

DEPARTMENT OF STATE**Bureau of Political-Military Affairs****22 CFR Part 121****Amendment to the International Traffic In Arms Regulations****AGENCY:** Department of State.**ACTION:** Final rule.

SUMMARY: This rule amends the International Traffic in Arms Regulations by removing from the U.S. Munitions List (USML), for transfer to the Department of Commerce's Commerce Control List (CCL), all cryptographic items except those specifically designed, developed, configured, adapted, or modified for military applications (including command, control and intelligence applications).

EFFECTIVE DATE: December 30, 1996.

FOR FURTHER INFORMATION CONTACT: Rose Biancaniello, Office of Defense Trade Controls, Department of State, Telephone (703) 812-2568 or FAX (703) 875-6647 ATTN: Regulatory Change, Cryptographic Items.

SUPPLEMENTARY INFORMATION: On October 1, 1996, the Administration announced a decision to transfer from the USML to the CCL all cryptographic items designated in USML Category XIII(b), except those specifically designed, developed, configured, adapted, or modified for military applications (including command, control and intelligence applications). New control procedures and regulations have been developed for the CCL that will provide for strong national security and foreign policy controls to all destinations and end users worldwide for these items. Enhanced interagency review of CCL licenses for these items has been established. This decision does not result in the decontrol of any of these items.

In order to ensure an orderly transition, the Department of Commerce is providing special authorization in a revision to the Export Administration Regulations being published in parallel with this amendment for U.S. persons to ship the remaining balances of outstanding USML licenses and to continue to carry-out overseas activities authorized by other approvals (e.g., distribution agreements), without applying for a new Department of Commerce license, through filing of Shippers' Export Declarations (SEDs) with District Directors of Customs and direct reporting to the Department of Commerce on previously authorized distribution activities. U.S. persons are

advised to consult the Department of Commerce's EAR publication for details. Therefore, effective upon the date of this publication, all USML licenses and other approvals issued by the Department of State, in accordance with ITAR, for Category XIII(b) items being removed from the USML are no longer valid.

In carrying out the decision, Category XIII(b) of the USML is amended.

This amendment involves a foreign affairs function of the United States and, thus, is excluded from the procedures of Executive Order 12866 (68 FR 51735) and 9 U.S.C. 553 and 554. However, interested parties are invited to submit written comments to the Department of State, Office of Defense Trade Controls, ATTN: Regulatory Change, Cryptographic Items, Room 200, SA-6, Washington, DC 20520-0602.

List of Subjects in 22 CFR Part 121

Arms and Munitions, Exports.

Accordingly, for the reasons set forth above, Title 22, Chapter I, Subchapter M, Part 121, is amended as follows:

PART 121—THE UNITED STATES MUNITIONS LIST

1. The authority citation for Part 121 continues to read as follows:

Authority: Secs. 2, 38, and 71, Pub. L. 90-629 Arms Export Control Act, 90 Stat. 744 (22 U.S.C. 2752, 2778, 2797); E.O. 11958, 42 FR 4311; 22 U.S.C. 2658.

2. In § 121.1, Category XIII(b) is revised to read as follows:

§ 121.1 General. The United States Munitions List.

* * * * *

Category XIII—Auxiliary Military Equipment

* * * * *

(b) Military Information Security Systems and equipment, cryptographic devices, software, and components specifically designed or modified therefor (i.e., such items when specifically designed, developed, configured, adapted or modified for military applications (including command, control and intelligence applications)). This includes:

(1) Military cryptographic (including key management) systems, equipment, assemblies, modules, integrated circuits, components or software with the capability of maintaining secrecy or confidentiality of information or information systems, except cryptographic equipment and software as follows:

(i) Tracking, telemetry and control (TT&C) encryption/decryption when

embedded in a commercial communications satellite identified in ECCN 9A004a of the Export Administration Regulations; embedded means that the device or system cannot feasibly be removed from the satellite and that it cannot be used for other purposes.

(2) Military cryptographic (including key management) systems, equipment, assemblies, modules, integrated circuits, components of software which have the capability of generating spreading or hopping codes for spread spectrum systems or equipment.

(3) Military cryptanalytic systems, equipment, assemblies, modules, integrated circuits, components or software.

(4) Military systems, equipment, assemblies, modules, integrated circuits, components or software providing certified or certifiable multi-level security or user isolation exceeding class B2 of the Trusted Computer System Evaluation Criteria (TCSEC) and software to certify such systems, equipment or software.

(5) Ancillary equipment specifically designed or modified for paragraphs (b) (1), (2), (3), and (4) of this category.

* * * * *

Dated: December 23, 1996.

Lynn E. Davis,

Under Secretary of State for Arms Control and International Security Affairs.

[FR Doc. 96-33010 Filed 12-26-96; 8:45 am]

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DEPARTMENT OF THE TREASURY**Internal Revenue Service****26 CFR Parts 1 and 602**

[TD 8702]

RIN 1545-AT42

Certain Transfers of Domestic Stock or Securities by U.S. Persons to Foreign Corporations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to certain transfers of stock or securities of domestic corporations by United States persons to foreign corporations pursuant to the corporate organization, reorganization, or liquidation provisions of the Internal Revenue Code. These final regulations modify the rules contained in the temporary regulations to reflect certain taxpayer comments received in response to those temporary regulations. This

action is necessary to provide the public with guidance to comply with the Tax Reform Act of 1984.

DATES: These regulations are effective January 29, 1997. For dates of applicability of these regulations, see § 1.367(a)-3(c)(11).

FOR FURTHER INFORMATION CONTACT: Philip L. Tretiak at (202) 622-3860 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these final regulations has 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 1545-1478. Responses to these collections of information are required in order for U.S. shareholders that transfer stock or securities in section 367(a) exchanges to qualify for an exception to the general rule of taxation under section 367(a)(1).

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 one-time burden per respondent: 10 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 20224, 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 a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

On May 16, 1986, temporary and proposed regulations under sections 367(a) and (d) and section 6038B were published in the Federal Register (51 FR 17936). These regulations were published to provide the public with guidance necessary to comply with changes made to the Internal Revenue Code by the Tax Reform Act of 1984. The IRS and the Treasury Department later issued Notice 87-85 (1987-2 C.B. 395), which set forth substantial changes to the 1986 regulations, effective with respect to transfers

occurring after December 16, 1987. A further notice of proposed rulemaking, containing rules under section 367(a), as well as under section 367(b), was published in the Federal Register on August 26, 1991 (56 FR 41993). The 1991 proposed section 367(a) regulations were generally based upon the positions announced in Notice 87-85, but the regulations made certain modifications to Notice 87-85, particularly with respect to transfers of stock or securities of foreign corporations. Subsequently, the IRS and the Treasury Department issued Notice 94-46 (1994-1 C.B. 356), announcing modifications to the positions set forth in Notice 87-85 (and the 1991 proposed regulations) with respect to transfers of stock or securities of domestic corporations occurring after April 17, 1994.

Most recently, temporary and proposed regulations were published in the Federal Register on December 26, 1995 (60 FR 66739 and 66771). The temporary regulations, which are generally effective for transfers occurring after April 17, 1994, but cease to be effective when the final regulations take effect, generally incorporated the positions announced in Notice 94-46, with certain modifications. These final regulations generally follow the rules set forth in the temporary regulations, with changes as described below.

Explanation of Provisions

Section 367(a)(1) generally treats a transfer of property (including stock or securities) by a U.S. person to a foreign corporation in connection with an exchange described in section 332, 351, 354, 356 or 361 as a taxable exchange unless the transfer qualifies for an exception to this general rule.

Rules that address transfers of stock or securities of domestic corporations are contained in the final regulations described herein. Rules that address transfers of stock or securities of foreign corporations under section 367(a) are contained in Notice 87-85.

The final regulations retain the general rules set forth in the temporary regulations, which provide that a U.S. person that exchanges stock or securities in a U.S. target company (UST) for stock of a foreign corporation (the transferee foreign corporation (or TFC)) in an exchange described in section 367(a) will qualify for nonrecognition treatment if certain reporting requirements are satisfied and each of the following conditions is met:

(i) U.S. transferors must receive no more than 50 percent of the voting power and value of the stock of the TFC

in the transfer (*i.e.*, the 50-percent ownership threshold is not exceeded);

(ii) U.S. officers, directors and 5-percent or greater shareholders of the U.S. target must not own, in the aggregate, more than 50 percent of the voting power and value of the TFC immediately after the transfer (*i.e.*, the control group case does not apply);

(iii) The U.S. person (exchanging U.S. shareholder) either must not be a 5-percent transferee shareholder immediately after the transfer or, if the U.S. person is a 5-percent transferee shareholder, must enter into a 5-year gain recognition agreement (GRA) with respect to the UST stock or securities it exchanged. (Without such GRA, the transfer by the 5-percent transferee shareholder will not qualify for nonrecognition treatment; however, transfer by other U.S. transferors not subject to the GRA requirement may qualify if all other requirements are met.); and

(iv) The active trade or business requirement must be satisfied.

If one or more of the foregoing requirements is not satisfied, the transfer by the U.S. person of stock or securities of a domestic corporation in exchange for stock of a TFC is taxable under section 367(a).

In response to suggestions from commentators, however, the final regulations make a number of modifications to the temporary regulations, principally in two areas: (i) the treatment of transfers of "other property" in the context of the 50-percent ownership threshold requirement, and (ii) the active trade or business requirement.

Transfers of "Other Property"

Under the temporary regulations, if U.S. transferors receive more than 50 percent of the stock (by vote or value) of the TFC, the 50-percent ownership threshold is exceeded and the transfer is taxable under section 367(a)(1). The temporary regulations define a "U.S. transferor" as a U.S. person who transfers (directly, indirectly or constructively) stock or securities of the U.S. target company or "other property" for stock of the TFC in an exchange described in section 367. Persons who transfer U.S. target company stock or other property are presumed to be U.S. persons.

The inclusion of "other property" in the class of tainted transferred property was designed to prevent the avoidance of the 50-percent ownership threshold through "stuffing" transactions. For example, assume that FC, a foreign corporation, and UST, an unrelated U.S. corporation, seek to combine their

operations in a new foreign joint venture company (JV). The shareholders of each company will transfer their respective stock interests in UST and FC to JV in a transaction that would qualify as a section 351 exchange unless the transaction was taxable under section 367(a)(1). Assume that FC has all foreign shareholders. The value of the stock of UST is 550x; the value of the stock of FC is 450x. Because UST is more valuable than FC, UST's shareholders would receive more than 50 percent of JV's stock. Consequently, even if the transaction would otherwise qualify for an exception to the general rule of taxation under section 367(a)(1), the transaction would be taxable because the 50-percent ownership threshold would be exceeded. If, however, a U.S. person (X) contributed at least 100x in cash (or property) to JV, JV would not issue more than 50 percent of its stock to the UST shareholders, and, therefore, the 50-percent ownership threshold would not be exceeded. The temporary regulations, however, treat X as a U.S. transferor, so that the 50-percent ownership threshold would be exceeded in this case.

Commentators have pointed out that the term "other property" raises issues in the joint venture context that are broader than the "stuffing" example described above. Because the term "other property" is broad enough to include stock of a foreign company, the transfer of UST stock could be taxable under section 367(a)(1) even if UST were less valuable than the foreign "target" company (i.e., in cases where U.S. transferors would receive less than 50 percent of the stock of the joint venture company/TFC). Assume similar facts as in the earlier example, except that FC is widely-held and the shareholders of UST receive 40 percent of the stock of JV, while the shareholders of FC receive the remaining 60 percent. No cash or any other property is transferred to the JV. In such case, if the stock of FC constitutes "other property," UST shareholders would not qualify for an exception to section 367(a)(1) if they were unable to prove that the U.S. shareholders of FC, if any, received no more than 10 percent of the stock of JV in the exchange.

Although the IRS and the Treasury Department remain concerned with "stuffing" transactions, the final regulations consider the active trade or business test to be the primary safeguard for preventing tax-motivated transactions from qualifying for an exception under these section 367(a) regulations. In particular, because the active trade or business test addresses

"stuffing" transactions that occur within the 36-month period prior to the acquisition, the final regulations eliminate consideration of transfers of other property with regard to the 50-percent ownership threshold. Thus, any TFC stock received by U.S. persons in exchange for transfers of other property will not be taken into account in determining whether the 50-percent ownership threshold is exceeded.

Active Trade or Business Test: In General

The final regulations modify the "active trade or business" requirement that must be satisfied for a U.S. transferor to qualify for an exception to the general rule of taxability under section 367(a)(1).

Under the requirement contained in the temporary regulations, no exception under section 367(a)(1) is available unless (i) the TFC or an affiliate was engaged in an active trade or business for the entire 36-month period prior to the exchange (the 36-month test), and (ii) such business was substantial in relation to the business of the U.S. target company (the substantiality test). For this purpose, an affiliate is generally defined by reference to the rules in section 1504(a) (without the exclusion of foreign corporations).

The active trade or business test under the final regulations includes (i) a modified 36-month test, (ii) a new anti-avoidance rule requiring that the transaction not be undertaken with an intention that the TFC cease its active trade or business, and (iii) a modified substantiality test. The final regulations make a number of other modifications and clarifications to the active trade or business test. For example, the final regulations permit the TFC to consider only an 80-percent owned foreign subsidiary (referred to as a "qualified subsidiary"), and not an affiliate, to satisfy the active trade or business test on its behalf.

Active Trade or Business Test: 36-Month Test and Intent Test

Under the 36-month test contained in the temporary regulations, the TFC or an affiliate is required to be engaged in an active trade or business for the entire 36 months immediately preceding the date of the transfer. Under the final regulations, this test can be satisfied by acquired businesses that have a 36-month operating history, unless they are acquired with the principal purpose of satisfying the active trade or business test.

In addition to the 36-month test, the active trade or business test in the final regulations contains a requirement that

the transaction not be undertaken with an intention that the TFC cease its active business. The IRS and the Treasury Department believe that if a TFC with a 36-month active business history does not intend to maintain such business, but is only used as a vehicle to acquire the UST, an "inversion" transaction rather than a synergy of two businesses has been effected.

Under the temporary regulations, there is uncertainty as to whether an affiliate of a newly-formed TFC can satisfy the active trade or business test on behalf of the TFC for the (36-month) period prior to the exchange. Subject to a stuffing rule, the final regulations clarify that, for purposes of determining whether a TFC satisfies the 36-month test, the TFC may take into account an active business of a company that is a qualified subsidiary immediately after the transaction, even if such company was not a qualified subsidiary for all or part of the 36 months prior to the transaction. Thus, for example, if the TFC is a new foreign joint venture company, it will not be disqualified from satisfying the active trade or business test solely because its qualifying active trade or business was engaged in by a qualified subsidiary whose stock is received in the exchange.

Under the temporary regulations, it is unclear whether a newly-formed joint venture TFC could satisfy the active trade or business test if, in the transaction, it received both stock of a UST (from U.S. transferors) and an active trade or business (i.e., a foreign branch) that had been operating for at least 36 months prior to the exchange (from foreign transferors). This uncertainty arose because the active trade or business test in the temporary regulations required that either the TFC or an affiliate satisfy the 36-month requirement. Although the temporary regulations did not intend to establish a preference for transfers of stock (i.e., affiliates) vis-a-vis assets, the temporary regulations did not expressly provide that a TFC could utilize a newly-transferred foreign branch to satisfy the TFC's active trade or business requirement.

The final regulations clarify that, subject to a stuffing rule, the TFC may satisfy the active trade or business test if it receives in the exchange foreign assets that constituted an active trade or business during such 36-month period.

Active Trade or Business Test: Qualified Subsidiaries

The final regulations permit a TFC to take into account only qualified subsidiaries, rather than affiliates, to satisfy the active trade or business test.

This aspect of the active trade or business test has been narrowed because the IRS and the Treasury Department do not believe that a TFC should satisfy the active trade or business exception merely because its parent company (or an affiliate of the parent company) is engaged in an active trade or business.

For example, assume that foreign parent (FP), which is engaged in an active business outside the United States (either directly or through a subsidiary), forms a foreign subsidiary (FS) and contributes cash to FS. Shareholders of a U.S. target company (UST) then transfer all of the stock of UST in exchange for 20 percent of the stock of FS in a transaction described in sections 368(a)(1)(B) and 367(a). If FS is permitted to satisfy the active trade or business test by taking into account FP's business, UST has effectively "gone offshore" in an inversion transaction. Because the shareholders of UST receive stock of FS (which is the TFC), and not FP, such shareholders will have no interest in FP's active business. In contrast, if the shareholders received stock of FP in an exchange described in section 367(a), such persons would participate in FP's active business, and the active trade or business test under the final regulations would be satisfied.

Active Trade or Business Test: Partnership Interests

The temporary regulations did not address whether the TFC could satisfy the active trade or business requirement by taking into account an interest in a partnership engaged in an active trade or business.

The final regulations permit a TFC (or a qualified subsidiary) to take into account the active trade or business engaged in outside the United States by any qualified partnership as there defined.

Active Trade or Business Test: Substantiality Test

Under the temporary regulations, the second prong of the active trade or business requirement is the substantiality test. The active trade or business of the TFC is required to be "substantial" vis-a-vis the active trade or business of the UST, but the temporary regulations do not define substantiality.

The final regulations modify the substantiality requirement. Under the final regulations, the substantiality test no longer compares the active trade or business of the TFC vis-a-vis the UST. Instead, it requires that the entire value of the TFC be at least equal to the entire value of the UST at the time of the transaction. However, for this purpose,

the value of the TFC may include the value of assets (including stock) acquired within the 36-month period prior to the transaction only if (i) such assets were acquired in the ordinary course of business, or (ii) such assets (or their proceeds) do not produce and are not held for the production of passive income (as defined under section 1296(b)), and were not acquired with the principal purpose of satisfying the active trade or business test. A special rule applies if the asset acquired by the TFC in the 36-month period prior to the exchange is stock of a qualified subsidiary or qualified partnership engaged in an active trade or business. In such case, the value of the stock or partnership interest may be taken into account, but must be reduced in accordance with the principles described above.

When formulating the substantiality test under the final regulations, the IRS and the Treasury Department considered and rejected other alternatives considered to be more complex and burdensome for taxpayers. For example, a comparison of the active business of the TFC vis-a-vis the active business of the UST for the 36-month period prior to the acquisition, taking into account the property, payroll and sales of the two companies, was considered and rejected.

Indirect and Constructive Transfers

One commentator suggested that the IRS clarify the definition of "U.S. Transferor" contained in the temporary regulations, which refers to a U.S. person who transfers "directly, indirectly or constructively" UST stock or other property. The IRS and the Treasury Department believe that the reference to "direct, indirect and constructive" transfers may have been unclear and, thus, the final regulations delete such reference. Such technical modification does not modify the substantive law in which indirect and constructive transfers may be treated as transfers subject to section 367(a)(1) (see § 1.367(a)-1T(c)(2) with respect to the "indirect" stock transfer rules; constructive transfers include, but are not limited to, section 367(a) transfers that result from section 304 transactions and section 367(a) transfers that result from a change in classification of an entity from a foreign partnership to a foreign corporation).

GRA Term

Under the temporary regulations, a 5-percent transferee shareholder is required to file a GRA. The duration is 5 years if all U.S. transferors own less than 50 percent of the total voting

power and total value of the TFC stock immediately after the transfer. The duration of the GRA is 10 years if the U.S. transferors own 50 percent or more of the TFC stock immediately after the transaction, or if the 5-percent transferee shareholder is unable to prove that all U.S. transferors own less than 50 percent of the total voting power and total value of the TFC immediately after the transfer. Thus, in determining whether a 5- or 10-year GRA is appropriate, the temporary regulations take into account cross-ownership (*i.e.*, consideration of stock owned independently of the transaction) by all U.S. transferors, and contain a presumption that a 10-year GRA is required.

For example, assume that UST shareholders receive 30 percent of the stock of the TFC in a nonrecognition transaction that qualifies for an exception under section 367(a). Assume further that one UST shareholder, X, a U.S. person, transfers stock of UST in the section 367(a) exchange and owns 5 percent of the TFC after the transaction. Under the temporary regulations, X is required to file a 10-year GRA unless X can prove that all U.S. transferors in the aggregate own less than 50 percent of the voting power and value of the TFC immediately after the transfer (taking into account the 30 percent received in the transaction by U.S. target shareholders plus any other stock that such persons may own independently of the transaction). If the companies are publicly traded or widely held, it is burdensome and may be impractical for X to rebut the presumption that U.S. transferors own 50 percent or more of the TFC stock.

In response to comments received and in the interest of simplification, the final regulations provide that any 5-percent transferee shareholder that is required to file a GRA upon the transfer of domestic stock or securities is required to file a 5-year GRA; 10-year GRAs will no longer be required in the case of 5-percent transferee shareholders who transfer domestic stock or securities.

Other Areas in Which Comments Were Received

After careful consideration by the IRS and the Treasury Department, the positions set forth in the temporary regulations were generally not modified in response to certain comments other than those described above. For example, the final regulations did not modify: (i) The amount of stock U.S. transferors could receive without exceeding the ownership threshold (*i.e.*, not more than 50 percent), (ii) testing the 50-percent ownership threshold at

the time of the exchange, and (iii) the presumption that all shareholders of the U.S. target company are U.S. persons.

PLR Option in Limited Instances

The final regulations provide that, in limited instances, the IRS may consider issuing private letter rulings to taxpayers that (i) satisfy all of the requirements contained in these regulations, with the exception of the active trade or business test, or (ii) make a good faith effort, but are unable to establish non-adverse applicability of the ownership attribution rules. The IRS and the Treasury Department are aware that the active trade or business test is mechanical in nature and, thus, in limited instances, a taxpayer may demonstrate an ongoing and substantial active trade or business even though it fails to meet the test set forth in the final regulations. However, in no event will the IRS rule on the issue of whether a TFC acquired an active business with the principal purpose of satisfying the 36-month test and/or the substantiality test.

Other Matters

The IRS and the Treasury Department expect to issue additional final regulations under section 367(a) to address the transfer of stock or securities of foreign corporations and other matters contained in the 1991 proposed regulations not addressed herein. Until the 1991 proposed regulations are finalized, the positions originally announced in Notice 87-85 will continue to govern the availability of section 367(a) exceptions for transfers of stock or securities of foreign corporations. See § 1.367(a)-3(d).

Special Analyses

It has been determined that this regulation is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It is hereby certified that this regulation does not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the number of U.S. target companies that are acquired by foreign corporations in nonrecognition transactions subject to section 367(a), and thus are subject to collection of information, is estimated to be only 100 per year. Moreover, because these regulations will primarily affect large shareholders and U.S. multinational corporations with foreign operations, it is estimated that very few of the 100 transactions will involve small entities. Thus, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C.

chapter 6) is not required. Pursuant to section 7805(f) of the Code, the 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 Philip L. Tretiak of the Office of Associate Chief Counsel (International), within the Office of Chief Counsel, 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 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 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 1.367(a)-3 is added to read as follows:

§ 1.367(a)-3 Treatment of transfers of stock or securities to foreign corporations.

(a) *In general.* This section provides rules concerning the transfer of stock or securities by a U.S. person to a foreign corporation in an exchange described in section 367(a). In general, a transfer of stock or securities by a U.S. person to a foreign corporation that is described in sections 351, 354 (pursuant to a reorganization described in section 368(a)(1)(B)) or section 361 (a) or (b) is subject to section 367(a)(1) and, therefore, is treated as a taxable exchange, unless one of the exceptions set forth in paragraph (c) or (d) of this section or § 1.367(a)-3T(b) applies. For additional rules relating to an exchange involving a foreign corporation in connection with which there is a transfer of stock, see section 367(b) and the regulations under that section. For additional rules regarding a transfer of stock or securities in an exchange described in section 361 (a) or (b), see section 367(a)(5) and any regulations under that section.

(b) [Reserved] For further guidance, see § 1.367(a)-3T(b).

(c) *Transfers by U.S. persons of stock or securities of domestic corporations to foreign corporations—*(1) *In general.*

Except as provided in section 367(a)(5), a transfer of stock or securities of a domestic corporation by a U.S. person to a foreign corporation that would otherwise be subject to section 367(a)(1) under paragraph (a) of this section shall not be subject to section 367(a)(1) if the domestic corporation the stock or securities of which are transferred (referred to as the U.S. target company) complies with the reporting requirements in paragraph (c)(6) of this section and if each of the following four conditions is met:

(i) Fifty percent or less of both the total voting power and the total value of the stock of the transferee foreign corporation is received in the transaction, in the aggregate, by U.S. transferors (*i.e.*, the amount of stock received does not exceed the 50-percent ownership threshold).

(ii) Fifty percent or less of each of the total voting power and the total value of the stock of the transferee foreign corporation is owned, in the aggregate, immediately after the transfer by U.S. persons that are either officers or directors of the U.S. target company or that are five-percent target shareholders (as defined in paragraph (c)(5)(iii) of this section) (*i.e.*, there is no control group). For purposes of this paragraph (c)(1)(ii), any stock of the transferee foreign corporation owned by U.S. persons immediately after the transfer will be taken into account, whether or not it was received in the exchange for stock or securities of the U.S. target company.

(iii) Either—

(A) The U.S. person is not a five-percent transferee shareholder (as defined in paragraph (c)(5)(ii) of this section); or

(B) The U.S. person is a five-percent transferee shareholder and enters into a five-year agreement to recognize gain with respect to the U.S. target company stock or securities it exchanged in the form provided in § 1.367(a)-3T(g); and

(iv) The active trade or business test (as defined in paragraph (c)(3) of this section) is satisfied.

(2) *Ownership presumption.* For purposes of paragraph (c)(1) of this section, persons who transfer stock or securities of the U.S. target company in exchange for stock of the transferee foreign corporation are presumed to be U.S. persons. This presumption may be rebutted in accordance with paragraph (c)(7) of this section.

(3) *Active trade or business test—*(i) *In general.* The tests of this paragraph (c)(3), collectively referred to as the

active trade or business test, are satisfied if:

(A) The transferee foreign corporation or any qualified subsidiary (as defined in paragraph (c)(5)(vii) of this section) or any qualified partnership (as defined in paragraph (c)(5)(viii) of this section) is engaged in an active trade or business outside the United States, within the meaning of § 1.367(a)-2T(b) (2) and (3), for the entire 36-month period immediately before the transfer;

(B) At the time of the transfer, neither the transferors nor the transferee foreign corporation (and, if applicable, the qualified subsidiary or qualified partnership engaged in the active trade or business) have an intention to substantially dispose of or discontinue such trade or business; and

(C) The substantiality test (as defined in paragraph (c)(3)(iii) of this section) is satisfied.

(ii) *Special rules.* For purposes of paragraphs (c)(3)(i) (A) and (B) of this section, the following special rules apply:

(A) The transferee foreign corporation, a qualified subsidiary, or a qualified partnership will be considered to be engaged in an active trade or business for the entire 36-month period preceding the exchange if it acquires at the time of, or any time prior to, the exchange a trade or business that has been active throughout the entire 36-month period preceding the exchange. This special rule shall not apply, however, if the acquired active trade or business assets were owned by the U.S. target company or any affiliate (within the meaning of section 1504(a) but excluding the exceptions contained in section 1504(b) and substituting "50 percent" for "80 percent" where it appears therein) at any time during the 36-month period prior to the acquisition. Nor will this special rule apply if the principal purpose of such acquisition is to satisfy the active trade or business test.

(B) An active trade or business does not include the making or managing of investments for the account of the transferee foreign corporation or any affiliate (within the meaning of section 1504(a) but excluding the exceptions contained in section 1504(b) and substituting "50 percent" for "80 percent" where it appears therein). (This paragraph (c)(3)(ii)(B) shall not create any inference as to the scope of § 1.367(a)-2T(b) (2) and (3) for other purposes.)

(iii) *Substantiality test*—(A) *General rule.* A transferee foreign corporation will be deemed to satisfy the substantiality test if, at the time of the transfer, the fair market value of the

transferee foreign corporation is at least equal to the fair market value of the U.S. target company.

(B) *Special rules.* (1) For purposes of paragraph (c)(3)(iii)(A) of this section, the value of the transferee foreign corporation shall include assets acquired outside the ordinary course of business by the transferee foreign corporation within the 36-month period preceding the exchange only if either—

(i) Both—

(A) At the time of the exchange, such assets or, as applicable, the proceeds thereof, do not produce, and are not held for the production of, passive income as defined in section 1296(b); and

(B) Such assets are not acquired for the principal purpose of satisfying the substantiality test; or

(ii) Such assets consist of the stock of a qualified subsidiary or an interest in a qualified partnership. See paragraph (c)(3)(iii)(B)(2) of this section.

(2) For purposes of paragraph (c)(3)(iii)(A) of this section, the value of the transferee foreign corporation shall not include the value of the stock of any qualified subsidiary or the value of any interest in a qualified partnership, held directly or indirectly, to the extent that such value is attributable to assets acquired by such qualified subsidiary or partnership outside the ordinary course of business and within the 36-month period preceding the exchange unless those assets satisfy the requirements in paragraph (c)(3)(iii)(B)(1) of this section.

(3) For purposes of paragraph (c)(3)(iii)(A) of this section, the value of the transferee foreign corporation shall not include the value of assets received within the 36-month period prior to the acquisition, notwithstanding the special rule in paragraph (c)(3)(iii)(B)(1) of this section, if such assets were owned by the U.S. target company or an affiliate (within the meaning of section 1504(a) but without the exceptions under section 1504(b) and substituting "50 percent" for "80 percent" where it appears therein) at any time during the 36-month period prior to the transaction.

(4) *Special rules*—(i) *Treatment of partnerships.* For purposes of this paragraph (c), if a partnership (whether domestic or foreign) owns stock or securities in the U.S. target company or the transferee foreign corporation, or transfers stock or securities in an exchange described in section 367(a), each partner in the partnership, and not the partnership itself, is treated as owning and as having transferred, or as owning, a proportionate share of the stock or securities. See § 1.367(a)-1T(c)(3).

(ii) *Treatment of options.* For purposes of this paragraph (c), one or more options (or an interest similar to an option) will be treated as exercised and thus will be counted as stock for purposes of determining whether the 50-percent threshold is exceeded or whether a control group exists if a principal purpose of the issuance or the acquisition of the option (or other interest) was the avoidance of the general rule contained in section 367(a)(1).

(iii) *U.S. target has a vestigial ownership interest in transferee foreign corporation.* In cases where, immediately after the transfer, the U.S. target company owns, directly or indirectly (applying the attribution rules of sections 267(c) (1) and (5)), stock of the transferee foreign corporation, that stock will not in any way be taken into account (and, thus, will not be treated as outstanding) in determining whether the 50-percent threshold under paragraph (c)(1)(i) of this section is exceeded or whether a control group under paragraph (c)(1)(ii) of this section exists.

(iv) *Attribution rule.* Except as otherwise provided in this section, the rules of section 318, as modified by the rules of section 958(b) shall apply for purposes of determining the ownership or receipt of stock, securities or other property under this paragraph (c).

(5) *Definitions*—(i) *Ownership statement.* An ownership statement is a statement, signed under penalties of perjury, stating—

(A) The identity and taxpayer identification number, if any, of the person making the statement;

(B) That the person making the statement is not a U.S. person (as defined in paragraph (c)(5)(iv) of this section);

(C) That the person making the statement either—

(1) Owns less than 1 percent of the total voting power and total value of a U.S. target company the stock of which is described in Rule 13d-1(d) of Regulation 13D (17 CFR 240.13d-1(d)) (or any rule or regulation to generally the same effect) promulgated by the Securities and Exchange Commission under the Securities and Exchange Act of 1934 (15 USC 78m), and such person did not acquire the stock with a principal purpose to enable the U.S. transferors to satisfy the requirement contained in paragraph (c)(1)(i) of this section; or

(2) Is not related to any U.S. person to whom the stock or securities owned by the person making the statement are attributable under the rules of section 958(b), and did not acquire the stock

with a principal purpose to enable the U.S. transferors to satisfy the requirement contained in paragraph (c)(1)(i) of this section;

(D) The citizenship, permanent residence, home address, and U.S. address, if any, of the person making the statement; and

(E) The ownership such person has (by voting power and by value) in the U.S. target company prior to the exchange and the amount of stock of the transferee foreign corporation (by voting power and value) received by such person in the exchange.

(ii) *Five-percent transferee shareholder.* A five-percent transferee shareholder is a person that owns at least five percent of either the total voting power or the total value of the stock of the transferee foreign corporation immediately after the transfer described in section 367(a)(1). For special rules involving cases in which stock is held by a partnership, see paragraph (c)(4)(i) of this section.

(iii) *Five-percent target shareholder and certain other 5-percent shareholders.* A five-percent target shareholder is a person that owns at least five percent of either the total voting power or the total value of the stock of the U.S. target company immediately prior to the transfer described in section 367(a)(1). If the stock of the U.S. target company (or any company through which stock of the U.S. target company is owned indirectly or constructively) is described in Rule 13d-1(d) of Regulation 13D (17 CFR 240.13d-1(d)) (or any rule or regulation to generally the same effect), promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934 (15 USC 78m), then, in the absence of actual knowledge to the contrary, the existence or absence of filings of Schedule 13-D or 13-G (or any similar schedules) may be relied upon for purposes of identifying five-percent target shareholders (or a five-percent shareholder of a corporation which itself is a five-percent shareholder of the U.S. target company). For special rules involving cases in which U.S. target company stock is held by a partnership, see paragraph (c)(4)(i) of this section.

(iv) *U.S. Person.* For purposes of this section, a U.S. person is defined by reference to § 1.367(a)-1T(d)(1). For application of the rules of this section to stock or securities owned or transferred by a partnership that is a U.S. person, however, see paragraph (c)(4)(i) of this section.

(v) *U.S. Transferor.* A U.S. transferor is a U.S. person (as defined in paragraph (c)(5)(iv) of this section) that transfers

stock or securities of one or more U.S. target companies in exchange for stock of the transferee foreign corporation in an exchange described in section 367.

(vi) *Transferee foreign corporation.* A transferee foreign corporation is the foreign corporation whose stock is received in the exchange by U.S. persons.

(vii) *Qualified subsidiary.* A qualified subsidiary is a foreign corporation whose stock is at least 80-percent owned (by total voting power and total value), directly or indirectly, by the transferee foreign corporation. However, a corporation will not be treated as a qualified subsidiary if it was affiliated with the U.S. target company (within the meaning of section 1504(a) but without the exceptions under section 1504(b) and substituting "50 percent" for "80 percent" where it appears therein) at any time during the 36-month period prior to the transfer. Nor will a corporation be treated as a qualified subsidiary if it was acquired by the transferee foreign corporation at any time during the 36-month period prior to the transfer for the principal purpose of satisfying the active trade or business test, including the substantiality test.

(viii) *Qualified partnership.* (A) Except as provided in paragraph (c)(5)(viii)(B) or (C) of this section, a qualified partnership is a partnership in which the transferee foreign corporation—

(1) Has active and substantial management functions as a partner with regard to the partnership business; or

(2) Has an interest representing a 25 percent or greater interest in the partnership's capital and profits.

(B) A partnership is not a qualified partnership if the U.S. target company or any affiliate of the U.S. target company (within the meaning of section 1504(a) but without the exceptions under section 1504(b) and substituting "50 percent" for "80 percent" where it appears therein) held a 5 percent or greater interest in the partnership's capital and profits at any time during the 36-month period prior to the transfer.

(C) A partnership is not a qualified partnership if the transferee foreign corporation's interest was acquired by that corporation at any time during the 36-month period prior to the transfer for the principal purpose of satisfying the active trade or business test, including the substantiality test.

(6) *Reporting requirements of U.S. target company.* (i) In order for a U.S. person that transfers stock or securities of a domestic corporation to qualify for the exception provided by this

paragraph (c) to the general rule under section 367(a)(1), in cases where 10 percent or more of the total voting power or the total value of the stock of the U.S. target company is transferred by U.S. persons in the transaction, the U.S. target company must comply with the reporting requirements contained in this paragraph (c)(6). The U.S. target company must attach to its timely filed U.S. income tax return for the taxable year in which the transfer occurs a statement titled "Section 367(a)—Reporting of Cross-Border Transfer Under Reg. § 1.367(a)-3(c)(6)," signed under penalties of perjury by an officer of the corporation to the best of the officer's knowledge and belief, disclosing the following information—

(A) A description of the transaction in which a U.S. person or persons transferred stock or securities in the U.S. target company to the transferee foreign corporation in a transfer otherwise subject to section 367(a)(1);

(B) The amount (specified as to the percentage of the total voting power and the total value) of stock of the transferee foreign corporation received in the transaction, in the aggregate, by persons who transferred stock or securities of the U.S. target company. For additional information that may be required to rebut the ownership presumption of paragraph (c)(2) of this section in cases where more than 50 percent of either the total voting power or the total value of the stock of the transferee foreign corporation is received in the transaction, in the aggregate, by persons who transferred stock or securities of the U.S. target company, see paragraph (c)(7) of this section;

(C) The amount (if any) of transferee foreign corporation stock owned directly or indirectly (applying the attribution rules of sections 267(c) (1) and (5)) immediately after the exchange by the U.S. target company;

(D) A statement that there is no control group within the meaning of paragraph (c)(1)(ii) of this section;

(E) A list of U.S. persons who are officers, directors or five-percent target shareholders and the percentage of the total voting power and the total value of the stock of the transferee foreign corporation owned by such persons both immediately before and immediately after the transaction; and

(F) A statement that includes the following—

(1) A statement that the active trade or business test described in paragraph (c)(3) of this section is satisfied by the transferee foreign corporation and a description of such business;

(2) A statement that on the day of the transaction, there was no intent on the

part of the transferee foreign corporation (or its qualified subsidiary, if relevant) or the transferors of the transferee foreign corporation (or qualified subsidiary, if relevant) to substantially discontinue its active trade or business; and

(3) A statement that the substantiality test described in paragraph (c)(3)(iii) of this section is satisfied, and documentation that such test is satisfied, including the value of the transferee foreign corporation and the value of the U.S. target company on the day of the transfer, and either one of the following—

(i) A statement demonstrating that the value of the transferee foreign corporation 36 months prior to the acquisition, plus the value of any assets described in paragraph (c)(3)(iii)(B) of this section (including stock) acquired by the transferee foreign corporation within the 36-month period, less the amount of any liabilities acquired during that period, exceeds the value of the U.S. target company on the acquisition date; or

(ii) A statement demonstrating that the value of the transferee foreign corporation on the date of the acquisition, reduced by the value of any assets not described in paragraph (c)(3)(iii)(B) of this section (including stock) acquired by the transferee foreign corporation within the 36-month period, exceeds the value of the U.S. target company on the date of the acquisition.

(ii) For purposes of this paragraph (c)(6), an income tax return will be considered timely filed if such return is filed, together with the statement required by this paragraph (c)(6), on or before the last date for filing a Federal income tax return (taking into account any extensions of time therefor) for the taxable year in which the transfer occurs. If a return is not timely filed within the meaning of this paragraph (c)(6), the District Director may make a determination, based on all facts and circumstances, that the taxpayer had reasonable cause for its failure to file a timely filed return and, if such a determination is made, the requirement contained in this paragraph (c)(6) shall be waived.

(7) *Ownership statements.* To rebut the ownership presumption of paragraph (c)(2) of this section, the U.S. target company must obtain ownership statements (described in paragraph (c)(5)(i) of this section) from a sufficient number of persons that transfer U.S. target company stock or securities in the transaction that are not U.S. persons to demonstrate that the 50-percent threshold of paragraph (c)(1)(i) of this section is not exceeded. In addition, the

U.S. target company must attach to its timely filed U.S. income tax return (as described in paragraph (c)(6)(ii) of this section) for the taxable year in which the transfer occurs a statement, titled "Section 367(a)—Compilation of Ownership Statements Under Reg. § 1.367(a)–3(c)," signed under penalties of perjury by an officer of the corporation, disclosing the following information:

(i) The amount (specified as to the percentage of the total voting power and the total value) of stock of the transferee foreign corporation received, in the aggregate, by U.S. transferors;

(ii) The amount (specified as to the percentage of total voting power and total value) of stock of the transferee foreign corporation received, in the aggregate, by foreign persons that filed ownership statements;

(iii) A summary of the information tabulated from the ownership statements, including—

(A) The names of the persons that filed ownership statements stating that they are not U.S. persons;

(B) The countries of residence and citizenship of such persons; and

(C) Each of such person's ownership (by voting power and by value) in the U.S. target company prior to the exchange and the amount of stock of the transferee foreign corporation (by voting power and value) received by such persons in the exchange.

(8) *Certain transfers in connection with performance of services.* Section 367(a)(1) shall not apply to a domestic corporation's transfer of its own stock or securities in connection with the performance of services, if the transfer is considered to be to a foreign corporation solely by reason of § 1.83–6(d)(1).

(9) *Private letter ruling option.* The Internal Revenue Service may, in limited circumstances, issue a private letter ruling to permit the taxpayer to qualify for an exception to the general rule under section 367(a)(1) if—

(i) A taxpayer is unable to satisfy all of the requirements of paragraph (c)(3) of this section relating to the active trade or business test of paragraph (c)(1)(iv) of this section, but such taxpayer meets all of the other requirements contained in paragraphs (c)(1)(i) through (c)(1)(iii) of this section, and such taxpayer is substantially in compliance with the rules set forth in paragraph (c)(3) of this section; or

(ii) A taxpayer is unable to satisfy any requirement of paragraph (c)(1) of this section due to the application of paragraph (c)(4)(iv) of this section. Notwithstanding the preceding sentence, in no event will the Internal

Revenue Service rule on the issue of whether the principal purpose of an acquisition was to satisfy the active trade or business test, including the substantiality test.

(10) *Examples.* This paragraph (c) may be illustrated by the following examples:

Example 1. Ownership presumption. (i) FC, a foreign corporation, issues 51 percent of its stock to the shareholders of S, a domestic corporation, in exchange for their S stock, in a transaction described in section 367(a)(1).

(ii) Under paragraph (c)(2) of this section, all shareholders of S who receive stock of FC in the exchange are presumed to be U.S. persons. Unless this ownership presumption is rebutted, the condition set forth in paragraph (c)(1)(i) of this section will not be satisfied, and the exception in paragraph (c)(1) of this section will not be available. As a result, all U.S. persons that transferred S stock will recognize gain on the exchange. To rebut the ownership presumption, S must comply with the reporting requirements contained in paragraph (c)(6) of this section, obtaining ownership statements (described in paragraph (c)(5)(i) of this section) from a sufficient number of non-U.S. persons who received FC stock in the exchange to demonstrate that the amount of FC stock received by U.S. persons in the exchange does not exceed 50 percent.

Example 2. Filing of Gain Recognition Agreement. (i) The facts are the same as in *Example 1*, except that FC issues only 40 percent of its stock to the shareholders of S in the exchange. FC satisfies the active trade or business test of paragraph (c)(1)(iv) of this section. A, a U.S. person, owns 10 percent of S's stock immediately before the transfer. All other shareholders of S own less than five percent of its stock. None of S's officers or directors owns any stock in FC immediately after the transfer. A will own 15 percent of the stock of FC immediately after the transfer, 4 percent received in the exchange, and the balance being stock in FC that A owned prior to and independent of the transaction. No S shareholder besides A owns five percent or more of FC immediately after the transfer. The reporting requirements under paragraph (c)(6) of this section are satisfied.

(ii) The condition set forth in paragraph (c)(1)(i) of this section is satisfied because, even after application of the presumption in paragraph (c)(2) of this section, U.S. transferors could not receive more than 50 percent of FC's stock in the transaction. There is no control group because five-percent target shareholders and officers and directors of S do not, in the aggregate, own more than 50 percent of the stock of FC immediately after the transfer (A, the sole five-percent target shareholder, owns 15 percent of the stock of FC immediately after the transfer, and no officers or directors of S own any stock of FC immediately after the transfer). Therefore, the condition set forth in paragraph (c)(1)(ii) of this section is satisfied. The facts assume that the condition set forth in paragraph (c)(1)(iv) of this section is satisfied. Thus, U.S. persons that are not five-percent transferee shareholders will not recognize gain on the exchange of S shares

for FC shares. A, a five-percent transferee shareholder, will not be required to include in income any gain realized on the exchange in the year of the transfer if he files a 5-year gain recognition agreement (GRA) and complies with section 6038B.

Example 3. Control Group. (i) The facts are the same as in *Example 2*, except that B, another U.S. person, is a 5-percent target shareholder, owning 25 percent of S's stock immediately before the transfer. B owns 40 percent of the stock of FC immediately after the transfer, 10 percent received in the exchange, and the balance being stock in FC that B owned prior to and independent of the transaction.

(ii) A control group exists because A and B, each a five-percent target shareholder within the meaning of paragraph (c)(5)(iii) of this section, together own more than 50 percent of FC immediately after the transfer (counting both stock received in the exchange and stock owned prior to and independent of the exchange). As a result, the condition set forth in paragraph (c)(1)(ii) of this section is not satisfied, and all U.S. persons (not merely A and B) who transferred S stock will recognize gain on the exchange.

Example 4. Partnerships. (i) The facts are the same as in *Example 3*, except that B is a partnership (domestic or foreign) that has five equal partners, only two of whom, X and Y, are U.S. persons. Under paragraph (c)(4)(i) of this section, X and Y are treated as the owners and transferors of 5 percent each of the S stock owned and transferred by B and as owners of 8 percent each of the FC stock owned by B immediately after the transfer. U.S. persons that are five-percent target shareholders thus own a total of 31 percent of the stock of FC immediately after the transfer (A's 15 percent, plus X's 8 percent, plus Y's 8 percent).

(ii) Because no control group exists, the condition in paragraph (c)(1)(ii) of this section is satisfied. The conditions in paragraphs (c)(1)(i) and (iv) of this section also are satisfied. Thus, U.S. persons that are not five-percent transferee shareholders will not recognize gain on the exchange of S shares for FC shares. A, X, and Y, each a five-percent transferee shareholder, will not be required to include in income in the year of the transfer any gain realized on the exchange if they file 5-year GRAs and comply with section 6038B.

(11) **Effective date.** This paragraph (c) applies to transfers occurring after January 29, 1997. However, taxpayers may elect to apply this section in its entirety to all transfers occurring after April 17, 1994, provided that the statute of limitations of the affected tax year or years is open.

(d) **Transfers of stock or securities of foreign corporations.** For guidance, see Notice 87-85 (1987-2 C.B. 395). See § 601.601(d)(2) of this chapter.

(e) through (h) [Reserved]. For further guidance, see § 1.367(a)-3T(e) through (h).

Par. 3. In § 1.367(a)-3T, paragraphs (a), (c) and (d) are revised to read as follows:

§ 1.367(a)-3T Treatment of transfers of stock or securities to foreign corporations (temporary).

(a) [Reserved]. For further information, see § 1.367(a)-3(a).

* * * * *

(c) and (d) [Reserved]. For further information, see § 1.367(a)-3(c) and (d).

* * * * *

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

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

Authority: 26 U.S.C. 7805.

Par. 5. Section 602.101, paragraph (c) is amended by revising the entry for 1.367(a)-3T and adding an entry to the table in numerical order to read as follows:

§ 602.101 OMB Control numbers.

* * * * *

(c) * * *

CFR part or section where identified and described	Current OMB control No.
* * * * *	
1.367(a)-3	1545-0026
1.367(a)-3T	1545-1478
1.367(a)-3T	1545-0026
* * * * *	

Margaret Milner Richardson,
Commissioner of Internal Revenue.

Approved: December 11, 1996.
Donald C. Lubick,
Assistant Secretary of the Treasury.
[FR Doc. 96-32375 Filed 12-27-96; 8:45 am]
BILLING CODE 4830-01-U

DEPARTMENT OF LABOR

Employment Standards Administration

Wage and Hour Division

Office of the Secretary

29 CFR Parts 1 and 5

Procedures for Predetermination of Wage Rates (29 CFR Part 1); Labor Standards Provisions Applicable to Contracts Covering Federally Financed and Assisted Construction and to Certain Nonconstruction Contracts (29 CFR Part 5)

AGENCY: Wage and Hour Division, Employment Standards Administration, Office of the Secretary, Labor.

ACTION: Final rule.

SUMMARY: This document adopts as a final rule the continued suspension of the regulations previously issued under the Davis-Bacon and Related Acts at 29 CFR 1.7(d), 29 CFR 5.2(n)(4), and 29 CFR 5.5(a)(1)(ii) and suspended at 58 FR 58954 (Nov. 5, 1993), while the Department conducts additional rulemaking proceedings to determine whether further amendments should be made to those regulations. These regulations govern the employment of "semi-skilled helpers" on federally-financed and federally-assisted construction contracts subject to the prevailing wage standards of the Davis-Bacon and Related Acts (DBRA).

EFFECTIVE DATE: December 30, 1996.

FOR FURTHER INFORMATION CONTACT: William W. Gross, Director, Office of Wage Determinations, Wage and Hour Division, Employment Standards Administration, U.S. Department of Labor, Room S-3028, 200 Constitution Avenue, NW, Washington, DC 20210. Telephone (202) 219-8353. (This is not a toll-free number.)

SUPPLEMENTARY INFORMATION:

I. Paperwork Reduction Act

This rule does not contain any new information collection requirements and does not modify any existing requirements. Thus, the rule contains no reporting or recordkeeping requirements subject to the Paperwork Reduction Act of 1995.

II. Background

On May 28, 1982, the Department published revised final regulations, 29 CFR Part 1, Procedures for Predetermination of Wage Rates, and 29 CFR Part 5, Subpart A—Davis-Bacon and Related Acts Provisions and Procedures (47 FR 23644 and 23658, respectively), which, among other things, would have allowed contractors to use semi-skilled helpers on Davis-Bacon projects at wages lower than those paid to skilled journeymen, wherever the helper classification, as defined in the regulations, was "identifiable" in the area. These rules represented a reversal of a longstanding Department of Labor practice by allowing some overlap between the duties of helpers and the duties of journeymen and laborers. To protect against possible abuse, a provision was included limiting the number of helpers which could be used on a covered project to a maximum of two helpers for every three journeymen. See 29 CFR 1.7(d), 29 CFR 5.2(n)(4), 29 CFR 5.5(a)(1)(ii)(A), and 29 CFR 5.5(a)(4)(iv) (1982).