided the taxpayer consistently applies the rules of this section to that taxable year and all subsequent taxable years. See section 7805(b)(7).

§ 1.809-2 [Removed and reserved]

Par. 11. Section 1.809-2 is removed and reserved.

§ 1.809-5 [Amended]

Par. 12. Section 1.809-5 is amended by removing the language “and § 1.810-3” from the last sentence of paragraph (a)(5) (iii).

§ 1.810-3 [Removed]

Par. 13. Section 1.810-3 is removed.

Par. 14. Section 1.816-1 is added before the undesignated center heading “Miscellaneous Provisions” to read as follows:

§ 1.816-1 Life insurance reserves.

(a) *Definition of life insurance reserves*. Except as provided in section 816(h), a reserve that meets the requirements of section 816(b)(1) and (2) will not be disqualified as a life insurance reserve solely because the method used to compute the reserve takes into account other factors, provided that the method used to compute the reserve is a tax reserve method as defined in section 807(d) (3) and that such reserve is not an asset adequacy reserve as described in § 1.807-1(b).

(b) *Applicability date*. The section applies to taxable years beginning after October 13, 2020. However, a taxpayer may choose to apply the rules of this section for a taxable year beginning after December 31, 2017, the effective date of the revision of section 807 by Public Law 115-97, and on or before October 13, 2020, provided the taxpayer consistently applies the rules of this section to that taxable year and all subsequent taxable years. See section 7805(b)(7).

§ 1.817A-0 [Removed]

Par. 15. Section 1.817A-0 is removed.

Par. 16. Section 1.817A-1 is amended by:

1. Removing paragraphs (a)(5) and (6).
2. Revising paragraph (b).
3. Removing paragraph (c).
4. Redesignating paragraph (d) as paragraph (c).
5. Revising newly designated paragraph (c).

The revisions read as follows:

§ 1.817A-1 Certain modified guaranteed contracts.

(b) *Waiver of section 811(d) for certain non-equity-indexed modified guaranteed contracts.* Section 811(d) is waived during the temporary guarantee period when applied to non-equity-indexed MGCs.

(c) *Applicability dates.* Paragraph (b) of this section applies to taxable years beginning after October 13, 2020. However, a taxpayer may choose to apply the rules of paragraph (b) of this section for a taxable year beginning after December 31, 2017, the effective date of the revision of section 807 by Public Law 115-97, and on or before October 13, 2020, provided the taxpayer consistently applies the rules of paragraph (b) of this section to that taxable year and all subsequent taxable years. See section 7805(b)(7). For taxable years beginning on or before October 13, 2020, see paragraph (b) of this section as contained in 26 CFR part 1 revised as of April 1, 2020.

§ 1.818-2 [Amended]

Par. 17. Section 1.818-2 is amended by removing paragraph (c).

§ 1.818-4 [Removed and reserved]

Par. 18. Section 1.818-4 is removed and reserved.

§ 1.848-1 [Amended]

Par. 19. Section 1.848-1 is amended in paragraph (b)(2)(i) by removing the language “section 807(e)(4)” and adding the language “section 807(e)(3)” in its place.

Par. 20. Section 1.6012-2 is amended by:

1. Revising paragraph (c)(4).
2. Revising paragraph (l).

The revisions read as follows:

§ 1.6012-2 Corporations required to make returns of income.

(c) ***

(4) *Special rule for insurance companies filing their Federal income tax returns electronically.* If an insurance company described in paragraph (c)(1), (2), or (3) of this section files its Federal income tax return electronically, it must include on or with such return its annual statement (or pro forma annual statement), or a portion thereof, as and to the extent required by forms or instructions. If the full annual statement is not required to be included with the return, such statement must be available at all times for inspection by authorized Internal Revenue Service officers or employees and retained for so long as such statements may be material in the administration of any internal revenue law. See § 1.6001-1(e).

(l) *Applicability date.* Paragraph (c) of this section applies to any taxable year beginning after October 13, 2020. For taxable years beginning on or before October 13, 2020, see paragraph (c) of this section as contained in 26 CFR part 1 in effect on April 1, 2020.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 21. The authority citation for part 301 continues to read in part as follows:

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

Par. 22. Section 301.9100-6T is amended by:

1. Adding a title to the table in paragraph (a)(1).
2. Removing from the table in paragraph (a)(1) the three entries for “211” and the entries for “216(c)(1),” “216(c)(2),” “217(i),” and “217(l)(2)(B).”
3. Removing and reserving paragraph (a)(2)(iii).
4. Removing paragraph (a)(3)(v).

5. In paragraph (a)(4):

i. Removing “211 (Code section 810(b)(3)), 216(c)(1) and (2), 217(l),” from the first sentence.

ii. Removing “211 (Code sections 806(d)(4), and 807(d)(4)(C)), 217(i),” from the second sentence.

iii. Removing the last sentence.

The addition reads as follows:

§ 301.9100-6T Time and manner of making certain elections under the Deficit Reduction Act of 1984.

(a) ***

(1) ***

TABLE 1 TO PARAGRAPH (a)(1)

Sunita Lough,
Deputy Commissioner for Services
and Enforcement.

Approved September 1, 2020.

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

(Filed by the Office of the Federal Register on October 09, 2020, 8:45 a.m., and published in the issue of the Federal Register for October 13, 2020, 85 FR 64386)

Section 152. — Dependent defined

26 CFR 1.152-2(b), (e); 26 CFR 1.24-1: Dependent Defined

T.D. 9913

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 1

Dependent Defined

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that clarify the definition of a “qualifying relative” for purposes of various provisions of the Internal Revenue Code (Code) for taxable years 2018 through 2025. These regulations generally affect taxpayers who claim Federal income tax benefits that require a taxpayer to have a qualifying relative.

DATES: *Effective Date:* These regulations are effective on October 13, 2020.

Applicability Date: Sections 1.24-1 and 1.152-2(b) of these regulations apply to taxable years beginning on or after October 13, 2020. Section 1.152-2(e) of these regulations applies to taxable years ending after August 28, 2018, the date the Department of the Treasury (Treasury Department) and the IRS issued Notice 2018-70, 2018-38 I.R.B. 441.

FOR FURTHER INFORMATION CONTACT: Victoria J. Driscoll at (202) 317-4718 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) under sections 24 and 152 of the Code relating to statutory amendments enacted in Public Law 115-97, 131 Stat. 2054 (2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA).

Section 152(a) generally defines a “dependent” as a “qualifying child” or a “qualifying relative.” The definition of a qualifying relative in section 152(d)(1) includes the requirement that the individual have gross income for the calendar year that is less than the “exemption amount” as defined in section 151(d) (exemption amount). Such an individual also must satisfy the requirement of section 152(d)(1)(C) that the individual receive more than one-half of his or her support from the taxpayer claiming the individual as a qualifying relative (support test). As described in parts I through IV of this Background, these final regulations provide that, in determining whether an individual is a qualifying relative for purposes of various provisions of the Code that refer to sec-

tion 152 in years in which the exemption amount is zero, the section 151(d) exemption amount will be the inflation-adjusted section 152(d)(1)(B) exemption amount in the annual revenue procedure setting forth inflation-adjusted items that is published in the Internal Revenue Bulletin.

I. Exemption Amount

Generally, section 151 allows a taxpayer to claim a deduction equal to the exemption amount for each of the taxpayer and his or her spouse, and for any dependents. Prior to the TCJA, section 151(d) provided for an exemption amount of \$2,000 that was adjusted annually for inflation beginning with calendar year 1990. Before the enactment of the TCJA, the IRS had determined that the exemption amount for taxable year 2018 was \$4,150. Rev. Proc. 2017-58, 2017-45 I.R.B. 489, modified and superseded by Rev. Proc. 2018-18, 2018-10 I.R.B. 392.

Section 11041(a)(2) of the TCJA added section 151(d)(5) to provide special rules for taxable years 2018 through 2025 regarding the exemption amount. Section 151(d)(5)(A) provides that, for a taxable year beginning after December 31, 2017, and before January 1, 2026, the exemption amount is zero, thereby suspending the deductions for personal exemptions and the dependency exemption. H.R. Rep. No. 115-466, at 202-204 (2017) (Conference Report). However, section 151(d)(5)(B) provides that the reduction of the exemption amount to zero is not taken into account in determining whether a deduction under section 151 is allowed or allowable to a taxpayer, or whether a taxpayer is entitled to a deduction under section 151, for purposes of any other provision of the Code. The Conference Report states that this provision clarifies that the reduction of the personal exemption to zero “should not alter the operation of those provisions of the Code which refer to a taxpayer allowed a deduction . . . under section 151,” including the child tax credit in section 24(a). *Id.* at 203 n.16. For example, the definition of head of household in section 2(b)(1)(A) includes the requirement that the taxpayer maintain as his or her home a household for a qualifying individual for a specified period of time. A qualifying

individual under section 2(b)(1)(A)(ii) includes a person who is a qualifying relative under section 152(d) if the taxpayer is entitled to a deduction under section 151 for the person for the taxable year.

II. Support Test

The section 152(d)(1)(C) support test requires that an individual receive more than one-half of his or her support from the taxpayer to be claimed as a qualifying relative of that taxpayer. Prior to the TCJA, payments of alimony or separate maintenance paid to a spouse or former spouse were not treated as support of a dependent provided by the payor spouse. Additionally, alimony and separate maintenance payments were deductible by the payor spouse and includible in income by the recipient spouse under sections 61(a)(8), 71(a), and 215(a) of the Code. Under section 71(c), child support payments were not treated as alimony includible in income.

Section 11051 of the TCJA repealed sections 61(a)(8), 71 and 215, and, in a conforming change, also repealed section 682 of the Code for any divorce or separation instrument executed after 2018, and for any instrument executed before 2019 and later modified to apply the provisions of the TCJA. Consistent with prior law, the TCJA provides that payments of alimony or separate maintenance paid to a spouse or former spouse are not treated as support of a dependent provided by the payor spouse. To conform with the repeal of sections 71 and 682 by the TCJA, section 11051(b)(3)(B) of the TCJA amended section 152(d)(5) of the Code regarding the source of a qualifying relative’s support by revising the language of section 152(d)(5) to eliminate references to former sections 71 and 682.

III. Credit for Other Dependents

Section 11022(a) of the TCJA amended section 24 of the Code to create a \$500 credit for certain dependents of a taxpayer other than a qualifying child described in section 24(c) for whom the child tax credit is allowed. The \$500 credit applies to two categories of dependents: (1) Qualifying children for whom a child tax credit is not allowed, and (2) qualifying

relatives as defined in section 152(d). Section 24(h)(4)(A) and (C). Like the amendment to section 151(d) reducing the exemption amount to zero, this new credit applies for taxable years 2018 through 2025. The Conference Report explains that “[t]he credit is further modified to temporarily provide for a \$500 nonrefundable credit for qualifying dependents other than qualifying children. The provision generally retains the present-law definition of dependent.” H.R. Rep. No. 115-466, at 227.

IV. Administrative Action

On August 28, 2018, the Treasury Department and the IRS issued Notice 2018-70. This notice announced the intent to issue proposed regulations providing that the reduction of the exemption amount to zero under section 151(d)(5)(A) for taxable years 2018 through 2025 will not be taken into account in determining whether an individual meets the requirement of section 152(d)(1)(B) to be a qualifying relative. Notice 2018-70 also stated that, before the issuance of the proposed regulations described in the notice, a taxpayer may rely on the rules described in the notice.

On June 9, 2020, the Treasury Department and the IRS published a notice of proposed rulemaking (REG-118997-19) in the **Federal Register** (85 FR 35233) proposing regulations under sections 24 and 152 (proposed regulations). Consistent with Notice 2018-70, the proposed regulations provide that, in determining whether an individual is a qualifying relative for purposes of various provisions of the Code that refer to section 152 in taxable years in which the exemption amount is zero, the section 151(d) exemption amount will be the inflation-adjusted section 152(d)(1)(B) exemption amount in the annual revenue procedure setting forth inflation-adjusted items that is published in the Internal Revenue Bulletin. Thus, the exemption amount to be used for this purpose is \$4,150 for taxable year 2018 (section 3.24 of Rev. Proc. 2017-58, 2017-45 I.R.B. 489, modified and superseded by Rev. Proc. 2018-18, 2018-10 I.R.B. 392); \$4,200 for taxable year 2019 (section 3.25 of Rev. Proc. 2018-57, 2018-49 I.R.B. 827); and \$4,300 for taxable year 2020

(section 3.25 of Rev. Proc. 2019-44, 2019-47 I.R.B. 1093).

Section 1.152-3(c)(3) and (d)(2) of the proposed regulations were proposed as changes to an earlier notice of proposed rulemaking (REG-137604-07) also providing rules regarding the definition of a dependent under section 152, which was published in the **Federal Register** (82 FR 6370) on January 19, 2017 (January 2017 Proposed Regulations). Section 1.152-3(d)(2) of the January 2017 Proposed Regulations, which have not yet been finalized, originally included references to sections 71 and 682. Accordingly, the proposed regulations withdrew §1.152-3(d)(2) of the January 2017 Proposed Regulations and replaced it with a proposed rule to reflect the amendments to section 152(d)(5) discussed in part II of this Background.

Summary of Comments and Explanation of Provisions

The Treasury Department and the IRS received three comments in response to the proposed regulations through the Federal eRulemaking Portal. As no request for a public hearing was received, no hearing was held.

Although two of the comments received did not relate to the proposed regulations, the third comment generally asked for additional clarity regarding the definition of a qualifying relative. As described in the Background, these regulations implement specific changes to the law enacted in the TCJA, which did not modify the definition of qualifying relative in section 152(d) other than to make conforming changes to section 152(d)(5) to account for the repeal of sections 71 and 682. When the January 2017 Proposed Regulations are finalized, they will provide additional clarity to the regulations under section 152 and related provisions.

The third comment also suggested that, because the final regulations would not be published earlier than 2020, it was not necessary to reference the exemption amount for purposes of section 152 for taxable years 2018 and 2019. Although these final regulations are being published in 2020, §1.152-2(e) of these final regulations applies to taxable years ending after August 28, 2018, the

date the Treasury Department and the IRS issued Notice 2018-70, pursuant to section 7805(b)(1)(C). Further, the Treasury Department and the IRS determined it appropriate to clarify that, in defining qualifying relative for purposes other than determining the amount allowable as a deduction under section 151(a), the exemption amount is not zero, but is the inflation-adjusted section 152(d)(1)(B) exemption amount in the annual revenue procedure setting forth inflation-adjusted items that is published in the Internal Revenue Bulletin.

This document adopts the proposed regulations as final regulations with no substantive change. However, because §1.152-3(c)(3) and 1.152-3(d)(2) of the proposed regulations originally were proposed as changes to provisions of the January 2017 Proposed Regulations, which have not yet been finalized, the proposed regulations have been redesignated in the final regulations to coordinate with the existing regulations. Specifically, proposed §1.152-3(c)(3)(i) and (ii) is finalized as new §1.152-2(e)(1) and (2) and proposed §1.152-3(d)(2) is finalized as §1.152-2(b). When the January 2017 Proposed Regulations are finalized, the provisions again will be appropriately redesignated.

Therefore, the provisions of the proposed regulations are adopted without substantive change to: (1) provide that the exemption amount, for purposes other than a deduction for a personal or dependency exemption under section 151, is \$4,150 for taxable year 2018, and for taxable years 2019 through 2025, the exemption amount, as adjusted for inflation, is the section 152(d)(1)(B) exemption amount, as set forth in guidance published in the Internal Revenue Bulletin; and (2) describe certain payments to a payee spouse for purposes of the support test without references to repealed sections 71 and 682.

Finally, these regulations clarify an issue raised regarding a statutory cross reference in section 24(h)(4) to “a qualifying child described in subsection (c).” As was proposed in the proposed regulations, these regulations clarify in §1.24-1 that the statutory cross reference is a reference to section 24(c), rather than to section 152(c).

Applicability Date

Section 7805(b)(1) of the Code generally provides that no temporary, proposed, or final regulation relating to the internal revenue laws may apply to any taxable period ending before the earliest of (A) the date on which the regulation is filed with the **Federal Register**, or (B) in the case of a final regulation, the date on which a proposed or temporary regulation to which the final regulation relates was filed with the **Federal Register**. However, section 7805(b)(1)(C) provides that a regulation may apply to a taxable period ending after the date on which any notice substantially describing the expected contents of a regulation is issued to the public.

Accordingly, §§1.24-1 and 1.152-2(b) of these regulations apply to taxable years beginning on or after October 13, 2020. Section 1.152-2(e) of these regulations applies to taxable years ending after August 28, 2018, the date the Treasury Department and the IRS issued Notice 2018-70.

Special Analyses

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

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is certified that these regulations will not have a significant economic impact on a substantial number of small entities. These regulations primarily affect individuals and therefore will not have a significant economic impact on a substantial number of small entities. Accordingly, the Secretary of the Treasury's delegate certifies that the rule will not have a significant economic impact on a substantial number of small entities.

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

Drafting Information

The principal author of the final regulations is Victoria Driscoll of the Office of Associate Chief Counsel (Income Tax and Accounting). However, other personnel from the Treasury Department and the IRS participated in their development.

Statement of Availability of IRS Documents

IRS notices and other guidance cited in this preamble are published in the Internal Revenue Bulletin (or Cumulative Bulletin) and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at <http://www.irs.gov>.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and record-keeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.24-1 is added to read as follows:

§1.24-1 Partial credit allowed for certain other dependents.

(a) *In general.* For purposes of section 24(h)(4)(A), a taxpayer may be eligible to increase the credit determined under section 24(a) by \$500 for a dependent of the taxpayer, as defined in section 152, other than a qualifying child described in section 24(c).

(b) *Applicability date.* This section applies to taxable years beginning on or after October 13, 2020.

Par. 3. Section 1.152-2, is amended by:

1. Revising paragraph (b); and

2. Adding paragraph (e).

The revision and addition read as follows:

§1.152-2 Rules relating to general definition of dependent.

* * * * *

(b)(1) A payment to a spouse (payee spouse) of alimony or separate maintenance is not treated as a payment by the payor spouse for the support of any dependent. Similarly, the distribution of income of an estate or trust to a divorced or legally separated payee spouse is not treated as a payment by the payor spouse for the support of any dependent. The preceding sentence will not apply, however, to the extent that such a distribution is in satisfaction of the amount or portion of income that, by the terms of a divorce decree, a written separation agreement, or the trust instrument is fixed as payable for the support of the minor children of the payor spouse.

(2) Paragraph (b)(1) of this section applies to taxable years beginning on or after October 13, 2020.

* * * * *

(e)(1) In defining a qualifying relative for taxable year 2018, the exemption amount in section 152(d)(1)(B) is \$4,150. For taxable years 2019 through 2025, the exemption amount, as adjusted for inflation, is set forth in annual guidance published in the **Internal Revenue Bulletin**. See §601.601(d)(2) of this chapter.

(2) Paragraph (e)(1) of this section applies to taxable years ending after August 28, 2018.

Sunita Lough,
Deputy Commissioner for Services
and Enforcement

Approved: September 8, 2020

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

(Filed by the Office of the Federal Register on October 09, 2020, 8:45 a.m., and published in the issue of the Federal Register for October 13, 2020, 85 F.R. 64386)

T.D. 9918

**DEPARTMENT OF THE
TREASURY**
Internal Revenue Service
26 CFR Part 1

**Effect of Section 67(g) on
Trusts and Estates**

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations clarifying that the following deductions allowed to an estate or non-grantor trust are not miscellaneous itemized deductions: costs paid or incurred in connection with the administration of an estate or non-grantor trust that would not have been incurred if the property were not held in the estate or trust, the personal exemption of an estate or non-grantor trust, the distribution deduction for trusts distributing current income, and the distribution deduction for estates and trusts accumulating income. Therefore, these deductions are not affected by the suspension of the deductibility of miscellaneous itemized deductions for taxable years beginning after December 31, 2017, and before January 1, 2026. The final regulations also provide guidance on determining the character, amount, and allocation of deductions in excess of gross income succeeded to by a beneficiary on the termination of an estate or non-grantor trust. The final regulations affect estates, non-grantor trusts (including the S portion of an electing small business trust), and their beneficiaries.

DATES: *Effective date:* These regulations are effective on October 19, 2020.

Applicability dates: For dates of applicability, see §§ 1.67-4(d), 1.642(h)-2(f) and 1.642(h)-5(c).

FOR FURTHER INFORMATION CONTACT: Margaret Burow at (202) 317-5279 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to Income Tax Regulations (26 CFR part 1) under sections 67 and 642 of the Internal Revenue Code (Code). On May 11, 2020, the Department of Treasury (Treasury Department) and the IRS published a notice of proposed rulemaking (REG-113295-18) in the **Federal Register** (85 FR 27693) containing proposed regulations under sections 67 and 642(h) (proposed regulations). The Summary of Comments and Explanation of Revisions section of this preamble summarizes the provisions of sections 67 and 642(h) and the provisions of the proposed regulations, which are explained in greater detail in the preamble to the proposed regulations.

On July 17, 2020, the Treasury Department and the IRS published in the **Federal Register** (85 FR 43512) a notice of public hearing on the proposed regulations scheduled for August 12, 2020. The Treasury Department and the IRS received no requests to speak at a hearing in response to that notice. On August 5, 2020, the Treasury Department and the IRS published in the **Federal Register** (85 FR 47323) a cancellation of the notice of public hearing.

The Treasury Department and the IRS received written and electronic comments in response to the proposed regulations. All comments were considered and are available at www.regulations.gov or upon request. After full consideration of the comments received, this Treasury decision adopts the proposed regulations with modifications described in the Summary of Comments and Explanation of Revisions.

**Summary of Comments and
Explanation of Revisions**

Most of the comments addressing the proposed regulations are summarized in this Summary of Comments and Explanation of Revisions. Comments merely summarizing or interpreting the proposed regulations or recommending statutory revisions are not discussed in this preamble. The Treasury Department and the

IRS continue to study comments on issues related to sections 67 and 642(h) that are beyond the scope of these regulations, which may be discussed in future guidance if guidance on those issues is published. The scope of the proposed regulations and these regulations is limited to the effect of section 67(g) on the deductibility of certain expenses described in section 67(b) and (e) that are incurred by estates and non-grantor trusts and the treatment of excess deductions on termination of an estate or trust under section 642(h). This Summary of Comments and Explanation of Revisions also describes each of the final rules contained in this document.

A. Section 67

Section 67(g) was added to the Code on December 22, 2017, by section 11045(a) of Public Law 115-97, 131 Stat. 2054, 2088 (2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA). Section 67(g) prohibits individual taxpayers from claiming miscellaneous itemized deductions for any taxable year beginning after December 31, 2017, and before January 1, 2026. Prior to the TCJA, miscellaneous itemized deductions were allowable for any taxable year only to the extent that the sum of such deductions exceeded two percent of adjusted gross income. See section 67(a). Section 67(b) defines miscellaneous itemized deductions as itemized deductions other than those listed in section 67(b)(1) through (12).

Section 67(e) provides that, for purposes of section 67, an estate or trust computes its adjusted gross income in the same manner as that of an individual, except that the following additional deductions are treated as allowable in arriving at adjusted gross income: (1) the deductions for costs which are paid or incurred in connection with the administration of the estate or trust and which would not have been incurred if the property were not held in such estate or trust, and (2) deductions allowable under section 642(b) (concerning the personal exemption of an estate or non-grantor trust), section 651 (concerning the deduction for trusts distributing current income), and section 661 (concerning the deduction for estates and trusts accumulating income). Accordingly, section 67(e) removes the

deductions described in section 67(e) (1) and (2) from the definition of itemized deductions under section 63(d), and thus from the definition of miscellaneous itemized deductions under section 67(b), and treats them as deductions allowable in arriving at adjusted gross income under section 62(a). Section 67(e) further provides regulatory authority to make appropriate adjustments in the application of part I of subchapter J of chapter 1 of the Code to take into account the provisions of section 67.

The proposed regulations under § 1.67-4 clarify that expenses described in section 67(e) remain deductible in determining the adjusted gross income of an estate or non-grantor trust during the taxable years in which section 67(g) applies. Accordingly, section 67(g) does not deny an estate or non-grantor trust (including the S portion of an electing small business trust) a deduction for expenses described in section 67(e)(1) and (2) because such deductions are allowable in arriving at adjusted gross income and are not miscellaneous itemized deductions under section 67(b). Commenters agreed with the proposed amendments. These regulations adopt the proposed regulations under § 1.67-4 without modification.

Two commenters requested that the regulations address the treatment of deductions described in section 67(e)(1) and (2) in determining an estate or non-grantor trust's income for alternative minimum tax (AMT) purposes. The commenters suggested that such deductions are allowable as deductible in computing the AMT. The treatment of deductions described in section 67(e) for purposes of determining the AMT is outside the scope of these regulations concerning the effects of section 67(g); therefore, these regulations do not address the AMT. Further, no conclusions should be drawn from the absence of a discussion of the AMT in these regulations regarding the treatment of deductions described in section 67(e) for purposes of determining the AMT.

One commenter suggested that the Treasury Department and the IRS exercise their regulatory authority under section 67(e) to exempt cemetery trusts under section 642(i) and qualified funeral trusts (QFTs) under section 685 from the application of section 67(g). The commenter

stated that the primary type of expense incurred by these trusts is investment advisory expenses, the tax treatment of which differs under the Code from management expenses. That is, trust management expenses generally are allowable in computing adjusted gross income under section 67(e)(1), while trust investment advisory expenses are miscellaneous itemized deductions. See § 1.67-4(b)(4). The commenter asserted that it was not the intent of Congress to disallow investment advisory expenses incurred by cemetery and funeral trusts when Congress enacted section 67(g).

The commenter suggested that exercising the regulatory authority under section 67(e) in this manner would be consistent with the exercise of regulatory authority under section 1411 to exempt section 642(i) cemetery perpetual care funds and QFTs. See § 1.1411-3(b)(1) (providing that certain types of trusts, including section 642(i) cemetery perpetual care funds, are excepted from the net investment income tax) and § 1.1411-3(b)(2) (providing a special rule for QFTs that, for purposes of calculating any tax under section 1411, section 1411 and the regulations thereunder are applied to each QFT by treating each beneficiary's interest in the trust as a separate trust). As stated in the preamble to TD 9644 (78 FR 72393), the Treasury Department and the IRS exercised their regulatory authority under section 1411 to exclude cemetery trusts from the net investment income tax because, by benefiting an operating company, such trusts are considered similar to the business trusts that are excluded from the operation of section 1411. The preamble also states that QFTs are not excluded from the application of the net income investment tax, but that the section 1411 tax is calculated consistent with the taxation of QFTs under chapter 1. The commenter noted that they advocated for the treatment of each beneficiary's interest in the QFT as a separate trust because such treatment reduces the likelihood of the QFT beneficiaries being subject to the net investment income tax. The Treasury Department and the IRS continue to consider these comments but providing an exemption for cemetery and funeral trusts under section 67(g) is outside the scope of these regulations.

B. Section 642(h)

1. In general

Section 642(h) provides that if, on the termination of an estate or trust, the estate or trust has: (1) a net operating loss carryover under section 172 or a capital loss carryover under section 1212, or (2) for the last taxable year of the estate or trust, deductions (other than the deductions allowed under section 642(b) (relating to the personal exemption) or section 642(c) (relating to charitable contributions)) in excess of gross income for such year, then such carryover or excess will be allowed as a deduction, in accordance with the regulations prescribed by the Secretary of the Treasury or his delegate (Secretary), to the beneficiaries succeeding to the property of the estate or trust.

Section 1.642(h)-2(a), as articulated in the proposed regulations and these final regulations, provides that if, on termination of an estate or trust, the estate or trust has for its last taxable year deductions (other than the deductions allowed under section 642(b) or section 642(c)) in excess of gross income, the excess deductions are allowed under section 642(h)(2) as items of deduction to the beneficiaries succeeding to the property of the terminated estate or trust.

2. Character and amount of excess deductions

Section 1.642(h)-2(b)(1) of the proposed regulations provides that each deduction comprising the excess deductions under section 642(h)(2) retains, in the hands of the beneficiary, its character (specifically, as allowable in arriving at adjusted gross income, as a non-miscellaneous itemized deduction, or as a miscellaneous itemized deduction) while in the estate or trust. The character of these deductions does not change when succeeded to by a beneficiary on termination of the estate or trust. Furthermore, an item of deduction succeeded to by a beneficiary remains subject to any limitation applicable under the Code in the computation of the beneficiary's tax liability.

One commenter noted that section 642(h) states that excess deductions on termination of an estate or trust are to be "al-

lowed as a deduction, in accordance with regulations prescribed by the Secretary” and that there is no express authority to treat excess deductions as miscellaneous or non-miscellaneous itemized deductions (or tax preference items for AMT purposes). The Treasury Department and the IRS disagree with this comment. The characterization of these excess deductions as a single miscellaneous itemized deduction in the current regulations was made before the enactment of section 67(g) and served as an administrative convenience. Making a change to that characterization is now appropriate to reflect the temporary disallowance of miscellaneous itemized deductions under section 67(g) since the regulations were written and is a proper exercise of the Secretary’s specific grant of regulatory authority in section 642(h).

Another commenter requested that non-miscellaneous itemized deductions included in excess deductions be fully deductible by the beneficiary and not subject to a second level of limitation applicable on the beneficiary’s return, because the amounts already would have been subject to limitation on the return of the estate or trust. The commenter provided an example of a terminated trust that paid \$25,000 of state income tax, for which the trust is limited to a \$10,000 deduction under section 164(b)(6)(B) for taxable years beginning after December 31, 2017, and before January 1, 2026. In the commenter’s example, the entire amount of the allowable \$10,000 deduction was passed through to the beneficiary as an excess deduction on termination of the trust. The excess of state income tax over the \$10,000 limitation (\$15,000) would not pass through as an excess deduction to the beneficiaries in this circumstance because the excess amount was not deductible to the trust. Excess state income tax on termination of the estate or trust may, however, pass through to a beneficiary if the estate or trust had insufficient income to absorb the entire \$10,000 of state income tax deduction. In that circumstance, the commenter opined that the limitation under section 164(b)(6)(B), having already been applied at the trust level, should not again be applied at the beneficiary level. The Treasury Department and the IRS carefully considered the comment but determined that beneficiaries remain subject to the limitation in

section 164(b)(6)(B). The Treasury Department and the IRS found no authority to exempt such items from the application of any limitations applicable to the beneficiary under the Code. The excess deductions retain their character in the hands of the beneficiary on termination of the trust, and all applicable limitations apply to all of the beneficiary’s items of that character, regardless of their origin.

One commenter noted that, under § 1.641(c)-1(j), if an electing small business trust (ESBT) election terminates or is revoked and the S portion has a net operating loss or capital loss carryover or deductions in excess of gross income, then any such loss, carryover or excess deductions are allowed as a deduction, in accordance with the regulations under section 642(h), to the trust or to the beneficiaries succeeding to the property of the trust if the entire trust terminates. However, the commenter also noted that under the TCJA, section 641(c)(2)(E) was amended to provide that ESBT charitable contributions are deductible under section 170, rather than under section 642(c), so that, unlike other trust charitable deductions, an ESBT’s charitable deduction could constitute part of the excess deductions on termination of the trust. The commenter stated that neither the legislative history nor the explanation of the staff of the Joint Committee on Taxation addressed whether this result was intended. The Treasury Department and the IRS note that charitable contribution deductions under both sections 170 and 642(c) are non-miscellaneous itemized deductions under sections 63(d) and 67(b)(4) to the estate or trust and maintain that such character is retained in the hands of the beneficiary in these regulations. Although the Treasury Department and the IRS continue to consider the application of section 170 to ESBT charitable contributions under section 641(c)(2)(E), this issue is outside the scope of these regulations.

Another commenter requested clarification of whether an excess deduction on termination of a trust or estate that is allowed in determining the net investment income under section 1411 of the estate or trust remains deductible in the hands of the beneficiary in determining the net investment income of the beneficiary under section 1411. These final regula-

tions provide that each excess deduction retains its separate character as a section 67(e) deduction, non-miscellaneous itemized deduction, or miscellaneous itemized deduction in the hands of the beneficiary. Whether a deduction retains its character as allowable in computing the net investment income of the beneficiary, however, is outside the scope of these regulations.

3. Reporting of excess deductions

Section 1.642(h)-2(b)(1) of the proposed regulations provides that an item of deduction succeeded to by a beneficiary remains subject to any additional applicable limitation under the Code and must be separately stated if it could be so limited, as provided in the instructions to Form 1041, *U.S. Income Tax Return for Estates and Trusts*, and the Schedule K-1 (Form 1041), *Beneficiary’s Share of Income, Deductions, Credit, etc.* Commenters requested that the Treasury Department and the IRS provide guidance on how the excess deductions are to be reported by both the terminated estate or trust and by its beneficiaries. The Treasury Department and the IRS released instructions for beneficiaries that chose to claim excess deductions on Form 1040 in the 2019 or 2018 taxable year based on the proposed regulations. In addition, the Treasury Department and the IRS plan to update the instructions for Form 1041, Schedule K-1 (Form 1041), and Form 1040, *U.S. Individual Income Tax Return*, for the 2020 and subsequent tax years to provide for the reporting of excess deductions that are section 67(e) expenses or non-miscellaneous itemized deductions.

The Treasury Department and the IRS are aware that the income tax laws of some U.S. states do not conform to the Code with respect to section 67(g), such that beneficiaries may need information on miscellaneous itemized deductions of a terminated estate or trust. However, because miscellaneous itemized deductions are currently not allowed for Federal income tax purposes, that information is not needed for Federal income tax purposes. Therefore, it would not be appropriate to modify Federal income tax forms to require or accommodate the collection of such information while this deduction is

suspended. Estates, trusts, and beneficiaries are advised to consult the relevant state taxing authority for information about deducting miscellaneous itemized expenses on their state tax returns.

4. Determinations of deductions in year of termination of the estate or trust

Section 1.642(h)-2(b)(2) of the proposed regulations provides that the provisions of § 1.652(b)-3 are used to allocate each item of deduction among the classes of income in the year of termination for purposes of determining the character and amount of the excess deductions under section 642(h)(2). Accordingly, the amount of each separate deduction remaining after application of § 1.652(b)-3 comprises the excess deductions available to the beneficiaries succeeding to the property of the estate or trust as provided under section 642(h)(2). In addition, as previously explained, an item of deduction succeeded to by a beneficiary remains subject to any additional applicable limitation under the Code. Furthermore, § 1.642(h)-2(c) of the proposed regulations provides that excess deductions are allowable only in the taxable year of the beneficiary in which or with which the estate or trust terminates. That is, excess deductions of a terminated estate or trust may not carry over to a subsequent year of the beneficiary.

One commenter requested that these regulations provide an ordering rule clarifying whether excess deductions on termination of an estate or trust allowed as a deduction to the beneficiary are claimed before, after, or ratably with the beneficiary's other deductions, particularly when the amount of the excess deductions and other deductions exceed the beneficiary's gross income. These final regulations clarify that beneficiaries may claim all or part of the excess deductions under section 642(h)(2) before, after, or together with the same character of deductions separately allowable to the beneficiary under the Code.

That commenter also requested that the final regulations include an exception for investment interest expense under section 163(d) from the general rule that excess deductions on termination of a trust or estate may be claimed only in the beneficiary's taxable year during which the trust

or estate terminated. That section permits the carryforward of investment interest under section 163(d)(2) to the taxpayer's subsequent taxable years if the taxpayer is unable to deduct the investment interest in the current taxable year. The commenter stated that the disallowance of the carryover of section 642(h)(2) excess deductions should not apply to those excess deductions that are no longer treated as miscellaneous itemized deductions under the proposed regulations, and that carryover should be permitted to the extent otherwise permitted under the Code. The preamble to the proposed regulations states that addressing suspended deductions under section 163(d) is beyond the scope of the regulations and the same is true of these final regulations.

A commenter requested that the amount of a beneficiary's net operating loss carryover to a later taxable year under section 172 should include all of the beneficiary's section 642(h)(2) excess deductions that are section 67(e) deductions, as deductions that are attributable to the beneficiary's trade or business and thus deductions attributable to a trade or business under section 172(d) (4). Section 642(h) makes it clear that a net operating loss carryover under paragraph (1) of that section is separate and distinct from the excess deductions on termination described in paragraph (2) of that section. Furthermore, § 1.642(h)-2(d) provides that a deduction based upon a net operating loss carryover generally will not be allowed to beneficiaries under both paragraphs (1) and (2) of section 642(h). Therefore, an excess deduction allowable to the beneficiary under section 642(h)(2) is not a net operating loss carryover succeeded to by the beneficiary under section 642(h)(1) and (with one exception) a net operating loss carryover is not an excess deduction on termination. Moreover, these regulations provide that it is the character of the excess deductions as section 67(e) deductions, non-miscellaneous itemized deductions, and miscellaneous itemized deductions, and not the character of a deduction as attributable to a trade or business, that is retained in the hands of the beneficiary. Thus, whether section 642(h)(2) excess deductions that are section 67(e) deductions may be included in a beneficiary's net operating loss carryovers under section 172, separate from those it succeeds to from a terminated

estate or trust, is beyond the scope of these regulations. Because § 1.642(h)-2(a) is clear that excess deductions on termination of an estate or trust are not carried over to future years and that such deductions are separate from a net operating loss carryover from the estate or trust, the Treasury Department and the IRS do not adopt this comment.

5. Example 1

Section 1.642(h)-5(a), *Example 1*, of the proposed regulations (*Example 1*) updates an existing example illustrating computations under section 642(h) when there is a net operating loss. Section 1.642-5(a)(2)(ii) of *Example 1* explains that the beneficiaries of the estate cannot carry back any of the net operating loss of the terminating estate that was made available to them under section 642(h)(1).

Two commenters requested that *Example 1* be revised to take into account the amendments to section 172(b)(1)(D) under sec. 2302(b) of the Coronavirus Aid, Relief, and Economic Security Act, Public Law 116-136, 134 Stat. 281 (2020) (CARES Act), by allowing a beneficiary to carry back the net operating loss carryover the beneficiary succeeds to under section 642(h)(1) for net operating losses arising in taxable years beginning after December 31, 2017, and before January 1, 2021. Under section 2303 of the CARES Act, net operating losses arising in taxable years beginning after December 31, 2017, and before January 1, 2021, generally may be carried back five years before being carried forward. One of these commenters further requested confirmation that a beneficiary is allowed a carryback of the net operating loss under section 642(h)(1) for net operating losses of an estate or trust arising in taxable years ending before January 1, 2018, to the extent the beneficiary succeeds to a net operating loss carryover attributable to those net operating losses on a termination of the estate or trust between January 1, 2018, and December 31, 2020.

Unless otherwise provided under the Code, a net operating loss incurred by a taxpayer may only be used as a deduction by that taxpayer and cannot be transferred to another taxpayer for use by that other taxpayer. *Calvin v. U.S.* 354 F.2d 202 (10th Cir. 1965), *Mellott v. U.S.*, 257 F.2d 798 (3d

Cir. 1958). As an exception to this general principle, section 642(h) provides that if, on termination of an estate or trust, the estate or trust has a net operating loss carryover under section 172, then such carryover is allowed as a deduction, in accordance with the regulations prescribed by the Secretary, to the beneficiaries succeeding to the property of the estate or trust. Section 1.642(h)-1(a) provides that if, on the termination of an estate or trust, a net operating loss carryover under section 172 would be allowable to the estate or trust in a taxable year subsequent to the taxable year of termination but for the termination, a carryover is allowed under section 642(h)(1) to the beneficiaries succeeding to the property of the estate or trust. In addition, § 1.642(h)-1(b) provides that the first taxable year of the beneficiary to which the net operating loss will be carried over is the taxable year of the beneficiary in which or with which the estate or trust terminates.

Section 642(h)(1) provides a specific rule that allows the beneficiary to succeed to a net operating loss carryover of the estate or trust and deduct the amount of the net operating loss over the remaining carryover period that would have been allowable to the estate or trust but for the termination of the estate or trust. The phrase in section 642(h)(1) “the estate or trust has a net operating loss *carryover*” means that the estate or trust incurred a net operating loss and either already carried it back to the earliest allowable year under section 172 or elected to waive the carryback period under section 172(b)(3), and now is limited to carrying over the remaining net operating loss. Accordingly, because the net operating loss is a carryover for the estate or trust, the beneficiary succeeding to that net operating loss may, under section 642(h)(1), only carry it forward.

The CARES Act amendments to section 172(b) mentioned by the commenters allow taxpayers a five-year carryback of certain net operating losses incurred by that taxpayer. The CARES Act amendments do not change the result that a beneficiary succeeding to the net operating loss carryover of a terminated estate or trust may only carryover that net operating loss in the same manner as the terminated estate or trust, but for the termination. Consequently, the Treasury Department and the IRS do not adopt these comments and add a citation to

§ 1.642(h)-1 to reference the rule that a beneficiary that succeeds to a net operating loss carryover of a terminated estate or trust may only carry forward the net operating loss.

6. Example 2

Section § 1.642(h)-5(b), *Example 2*, of the proposed regulations (*Example 2*) demonstrates computations under section 642(h)(2). The expenses in *Example 2* include rental real estate taxes in an attempt to illustrate a deduction subject to limitation under section 164(b)(6) to the beneficiary that must be separately stated as provided in § 1.642(h)-2(b)(1).

Multiple commenters noted that *Example 2* raises several issues that could be potentially relevant to that example, such as whether the decedent was in a trade or business and the application of section 469 to estates and trusts. To avoid these issues, which are extraneous to the point being illustrated, one commenter suggested that the example be revised so that the entire amount of real estate expenses on rental property equals the amount of rental income. The Treasury Department and the IRS did not intend to raise such issues in the example and consider both issues to be outside the scope of these regulations. Accordingly, the Treasury Department and the IRS adopt the suggestion by the commenter and modify *Example 2* to avoid these issues by having rental real estate expenses entirely offset rental income with no unused deduction.

Commenters also noted that *Example 2* does not properly allocate rental real estate expenses because the example characterizes the rental real estate taxes as itemized deductions. These commenters asserted that real estate taxes on property held for the production of rental income are not itemized deductions but instead are allowed in computing gross income and cited to section 62(a)(4) as providing that ordinary and necessary expenses paid or incurred during the taxable year for the management, conservation, or maintenance of property held for the production of income under section 212(2) that are attributable to property held for the production of rents are deductible as above-the-line deductions in arriving at adjusted gross income. One commenter suggested that, if the goal of *Example 2* is to illustrate state and local taxes passing through to the beneficiary, then the exam-

ple should include state income taxes rather than real estate taxes on rental real estate. The Treasury Department and the IRS have revised this example in the final regulations to include personal property tax paid by the trust rather than taxes attributable to rental real estate.

Lastly, commenters noted that *Example 2* does not demonstrate the broad range of trustee discretion in § 1.652(b)-3(b) and (d) for deductions that are not directly attributable to a class of income, or deductions that are, but which exceed such class of income, respectively. In response to these comments, the Treasury Department and the IRS have modified *Example 2* to illustrate the application of trustee discretion as found in § 1.652(b)-3(b) and (d).

C. Applicability Dates

The proposed regulations provide that the changes to §§ 1.67-4, 1.642(h)-2, and 1.642(h)-5 apply to taxable years beginning after the date the regulations are published as final. The preamble to the proposed regulations explains that estates, non-grantor trusts, and their beneficiaries may rely on the proposed regulations under section 67 for taxable years beginning after December 31, 2017, and on or before the date these regulations are published as final. Taxpayers may also rely on the proposed regulations under section 642(h) for taxable years of beneficiaries beginning after December 31, 2017, and on or before the date the regulations are published as final, in which an estate or trust terminates.

One commenter requested that § 1.642(h)-2 of the proposed regulations be applied retroactively not only to taxable years beginning after December 31, 2017, but to all open years. The commenter asserted that the existing regulation treating excess deductions on termination of an estate or trust as a miscellaneous itemized deduction was in error. As an example, the commenter argues that the current regulations mistakenly describe section 67(e) expenses as an exception to the rules applicable to miscellaneous itemized deductions, and therefore requested that the final regulations be applicable to all open years. The Treasury Department and the IRS have the authority to treat an excess deduction on termination of an estate or trust as a single miscellaneous itemized deduction. See

section 642(h). The suspension under section 67(g) of miscellaneous itemized deductions caused the Treasury Department and the IRS to reconsider the treatment of excess deductions under section 642(h)(2) because the Treasury Department and the IRS do not interpret section 67(g) as suspending such deductions allowable under section 642(h)(2). The Treasury Department and the IRS interpret section 67(g) as not disallowing excess deductions succeeded to beneficiaries from terminated estates and trusts under section 642(h)(2). Therefore, taxpayers may rely on these regulations as of the effective date of section 67(g), but not for earlier periods.

The final regulations apply to taxable years beginning after October 19, 2020. Pursuant to section 7805(b)(7), taxpayers may choose to apply the amendments to § 1.67-4 and §§ 1.642(h)-2 and 1.642(h)-5 set forth in this Treasury decision to taxable years beginning after December 31, 2017, and on or before October 19, 2020.

Special Analysis

These regulations are not subject to review under section 6(b) of Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget regarding review of tax regulations. Therefore, a regulatory impact assessment is not required.

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the amount of time necessary to report the required information will be minimal in that it requires fiduciaries of estates and trusts to provide on the Schedule K-1 (Form 1041) issued to beneficiaries information that is already maintained and reported to the IRS on Form 1041. Moreover, it should take an estate or trust no more than 2 hours to satisfy the information requirement in these regulations. Accordingly, the Secretary certifies that the rule will not have a significant economic impact on a substantial number of small entities.

Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking that preceded these regulations was submitted to

the Chief Counsel for the Office of Advocacy of the Small Business Administration for comment on its impact on small businesses, and no comments were received.

Paperwork Reduction Act (PRA)

The collection of information related to these regulations under section 642(h) is reported on Schedule K-1 (Form 1041), *Beneficiary's Share of Income, Deductions, Credits, etc.*, and has been reviewed in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) and approved by the Office of Management and Budget under control number 1545-0092.

The collection of information in these regulations is in § 1.642(h)-2(b)(1). The IRS requires this information to ensure that excess deductions on an estate's or trust's termination that are subject to additional applicable limitations retain their character when taken into account by beneficiaries on their returns. The respondents will be estates, trusts, and their fiduciaries.

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 tax return information are confidential, as required by section 6103.

Drafting Information

The principal author of these regulations is Margaret Burow of the Office of Associate Chief Counsel (Passthroughs and Special Industries). Other personnel from the Treasury Department and the IRS, however, participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and record-keeping 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 is amended by adding entries for §§ 1.67-4, 1.642(h)-2, and 1.642(h)-5 in numerical order to read in part as follows:

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

Section 1.67-4 also issued under 26 U.S.C. 67(e).

* * * * *

Section 1.642(h)-2 also issued under 26 U.S.C. 642(h).

Section 1.642(h)-5 also issued under 26 U.S.C. 642(h).

* * * * *

Par. 2. Section 1.67-4 is amended by revising paragraph (a) and the heading of paragraph (d) and adding two sentences to the end of paragraph (d) to read as follows:

§ 1.67-4 Costs paid or incurred by estates or non-grantor trusts.

(a) *Deductions*—(1) *Section 67(e) deductions*—(i) *In general.* An estate or trust (including the S portion of an electing small business trust) not described in § 1.67-2T(g) (1)(i) (a non-grantor trust) must compute its adjusted gross income in the same manner as an individual, except that the following deductions (section 67(e) deductions) are allowed in arriving at adjusted gross income:

(A) Costs that are paid or incurred in connection with the administration of the estate or trust that would not have been incurred if the property were not held in such estate or trust; and

(B) Deductions allowable under section 642(b) (relating to the personal exemption) and sections 651 and 661 (relating to distributions).

(ii) *Not disallowed under section 67(g).* Section 67(e) deductions are not itemized deductions under section 63(d) and are not miscellaneous itemized deductions under section 67(b). Therefore, section 67(e) deductions are not disallowed under section 67(g).

(2) *Deductions subject to 2-percent floor.* A cost is not a section 67(e) deduction and thus is subject to both the 2-percent floor in section 67(a) and section 67(g) to the extent that it is included in the definition of miscellaneous itemized deductions under section 67(b), is incurred by an estate or non-grantor trust (includ-

ing the S portion of an electing small business trust), and commonly or customarily would be incurred by a hypothetical individual holding the same property.

(d) *Applicability date.* *** Paragraph (a) of this section applies to taxable years beginning after October 19, 2020. Taxpayers may choose to apply paragraph (a) of this section to taxable years beginning after December 31, 2017, and on or before October 19, 2020.

Par. 3. Section 1.642(h)–2 is amended by:

1. Revising paragraph (a).
2. Redesignating paragraph (b) as paragraph (d) and adding a heading for newly redesignated paragraph (d).
3. Redesignating paragraph (c) as paragraph (e) and adding a heading for newly redesignated paragraph (e).
4. Adding new paragraphs (b) and (c) and paragraph (f).

The revisions and additions read as follows:

§ 1.642(h)–2 Excess deductions on termination of an estate or trust.

(a) *Excess deductions*—(1) *In general.* If, on the termination of an estate or trust, the estate or trust has for its last taxable year deductions (other than the deductions allowed under section 642(b) (relating to the personal exemption) or section 642(c) (relating to charitable contributions)) in excess of gross income, the excess deductions as determined under paragraph (b) of this section are allowed under section 642(h)(2) as items of deduction to the beneficiaries succeeding to the property of the estate or trust.

(2) *Treatment by beneficiary.* A beneficiary may claim all or part of the amount of the deductions provided for in paragraph (a) of this section, as determined after application of paragraph (b) of this section, before, after, or together with the same character of deductions separately allowable to the beneficiary under the Internal Revenue Code for the beneficiary's taxable year during

which the estate or trust terminated as provided in paragraph (c) of this section.

(b) *Character and amount of excess deductions*—(1) *Character.* The character and amount of the excess deductions on termination of an estate or trust will be determined as provided in this paragraph (b). Each deduction comprising the excess deductions under section 642(h)(2) retains, in the hands of the beneficiary, its character (specifically, as allowable in arriving at adjusted gross income, as a non-miscellaneous itemized deduction, or as a miscellaneous itemized deduction) while in the estate or trust. An item of deduction succeeded to by a beneficiary remains subject to any additional applicable limitation under the Internal Revenue Code and must be separately stated if it could be so limited, as provided in the instructions to Form 1041, *U.S. Income Tax Return for Estates and Trusts*, and the Schedule K–1 (Form 1041), *Beneficiary's Share of Income, Deductions, Credit, etc.*, or successor forms.

(2) *Amount.* The amount of the excess deductions in the final year is determined as follows:

- (i) Each deduction directly attributable to a class of income is allocated in accordance with the provisions in § 1.652(b)–3(a);
- (ii) To the extent of any remaining income after application of paragraph (b)(2)(i) of this section, deductions are allocated in accordance with the provisions in § 1.652(b)–3(b) and (d); and
- (iii) Deductions remaining after the application of paragraph (b)(2)(i) and (ii) of this section comprise the excess deductions on termination of the estate or trust. These deductions are allocated to the beneficiaries succeeding to the property of the estate or trust in accordance with § 1.642(h)–4.

(c) *Year of termination*—(1) *In general.* The deductions provided for in paragraph (a) of this section are allowable only in the taxable year of the beneficiary in which or with which the estate or trust terminates, whether the year of termination of the estate or trust is of normal duration or is a short taxable year.

(2) *Example.* Assume that a trust distributes all its assets to B and terminates on December 31, Year X. As of that date, it has excess deductions of \$18,000, all characterized as allowable in arriving at adjusted gross income under section 67(e). B, who reports on the calendar year basis, could claim the \$18,000 as a deduction allowable in arriving at B's adjusted gross income for Year X. However, if the deduction (when added to other allowable deductions that B claims for the year) exceeds B's gross income, the excess may not be carried over to any year subsequent to Year X.

(d) *Net operating loss carryovers.* ***

(e) *Items included in net operating loss or capital loss carryovers.* ***

(f) *Applicability date.* Paragraphs (a) through (c) of this section apply to taxable years beginning after October 19, 2020. The rules applicable to taxable years beginning on or before October 19, 2020, are contained in § 1.642(h)–2 as in effect prior to October 19, 2020 (see 26 CFR part 1 revised as of April 1, 2020). Taxpayers may choose to apply paragraphs (a) through (c) of this section to taxable years beginning after December 31, 2017, and on or before October 19, 2020.

Par. 4. Section 1.642(h)–5 is revised to read as follows:

§ 1.642(h)–5 Examples.

Paragraphs (a) and (b) of this section (*Examples 1 and 2*) illustrate the application of section 642(h).

(a) *Example 1: Computations under section 642(h) when an estate has a net operating loss*—(1) *Facts.* On January 31, 2020, A dies leaving a will that provides for the distribution of all of A's estate equally to B and an existing trust for C. The period of administration of the estate terminates on December 31, 2020, at which time all the property of the estate is distributed to B and the trust. For tax purposes, B and the trust report income on a calendar year basis. During the period of administration, the estate has the following items of income and deductions:

TABLE 1 TO PARAGRAPH (a)(1)

| | |
|------------------------|--------------|
| <i>Income</i> | |
| Taxable interest | \$2,500 |
| Business income | <u>3,000</u> |
| Total income | 5,500 |

TABLE 2 TO PARAGRAPH (a)(1)

Deductions

| | |
|--|--------------|
| Business expenses (including administrative expense allocable to business income) | 5,000 |
| Administrative expenses not allocable to business income that would not have been incurred if property had not been held in a trust or estate (section 67(e) deductions) | <u>9,800</u> |
| Total deductions | 14,800 |

(2) *Computation of net operating loss.* (i) The amount of the net operating loss carryover is computed as follows:

TABLE 3 TO PARAGRAPH (a)(2)(i)

| | |
|--|--------------|
| Gross income | \$5,500 |
| Total deductions | 14,800 |
| Less adjustment under section 172(d)(4) (allowable non-business expenses (\$9,800) limited to non-business income (\$2,500)) | <u>7,300</u> |
| Deductions as adjusted | <u>7,500</u> |
| Net operating loss | 2,000 |

(ii) Under section 642(h)(1), B and the trust are each allocated \$1,000 of the \$2,000 unused net operating loss carryover of the terminated estate in 2020, with the allowance of any net operating loss carryover to B and the trust determined under section 172. Neither B nor the trust can carry back any of the net operating loss of A's estate made available to them under section 642(h)(1). See § 1.642(h)-1(b).

(3) *Section 642(h)(2) excess deductions.* The \$7,300 of non-business deduc-

tions not taken into account in determining the net operating loss of the estate are excess deductions on termination of the estate under section 642(h)(2). Under § 1.642(h)-2(b)(1), such deductions retain their character as section 67(e) deductions. Under § 1.642(h)-4, B and the trust each are allocated \$3,650 of excess deductions based on B's and the trust's respective shares of the burden of each cost.

(4) *Consequences for C.* The net operating loss carryover and excess deductions

are not allowable directly to C, the trust beneficiary. To the extent the distributable net income of the trust is reduced by the net operating loss carryover and excess deductions, however, C may receive an indirect benefit from the carryover and excess deductions.

(b) *Example 2: Computations under section 642(h)(2)—(1) Facts.* D dies in 2019 leaving an estate of which the residuary legatees are E (75%) and F (25%). The estate's income and deductions in its final year are as follows:

TABLE 4 TO PARAGRAPH (b)(1)

| | |
|------------------------|--------------|
| <i>Income</i> | |
| Dividends | \$3,000 |
| Taxable Interest | 500 |
| Rent | 2,000 |
| Capital Gain | <u>1,000</u> |
| Total Income | 6,500 |

TABLE 5 TO PARAGRAPH (b)(1)

Deductions

Section 62(a)(4) deductions:

| | |
|-----------------------------------|-------|
| Rental real estate expenses | 2,000 |
|-----------------------------------|-------|

Section 67(e) deductions:

| | |
|--------------------|-------|
| Probate fees | 1,500 |
|--------------------|-------|

| | |
|-----------------------------------|-------|
| Estate tax preparation fees | 8,000 |
|-----------------------------------|-------|

| | |
|------------------|-------|
| Legal fees | 2,500 |
|------------------|-------|

| | |
|--------------------------------------|--------|
| Total Section 67(e) deductions | 12,000 |
|--------------------------------------|--------|

Non-miscellaneous itemized deductions:

| | |
|-------------------------------|-------|
| Personal property taxes | 3,500 |
|-------------------------------|-------|

| | |
|------------------------|--------|
| Total deductions | 17,500 |
|------------------------|--------|

(2) *Determination of character.* Pursuant to § 1.642(h)–2(b)(2), the character and amount of the excess deductions is determined by allocating the deductions among the estate’s items of income as provided under § 1.652(b)–3. Under § 1.652(b)–3(a), the \$2,000 of rental real estate expenses is allocated to the \$2,000 of rental income. In the exercise of the executor’s discretion pursuant to § 1.652(b)–3(b), D’s executor allocates \$3,500 of personal property taxes and \$1,000 of section 67(e) deductions to the remaining income. As a result, the excess deductions on termination of the estate are \$11,000, all consisting of section 67(e) deductions.

(3) *Allocations among beneficiaries.* Pursuant to § 1.642(h)–4, the excess deductions are allocated in accordance

with E’s (75 percent) and F’s (25 percent) interests in the residuary estate. E’s share of the excess deductions is \$8,250, all consisting of section 67(e) deductions. F’s share of the excess deductions is \$2,750, also all consisting of section 67(e) deductions.

(4) *Separate statement.* If the executor instead allocated \$4,500 of section 67(e) deductions to the remaining income of the estate, the excess deductions on termination of the estate would be \$11,000, consisting of \$7,500 of section 67(e) deductions and \$3,500 of personal property taxes. The non-miscellaneous itemized deduction for personal property taxes may be subject to limitation on the returns of both B and C’s trust under section 164(b)(6)(B) and would have to be separately stated as provided in § 1.642(h)–2(b)(1).

(c) *Applicability date.* This section is applicable to taxable years beginning after October 19, 2020. Taxpayers may choose to apply this section to taxable years beginning after December 31, 2017, and on or before October 19, 2020.

Sunita Lough,
*Deputy Commissioner for Services
and Enforcement.*

Approved: September 16, 2020.

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

(Filed by the Office of the Federal Register on October 16, 2020, 8:45 a.m., and published in the issue of the Federal Register for October 19, 2020, 85 F.R. 66219)

Part III

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

Notice 2020-77

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

YIELD CURVE AND SEGMENT RATES

Section 430 specifies the minimum funding requirements that apply to single-employer plans (except for CSEC plans under § 414(y)) pursuant to § 412.

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

Notice 2007-81, 2007-44 I.R.B. 899, provides guidelines for determining the monthly corporate bond yield curve, and the 24-month average corporate bond segment rates used to compute the target normal cost and the funding target. Consistent with the methodology specified in Notice 2007-81, the monthly corporate bond yield curve derived from September 2020 data is in Table 2020-9 at the end of this notice. The spot first, second, and third segment rates for the month of Sep-

tember 2020 are, respectively, 0.51, 2.31, and 3.15.

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

24-MONTH AVERAGE CORPORATE BOND SEGMENT RATES

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

| <i>24-Month Average Segment Rates Without 25-Year Average Adjustment</i> | | | |
|--|---------------|----------------|---------------|
| Applicable Month | First Segment | Second Segment | Third Segment |
| October 2020 | 2.11 | 3.30 | 3.86 |

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

| <i>Adjusted 24-Month Average Segment Rates</i> | | | | |
|--|------------------|---------------|----------------|---------------|
| For Plan Years Beginning In | Applicable Month | First Segment | Second Segment | Third Segment |
| 2019 | October 2020 | 3.74 | 5.35 | 6.11 |
| 2020 | October 2020 | 3.64 | 5.21 | 5.94 |
| 2021 | October 2020 | 3.32 | 4.79 | 5.47 |

30-YEAR TREASURY SECURITIES INTEREST RATES

Section 431 specifies the minimum

funding requirements that apply to multi-employer plans pursuant to § 412. Section 431(c)(6)(B) specifies a minimum amount for the full-funding limitation described in

§ 431(c)(6)(A), based on the plan's current liability. Section 431(c)(6)(E)(ii)(I) provides that the interest rate used to calculate current liability for this purpose must be

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

no more than 5 percent above and no more than 10 percent below the weighted average of the rates of interest on 30-year Treasury securities during the four-year period ending on the last day before the beginning of the plan year. Notice 88-73, 1988-2 C.B.

383, provides guidelines for determining the weighted average interest rate. The rate of interest on 30-year Treasury securities for September 2020 is 1.42 percent. The Service determined this rate as the average of the daily determinations of yield on the

30-year Treasury bond maturing in August 2050. For plan years beginning in October 2020, the weighted average of the rates of interest on 30-year Treasury securities and the permissible range of rates used to calculate current liability are as follows:

| <i>Treasury Weighted Average Rates</i> | | |
|--|--|--------------------------------------|
| For Plan Years Beginning In | 30-Year Treasury Weighted Average | Permissible Range 90% to 105% |
| October 2020 | 2.43 | 2.19 to 2.55 |

MINIMUM PRESENT VALUE SEGMENT RATES

In general, the applicable interest rates

under § 417(e)(3)(D) are segment rates computed without regard to a 24-month average. Notice 2007-81 provides guidelines for determining the minimum pres-

ent value segment rates. Pursuant to that notice, the minimum present value segment rates determined for September 2020 are as follows:

| <i>Minimum Present Value Segment Rates</i> | | | |
|--|----------------------|-----------------------|----------------------|
| Month | First Segment | Second Segment | Third Segment |
| September 2020 | 0.51 | 2.31 | 3.15 |

DRAFTING INFORMATION

The principal author of this notice is Tom Morgan of the Office of the Asso-

ciate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the IRS participated in the development

of this guidance. For further information regarding this notice, contact Mr. Morgan at 202-317-6700 or Paul Stern at 202-317-8702 (not toll-free numbers).

Table 2020-9
Monthly Yield Curve for September 2020
Derived from September 2020 Data

| <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> | <i>Maturity</i> | <i>Yield</i> |
|-----------------|--------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|
| 0.5 | 0.16 | 20.5 | 2.97 | 40.5 | 3.18 | 60.5 | 3.25 | 80.5 | 3.29 |
| 1.0 | 0.28 | 21.0 | 2.98 | 41.0 | 3.18 | 61.0 | 3.26 | 81.0 | 3.30 |
| 1.5 | 0.39 | 21.5 | 2.99 | 41.5 | 3.18 | 61.5 | 3.26 | 81.5 | 3.30 |
| 2.0 | 0.47 | 22.0 | 3.00 | 42.0 | 3.18 | 62.0 | 3.26 | 82.0 | 3.30 |
| 2.5 | 0.52 | 22.5 | 3.00 | 42.5 | 3.19 | 62.5 | 3.26 | 82.5 | 3.30 |
| 3.0 | 0.55 | 23.0 | 3.01 | 43.0 | 3.19 | 63.0 | 3.26 | 83.0 | 3.30 |
| 3.5 | 0.59 | 23.5 | 3.02 | 43.5 | 3.19 | 63.5 | 3.26 | 83.5 | 3.30 |
| 4.0 | 0.64 | 24.0 | 3.02 | 44.0 | 3.20 | 64.0 | 3.26 | 84.0 | 3.30 |
| 4.5 | 0.71 | 24.5 | 3.03 | 44.5 | 3.20 | 64.5 | 3.26 | 84.5 | 3.30 |
| 5.0 | 0.80 | 25.0 | 3.03 | 45.0 | 3.20 | 65.0 | 3.27 | 85.0 | 3.30 |
| 5.5 | 0.91 | 25.5 | 3.04 | 45.5 | 3.20 | 65.5 | 3.27 | 85.5 | 3.30 |
| 6.0 | 1.03 | 26.0 | 3.05 | 46.0 | 3.20 | 66.0 | 3.27 | 86.0 | 3.30 |
| 6.5 | 1.16 | 26.5 | 3.05 | 46.5 | 3.21 | 66.5 | 3.27 | 86.5 | 3.30 |
| 7.0 | 1.30 | 27.0 | 3.06 | 47.0 | 3.21 | 67.0 | 3.27 | 87.0 | 3.30 |
| 7.5 | 1.44 | 27.5 | 3.06 | 47.5 | 3.21 | 67.5 | 3.27 | 87.5 | 3.30 |
| 8.0 | 1.58 | 28.0 | 3.07 | 48.0 | 3.21 | 68.0 | 3.27 | 88.0 | 3.30 |
| 8.5 | 1.72 | 28.5 | 3.08 | 48.5 | 3.22 | 68.5 | 3.27 | 88.5 | 3.31 |
| 9.0 | 1.85 | 29.0 | 3.08 | 49.0 | 3.22 | 69.0 | 3.27 | 89.0 | 3.31 |
| 9.5 | 1.97 | 29.5 | 3.09 | 49.5 | 3.22 | 69.5 | 3.28 | 89.5 | 3.31 |
| 10.0 | 2.08 | 30.0 | 3.09 | 50.0 | 3.22 | 70.0 | 3.28 | 90.0 | 3.31 |
| 10.5 | 2.19 | 30.5 | 3.10 | 50.5 | 3.22 | 70.5 | 3.28 | 90.5 | 3.31 |
| 11.0 | 2.29 | 31.0 | 3.10 | 51.0 | 3.23 | 71.0 | 3.28 | 91.0 | 3.31 |
| 11.5 | 2.37 | 31.5 | 3.11 | 51.5 | 3.23 | 71.5 | 3.28 | 91.5 | 3.31 |
| 12.0 | 2.45 | 32.0 | 3.11 | 52.0 | 3.23 | 72.0 | 3.28 | 92.0 | 3.31 |
| 12.5 | 2.53 | 32.5 | 3.12 | 52.5 | 3.23 | 72.5 | 3.28 | 92.5 | 3.31 |
| 13.0 | 2.59 | 33.0 | 3.12 | 53.0 | 3.23 | 73.0 | 3.28 | 93.0 | 3.31 |
| 13.5 | 2.64 | 33.5 | 3.13 | 53.5 | 3.23 | 73.5 | 3.28 | 93.5 | 3.31 |
| 14.0 | 2.69 | 34.0 | 3.13 | 54.0 | 3.24 | 74.0 | 3.28 | 94.0 | 3.31 |
| 14.5 | 2.74 | 34.5 | 3.14 | 54.5 | 3.24 | 74.5 | 3.28 | 94.5 | 3.31 |
| 15.0 | 2.77 | 35.0 | 3.14 | 55.0 | 3.24 | 75.0 | 3.29 | 95.0 | 3.31 |
| 15.5 | 2.80 | 35.5 | 3.14 | 55.5 | 3.24 | 75.5 | 3.29 | 95.5 | 3.31 |
| 16.0 | 2.83 | 36.0 | 3.15 | 56.0 | 3.24 | 76.0 | 3.29 | 96.0 | 3.31 |
| 16.5 | 2.86 | 36.5 | 3.15 | 56.5 | 3.24 | 76.5 | 3.29 | 96.5 | 3.31 |
| 17.0 | 2.88 | 37.0 | 3.15 | 57.0 | 3.25 | 77.0 | 3.29 | 97.0 | 3.31 |
| 17.5 | 2.90 | 37.5 | 3.16 | 57.5 | 3.25 | 77.5 | 3.29 | 97.5 | 3.32 |
| 18.0 | 2.91 | 38.0 | 3.16 | 58.0 | 3.25 | 78.0 | 3.29 | 98.0 | 3.32 |
| 18.5 | 2.93 | 38.5 | 3.16 | 58.5 | 3.25 | 78.5 | 3.29 | 98.5 | 3.32 |
| 19.0 | 2.94 | 39.0 | 3.17 | 59.0 | 3.25 | 79.0 | 3.29 | 99.0 | 3.32 |
| 19.5 | 2.95 | 39.5 | 3.17 | 59.5 | 3.25 | 79.5 | 3.29 | 99.5 | 3.32 |
| 20.0 | 2.96 | 40.0 | 3.17 | 60.0 | 3.25 | 80.0 | 3.29 | 100.0 | 3.32 |

SECTION 1. PURPOSE AND SCOPE

This revenue procedure provides the maximum amount allowed to be newly made available for plan years beginning after December 31, 2020, and before January 1, 2022, for excepted benefit health reimbursement arrangements provided under § 54.9831-1(c)(3)(viii). The maximum amount indexed pursuant to § 54.9831-1(c)(3)(viii)(B)(1) will not change for plan years beginning after December 31, 2020, and before January 1, 2022, and remains \$1,800.

SECTION 2. BACKGROUND

Under § 54.9831-1(c)(3), certain group health plans qualify as limited excepted benefits that are not subject to the requirements of Chapter 100 of the Internal Revenue Code. Section 54.9831-1(c)(3)(viii) provides rules for health reimbursement arrangements (HRAs) and other account-based group health plans to qualify as limited excepted benefits. Section 54.9831-1(c)(3)(viii)(B) provides that amounts newly made available for each plan year under the HRA or other account-based group health plan (excepted benefit HRA) may not exceed \$1,800. For plan years beginning after December 31, 2020, the \$1,800 dollar amount is increased by an amount equal to \$1,800 multiplied by the applicable cost-of-living adjustment.

The applicable cost-of-living adjustment for plan years beginning after December 31, 2020, and before January 1, 2022, is the percentage (if any) by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the Bureau of Labor Statistics of the Department of Labor, for the preceding year exceeds the C-CPI-U for calendar year 2019. The C-CPI-U for any calendar year is the average of the C-CPI-U as of the close of the 12-month period ending on March 31 of that calendar year. Any increase that is not a multiple of \$50 is rounded down to the next lowest multiple of \$50.

SECTION 3. PROCEDURE

For plan years beginning after December 31, 2020, and before January 1, 2022, the maximum amount that may be made newly available for the plan year for an excepted benefit HRA under § 54.9831-1(c)(3)(viii) is \$1,800. The Department of the Treasury and the Internal Revenue Service intend to publish, by June 1, 2021, the adjusted amount for plan years beginning after December 31, 2021, and before January 1, 2023.

SECTION 4. EFFECTIVE DATE

The effective date of this revenue procedure is the date of publication of this revenue procedure in the Internal Revenue Bulletin.

SECTION 5. DRAFTING INFORMATION

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

**Revenue Procedure
2020-44**
SECTION 1. PURPOSE

The purpose of this revenue procedure is to facilitate the market's transition from the London Interbank Offered Rate (LIBOR) and other interbank offered rates (IBORs) to alternative reference rates through adoption of fallback language recommended by the Alternative Reference Rates Committee (ARRC) and the International Swaps and Derivatives Association (ISDA). In support of the ARRC's phased transition plan to assist market participants as they prepare for this transition away from IBORs, this revenue procedure provides that certain modifications to a contract with terms referencing an IBOR will not be treated as

an exchange of property for other property differing materially in kind or extent for purposes of § 1.1001-1(a) of the Income Tax Regulations. In addition, this revenue procedure provides that such modifications will not be treated as a legging out of an integrated transaction, a termination of a qualified hedge, or as a disposition or termination of either leg of a hedging transaction.

SECTION 2. BACKGROUND

.01 *LIBOR and other IBORs.* On July 27, 2017, the Financial Conduct Authority, the United Kingdom regulator tasked with overseeing LIBOR, announced that all currency and term variants of LIBOR, including U.S.-dollar LIBOR (USD LIBOR), may be phased out after the end of 2021. The Financial Stability Board and the Financial Stability Oversight Council have publicly acknowledged that, in light of the prevalence of USD LIBOR as the reference rate in a broad range of financial instruments, the probable elimination of USD LIBOR has created risks that pose a potential threat not only to the safety and soundness of individual financial institutions but also to financial stability generally.

.02 *The ARRC and SOFR.* The ARRC, whose ex officio members include the Board of Governors of the Federal Reserve System, the Department of the Treasury (Treasury Department), the Commodity Futures Trading Commission, and the Office of Financial Research, was convened by the Board of Governors of the Federal Reserve System and the Federal Reserve Bank of New York to identify an alternative reference rate that would be more robust than USD LIBOR and that would comply with standards such as the International Organization of Securities Commissions' "Principles for Financial Benchmarks." After considering a comprehensive list of alternatives, the ARRC recommended the Secured Overnight Financing Rate (SOFR) as the replacement for USD LIBOR. Since April 3, 2018, the Federal Reserve Bank of New York has published SOFR daily.

.03 *ARRC contract fallback language.* The ARRC was also tasked with facilitating the voluntary acceptance of SOFR as the replacement for USD LIBOR. Many

cash products, including newly issued cash products, refer to USD LIBOR and contain fallback provisions that do not adequately protect against the cessation of that benchmark. To support the transition from USD LIBOR, the ARRC has published recommended fallback language for inclusion in the terms of certain newly issued cash products, including floating rate notes, bilateral business loans, syndicated loans, securitizations, adjustable rate mortgages, and variable-rate private student loans. In each case, the fallback language describes the circumstances under which references to the current benchmark rate are replaced. When such a circumstance arises, the fallback language generally provides a mechanism for determining the replacement benchmark rate that supplants the current benchmark rate. The fallback language generally also provides a mechanism for determining a spread adjustment that is added to the replacement benchmark rate to account for any difference between the replacement benchmark rate and the current benchmark rate. Although the ARRC has recommended this fallback language for use in newly issued cash products, the ARRC believes that parties to outstanding cash products that refer to USD LIBOR will also modify the contracts relating to those cash products to incorporate the appropriate fallback language.

.04 ISDA and derivative contracts. The ARRC has also been actively engaged in work led by ISDA to ensure that the contractual fallback provisions in derivative contracts are sufficiently robust to prevent serious market disruptions if LIBOR is permanently discontinued. Documents published by ISDA, such as the 2002 ISDA Master Agreement and the 2006 ISDA Definitions, form the basic framework of many derivative contracts. Section 7.1 of the 2006 ISDA Definitions lists and defines the various standard floating rates from which the parties may choose in creating a derivative contract (rate options). These rate options may be combined with other elements, such as the addition of a fixed spread, to determine the overall floating rate under the derivative contract. Generally, the 2006 ISDA

Definitions define each rate option by describing the methodology for determining the value of the rate option at each reset date. In the case of rate options that refer to IBORs, the 2006 ISDA Definitions also provide fallback provisions that generally designate another rate to stand in for the relevant IBOR if the IBOR is unavailable.

(1) *The ISDA Supplement.* By publishing supplements to the 2006 ISDA Definitions, ISDA can amend the provisions of the 2006 ISDA Definitions to address developments in the market. ISDA posted Supplement number 70 to the 2006 ISDA Definitions on <https://www.isda.org> on October 9, 2020, (ISDA Supplement) to facilitate inclusion of new fallbacks for certain key IBORs in derivatives transactions entered into on or after the date the ISDA Supplement takes effect. The ISDA Supplement has a final date of October 23, 2020, and a publication and effectiveness date of January 25, 2021. Among other things, the ISDA Supplement amends the fallback provisions for rate options that refer to IBORs to provide that, upon the occurrence of certain events, a substitute rate identified in the ISDA Supplement replaces the relevant IBOR. For example, upon an official announcement or publication regarding the permanent discontinuation or unreliability of USD LIBOR, the ISDA Supplement generally provides that USD LIBOR is replaced by a rate that is the sum of tenor-adjusted SOFR and an adjustment spread based on the historical difference between USD LIBOR and tenor-adjusted SOFR. Derivative contracts entered into on or after the effective date of the ISDA Supplement will generally include the relevant terms of the 2006 ISDA Definitions as amended by the ISDA Supplement.

(2) *The ISDA Protocol.* Unless modified by the parties, the terms of derivative contracts entered into prior to the effective date of the ISDA Supplement (legacy derivative contracts) will not incorporate the terms of the ISDA Supplement. ISDA posted the final ISDA 2020 IBOR Fallbacks Protocol on <https://www.isda.org> on October 9, 2020, (ISDA Protocol) to facilitate adoption of the ISDA Supplement by parties to legacy derivative contracts. The ISDA Protocol will launch publicly and

open for adherence on October 23, 2020. If parties adhere to the ISDA Protocol, all covered derivative contracts between those parties are generally modified to incorporate the terms of the ISDA Supplement or, in some cases, to incorporate a version of the terms of the ISDA Supplement adapted to fit the existing terms of the contract.

(3) *Bilateral agreements.* In some circumstances, legacy derivative contracts and other contracts may incorporate the terms of an ISDA Fallback (as defined in section 3.02 of this revenue procedure) on a transaction-by-transaction basis through an agreement between the parties to the contract (bilateral agreement) rather than through adherence to the ISDA Protocol. For example, bilateral agreements may be necessary when some aspect of the law of a non-U.S. jurisdiction prevents adherence to the ISDA Protocol.

.05 Guidance on modifications to replace an IBOR. The Treasury Department and the Internal Revenue Service (IRS) have determined that it is appropriate to provide guidance on the tax consequences of modifying debt instruments, derivative contracts, and other contracts to replace IBORs or add fallback provisions to IBORs. The Treasury Department and the IRS published proposed regulations (84 F.R. 54068) on October 9, 2019 (Proposed Regulations).¹ On March 12, 2020, the ARRC submitted a letter to the Treasury Department and the IRS in which the ARRC provided comments on the Proposed Regulations.

In connection with development of the ISDA Protocol, the ARRC submitted written comments to the Treasury Department and the IRS on December 9, 2019, December 20, 2019, January 30, 2020, and July 10, 2020, recommending guidance on the tax consequences of modifying a contract as provided in the ISDA Protocol. (Those written comments and the ARRC's letter dated March 12, 2020, are collectively referred to as the "ARRC Letters.") The ARRC also recommended similar guidance for the ARRC Fallbacks (as defined in section 3.01 of this revenue procedure). For reasons detailed in the ARRC Letters, the ARRC has recommended is-

¹The preamble to the Proposed Regulations generally provides that a taxpayer may rely on the Proposed Regulations before the publication of the final regulations in the Federal Register.

suing guidance that is separate from the Proposed Regulations and specific to the ARRC Fallbacks and the ISDA Protocol. Having reviewed the ARRC Fallbacks and the ISDA Protocol, the Treasury Department and the IRS have concluded that interim guidance in advance of finalizing the Proposed Regulations is needed to support the adoption of the ARRC Fallbacks and the ISDA Protocol. The following paragraphs of this section 2.05 describe the guidance recommended by the ARRC.

(1) *Guidance recommended under section 1001.* Section 1001 of the Internal Revenue Code (Code) provides rules for determining the amount and recognition of gain or loss from the sale or other disposition of property. Section 1.1001-1(a) generally provides that gain or loss is realized upon the exchange of property for other property differing materially either in kind or in extent. In the case of a debt instrument, § 1.1001-3 provides rules for determining whether a modification of the terms of the debt instrument results in an exchange of the original debt instrument for a modified debt instrument that differs materially either in kind or in extent for purposes of § 1.1001-1(a). The ARRC Letters generally recommend guidance providing that the modification of a contract to incorporate the terms of an ARRC Fallback, an ISDA Fallback, or certain variants of an ARRC or ISDA Fallback described in section 4.02(3) of this revenue procedure does not result in an exchange under § 1.1001-1(a).

(2) *Guidance recommended on integrated transactions.* A debt instrument and one or more derivative contracts may be treated in certain circumstances as a single, integrated instrument for certain specified purposes. For example, § 1.1275-6 describes the circumstances under which a debt instrument may be integrated with a derivative contract for the purpose of determining the amount and timing of the taxpayer's income, deduction, gain, or loss. Sections 1.148-4(h) (regarding arbitrage investment restrictions on tax-exempt bonds) and 1.988-5(a)

(regarding foreign currency transactions) also provide rules by which a debt instrument may be integrated with a derivative contract. Similarly, § 1.446-4 generally provides that the method of accounting used by a taxpayer for a derivative contract that qualifies as a hedging transaction must reasonably match the timing of income, deduction, gain, or loss from the hedging transaction with the timing of the income, deduction, gain, or loss from the item or items being hedged. The modification or termination of a derivative contract or debt instrument that is part of an integrated transaction or hedging transaction under one of the foregoing regulations may result in unfavorable tax consequences, such as accelerating the recognition of gain. The ARRC Letters recommend guidance providing that the modification of an integrated transaction or hedging transaction to incorporate the terms of an ARRC Fallback, an ISDA Fallback, or certain variants of an ARRC or ISDA Fallback described in section 4.02(3) of this revenue procedure does not result in legging out of the integrated transaction, terminating either leg of the hedging transaction, or otherwise severing the integration authorized or required by the foregoing regulations.

SECTION 3. DEFINITIONS

This section 3 defines certain terms for the purpose of this revenue procedure.

.01 ARRC Fallback.

(1) *In general.* An “ARRC Fallback” is contract language that is recommended by the ARRC and identified in any one of sections 3.01(2)(i) through (ix) of this revenue procedure.² An ARRC Fallback includes any option or variant provided in the contract language identified in sections 3.01(2)(i) through (ix) of this revenue procedure and excludes any option or variant not provided in the contract language identified in sections 3.01(2)(i) through (ix) of this revenue procedure, even if that option or variant is recommended elsewhere by the ARRC. As of October

9, 2020, the ARRC Fallbacks consist of recommended contract language for adjustable rate mortgages, bilateral business loans, floating rate notes, securitizations, syndicated loans, and variable-rate private student loans and are publicly available at <https://www.newyorkfed.org/arrc/fallbacks-contract-language>.

(2) *Identification of contract language.* The contract language contained in each of the following materials is identified in this section 3.01(2)—

(i) *Part II: Fallback Language for New Closed-End, Residential Adjustable Rate Mortgages* of the document entitled *ARRC Recommendations Regarding More Robust LIBOR Fallback Contract Language for New Closed-End, Residential Adjustable Mortgages*, dated November 15, 2019;

(ii) The section entitled “*Hardwired Approach*” *Fallback Language of Part II: Fallback Language for New Originations of LIBOR Bilateral Business Loans* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Originations of LIBOR Bilateral Business Loans*, dated May 30, 2019;

(iii) The section entitled *Hedged Loan Approach of Part II: Fallback Language for New Originations of LIBOR Bilateral Business Loans* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Originations of LIBOR Bilateral Business Loans*, dated May 30, 2019;

(iv) *Part II: Fallback Language for New Originations of LIBOR Bilateral Business Loans* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Originations of LIBOR Bilateral Business Loans*, dated August 27, 2020.

(v) *Part II: Fallback Language for New Issuances of LIBOR Floating Rate Notes* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Issuances of LIBOR Floating Rate Notes*, dated April 25, 2019;

²The ARRC Fallbacks do not include the amendment approach that the ARRC once recommended for bilateral business loans and syndicated loans. Rather than the more formulaic approach used by the ARRC in the ARRC Fallbacks, the fallback rate under the amendment approach is effectively determined by negotiation of the parties to the contract. As a result, the Treasury Department and the IRS have concluded that the addition and operation of the fallback provisions in the amendment approach should be evaluated under the standards provided in either the Proposed Regulations or, when published, the final regulations.

(vi) *Part II: Fallback Language for New Issuances of LIBOR Securitizations* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Issuances of LIBOR Securitizations*, dated May 31, 2019;

(vii) The section entitled “*Hardwired Approach*” *Fallback Language of Part II: Fallback Language for New Originations of LIBOR Syndicated Loans* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Originations of LIBOR Syndicated Loans*, dated April 25, 2019;

(viii) *Part II: Fallback Language for New Originations of LIBOR Syndicated Loans* of the document entitled *ARRC Recommendations Regarding More Robust Fallback Language for New Originations of LIBOR Syndicated Loans*, dated June 30, 2020; and

(ix) *Part II: Fallback Language for New Variable-Rate Private Student Loans* of the document entitled *ARRC Consultation Regarding More Robust LIBOR Fallback Contract Language for New Variable Rate Private Student Loans*, dated June 30, 2020.

.02 *ISDA Fallback*. An “ISDA Fallback” is the set of terms provided in any one of the sections numbered one through six in the version of the Attachment to the ISDA Protocol that is publicly available at <https://www.isda.org> as of October 9, 2020.

SECTION 4. SCOPE

.01 This revenue procedure applies to any contract with terms that reference an IBOR and that are modified as described in section 4.02 of this revenue procedure. For this purpose, a contract includes but is not limited to a derivative contract, a debt instrument, stock, an insurance contract, and a lease agreement.

.02 This revenue procedure applies to any of the following modifications—

(1) The contract is modified to incorporate an ISDA Fallback, regardless of whether that modification results from adherence to the ISDA Protocol or a bilateral agreement between the parties to the contract.

(2) The contract is modified to incorporate an ARRC Fallback.

(3) The contract is modified to incorporate the terms of either an ARRC Fallback or an ISDA Fallback with certain deviations, provided all deviations fall into one or more of the following categories—

(i) Deviations from the terms of an ARRC Fallback or an ISDA Fallback that are reasonably necessary to make the terms incorporated into the contract legally enforceable in a relevant jurisdiction or to satisfy legal requirements of that jurisdiction;

(ii) Deviations from the terms of an ISDA Fallback that are reasonably necessary to incorporate the ISDA Fallback into a contract that is not a Protocol Covered Document (as defined in the ISDA Protocol);

(iii) Deviations from the terms of an ARRC Fallback or an ISDA Fallback to omit terms of an ARRC Fallback or an ISDA Fallback that cannot under any circumstances affect the operation of the modified contract (for example, for a contract that refers only to USD LIBOR, omission of the portions of an ISDA Fallback that relate exclusively to contracts referring to another IBOR); or

(iv) Deviations from the terms of an ARRC Fallback or an ISDA Fallback to add, to revise, or to remove technical, administrative, or operational terms, provided that the addition, revision, or removal is reasonably necessary to adopt or to implement the ARRC Fallback or the ISDA Fallback. Examples of technical, administrative, or operational terms include the definition of interest period, the timing and frequency of determining rates, and the timing and frequency of making payments of interest. This section 4.02(3)(iv) does not apply to the addition of a term that obligates one party to make a one-time payment (or similar payments) as a substitute for any portion of an ARRC Fallback or an ISDA Fallback or as consideration for the modification.

SECTION 5. APPLICATION

.01 If a contract described in section 4.01 of this revenue procedure is modified as described in section 4.02 of this revenue procedure, that modification is not treated as the exchange of property for other property differing materially in kind or extent for purposes of § 1.1001-

1(a). For example, in the case of a debt instrument that is described in section 4.01 of this revenue procedure and that is modified as described in section 4.02 of this revenue procedure, the modification is not treated as a significant modification for purposes of § 1.1001-3, which provides rules for determining whether the modification results in an exchange of the original debt instrument for a modified debt instrument that differs materially either in kind or in extent for purposes of § 1.1001-1(a).

.02 If a contract described in section 4.01 of this revenue procedure is one leg of a transaction integrated under § 1.1275-6 or § 1.988-5(a), the modification of that contract as described in section 4.02 of this revenue procedure is not treated as legging out of the integrated transaction under § 1.1275-6 or § 1.988-5(a). If a contract described in section 4.01 of this revenue procedure is integrated under § 1.148-4(h), the modification of that contract as described in section 4.02 of this revenue procedure is not treated as terminating the qualified hedge under § 1.148-4(h). If a contract described in section 4.01 of this revenue procedure is part of a hedging transaction under § 1.446-4, the modification of that contract as described in section 4.02 of this revenue procedure is not treated as a disposition or termination of either leg of the transaction under § 1.446-4.

.03 If a contract described in section 4.01 of this revenue procedure is modified as described in section 4.02 of this revenue procedure (covered modification) and is contemporaneously modified in a manner not described in section 4.02 of this revenue procedure (noncovered modification), the regulations identified in sections 5.01 and 5.02 of this revenue procedure apply to the noncovered modifications without regard to the special rules provided in sections 5.01 and 5.02 of this revenue procedure. In addition, when applying each regulation identified in sections 5.01 and 5.02 of this revenue procedure, the covered modifications are treated as part of the terms of the contract prior to any modification that is not a covered modification. As a result, covered modifications are treated as part of the existing terms of the contract against which other contemporaneous, subsequent, or cumulative

modifications are tested under the regulations identified in sections 5.01 and 5.02 of this revenue procedure.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective for modifications to contracts occurring on or after October 9, 2020, and before January 1, 2023. A taxpayer, however, may rely on this revenue procedure for modifications to contracts occurring before October 9, 2020.

SECTION 7. ADDITIONAL GUIDANCE

In future guidance published in the Internal Revenue Bulletin, the Treasury Department and the IRS may provide additional relief as necessary to address developments in the transition away from IBORs. For example, if the ARRC modifies the contract language identified in section 3.01(2) of this revenue procedure or recommends similar contract language for inclusion in other cash products after October 9, 2020, the Treasury Department and the IRS will evaluate the ARRC's new or revised contract language and may supplement the definition of an ARRC Fallback accordingly. The Treasury Department and the IRS request comments on the list of deviations in section 4.02(3) of this revenue procedure, including the need for additional categories of deviation in that list. Comments should be submitted in writing on or before December 31, 2022, and should contain a reference to this Rev. Proc. 2020-44.

All comments will be available for public inspection and copying. Commenters are strongly suggested to submit comments electronically, as access to mail may be limited. Comments may be submitted in one of two ways:

(1) Electronically via the Federal eRulemaking Portal at <https://www.regulations.gov> (type "IRS-2020-0029" in the search field on the homepage to find this revenue procedure and submit comments); or

(2) Alternatively, by mail to Internal Revenue Service, CC:PA:LPD:PR (Rev. Proc. 2020-44), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

SECTION 8. DRAFTING INFORMATION

The principal author of this revenue procedure is Spence Hanemann of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue procedure contact Caitlin Holzem or Spence Hanemann at (202) 317-6842 (not a toll-free call).

Revenue Procedure 2020-46

SECTION 1. PURPOSE

This revenue procedure modifies and updates Rev. Proc. 2016-47, 2016-37 I.R.B. 346. Section 3.02(2) of Rev. Proc. 2016-47 provides a list of permissible reasons for self-certification of eligibility for a waiver of the 60-day rollover requirement. In response to requests from stakeholders, this revenue procedure modifies that list by adding a new reason: a distribution was made to a state unclaimed property fund. As under Rev. Proc. 2016-47, a self-certification relates only to the reasons for missing the 60-day deadline, not to whether a distribution is otherwise eligible to be rolled over. Section 3.04(1) of this revenue procedure provides examples of situations in which a distribution would not be eligible to be rolled over. The appendix sets forth model language that may be used for self-certification.

SECTION 2. BACKGROUND

.01 Sections 402(c)(3)(A) and 408(d)(3)(A) of the Internal Revenue Code provide that any amount distributed from a qualified plan or individual retirement arrangement (IRA) will be excluded from income if it is transferred to an eligible retirement plan no later than the 60th day following the day of receipt. A similar rule applies to § 403(a) annuity plans, § 403(b) tax sheltered annuities, and § 457 eligible governmental plans. See §§ 403(a)(4)(B), 403(b)(8)(B), and 457(e)(16)(B).

.02 Section 401(a)(31) requires that a plan qualified under § 401(a) provide for the direct transfer of eligible rollover distributions. A similar rule applies to § 403(a) annuity plans, § 403(b) tax-sheltered annuities, and § 457 eligible governmental plans. See §§ 403(a)(1), 403(b)(10), and 457(d)(1)(C). Section 1.401(a)(31)-1, Q&A-14, provides examples of situations in which a plan administrator may reasonably conclude that a contribution, whether made via a direct transfer or a 60-day rollover, is a valid rollover contribution to a § 401(a) or 403(a) plan. Several of the examples illustrate circumstances under which a plan administrator may rely on certain certifications and documentation that a rollover contribution that is not a direct transfer is being made no later than 60 days following receipt.

.03 An IRA trustee reports a rollover contribution received during a year on a Form 5498, *IRA Contribution Information*, for that year.

.04 Sections 402(c)(3)(B) and 408(d)(3)(I) provide that the Secretary may waive the 60-day rollover requirement "where the failure to waive such requirement would be against equity or good conscience, including casualty, disaster, or other events beyond the reasonable control of the individual subject to such requirement."

.05 Under §§ 7508 and 7508A, the time for making a rollover may be postponed in the event of service in a combat zone or in the case of a federally declared disaster or a terroristic or military action. See § 301.7508-1 and Rev. Proc. 2018-58, 2018-50 I.R.B. 990. Also, under § 402(c)(3)(C), the time for making a rollover of a qualified plan loan offset amount is postponed until the tax return due date (including extensions) for the taxable year in which the plan loan offset is treated as distributed.

.06 Rev. Proc. 2003-16, 2003-4 I.R.B. 359, establishes a letter-ruling procedure for taxpayers to apply to the Internal Revenue Service (IRS) for a waiver of the 60-day rollover requirement, under § 402(c)(3)(B) or 408(d)(3)(I). Section 3.03 of Rev. Proc. 2003-16 also provides for automatic approval for a waiver of the 60-day rollover requirement in certain circumstances in which a rollover is not

made timely due to an error on the part of a financial institution.

.07 Rev. Proc. 2016-47 provides guidance concerning waivers of the 60-day rollover requirement in §§ 402(c)(3) and 408(d)(3). Specifically, it provides for a self-certification procedure (subject to verification on audit) that may be used by a taxpayer claiming eligibility for a waiver under § 402(c)(3)(B) or 408(d)(3)(I) with respect to a rollover into a plan or IRA. It provides that a plan administrator, or an IRA trustee, custodian, or issuer (IRA trustee), may rely on the certification in accepting and reporting receipt of a rollover contribution. It also modifies Rev. Proc. 2003-16 by providing that the IRS may grant a waiver during an examination of the taxpayer's income tax return.

.08 Rev. Proc. 2020-4, 2020-1 I.R.B. 148, provides the procedures for issuing letter rulings on matters under the jurisdiction of the Commissioner, Tax Exempt and Government Entities Division.

SECTION 3. SELF-CERTIFICATION

.01 *Written self-certification.* A taxpayer may make a written certification to a plan administrator or an IRA trustee that a contribution satisfies the conditions in Section 3.02 of this revenue procedure. This self-certification has the effects described in Section 3.04 of this revenue procedure. Taxpayers may make the certification by using the model language in the appendix on a word-for-word basis or by using language that is substantially similar in all material respects. A copy of the certification should be kept in the taxpayer's files and be available if requested on audit.

.02 *Conditions for self-certification.*

(1) *No prior denial by the IRS.* The IRS must not have previously denied a waiver request with respect to a rollover of all or part of the distribution to which the contribution relates.

(2) *Reason for missing 60-day deadline.* The taxpayer must have missed the 60-day deadline because of the taxpayer's inability to complete a rollover due to one or more of the following reasons:

(a) an error was committed by the financial institution receiving the contribution or making the distribution to which the contribution relates;

(b) the distribution, having been made in the form of a check, was misplaced and never cashed;

(c) the distribution was deposited into and remained in an account that the taxpayer mistakenly thought was an eligible retirement plan;

(d) the taxpayer's principal residence was severely damaged;

(e) a member of the taxpayer's family died;

(f) the taxpayer or a member of the taxpayer's family was seriously ill;

(g) the taxpayer was incarcerated;

(h) restrictions were imposed by a foreign country;

(i) a postal error occurred;

(j) the distribution was made on account of a levy under § 6331 and the proceeds of the levy have been returned to the taxpayer;

(k) the party making the distribution to which the rollover relates delayed providing information that the receiving plan or IRA required to complete the rollover despite the taxpayer's reasonable efforts to obtain the information; or

(l) the distribution was made to a state unclaimed property fund.

(3) *Contribution as soon as practicable; 30-day safe harbor.* The contribution must be made to the plan or IRA as soon as practicable after the reason or reasons listed in the preceding paragraph no longer prevent the taxpayer from rolling over the amount distributed (which includes any amount withheld for income tax) or a lesser amount if the taxpayer wants to roll over less than the total amount distributed or if part of the amount distributed is ineligible for rollover. This requirement is deemed to be satisfied if the contribution is made within 30 days after the reason or reasons no longer prevent the taxpayer from making the contribution.

.03 *Reporting on Form 5498.* An IRA trustee that accepts a rollover contribution after the 60-day deadline reports on Form 5498 that the contribution was accepted after the 60-day deadline.

.04 *Effect of self-certification.*

(1) *Only for 60-day deadline.* A self-certification under this revenue procedure applies only for purposes of a waiver of the 60-day requirement for a valid rollover; it does not apply for purposes of any other requirement for a valid rollover. For example,

a taxpayer may not roll over a distribution if it is a required minimum distribution or if the taxpayer is a nonspouse beneficiary. In addition, in the case of a distribution from an IRA, (i) a rollover to another IRA is not permitted if the taxpayer has made an IRA rollover of another IRA distribution made in the prior 1-year period, and (ii) any rollover must consist of the same property distributed (for example, if shares of a company are distributed from an IRA, some or all of the shares may be rolled over, but no proceeds from the sale of those shares can be rolled over). The one-rollover-per-year limitation described in the preceding sentence does not apply to trustee-to-trustee transfers or to conversions (that is, rollovers from traditional IRAs to Roth IRAs). See IRS Publication 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*.

(2) *Effect on plan administrator or IRA trustee.* For purposes of accepting and reporting a rollover contribution into a plan or IRA, a plan administrator or IRA trustee may rely on a taxpayer's self-certification described in this Section 3 in determining whether the taxpayer has satisfied the conditions for a waiver of the 60-day rollover requirement under § 402(c)(3)(B) or 408(d)(3)(I). However, a plan administrator or an IRA trustee may not rely on the self-certification for other purposes or if the plan administrator or IRA trustee has actual knowledge that is contrary to the self-certification.

(3) *Effect on taxpayer.* A self-certification is not a waiver by the IRS of the 60-day rollover requirement. However, a taxpayer may report the contribution as a valid rollover unless later informed otherwise by the IRS. The IRS, in the course of an examination, may consider whether a taxpayer's contribution meets the requirements for a waiver. For example, the IRS may determine that the requirements for a waiver were not met because of a material misstatement in the self-certification, the reason or reasons claimed by the taxpayer for missing the 60-day deadline did not prevent the taxpayer from completing the rollover within 60 days following receipt, or the taxpayer failed to make the contribution as soon as practicable after the reason or reasons no longer prevented the taxpayer from making the contribution. In such a case, the taxpayer may be subject to income and excise taxes, interest, and penalties, such as the penalty for failure

to pay the proper amount of tax under § 6651.

SECTION 4. ADDITIONAL WAIVERS DURING EXAM

In addition to automatic waivers and waivers through application to the IRS under Section 3 of Rev. Proc. 2003-16, the IRS, in the course of examining a taxpayer's individual income tax return, may determine that the taxpayer qualifies for a waiver of the 60-day rollover requirement under § 402(c)(3)(B) or 408(d)(3)(I).

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective on October 16, 2020.

SECTION 6. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 2016-47 is modified and superseded by this revenue procedure, and

Rev. Proc. 2003-16 is modified by Section 4 of this revenue procedure.

SECTION 7. PAPERWORK REDUCTION ACT

The collections of information contained in this revenue procedure have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-2269.

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

The collections of information in this revenue procedure are in Section 3.01. The collection of information relates to a certification by taxpayers wanting a waiver of the 60-day requirement for rollovers of distributions from plans or IRAs. The

collections of information are required to obtain a benefit.

The likely recordkeepers are individuals. Estimates of the annualized cost to respondents are not relevant, because each collection of information in this revenue procedure is a one-time collection.

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 tax return information are confidential, as required by § 6103.

DRAFTING INFORMATION

The principal author of this revenue procedure is Angelique Carrington of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). For further information regarding this revenue procedure, contact Ms. Carrington at (202) 317-4148 (not a toll-free number).

Appendix

Certification for Late Rollover Contribution

Name _____
Address _____
City, State, ZIP Code _____
Date: _____

Plan Administrator/Financial Institution
Address _____
City, State, ZIP Code _____

Dear Sir or Madam:

Pursuant to Internal Revenue Service (IRS) Revenue Procedure 2020-46, I certify that my contribution of \$ [ENTER AMOUNT] missed the 60-day rollover deadline for the reason(s) listed below under Reasons for Late Contribution. I am making this contribution as soon as practicable after the reason or reasons listed below no longer prevent me from making the contribution. I understand that this certification concerns only the 60-day requirement for a rollover and that, to complete the rollover, I must comply with all other tax law requirements for a valid rollover and with your rollover procedures.

Pursuant to Revenue Procedure 2020-46, unless you have actual knowledge to the contrary, you may rely on this certification to show that I have satisfied the conditions for a waiver of the 60-day rollover requirement for the amount identified above. You may not rely on this certification in determining whether the contribution satisfies other requirements for a valid rollover.

Reasons for Late Contribution

I missed the 60-day rollover deadline for the following reason(s) (check all that apply):

- ☐ An error was committed by the financial institution making the distribution or receiving the contribution.
- ☐ The distribution was in the form of a check and the check was misplaced and never cashed.
- ☐ The distribution was deposited into and remained in an account that I mistakenly thought was a retirement plan or IRA.
- ☐ My principal residence was severely damaged.
- ☐ One of my family members died.
- ☐ I or one of my family members was seriously ill.
- ☐ I was incarcerated.
- ☐ Restrictions were imposed by a foreign country.
- ☐ A postal error occurred.
- ☐ The distribution was made on account of an IRS levy and the proceeds of the levy have been returned to me.
- ☐ The party making the distribution delayed providing information that the receiving plan or IRA required to complete the rollover despite my reasonable efforts to obtain the information.
- ☐ The distribution was made to a state unclaimed property fund.

Signature

I declare that the representations made in this certification are true and that the IRS has not previously denied a request for a waiver of the 60-day rollover requirement with respect to a rollover of all or part of the distribution to which this contribution relates. I understand that in the event I am audited and the IRS does not grant a waiver for this contribution, I may be subject to income and excise taxes, interest, and penalties. If the contribution is made to an IRA, I understand you will report the contribution to the IRS. I also understand that I should retain a copy of this signed certification with my tax records.

Signature: _____

Part IV

Announcement Regarding the Effective Date of Termination of the United States-Hong Kong Shipping Agreement

Announcement 2020-40

In August 1989, the United States and Hong Kong concluded, through an exchange of diplomatic notes, an agreement to exempt from income tax, on a reciprocal basis, income from the international operation of ships (herein referred to as the “shipping agreement”), TIAS 11892.

The shipping agreement entered into force on August 16, 1989, and took effect for taxable years on or after January 1, 1987. Paragraph 8 of the shipping agreement provides that either government may terminate the agreement by giving written notice of termination.

On July 14, 2020, the President issued an Executive Order on Hong Kong Normalization, which, among other things, directed the heads of agencies to commence all appropriate actions to further the purposes of the order, including to give Hong Kong notice of intent to terminate the shipping agreement. See E.O. 13936 available at <https://www.whitehouse.gov/presidential-actions/presi->

[dents-executive-order-hong-kong-normalization/](#). The United States, through its Consulate General in Hong Kong, provided a written notification dated August 18, 2020 to the Government of the Hong Kong Special Administrative Region of its termination of the shipping agreement. The Department of the Treasury and the Internal Revenue Service announce that the termination shall take effect on January 1, 2021, and shall have effect for taxable years beginning on or after that date.

For further information regarding this announcement contact the Office of Associate Chief Counsel (International) at (202) 317-3800 (not a toll-free number).

Definition of Terms

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

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

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

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

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the

new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

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

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

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the

new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

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

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

Abbreviations

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

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.

ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
FR—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.

PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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¹ A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2019–27 through 2019–52 is in Internal Revenue Bulletin 2019–52, dated December 27, 2019.

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