column of page 65824, states: ''Only AUSs developed, operated, owned, or used by FHA-approved Direct Endorsement mortgages, Fannie Mae, or Freddie Mac will be able to access the scorecard, and only FHA-approved mortgagees will be able to obtain risk assessments using the TOTAL Mortgage Scorecard.'' The reference in this sentence to ''Direct Endorsement mortgages'' should have read ''Direct Endorsement mortgagees'' instead. A conforming change removing ''FHA-approved'' as a modifier of ''automatic underwriting systems (AUSs)'' and changing ''Direct Endorsement mortgages'' to ''Direct Endorsement mortgagees'' is also made to the regulation, at § 203.255(b)(5)(i)(A).

■ Accordingly, FR Doc. 03–29055, FHA TOTAL Mortgage Scorecard, (FR–4835–I–01), published in the **Federal Register** on November 21, 2003 (68 FR 65824), is corrected as follows:

■ 1. On page 65824, third column, the fourth complete sentence under the heading, ''II. This Interim Rule,'' is revised to read as follows: ''Only AUSs developed, operated, owned, or used by FHA-approved Direct Endorsement mortgagees, Fannie Mae, or Freddie Mac will be able to access the scorecard, and only FHA-approved mortgagees will be able to obtain risk assessments using the TOTAL Mortgage Scorecard.''

■ 2. On page 65827, second column, § 203.255(b)(5)(i)(A) is revised to read as follows:

§ 203.255 Insurance of mortgage.

* * * * *

(b) * * *

(5) * * *

(i) * * *

(A) *Permissible users.* Only automatic underwriting systems (AUSs) developed, operated, owned, or used by FHA-approved Direct Endorsement mortgagees, Fannie Mae, or Freddie Mac, may access TOTAL, and only FHA-approved mortgagees will be able to obtain risk-assessments using TOTAL;

* * * * *

Dated: December 23, 2003.

Aaron Santa Anna,

Assistant, General Counsel for Regulations.

[FR Doc. 03–32021 Filed 12–31–03; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9105]

RIN 1545–BC17

Changes in Computing Depreciation

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains regulations relating to a change in computing depreciation or amortization as well as a change from a nondepreciable or nonamortizable asset to a depreciable or amortizable asset (or vice versa). Specifically, these regulations provide guidance to any taxpayer that makes a change in depreciation or amortization on whether such change is a change in method of accounting under section 446(e) of the Internal Revenue Code and on the application of section 1016(a)(2) in determining whether the change is a change in method of accounting. The text of these temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section in this issue of the **Federal Register**.

DATES: *Effective Dates:* These regulations are effective January 2, 2004.

Applicability Dates: For dates of applicability, *see* §§ 1.167(e)–1T(e), 1.446(e)–1T(e)(4), and 1.1016–3T(j).

FOR FURTHER INFORMATION CONTACT: Sara Logan or Douglas Kim, (202) 622–3110 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 to provide regulations under sections 167, 446(e), and 1016(a)(2) of the Internal Revenue Code (Code). These regulations provide the changes in depreciation or amortization that are, and are not, a change in method of accounting under § 1.446–1(e). Additionally, these regulations amend § 1.167(e)–1 to provide that certain changes in depreciation method for property for which depreciation is determined only under section 167 are made without the consent of the Commissioner of Internal Revenue, and amend § 1.1016–3 to provide that section 1016(a)(2) does not permanently affect a taxpayer's lifetime income for purposes of determining whether a change in depreciation or amortization is a change in method of accounting.

Explanation of Provisions

Background

Section 446 provides in general that taxable income shall be computed under the method of accounting on the basis of which the taxpayer regularly computes the taxpayer's income in keeping the taxpayer's books. Section 446(e) provides that, except as otherwise expressly provided in chapter 1 of the Code, a taxpayer who changes the method of accounting on the basis of which the taxpayer regularly computes the taxpayer's income in keeping the taxpayer's books shall, before computing the taxpayer's taxable income under the new method, secure the consent of the Secretary.

Section 1.446–1(e)(2)(ii)(a) provides in pertinent part that a change in method of accounting includes a change in the overall plan of accounting for gross income or deductions or a change in the treatment of any material item used in such overall plan. A material item is any item that involves the proper time for the inclusion of the item in income or the taking of a deduction. However, § 1.446–1(e)(2)(ii)(*b*) provides in pertinent part that a change in method of accounting does not include an adjustment in the useful life of a depreciable asset. Although such adjustment may involve the question of the proper time for the taking of a deduction, such item is traditionally corrected by adjustments in the current and future years.

Section 1.167(e)–1(a) provides that in general, any change in the method of computing the depreciation allowances with respect to a particular account (other than a change in method permitted or required by reason of the operation of former section 167(j)(2) and § 1.167(j)–3(c)) is a change in method of accounting, and such a change will be permitted only with the consent of the Commissioner, except that certain changes to the straight line method of depreciation will be permitted without consent as provided in former section 167(e)(1), (2), and (3). Any request for a change in method of depreciation shall be made in accordance with section 446 and the regulations under section 446.

In 1996, the IRS issued Rev. Proc. 96–31 (1996–1 C.B. 714), providing that a change from not claiming the depreciation or amortization allowable to claiming the depreciation or amortization allowable is a change in method of accounting for which the consent of the Commissioner of Internal Revenue is required.

In *Kurzet* v. *Commissioner,* 222 F.2d 830, 842–845 (10th Cir. 2000), the taxpayer sought to change the classification of property under section 168 from nonresidential real property to 15-year property thereby resulting in a change in recovery period from 31.5 years to 15 years. The Tenth Circuit held that a change in recovery period under section 168 is a change in method of accounting under section 446(e). In reaching its holding, the Tenth Circuit considered the taxpayer's argument that a change in recovery period is analogous to a change in useful life, but concluded that the Commissioner's interpretation of § 1.446–1(e)(2)(ii) in Rev. Proc. 96–31 as requiring a taxpayer to obtain permission for a change in recovery period is not plainly erroneous or inconsistent with § 1.446–1(e)(2)(ii).

In *Brookshire Brothers Holding, Inc. & Subsidiaries* v. *Commissioner,* 320 F.3d 507 (5th Cir. 2003), *aff'g.* T.C. Memo. 2001–150, *reh'g en banc denied,* 65 Fed. Appx. 511 (5th Cir. 2003), the Fifth Circuit held that a change in classification of property under section 168 is not a change in method of accounting under section 446(e) because the change is the functional equivalent of a change in useful life thereby resulting in the change falling under the useful life exception in § 1.446–1(e)(2)(ii)(*b*). The Eighth Circuit in *O'Shaughnessy* v. *Commissioner,* 332 F.3d 1125 (8th Cir. 2003), *rev'g in part* 2002–1 U.S.T.C. (CCH) ¶ 50,235 (D. Minn. 2001), adopted the analysis in *Brookshire* and held that a change in classification of property under section 168 falls within the useful life exception and, thus, does not constitute a change in method of accounting under section 446(e).

Further, in *Green Forest Manufacturing Inc.* v. *Commissioner,* T.C.Memo. 2003–75, the Tax Court extended its reasoning in *Brookshire.* The court held that a change in computing depreciation from the general depreciation system in section 168(a) to the alternative depreciation system in section 168(g) is a change in classification that falls within the useful life exception and, therefore, is not a change in method of accounting.

As a result of these decisions, there is inconsistent treatment of taxpayers with respect to whether a change in computing depreciation under section 168 is a change in method of accounting under section 446(e). These regulations clarify the changes in depreciation or amortization (depreciation) that are (and are not) changes in method of accounting under section 446(e).

Scope

The regulations provide the changes in depreciation for property for which depreciation is determined under section 167, 168, 197, 1400I, 1400L(b), or 1400L(c), or former section 168, of the Code that are (and are not) changes in method of accounting under section 446(e). The regulations also clarify that the rules in § 1.167(e)–1 with respect to a change in the depreciation method made without the consent of the Commissioner apply only to property for which depreciation is determined under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168).

Changes in Depreciation That Are Changes in Method of Accounting

In general, the regulations provide that a change in the depreciation method, period of recovery, or convention of a depreciable or amortizable asset is a change in method of accounting. This change may be the result of, for example, a change in the classification of property under section 168(e) or a change in computing depreciation from the general depreciation system under section 168(a) to the alternative depreciation system of section 168(g). Further, a change to or from claiming the additional first year depreciation deduction provided by section 168(k) or 1400L(b) is a change in method of accounting under certain circumstances.

The regulations clarify that the useful life exception, which has been moved from § 1.446–1(e)(2)(ii)(*b*) to § 1.446–1T(e)(2)(ii)(*d*), applies only to property for which the depreciation is determined under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168). However, a change to or from a useful life (or recovery period or amortization period) that is specifically assigned by the Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin is a change in method of accounting.

The regulations also provide that a change in salvage value to zero for a depreciable or amortizable asset for which the salvage value is expressly treated as zero by the Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin, is treated as a change in method of accounting. Any other change in salvage value is not treated as a change in method of accounting.

Further, the regulations provide that a change in the accounting for depreciable or amortizable assets from single asset accounting to multiple asset accounting (pooling), or vice versa, or from one type of multiple asset accounting (pooling) to a different type of multiple asset accounting (pooling) is a change in method of accounting. Also, for depreciable or amortizable assets that are mass assets accounted for in multiple asset accounts or pools, a change in the method of identifying which assets have been disposed is a change in method of accounting (for example, from specific identification to a first-in, first-out method).

Finally, the regulations provide that a change in the treatment of an asset from nondepreciable or nonamortizable (nondepreciable) to depreciable or amortizable (depreciable), or vice versa, is a change in method of accounting. For example, a change in the treatment of an asset that was used entirely in the taxpayer's trade or business and was never held for sale from being treated as inventory to being treated as depreciable property is a change in method of accounting.

Exceptions

The regulations provide that a change in computing depreciation allowances in the taxable year in which the use of property changes in the hands of the same taxpayer is not a change in method of accounting.

The regulations also provide that the making of a late depreciation election or the revocation of a timely valid depreciation election generally is not a change in method of accounting. This rule also applies to the making of a late election or the revocation of a timely valid election under section 13261(g)(2) or (3) of the Revenue Reconciliation Act of 1993 (107 Stat. 312, 540) (relating to amortizable section 197 intangibles). To make a late depreciation election or to revoke a timely valid depreciation election, a taxpayer must submit a request for a private letter ruling. Elections made under section 168(b)(2)(C), 168(b)(3)(D), or 168(g)(7) are irrevocable.

Finally, the regulations provide that any change in the placed-in-service date of a depreciable or amortizable asset is not treated as a change in method of accounting.

Item Being Changed

The regulations clarify that for purposes of changes in depreciation, the item being changed is the depreciation treatment of each individual depreciable or amortizable asset. However, the item is the depreciation treatment of each vintage account with respect to depreciable assets for which depreciation is determined under § 1.167(a)–11 (CLADR property).

Further, a change in computing depreciation under section 167 (other than a change under section 168, section 1400I, section 1400L, or former section 168) is permitted only with respect to all assets in a particular account (as defined in § 1.167(a)–7) or vintage account.

Special Rules

The regulations also provide rules for the following: (1) A change from a declining balance method under section 168(b)(1) or (2) to the straight line method; (2) changes in certain depreciation methods under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168); and (3) section 481 adjustments.

With respect to a change from the 200-percent or 150-percent declining balance method under section 168(b)(1) or (2) to the straight line method, the regulations provide that this change may be made without the consent of the Commissioner in the first taxable year in which the depreciation allowance under the straight line method is greater than the depreciation allowance under the declining balance method.

With respect to changes in depreciation methods under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168), the regulations provide cross-references to regulations under section 167 that allow certain depreciation method changes to be made without the consent of the Commissioner.

With respect to section 481 adjustments, the regulations also clarify that except as otherwise expressly provided by the Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin, a change from one permissible method of computing depreciation to another permissible method of computing depreciation for a depreciable or amortizable asset is implemented on either a cut-off method (as described in section 2.06 of Rev. Proc. 97–27 (1997–1 C.B. 680) and in section 2.06 of Rev. Proc. 2002–9 (2002–1 C.B. 327)) or a modified cut-off method (under which the adjusted depreciable basis of the asset as of the beginning of the year of change is recovered using the new permissible method of accounting). Because no items are duplicated or omitted from income when the cut-off method or the modified cut-off method is used to effect the change in method of accounting, no section 481 adjustment is required or permitted. However, a change from an impermissible method of computing depreciation to a permissible method of computing depreciation results in a negative or positive section 481 adjustment because the adjusted depreciable basis of the asset as of the beginning of the year of change is changed as a result of the change in computing depreciation. Similarly, a change in the treatment of an asset from nondepreciable to depreciable (or vice versa) or a change from expensing to depreciating an asset (or vice versa) will also result in a negative or positive section 481 adjustment.

Application of the Allowed or Allowable Rule to Changes in Method of Accounting

Section 1016(a)(2) provides that the basis of property is adjusted in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent of the amount allowed as deductions in computing taxable income and resulting in a reduction for any taxable year of the taxpayer's taxes, but not less than the amount allowable.

Concurrently with the issuance of these regulations, the IRS and Treasury Department will issue a revenue procedure that will allow a taxpayer to change the taxpayer's method of determining depreciation for a depreciable or amortizable asset after its disposition if the taxpayer did not take into account any depreciation allowance, or did take into account some depreciation but less than the depreciation allowable, for the asset in computing taxable income in the year of disposition or in prior taxable years. Because the taxpayer is permitted to claim the allowable depreciation not taken into account for this asset, the taxpayer's lifetime income is not permanently affected by the ''allowed or allowable'' rule under section 1016(a)(2). Accordingly, the regulations provide that section 1016(a)(2) does not permanently affect a taxpayer's lifetime income for purposes of determining whether a change in depreciation is a change in method of accounting under section 446(e) and the regulations under section 446(e).

The revenue procedure also will revise the depreciation changes included in Rev. Proc. 2002–9 (2002–1 C.B. 327), the automatic change in method of accounting revenue procedure, to conform with these regulations and will waive the application of Rev. Rul. 90–38 (1990–1 C.B. 57) for changes in depreciation made under Rev. Proc. 97–27 (1997–1 C.B. 680) or Rev. Proc. 2002–9.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. For the applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), refer to the Special Analyses section of the preamble to the cross-reference notice of proposed rulemaking published in the **Federal Register**. Pursuant to section 7805(f) of the Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Sara Logan, Office of Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Amendments to the Regulations

■ Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

■ **Par. 2.** Section 1.167(e)–1 is amended by:

■ 1. Revising paragraph (a).

■ 2. Adding new paragraph (e).

The addition and revision read as follows:

§ 1.167(e)–1 Change in method.

(a) *In general.* [Reserved]. For further guidance, see § 1.167(e)–1T(a).

* * * * *

(e) *Effective date.* [Reserved]. For further guidance, see the first two sentences of § 1.167(e)–1T(e).

■ **Par. 3.** Section 1.167(e)–1T is added to read as follows:

§ 1.167(e)–1T Change in method (temporary).

(a) *In general.* (1) Any change in the method of computing the depreciation allowances with respect to a particular account (other than a change in method

permitted or required by reason of the operation of former section 167(j)(2) and § 1.167(j)–3(c)) is a change in method of accounting, and such a change will be permitted only with the consent of the Commissioner, except that certain changes to the straight line method of depreciation will be permitted without consent as provided in former section 167(e)(1), (2), and (3). Except as provided in paragraphs (c) and (d) of this section, a change in method of computing depreciation will be permitted only with respect to all the assets contained in a particular account as defined in § 1.167(a)–7. Any change in the percentage of the current straight line rate under the declining balance method, for example, from 200 percent of the straight line rate to any other percent of the straight line rate, or any change in the interest factor used in connection with a compound interest or sinking fund method, will constitute a change in method of depreciation. Any request for a change in method of depreciation shall be made in accordance with section 446(e) and the regulations under section 446(e). For rules covering the use of depreciation methods by acquiring corporations in the case of certain corporate acquisitions, see section 381(c)(6) and the regulations under section 381(c)(6).

(2) Paragraphs (b), (c), and (d) of this section apply to property for which depreciation is determined under section 167 (other than under section 168, section 1400I, section 1400L, or under section 168 prior to its amendment by the Tax Reform Act of 1986 (100 Stat. 2121)) of the Internal Revenue Code.

(b) through (d) [Reserved]. For further guidance, see § 1.167(e)–1(b) through (d).

(e) *Effective date.* This section applies on or after December 30, 2003. For the applicability of regulations before December 30, 2003, see § 1.167(e)–1 in effect prior to December 30, 2003 (§ 1.167(e)–1 as contained in 26 CFR part 1 edition revised as of April 1, 2003). The applicability of this section expires on or before January 2, 2007.

■ **Par. 4.** Section 1.446–1 is amended by:

■ 1. Revising paragraphs (e)(2)(ii)(*a*), (e)(2)(ii)(*b*), and (e)(2)(iii).

■ 2. Adding new paragraphs (e)(2)(ii)(*d*) and (e)(4).

The additions and revisions read as follows:

§ 1.446–1 General rule for methods of accounting.

* * * * *

(e) * * *

(2) * * *

(ii) (*a*) [Reserved]. For further guidance, see § 1.446–1T(e)(2)(ii)(*a*).

(*b*) [Reserved]. For further guidance, see § 1.446–1T(e)(2)(ii)(*b*).

* * * * *

(*d*) *Changes involving depreciable or amortizable assets.* [Reserved]. For further guidance, see § 1.446–1T(e)(2)(ii)(*d*).

(iii) *Examples.* [Reserved]. For further guidance, see § 1.446–1T(e)(2)(iii).

* * * * *

(4) *Effective date.* [Reserved]. For further guidance, see § 1.446(e)–1T(e)(4)(i) and (ii).

■ **Par. 5.** Section 1.446–1T is added to read as follows:

§ 1.446–1T General rule for methods of accounting (temporary).

(a) through (e)(2)(i) [Reserved]. For further guidance, see § 1.446–1(a) through (e)(2)(i).

(e)(2)(ii)(*a*) A change in the method of accounting includes a change in the overall plan of accounting for gross income or deductions or a change in the treatment of any material item used in such overall plan. Although a method of accounting may exist under this definition without the necessity of a pattern of consistent treatment of an item, in most instances a method of accounting is not established for an item without such consistent treatment. A material item is any item that involves the proper time for the inclusion of the item in income or the taking of a deduction. Changes in method of accounting include a change from the cash receipts and disbursement method to an accrual method, or vice versa, a change involving the method or basis used in the valuation of inventories (see sections 471 and 472 and the regulations under sections 471 and 472), a change from the cash or accrual method to a long-term contract method, or vice versa (see § 1.460–4), certain changes in computing depreciation or amortization (see paragraph (e)(2)(ii)(*d*) of this section), a change involving the adoption, use or discontinuance of any other specialized method of computing taxable income, such as the crop method, and a change where the Internal Revenue Code and regulations under the Code specifically require that the consent of the Commissioner must be obtained before adopting such a change.

(*b*) A change in method of accounting does not include correction of mathematical or posting errors, or errors in the computation of tax liability (such as errors in computation of the foreign tax credit, net operating loss, percentage depletion, or investment credit). Also, a change in method of accounting does not include adjustment of any item of income or deduction that does not involve the proper time for the inclusion of the item of income or the taking of a deduction. For example, corrections of items that are deducted as interest or salary, but that are in fact payments of dividends, and of items that are deducted as business expenses, but which are in fact personal expenses, are not changes in method of accounting. In addition, a change in the method of accounting does not include an adjustment with respect to the addition to a reserve for bad debts. Although such adjustment may involve the question of the proper time for the taking of a deduction, such items are traditionally corrected by adjustment in the current and future years. For the treatment of the adjustment of the addition to a bad debt reserve (for example, for banks under section 585 of the Internal Revenue Code), *see* the regulations under section 166 of the Internal Revenue Code. A change in the method of accounting also does not include a change in treatment resulting from a change in underlying facts. For further guidance on changes involving depreciable or amortizable assets, see paragraph (e)(2)(ii)(*d*) of this section and § 1.1016–3T(h).

(*c*) [Reserved]. For further guidance, *see* § 1.446–1(e)(2)(ii)(*c*).

(*d*) *Changes involving depreciable or amortizable assets*—(*1*) *Scope.* This paragraph (e)(2)(ii)(*d*) applies to property subject to section 167, 168, 197, 1400I, 1400L(b), or 1400L(c), or to section 168 prior to its amendment by the Tax Reform Act of 1986 (100 Stat. 2121) (former section 168).

(*2*) *Changes in depreciation or amortization that are a change in method of accounting.* Except as provided in paragraph (e)(2)(ii)(*d*)(*3*) of this section, a change in the treatment of an asset from nondepreciable or nonamortizable to depreciable or amortizable, or vice versa, is a change in method of accounting. Additionally, a correction to require depreciation or amortization in lieu of a deduction for the cost of depreciable or amortizable assets that had been consistently treated as an expense in the year of purchase, or vice versa, is a change in method of accounting. Further, except as provided in paragraph (e)(2)(ii)(*d*)(*3*) of this section, the following changes in computing depreciation or amortization are a change in method of accounting:

(*i*) A change in the depreciation or amortization method, period of recovery, or convention of a depreciable or amortizable asset.

(*ii*) A change from not claiming to claiming the additional first year depreciation deduction provided by section 168(k) or 1400L(b) for, and the resulting change to the amount otherwise allowable as a depreciation deduction for the remaining adjusted depreciable basis (or similar basis) of, qualified property, 50-percent bonus depreciation property, or qualified New York Liberty Zone property, provided the taxpayer did not make the election out of the additional first year depreciation deduction (or did not make a deemed election out of the additional first year depreciation deduction; for further guidance, *see* Rev. Proc. 2002–33 (2002–1 C.B. 963), Rev. Proc. 2003–50 (2003–29 I.R.B. 119), and § 601.601(d)(2)(ii)(*b*) of this chapter) for the class of property in which the qualified property, the 50-percent bonus depreciation property, or the qualified New York Liberty Zone property is included.

(*iii*) A change from claiming the 30-percent additional first year depreciation deduction to claiming the 50-percent additional first year depreciation deduction for 50-percent bonus depreciation property (provided the property is not included in any class of property for which the taxpayer elected the 30-percent, instead of the 50-percent, additional first year depreciation deduction) or a change from claiming the 50-percent additional first year depreciation deduction to claiming the 30-percent additional first year depreciation deduction for qualified property (including property that is included in a class of property for which the taxpayer elected the 30-percent, instead of the 50-percent, additional first year depreciation deduction) or qualified New York Liberty Zone property, and the resulting change to the amount otherwise allowable as a depreciation deduction for the property's remaining adjusted depreciable basis (or similar basis). This paragraph (e)(2)(ii)(*d*)(*2*)(*iii*) does not apply if a taxpayer is making a late election or revoking a timely valid election under section 168(k) or 1400L(b) (see paragraph (e)(2)(ii)(*d*)(*3*)(*iii*) of this section).

(*iv*) A change from claiming to not claiming the additional first year depreciation deduction for an asset that is not qualified property, 50-percent bonus depreciation property, or qualified New York Liberty Zone property, and the resulting change to the amount otherwise allowable as a depreciation deduction for the property's depreciable basis.

(*v*) A change in salvage value to zero for a depreciable or amortizable asset for which the salvage value is expressly treated as zero by the Internal Revenue Code (for example, section 168(b)(4)), the regulations under the Code (for example, § 1.197–2(f)(1)(ii)), or other guidance published in the Internal Revenue Bulletin.

(*vi*) A change in the accounting for depreciable or amortizable assets from a single asset account to a multiple asset account (pooling), or vice versa, or from one type of multiple asset account (pooling) to a different type of multiple asset account (pooling).

(*vii*) For depreciable or amortizable assets that are mass assets accounted for in multiple asset accounts or pools, a change in the method of identifying which assets have been disposed. For purposes of this paragraph (e)(2)(ii)(*d*)(*2*)(*vii*), the term *mass assets* means a mass or group of individual items of depreciable or amortizable assets that are not necessarily homogeneous, each of which is minor in value relative to the total value of the mass or group, numerous in quantity, usually accounted for only on a total dollar or quantity basis, with respect to which separate identification is impracticable, and placed in service in the same taxable year.

(*viii*) Any other change in depreciation or amortization as the Secretary may designate by publication in the **Federal Register** or in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter).

(*3*) *Changes in depreciation or amortization that are not a change in method of accounting*—(*i*) *Useful life.* An adjustment in the useful life of a depreciable or amortizable asset for which depreciation is determined under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168) is not a change in method of accounting. This adjustment in useful life is corrected by adjustments in the taxable year in which the conditions known to exist at the end of that taxable year changed thereby resulting in a redetermination of the useful life under § 1.167(a)–1(b) (or if the period of limitation for assessment under section 6501(a) has expired for that taxable year, in the first succeeding taxable year open under the period of limitation for assessment), and in subsequent taxable years. In other situations, the adjustment in useful life may be corrected by adjustments in the earliest taxable year open under the period of limitation for assessment under section 6501(a) or the earliest taxable year under examination by the Internal Revenue Service (IRS) but in no event earlier than the placed-in-service year of the asset, and in subsequent taxable years. However, if a taxpayer initiates the correction in useful life, in lieu of filing amended Federal tax returns (for example, because the conditions known to exist at the end of a prior taxable year changed thereby resulting in a redetermination of the useful life under § 1.167(a)–1(b)), the taxpayer may correct the adjustment in useful life by adjustments in the current and subsequent taxable years. This paragraph (e)(2)(ii)(*d*)(*3*)(*i*) does not apply if a taxpayer is changing to or from a useful life (or recovery period or amortization period) that is specifically assigned by the Internal Revenue Code (for example, section 167(f)(1), section 168(c), section 197), the regulations under the Code, or other guidance published in the Internal Revenue Bulletin and, therefore, such change is a change in method of accounting (unless paragraph (e)(2)(ii)(*d*)(*3*)(*v*) of this section applies).

(*ii*) *Change in use.* A change in computing depreciation or amortization allowances in the taxable year in which the use of an asset changes in the hands of the same taxpayer is not a change in method of accounting.

(*iii*) *Elections.* Generally, the making of a late depreciation or amortization election or the revocation of a timely valid depreciation or amortization election is not a change in method of accounting, except as otherwise expressly provided by the Internal Revenue Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin. This paragraph (e)(2)(ii)(*d*)(*3*)(*iii*) also applies to making a late election or revoking a timely valid election made under section 13261(g)(2) or (3) of the Revenue Reconciliation Act of 1993 (107 Stat. 312, 540) (relating to amortizable section 197 intangibles). A taxpayer may request consent to make a late election or revoke a timely valid election by submitting a request for a private letter ruling.

(*iv*) *Salvage value.* Except as provided under paragraph (e)(2)(ii)(*d*)(*2*)(*v*) of this section, a change in salvage value of a depreciable or amortizable asset is not treated as a change in method of accounting.

(*v*) *Placed-in-service date.* Any change in the placed-in-service date of a depreciable or amortizable asset is not treated as a change in method of accounting. The change in placed-in-service date may be corrected by adjustments in the earliest taxable year open under the period of limitation for assessment under section 6501(a) or the earliest taxable year under examination by the IRS but in no event earlier than the placed-in-service year of the asset,

and in subsequent taxable years. However, if a taxpayer initiates the change in placed-in-service date, in lieu of filing amended federal tax returns, the taxpayer may correct the placed-in-service date by adjustments in the current and subsequent taxable years.

(*vi*) Any other change in depreciation or amortization as the Secretary may designate by publication in the **Federal Register** or in the Internal Revenue Bulletin (*see* § 601.601(d)(2) of this chapter).

(*4*) *Item being changed.* For purposes of a change in depreciation or amortization to which this paragraph (e)(2)(ii)(*d*) applies, the item being changed generally is the depreciation treatment of each individual depreciable or amortizable asset. However, the item is the depreciation treatment of each vintage account with respect to a depreciable asset for which depreciation is determined under § 1.167(a)–11 (CLADR property). Further, a change in computing depreciation or amortization under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168) is permitted only with respect to all assets in a particular account (as defined in § 1.167(a)–7) or vintage account.

(*5*) *Special rules.* For purposes of a change in depreciation or amortization to which this paragraph (e)(2)(ii)(*d*) applies—

(*i*) *Declining balance method to the straight line method for MACRS property.* For tangible, depreciable property subject to section 168 (MACRS property) that is depreciated using the 200-percent or 150-percent declining balance method of depreciation under section 168(b)(1) or (2), a taxpayer may change without the consent of the Commissioner from the declining balance method of depreciation to the straight line method of depreciation in the first taxable year in which the use of the straight line method with respect to the adjusted depreciable basis of the MACRS property as of the beginning of that year will yield a depreciation allowance that is greater than the depreciation allowance yielded by the use of the declining balance method. When the change is made, the adjusted depreciable basis of the MACRS property as of the beginning of the taxable year is recovered through annual depreciation allowances over the remaining recovery period (for further guidance, *see* section 6.06 of Rev. Proc. 87–57 (1987–2 C.B. 687) and § 601.601(d)(2)(ii)(*b*) of this chapter).

(*ii*) *Depreciation method changes for section 167 property.* For a depreciable or amortizable asset for which depreciation is determined under section 167 (other than under section 168, section 1400I, section 1400L, or former section 168), see § 1.167(e)–1T(b), (c), and (d) for the changes in depreciation method that are permitted to be made without the consent of the Commissioner. For CLADR property, see § 1.167(a)–11(c)(1)(iii) for the changes in depreciation method for CLADR property that are permitted to be made without the consent of the Commissioner. Further, *see* § 1.167(a)–11(b)(4)(iii)(c) for how to correct an incorrect classification or characterization of CLADR property.

(*iii*) *Section 481 adjustment.* Except as otherwise expressly provided by the Internal Revenue Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin, no section 481 adjustment is required or permitted for a change from one permissible method of computing depreciation or amortization to another permissible method of computing depreciation or amortization for an asset because this change is implemented by either a cut-off method (for further guidance, see section 2.06 of Rev. Proc. 97–27 (1997–1 C.B. 680), section 2.06 of Rev. Proc. 2002–9 (2002–1 C.B. 327), and § 601.601(d)(2)(ii)(*b*) of this chapter) or a modified cut-off method (under which the adjusted depreciable basis of the asset as of the beginning of the year of change is recovered using the new permissible method of accounting), as appropriate. However, a change from an impermissible method of computing depreciation or amortization to a permissible method of computing depreciation or amortization for an asset results in a section 481 adjustment. Similarly, a change in the treatment of an asset from nondepreciable or nonamortizable to depreciable or amortizable (or vice versa) or a change in the treatment of an asset from expensing to depreciating (or vice versa) results in a section 481 adjustment.

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

Example 1. Although the sale of merchandise is an income producing factor, and therefore inventories are required, a taxpayer in the retail jewelry business reports his income on the cash receipts and disbursements method of accounting. A change from the cash receipts and disbursements method of accounting to the accrual method of accounting is a change in the overall plan of accounting and thus is a change in method of accounting.

Example 2. A taxpayer in the wholesale dry goods business computes its income and expenses on the accrual method of accounting and files its Federal income tax returns on such basis except for real estate taxes which have been reported on the cash receipts and disbursements method of accounting. A change in the treatment of real estate taxes from the cash receipts and disbursements method to the accrual method is a change in method of accounting because such change is a change in the treatment of a material item within his overall accounting practice.

Example 3. A taxpayer in the wholesale dry goods business computes its income and expenses on the accrual method of accounting and files its Federal income tax returns on such basis. Vacation pay has been deducted in the year in which paid because the taxpayer did not have a completely vested vacation pay plan, and, therefore, the liability for payment did not accrue until that year. Subsequently, the taxpayer adopts a completely vested vacation pay plan that changes its year for accruing the deduction from the year in which payment is made to the year in which the liability to make the payment now arises. The change for the year of deduction of the vacation pay plan is not a change in method of accounting but results, instead, because the underlying facts (that is, the type of vacation pay plan) have changed.

Example 4. From 1968 through 1970, a taxpayer has fairly allocated indirect overhead costs to the value of inventories on a fixed percentage of direct costs. If the ratio of indirect overhead costs to direct costs increases in 1971, a change in the underlying facts has occurred. Accordingly, an increase in the percentage in 1971 to fairly reflect the increase in the relative level of indirect overhead costs is not a change in method of accounting but is a change in treatment resulting from a change in the underlying facts.

Example 5. A taxpayer values inventories at cost. A change in the basis for valuation of inventories from cost to the lower of cost or market is a change in an overall practice of valuing items in inventory. The change, therefore, is a change in method of accounting for inventories.

Example 6. A taxpayer in the manufacturing business has for many taxable years valued its inventories at cost. However, cost has been improperly computed since no overhead costs have been included in valuing the inventories at cost. The failure to allocate an appropriate portion of overhead to the value of inventories is contrary to the requirement of the Internal Revenue Code and the regulations under the Code. A change requiring appropriate allocation of overhead is a change in method of accounting because it involves a change in the treatment of a material item used in the overall practice of identifying or valuing items in inventory.

Example 7. A taxpayer has for many taxable years valued certain inventories by a method which provides for deducting 20 percent of the cost of the inventory items in determining the final inventory valuation. The 20 percent adjustment is taken as a ''reserve for price changes.'' Although this method is not a proper method of valuing inventories under the Internal Revenue Code or the regulations under the Code, it involves the treatment of a material item used in the overall practice of valuing inventory. A change in such practice or procedure is a change of method of accounting for inventories.

Example 8. A taxpayer has always used a base stock system of accounting for inventories. Under this system a constant price is applied to an assumed constant normal quantity of goods in stock. The base stock system is an overall plan of accounting for inventories which is not recognized as a proper method of accounting for inventories under the regulations. A change in this practice is, nevertheless, a change of method of accounting for inventories.

Example 9. In 2000, A1, a calendar year taxpayer engaged in the trade or business of manufacturing knitted goods, purchased and placed in service a building and its components at a total cost of $10,000,000 for use in its manufacturing operations. A1 classified the $10,000,000 as nonresidential real property under section 168(e). A1 did not make any elections under section 168 on its 2000 Federal tax return. As a result, on its 2000, 2001, and 2002 federal tax returns, A1 depreciated the $10,000,000 under the general depreciation system of section 168(a), using the straight line method of depreciation, a 39-year recovery period, and the mid-month convention. In 2003, A1 completes a cost segregation study on the building and its components and identifies items that cost a total of $1,500,000 as section 1245 property. As a result, the $1,500,000 should have been classified in 2000 as 5-year property under section 168(e) and depreciated on A1's 2000, 2001, and 2002 Federal tax returns under the general depreciation system, using the 200-percent declining balance method of depreciation, a 5-year recovery period, and the half-year convention. Pursuant to paragraph (e)(2)(ii)(*d*)(*2*)(*i*) of this section, A1's change to this depreciation method, recovery period, and convention is a change in method of accounting. This method change results in a section 481 adjustment. The useful life exception under paragraph (e)(2)(ii)(*d*)(*3*)(*i*) of this section does not apply because the assets are depreciated under section 168.

Example 10. In 1996, B, a calendar year taxpayer, purchased and placed in service new equipment at a total cost of $1,000,000 for use in its plant located outside the United States. The equipment is 15-year property under section 168(e) with a class life of 20 years. The equipment is required to be depreciated under the alternative depreciation system of section 168(g). However, B incorrectly depreciated the equipment under the general depreciation system of section 168(a), using the 150-percent declining balance method, a 15-year recovery period, and the half-year convention. In 2003, the IRS examines B's 2000 Federal income tax return and changes the depreciation of the equipment to the alternative depreciation system, using the straight line method of depreciation, a 20-year recovery period, and the half-year convention. Pursuant to paragraph (e)(2)(ii)(*d*)(*2*)(*i*) of this section, this change in depreciation method and recovery period made by the IRS is a change in method of accounting. This method change results in a section 481 adjustment. The useful life exception under paragraph (e)(2)(ii)(*d*)(*3*)(*i*) of this section does not apply because the assets are depreciated under section 168.

Example 11. In May 2001, C, a calendar year taxpayer, purchased and placed in service equipment for use in its trade or business. C never held this equipment for sale. However, C incorrectly treated the equipment as inventory on its 2001 and 2002 Federal tax returns. In 2003, C realizes that the equipment should have been treated as a depreciable asset. Pursuant to paragraph (e)(2)(ii)(*d*)(*2*) of this section, C's change in the treatment of the equipment from inventory to a depreciable asset is a change in method of accounting. This method change results in a section 481 adjustment.

Example 12. Since 2001, D, a calendar year taxpayer, has used the distribution fee period method to amortize distributor commissions and, under that method, established pools to account for the distributor commissions (for further guidance, see Rev. Proc. 2000–38 (2000–2 C.B. 310) and § 601.601(d)(2)(ii)(*b*) of this chapter). A change in the accounting of distributor commissions under the distribution fee period method from pooling to single asset accounting is a change in method of accounting pursuant to paragraph (e)(2)(ii)(*d*)(*2*)(*vi*) of this section. This method change results in no section 481 adjustment because the change is from one permissible method to another permissible method.

Example 13. Since 2000, E, a calendar year taxpayer, has accounted for items of MACRS property that are mass assets in pools. Each pool includes only the mass assets that are placed in service by E in the same taxable year. E is able to identify the cost basis of each asset in each pool. None of the pools are general asset accounts under section 168(i)(4) and the regulations under section 168(i)(4). E identified any dispositions of these mass assets by specific identification. Because of changes in E's recordkeeping in 2003, it is impracticable for E to continue to identify disposed mass assets using specific identification. As a result, E wants to change to a first-in, first-out method under which the mass assets disposed of in a taxable year are deemed to be from the pool with the earliest placed-in-service year in existence as of the beginning of the taxable year of each disposition. Pursuant to paragraph (e)(2)(ii)(*d*)(*2*)(*vii*) of this section, this change is a change in method of accounting. This method change results in no section 481 adjustment because the change is from one permissible method to another permissible method.

Example 14. In August 2001, F, a calendar taxpayer, purchased and placed in service a copier for use in its trade or business. F incorrectly classified the copier as 7-year property under section 168(e). F made no elections under section 168 on its 2001 Federal tax return. As a result, on its 2001 and 2002 Federal tax returns, F depreciated the copier under the general depreciation system of section 168(a), using the 200-percent declining balance method of depreciation, a 7-year recovery period, and the half-year convention. In 2003, F realizes that the copier is 5-year property and should have been depreciated on its 2001 and 2002 Federal tax returns under the general depreciation system using a 5-year recovery period rather than a 7-year recovery period. Pursuant to paragraph (e)(2)(ii)(*d*)(*2*)(*i*) of this section, F's change in recovery period from 7 to 5 years is a change in method of accounting. This method change results in a section 481 adjustment. The useful life exception under paragraph (e)(2)(ii)(*d*)(*3*)(*i*) of this section does not apply because the copier is depreciated under section 168.

Example 15. In 1998, G, a calendar year taxpayer, purchased and placed in service an intangible asset that is not an amortizable section 197 intangible and that is not described in section 167(f). G amortized the cost of the intangible asset under section 167(a) using the straight line method of depreciation and a useful life of 13 years. In 2003, because of changing conditions, G changes the remaining useful life of the intangible asset to 2 years. Pursuant to paragraph (e)(2)(ii)(*d*)(*3*)(*i*) of this section, G's change in useful life is not a change in method of accounting because the intangible asset is depreciated under section 167 and G is not changing to or from a useful life that is specifically assigned by the Internal Revenue Code, the regulations under the Code, or other guidance published in the Internal Revenue Bulletin.

Example 16. In July 2001, H, a calendar year taxpayer, purchased and placed in service ''off-the-shelf'' computer software and a new computer. The cost of the new computer and computer software are separately stated. H incorrectly included the cost of this software as part of the cost of the computer, which is 5-year property under section 168(e). On its 2001 Federal tax return, H elected to depreciate its 5-year property placed in service in 2001 under the alternative depreciation system of section 168(g). The class life for a computer is 5 years. As a result, because H included the cost of the computer software as part of the cost of the computer hardware, H depreciated the cost of the software under the alternative depreciation system, using the straight line method of depreciation, a 5-year recovery period, and the half-year convention. In 2003, H realizes that the cost of the software should have been amortized under section 167(f)(1), using the straight line method of depreciation, a 36-month useful life, and a monthly convention. H's change from 5-years to 36-months is a change in method of accounting because H is changing to a useful life that is specifically assigned by section 167(f)(1). The change in convention from the half-year to the monthly convention also is a change in method of accounting. Both changes result in a section 481 adjustment.

Example 17. On September 15, 2001, I2, a calendar year taxpayer, purchased and placed in service new equipment at a total cost of $500,000 for use in its business. The equipment is 5-year property under section 168(e) with a class life of 9 years and is qualified property under section 168(k). I2 did not place in service any other depreciable property in 2001. Section 168(g)(1)(A) through (D) do not apply to the equipment. I2 intended to elect the alternative depreciation system under section 168(g) for 5-year property placed in service in 2001. However, I2 did not make the election. Instead, I2 deducted on its 2001 Federal tax return the 30-percent additional first year depreciation attributable to the equipment

and, on its 2001 and 2002 Federal tax returns, depreciated the remaining adjusted depreciable basis of the equipment under the general depreciation system under 168(a), using the 200-percent declining balance method, a 5-year recovery period, and the half-year convention. In 2003, I2 realizes its failure to make the alternative depreciation system election in 2001 and files a Form 3115 to change its method of depreciating the remaining adjusted depreciable basis of the 2001 equipment to the alternative depreciation system. Because this equipment is not required to be depreciated under the alternative depreciation system, I2 is attempting to make an election under section 168(g)(7). However, this election must be made in the taxable year in which the equipment is placed in service (2001) and, consequently, I2 is attempting to make a late election under section 168(g)(7). Accordingly, I2's change to the alternative depreciation system is not a change in accounting method pursuant to paragraph (e)(2)(ii)(*d*)(*3*)(*iii*) of this section. Instead, I2 must submit a request for a private letter ruling under § 301.9100–3 of this chapter, requesting an extension of time to make the alternative depreciation system election on its 2001 Federal tax return.

(3) [Reserved]. For further guidance, see § 1.446–1(e)(3).

(4) *Effective date*—(i) *In general.* Except as provided in paragraphs (e)(3)(iii) and (e)(4)(ii) of this section, paragraph (e) of this section applies on or after December 30, 2003. For the applicability of regulations before December 30, 2003, *see* § 1.446–1(e) in effect prior to December 30, 2003 (§ 1.446–1(e) as contained in 26 CFR part 1 edition revised as of April 1, 2003).

(ii) *Changes involving depreciable or amortizable assets.* With respect to paragraph (e)(2)(ii)(*d*) of this section, paragraph (e)(2)(iii) *Examples 9* through *17* of this section, the addition of the language ''certain changes in computing depreciation or amortization (see paragraph (e)(2)(ii)(*d*) of this section)'' to the last sentence of paragraph (e)(2)(ii)(*a*) of this section, and the removal of all language regarding useful life and the sentence ''On the other hand, a correction to require depreciation in lieu of a deduction for the cost of a class of depreciable assets which had been consistently treated as an expense in the year of purchase involves the question of the proper timing of an item, and is to be treated as a change in method of accounting'' from paragraph (e)(2)(ii)(*b*) of this section—

(A) For any change in depreciation or amortization that is a change in method of accounting, this section applies to such a change in method of accounting made for taxable years ending on or after December 30, 2003; and

(B) For any change in depreciation or amortization that is not a change in method of accounting, this section applies to such a change made for taxable years ending on or after December 30, 2003.

(iii) The applicability of paragraph (e) of this section expires on or before January 2, 2007.

■ **Par. 6.** Section 1.1016–3 is amended by:

■ 1. Redesignating paragraph (h) as paragraph (i).

■ 2. Adding new paragraphs (h) and (j). The additions read as follows:

§ 1.1016–3 Exhaustion, wear and tear, obsolescence, amortization, and depletion for periods since February 28, 1913.

* * * * *

(h) *Application to a change in method of accounting.* [Reserved]. For further guidance, see § 1.1016–3T(h).

* * * * *

(j) *Effective date.* [Reserved]. For further guidance, see § 1.1016–3T(j)(1) and (2).

■ **Par. 7.** Section 1.1016–3T is added to read as follows:

§ 1.1016–3T Exhaustion, wear and tear, obsolescence, amortization, and depletion for periods since February 28, 1913 (temporary).

(a) through (g) [Reserved]. For further guidance, *see* § 1.1016–3(a) through (g).

(h) *Application to a change in method of accounting.* For purposes of determining whether a change in depreciation or amortization for property subject to section 167, 168, 197, 1400I, 1400L(b), or 1400L(c), or to section 168 prior to its amendment by the Tax Reform Act of 1986 (100 Stat. 2121) (former section 168) is a change in method of accounting under section 446(e) and the regulations under section 446(e), section 1016(a)(2) does not permanently affect a taxpayer's lifetime income.

(i) [Reserved]. For further guidance, see § 1.1016–3(i).

(j) *Effective date*—(1) *In general.* Except as provided in paragraph (j)(2) of this section, this section applies on or after December 30, 2003. For the applicability of regulations before December 30, 2003, see § 1.1016–3 in effect prior to December 30, 2003 (§ 1.1016–3 as contained in 26 CFR part 1 edition revised as of April 1, 2003).

(2) *Depreciation or amortization changes.* Paragraph (h) of this section applies to a change in depreciation or amortization for property subject to section 167, 168, 197, 1400I, 1400L(b), or 1400L(c), or former section 168 for taxable years ending on or after December 30, 2003.

(3) The applicability of this section expires on or before January 2, 2007.

Mark E. Matthews,

Deputy Commissioner for Services and Enforcement.

Approved: December 18, 2003.

Pamela F. Olson,

Assistant Secretary of the Treasury (Tax Policy).

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1, 20, 25, and 26

[TD 9102]

RIN 1545–AX96

Definition of Income for Trust Purposes

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations revising the definition of income under section 643(b) of the Internal Revenue Code. The regulations are necessary to reflect changes in the definition of trust accounting income under state laws. The final regulations also clarify the situations in which capital gains are included in distributable net income under section 643(a)(3). Conforming amendments are made to regulations affecting ordinary trusts, pooled income funds, charitable remainder trusts, trusts that qualify for the gift and estate tax marital deduction, and trusts that are exempt from generation-skipping transfer taxes. The regulations affect the grantors, beneficiaries, and fiduciaries of trusts.

DATES: *Effective Date:* These regulations are effective January 2, 2004.

Applicability date: Generally, the final regulations are applicable to trusts and estates for taxable years ending after January 2, 2004. *See* revised §§ 1.642(c)–2, 1.642(c)–5, and 1.664–3 for special dates of applicability affecting those sections.

FOR FURTHER INFORMATION CONTACT: Bradford R. Poston at (202) 622–3060 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

On February 15, 2001, proposed regulations (REG–106513–00) were published in the **Federal Register** [66 FR 10396] containing proposed amendments to the Income Tax