

LISTING OF DEVICES FOR WHICH COMPLIANCE IS REQUIRED EFFECTIVE—Continued

May 11, 1998

Phase	Product code	21 CFR section	Class	Device name
1 .....	74 DPS	870.2340	II	Electrocardiograph.
1 .....	74 DRG	870.2910	II	Transmitters and Receivers, Physiological Signal, Radio Frequency.
1 .....	74 DRT	870.2300	II	Monitor, Cardiac (including Cardiotachometer and Rate Alarm).
1 .....	74 DRX	870.2360	II	Electrode, Electrocardiograph.
1 .....	74 DSA	870.2900	II	Cable, Transducer and Electrode, Patient (including Connector).
1 .....	74 DSH	870.2800	II	Recorder, Magnetic Tape, Medical.
1 .....	74 DSI	870.1025	III	Detector and Alarm, Arrhythmia.
1 .....	74 DXH	870.2920	II	Transmitters and Receivers, Electrocardiograph, Telephone.

(b) For electrode lead wires and patient cables used with, or intended for use with, any other device, the date for which compliance is required is May 9, 2000.

**§ 898.14 Exemptions and variances.**

(a) A request for an exemption or variance shall be submitted in the form of a petition under §10.30 of this chapter and shall comply with the requirements set out therein. The petition shall also contain the following:

(1) The name of the device, the class in which the device has been classified, and representative labeling showing the intended uses(s) of the device;

(2) The reasons why compliance with the performance standard is unnecessary or unfeasible;

(3) A complete description of alternative steps that are available, or that the petitioner has already taken, to ensure that a patient will not be inadvertently connected to hazardous voltages via an unprotected patient cable or electrode lead wire for intended use with the device; and

(4) Other information justifying the exemption or variance.

(b) An exemption or variance is not effective until the agency approves the request under § 10.30(e)(2)(i) of this chapter.

Dated: April 28, 1997.

**William B. Schultz,**

*Deputy Commissioner for Policy.*

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**DEPARTMENT OF THE TREASURY**

**Internal Revenue Service**

**26 CFR Parts 1 and 301**

[TD 8717]

RIN 1545-AU14

**Termination of a Partnership Under Section 708(b)(1)(B)**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final regulations.

**SUMMARY:** This document contains final regulations relating to the termination of a partnership upon the sale or exchange of 50 percent or more of the total interest in partnership capital and profits within a 12-month period. The final regulations affect all partnerships that terminate under section 708(b)(1)(B).

**DATES:** These regulations are effective May 9, 1997.

For applicability dates, see Effective Dates under Supplementary Information.

**FOR FURTHER INFORMATION CONTACT:** Steven R. Schneider, (202) 622-3060 (not a toll-free number).

**SUPPLEMENTARY INFORMATION:**

**Background**

On May 13, 1996, a notice of proposed rulemaking (PS-5-96) was published in the **Federal Register** (61 FR 21985) containing proposed amendments to the Income Tax Regulations (26 CFR part 1) under section 708 of the Internal Revenue Code (Code). The notice of proposed rulemaking also contained proposed amendments to other sections of the Income Tax Regulations to reflect the amendments to the regulations under section 708. Written comments responding to this notice were received. A public hearing was held on September 5, 1996, pursuant to the notice published in the **Federal Register**

on May 13, 1996. After consideration of all comments received, the proposed amendments are adopted as revised by this Treasury decision.

**Explanation of Provisions**

Section 708(b)(1)(B) provides that, for purposes of section 708(a), a partnership shall be considered terminated if within a 12-month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits. The existing regulations under § 1.708-1(b)(1)(iv) provide that, if a partnership is terminated by a sale or exchange of an interest, the following is deemed to occur: The partnership distributes its properties to the purchaser and the other remaining partners in proportion to their respective interests in the partnership properties; and, immediately thereafter, the purchaser and the other remaining partners contribute the properties to a new partnership, either for the continuation of the business or for its dissolution and winding up. The final regulations adopt the proposed regulations and change the mechanics of a termination under section 708(b)(1)(B) so that the following is deemed to occur on a termination: The partnership contributes all of its assets and liabilities to a new partnership in exchange for an interest in the new partnership; and, immediately thereafter, the partnership liquidates by distributing interests in the new partnership to the purchaser and the other remaining partners, followed by the continuation of the business by the new partnership or its dissolution and winding up. The final regulations also clarify certain aspects of the proposed regulations in response to comments received.

One commentator requested clarification of the section 704(c) consequences of a termination. The proposed regulations provide for a section 704(b) capital account "book up" upon the deemed contribution of assets by the terminated partnership to

the new partnership and also upon the deemed distribution in liquidation of the terminated partnership. This would have resulted in a new layer of section 704(c) property. The final regulations amend the regulations under section 704(b) to provide that the deemed contribution of assets to a new partnership and the distribution of the new partnership interests to the partners of the terminated partnership are disregarded for purposes of maintaining capital accounts. As a result, the termination of a partnership does not change the capital accounts of the partners or the books of the partnership and the deemed contribution of assets to a new partnership does not create additional section 704(c) property. The final regulations also provide that the new partnership is not bound by the section 704(c) method used by the terminated partnership.

A commentator requested clarification of whether a termination under the new section 708(b)(1)(B) construct will trigger recapture of investment tax credit under section 47.

Although not specifically addressed in the regulations, a section 708(b)(1)(B) termination no longer triggers recapture of the investment tax credit under the "mere change in form" exception in § 1.47-3(f) of the regulations.

Commentators also requested guidance on whether a section 1491 excise tax may be triggered upon a section 708(b)(1)(B) termination of a foreign partnership with U.S. partners. This issue is currently under study and the IRS and Treasury welcome comments from interested taxpayers and practitioners.

One commentator requested clarification of whether the distribution of the interests in the new partnership will be subject to section 731(c). The section 731(c) final regulations, December 26, 1996 (61 FR 67936), provide that the deemed distribution of partnership interests under § 1.708-1(b)(1)(iv) does not trigger the application of section 731(c).

Several commentators suggested that partnerships should be allowed to apply the final regulations to terminations under section 708(b)(1)(B) occurring on or after the date the proposed regulations were filed with the **Federal Register**. In response, the final regulations provide that the regulations may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply the regulations to the termination in a consistent manner.

The final regulations also provide an example illustrating the mechanics of a termination under section 708(b)(1)(B).

In addition, the final regulations provide that the new partnership retains the TIN of the terminated partnership. However, if the new partnership has already applied for a new TIN, the partnership should continue to use the new TIN.

Finally, the regulations make several revenue rulings obsolete. The holdings of revenue rulings 87-50 and 87-51 (dealing with the effect of terminations under section 708(b)(1)(B) on lower-tier partnerships) and revenue rulings 86-73 and 88-42 (dealing with the effect of a § 754 election made by the terminating partnership) are now incorporated, without substantive change, into the regulations under § 1.708-1. Additionally, the final regulations make revenue ruling 93-90 (dealing with minimum gain chargeback in a section 708(b)(1)(B) termination) obsolete because the § 704(b) capital account "book up" that is the subject of the revenue ruling is eliminated.

#### Effective Date

These regulations apply to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, these regulations may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply these regulations to the termination in a consistent manner.

#### Effect on Other Documents

The following publications are obsolete as of May 9, 1997:

Rev. Rul. 86-73, 1986-1 C.B. 282  
 Rev. Rul. 87-50, 1987-1 C.B. 157  
 Rev. Rul. 87-51, 1987-1 C.B. 158  
 Rev. Rul. 88-42, 1988-1 C.B. 265  
 Rev. Rul. 93-90, 1993-2 C.B. 238

#### Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Small Business Administration for comment on its impact on small business.

#### Drafting Information

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

#### List of Subjects

##### 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

##### 26 CFR Part 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 continues to read in part as follows:

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

**Par. 2.** Section 1.704-1 is amended as follows:

1. Paragraph (b)(2)(iv)(d)(1) is amended by revising the second sentence.

2. Paragraph (b)(2)(iv)(l) is amended by removing the last three sentences and adding four sentences in their place.

3. Paragraph (b)(5) *Example 13(v)* is amended by removing all the text following the third sentence and adding four sentences in its place.

The revisions and additions read as follows:

#### § 1.704-1 Partner's distributive share.

\* \* \* \* \*

(b) \* \* \*

(2) \* \* \*

(iv) \* \* \*

(d) \* \* \*

(1) \* \* \* See *Example 13(i)* of paragraph (b)(5) of this section. \* \* \*

\* \* \* \* \*

(l) \* \* \* If the transfer of an interest in a partnership causes a termination of the partnership under section 708(b)(1)(B), the capital account of the transferee partner and the capital accounts of the other partners of the terminated partnership carry over to the new partnership that is formed as a result of the termination of the partnership under § 1.708-1(b)(1)(iv). Moreover, the deemed contribution of assets and liabilities by the terminated partnership to a new partnership and

the deemed liquidation of the terminated partnership that occur under § 1.708-1(b)(1)(iv) are disregarded for purposes of this paragraph (b)(2)(iv). See Example 13 of paragraph (b)(5) of this section and the example in § 1.708-1(b)(1)(iv). The previous three sentences apply to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, the sentences may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply the sentences to the termination in a consistent manner.

\* \* \* \* \*

(5) \* \* \*

Example 13. \* \* \*

(v) \* \* \* Immediately preceding the constructive liquidation, the capital accounts of Z and LK equal \$11,000 each (LK having inherited Y's \$11,000 capital account) and the book value of the G Corp. securities is \$22,000 (original purchase price of securities). Under paragraph (b)(2)(iv)(I) of this section, the deemed contribution of assets and liabilities by the terminated partnership to the new partnership and the deemed liquidation of the terminated partnership that occur under § 1.708-1(b)(1)(iv) in connection with the constructive liquidation of the terminated partnership are disregarded in the maintenance and computation of the partners' capital accounts. As a result, the capital accounts of Z and LK in the new partnership equal \$11,000 each (their capital accounts in the terminated partnership immediately prior to the termination), and the book value of the G Corp. securities remains \$22,000 (its book value immediately prior to the termination). This Example 13(v) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this Example 13(v) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this Example 13(v) to the termination in a consistent manner.

\* \* \* \* \*

Par. 3. Section 1.704-3 is amended as follows:

1. Paragraph (a)(2) is amended by adding two sentences at the end of the paragraph.

2. Paragraph (a)(3)(i) is amended by adding three sentences at the end of the paragraph.

The additions read as follows:

§ 1.704-3 Contributed property.

(a) \* \* \*

(2) \* \* \* A new partnership formed as the result of the termination of a partnership under section 708(b)(1)(B) is not required to use the same method as the terminated partnership with respect to section 704(c) property deemed contributed to the new partnership by the terminated partnership under § 1.708-1(b)(1)(iv). The previous

sentence applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, the sentence may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply the sentence to the termination in a consistent manner.

(3) \* \* \*

(i) \* \* \* Property deemed contributed to a new partnership as the result of the termination of a partnership under section 708(b)(1)(B) is treated as section 704(c) property in the hands of the new partnership only to the extent that the property was section 704(c) property in the hands of the terminated partnership immediately prior to the termination. See § 1.708-1(b)(1)(iv) for an example of the application of this rule. The previous two sentences apply to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, the sentences may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply the sentences to the termination in a consistent manner.

\* \* \* \* \*

Par. 4. Section 1.704-4 is amended by revising paragraphs (a)(4)(ii) and (c)(3) to read as follows:

§ 1.704-4 Distribution of contributed property.

(a) \* \* \*

(4) \* \* \*

(ii) Section 708(b)(1)(B) terminations.

A termination of the partnership under section 708(b)(1)(B) does not begin a new five-year period for each partner with respect to the built-in gain and built-in loss property that the terminated partnership is deemed to contribute to the new partnership under § 1.708-1(b)(1)(iv). See § 1.704-3(a)(3)(ii) for the definitions of built-in gain and built-in loss on section 704(c) property. This paragraph (a)(4)(ii) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (a)(4)(ii) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (a)(4)(ii) to the termination in a consistent manner.

\* \* \* \* \*

(c) \* \* \*

(3) Section 708(b)(1)(B) terminations. Section 704(c)(1)(B) and this section do not apply to the deemed distribution of interests in a new partnership caused by the termination of a partnership under section 708(b)(1)(B). A subsequent

distribution of section 704(c) property by the new partnership to a partner of the new partnership is subject to section 704(c)(1)(B) to the same extent that a distribution by the terminated partnership would have been subject to section 704(c)(1)(B). See also § 1.737-2(a) for a similar rule in the context of section 737. This paragraph (c)(3) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (c)(3) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (c)(3) to the termination in a consistent manner.

\* \* \* \* \*

Par. 5. Section 1.708-1 is amended as follows:

1. Paragraph (b)(1)(ii) is amended by adding three sentences after the third sentence.

2. Paragraph (b)(1)(iv) is revised.

3. Paragraph (b)(1)(v) is added.

The additions and revisions read as follows:

1.708-1 Continuation of partnership.

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(ii) \* \* \* Moreover, if the sale or exchange of an interest in a partnership (upper-tier partnership) that holds an interest in another partnership (lower-tier partnership) results in a termination of the upper-tier partnership, the upper-tier partnership is treated as exchanging its entire interest in the capital and profits of the lower-tier partnership. If the sale or exchange of an interest in an upper-tier partnership does not terminate the upper-tier partnership, the sale or exchange of an interest in the upper-tier partnership is not treated as a sale or exchange of a proportionate share of the upper-tier partnership's interest in the capital and profits of the lower-tier partnership. The previous two sentences apply to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, the sentences may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply the sentences to the termination in a consistent manner. \* \* \*

\* \* \* \* \*

(iv) If a partnership is terminated by a sale or exchange of an interest, the following is deemed to occur: The partnership contributes all of its assets and liabilities to a new partnership in exchange for an interest in the new partnership; and, immediately

thereafter, the terminated partnership distributes interests in the new partnership to the purchasing partner and the other remaining partners in proportion to their respective interests in the terminated partnership in liquidation of the terminated partnership, either for the continuation of the business by the new partnership or for its dissolution and winding up. In the latter case, the new partnership terminates in accordance with (b)(1)(i) of this section. This paragraph (b)(1)(iv) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (b)(1)(iv) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (b)(1)(iv) to the termination in a consistent manner. The provisions of this paragraph (b)(1)(iv) are illustrated by the following example:

*Example.* (i) A and B each contribute \$10,000 cash to form AB, a general partnership, as equal partners. AB purchases depreciable Property X for \$20,000. Property X increases in value to \$30,000, at which time A sells its entire 50 percent interest to C for \$15,000 in a transfer that terminates the partnership under section 708(b)(1)(B). At the time of the sale, Property X had an adjusted tax basis of \$16,000 and a book value of \$16,000 (original \$20,000 tax basis and book value reduced by \$4,000 of depreciation). In addition, A and B each had a capital account balance of \$8,000 (original \$10,000 capital account reduced by \$2,000 of depreciation allocations with respect to Property X).

(ii) Following the deemed contribution of assets and liabilities by the terminated AB partnership to a new partnership (new AB) and the liquidation of the terminated AB partnership, the adjusted tax basis of Property X in the hands of new AB is \$16,000. See Section 723. The book value of Property X in the hands of new partnership AB is also \$16,000 (the book value of Property X immediately before the termination) and B and C each have a capital account of \$8,000 in new AB (the balance of their capital accounts in AB prior to the termination). See § 1.704-1(b)(2)(iv)(I) (providing that the deemed contribution and liquidation with regard to the terminated partnership are disregarded in determining the capital accounts of the partners and the books of the new partnership). Additionally, under § 301.6109-1(d)(2)(iii) of this chapter, new AB retains the taxpayer identification number of the terminated AB partnership.

(iii) Property X was not section 704(c) property in the hands of terminated AB and is therefore not treated as section 704(c) property in the hands of new AB, even though Property X is deemed contributed to new AB at a time when the fair market value of Property X (\$30,000) was different from its adjusted tax basis (\$16,000). See § 1.704-3(a)(3)(i) (providing that property contributed to a new partnership under § 1.708-1(b)(1)(iv) is treated as section 704(c)

property only to the extent that the property was section 704(c) property in the hands of the terminated partnership immediately prior to the termination).

(v) If a partnership is terminated by a sale or exchange of an interest in the partnership, a section 754 election (including a section 754 election made by the terminated partnership on its final return) that is in effect for the taxable year of the terminated partnership in which the sale occurs, applies with respect to the incoming partner. Therefore, the bases of partnership assets are adjusted pursuant to sections 743 and 755 prior to their deemed contribution to the new partnership. This paragraph (b)(1)(v) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (b)(1)(v) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (b)(1)(v) to the termination in a consistent manner.

**Par. 6.** Section 1.737-2 is amended as follows:

1. Paragraph (a) is revised.
2. In paragraph (d)(1), the first sentence is revised and one sentence is added after the first sentence.

The additions and revisions read as follows:

**§ 1.737-2 Exceptions and special rules.**

(a) *Section 708(b)(1)(B) terminations.* Section 737 and this section do not apply to the deemed distribution of interests in a new partnership caused by the termination of a partnership under section 708(b)(1)(B). A subsequent distribution of property by the new partnership to a partner of the new partnership that was formerly a partner of the terminated partnership is subject to section 737 to the same extent that a distribution from the terminated partnership would have been subject to section 737.

See also § 1.704-4(c)(3) for a similar rule in the context of section 704(c)(1)(B). This paragraph (a) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (a) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (a) to the termination in a consistent manner.

(d) \* \* \* (1) \* \* \* Any portion of the distributed property that consists of property previously contributed by the distributee partner (previously

contributed property) is not taken into account in determining the amount of the excess distribution or the partner's net precontribution gain. The previous sentence applies on or after May 9, 1997. \* \* \*

**Par. 7.** In section 1.743-1, paragraph (d) is added to read as follows:

**§ 1.743-1 Optional adjustment to basis of partnership property.**

(d) *Section 708(b)(1)(B) terminations.* A partner with a special basis adjustment in property held by a partnership that terminates under section 708(b)(1)(B) will continue to have the same special basis adjustment with respect to property deemed contributed by the terminated partnership to the new partnership under § 1.708-1(b)(1)(iv), regardless of whether the new partnership makes a section 754 election. This paragraph (d) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (d) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (d) to the termination in a consistent manner.

**Par. 8.** In § 1.761-1, paragraph (e) is added to read as follows:

**§ 1.761-1 Terms defined.**

(e) *Distribution of partnership interest.* For purposes of section 708(b)(1)(B) and § 1.708-1(b)(1)(iv), the deemed distribution of an interest in a new partnership by a partnership that terminates under section 708(b)(1)(B) is not a sale or exchange of an interest in the new partnership. However, the deemed distribution of an interest in a new partnership by a partnership that terminates under section 708(b)(1)(B) is treated as an exchange of the interest in the new partnership for purposes of section 743. This paragraph (e) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (e) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (e) to the termination in a consistent manner.

**PART 301—PROCEDURE AND ADMINISTRATION**

**Par. 9.** The authority citation for part 301 continues to read in part as follows:

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

**Par. 10.** Section 301.6109-1 is amended by adding paragraph (d)(2)(iii) as follows:

**§ 301.6109-1 Identifying numbers.**

\* \* \* \* \*

(d) \* \* \*

(2) \* \* \*

(iii) *Special rule for Section 708(b)(1)(B) terminations.* A new partnership that is formed as a result of the termination of a partnership under section 708(b)(1)(B) will retain the employer identification number of the terminated partnership. This paragraph (d)(2)(iii) applies to terminations of partnerships under section 708(b)(1)(B) occurring on or after May 9, 1997; however, this paragraph (d)(2)(iii) may be applied to terminations occurring on or after May 9, 1996, provided that the partnership and its partners apply this paragraph (d)(2)(iii) to the termination in a consistent manner.

\* \* \* \* \*

**Margaret Milner Richardson,**  
*Commissioner of Internal Revenue.*

Approved: May 1, 1997.

**Donald C. Lubick,**  
*Acting Assistant Secretary of the Treasury*  
*(Tax Policy).*

[FR Doc. 97-12061 Filed 5-8-97; 8:45 am]

BILLING CODE 4830-01-U

## DEPARTMENT OF THE TREASURY

### Internal Revenue Service

#### 26 CFR Parts 1 and 602

[TD 8718]

RIN 1545-AS49

#### Arbitrage Restrictions on Tax-Exempt Bonds

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final regulations.

**SUMMARY:** This document contains final regulations on the arbitrage and related restrictions applicable to tax-exempt bonds issued by State and local governments. Changes to the applicable law were made by the Tax Reform Act of 1986, the Technical and Miscellaneous Revenue Act of 1988, the Revenue Reconciliation Act of 1989, and the Revenue Reconciliation Act of 1990. These regulations affect issuers of tax-exempt bonds and provide guidance for complying with the arbitrage and related restrictions.

**DATES:** These regulations are effective May 9, 1997.

For dates of applicability of these regulations, see §§ 1.103-8(a)(5), 1.142-

4(d), 1.148-11, 1.148-11A, 1.149(d)-1(g)(3), and 1.150-1(a)(2).

**FOR FURTHER INFORMATION CONTACT:** Brigitte Finley, (202) 622-3980 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

##### Paperwork Reduction Act

The collections of information contained in these final regulations have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1347. Responses to these collections of information are required to obtain a benefit from treating a contract as a qualified hedge or treating certain general obligation bonds as a single issue.

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 control number.

The estimated average annual burden hours per recordkeeper: 2 hours.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, T:FP, Washington, DC 20024, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

Books or records relating to collections 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 26 U.S.C. 6103.

##### Background

Section 148 of the Internal Revenue Code restricts the use of proceeds of tax-exempt State and local bonds to acquire higher yielding investments. On June 18, 1993, final regulations (TD 8476) relating to the arbitrage restrictions and related rules under sections 103, 148, 149, and 150 (the June 1993 regulations) were published in the **Federal Register** (59 FR 33510). Corrections to the June 1993 regulations were published in the **Federal Register** on August 23, 1993 (58 FR 44451), and May 11, 1994 (59 FR 24350).

On May 10, 1994, temporary and final regulations (TD 8538) to clarify and revise certain provisions of the June 1993 regulations were published in the **Federal Register** (59 FR 24039). A notice of proposed rulemaking (FI-7-

94) cross-referencing the temporary regulations and proposing additional changes to the June 1993 regulations was published in the **Federal Register** on the same day (59 FR 24094). Written comments were received, and a public hearing was held on September 25, 1995.

After consideration of all the comments, the proposed regulations have been modified and are adopted in final form, and the corresponding temporary regulations are redesignated as final regulations. The principal changes to the regulations, as well as the major comments and suggestions, are discussed below. Comments relating to regulations under section 148 other than those in the proposed regulations also were received. The changes requested by those comments are not addressed in these final regulations, but are under consideration.

##### Explanation of Provisions

###### A. Section 1.142-4—Interest on Bonds To Finance Certain Exempt Facilities

The proposed regulations provide generally that costs incurred before the issue date of an exempt facility bond may not be financed with the proceeds of that bond unless an official action was taken within 60 days of the date those costs were incurred. For tax-exempt bonds subject to § 1.150-2, however, a reimbursement allocation may be made if the official action was taken within 60 days of the date that the costs were paid. One commentator requested that the official action and reimbursement allocation rules for exempt facility bonds be the same as the rules in § 1.150-2. The final regulations generally adopt this suggestion. The final regulations also clarify that a refinancing of a taxable debt other than a State or local bond is not treated as a refunding for purposes of this rule. In addition, the final regulations redesignate this provision, which was previously contained in § 1.103-8(a)(5), as new § 1.142-4.

###### B. Section 1.148-1—Definitions and Elections

###### 1. Bonds Financing a Working Capital Reserve

The June 1993 regulations provide that replacement proceeds may arise if a working capital reserve is directly or indirectly financed with bond proceeds, but not to the extent the issuer has maintained a working capital reserve. The proposed regulations provide a method for determining whether an issuer has maintained a working capital reserve. This method is based on the average amount of working capital