• How can we best take advantage of clinical information captured electronically using standardized codes to specify the nature of the impairment?

• What do you think about our idea of a more extensive and specific list of impairments based on established diagnoses?

• What should the *general* criteria for inclusion on such a list be?

• What *specific* impairment(s) or kinds of impairments do you believe we should include on such a list, and what specific criteria for inclusion should we use for those impairments (including specific standardized codes if appropriate)?

• How should the rules or procedures for such a list be structured; for example, should we include a list of all of the diagnoses in the regulations, or should we have the list on SSA's Internet site or somewhere else?

• What sources should we consult to create such a list; for example, our Listing of Impairments, the latest edition of the World Health Organization's *International Classification of Diseases* (ICD), and the latest edition of the American Psychiatric Association's *Diagnostic and Statistical Manual of Mental Disorders* (DSM)? Are there individuals and organizations we should also be consulting?

• How should we keep the list up to date?

• We intend to undertake special outreach efforts in order to encourage public discussion regarding potential methods and standards for identifying compassionate allowances, including periodic quarterly hearings. What methods should we use for community outreach, and where should the outreach take place?

We will not respond directly to comments you send us because of this notice. After we consider your comments in response to this notice, we will decide whether and how to revise the rules we use to determine disability. If we propose specific revisions to the rules, we will publish a notice of proposed rulemaking (NPRM) in the **Federal Register**. In accordance with the usual rulemaking procedures we follow, you will have a chance to comment on the revisions we propose when we publish the NPRM, and we will summarize and respond to the significant comments on the NPRM in the preamble to any final rules.

List of Subjects

20 CFR Part 404

Administrative practice and procedure, Blind, Disability benefits, Old-Age, Survivors and Disability Insurance, Reporting and recordkeeping requirements, Social Security.

20 CFR Part 405

Administrative practice and procedure; Blind, Disability benefits; Old-Age, Survivors, and Disability Insurance, Public assistance programs, Reporting and recordkeeping requirements, Social Security, Supplemental Security Income (SSI).

20 CFR Part 416

Administrative practice and procedure, Aged, Blind, Disability benefits, Public assistance programs, Reporting and recordkeeping requirements, Supplemental Security Income (SSI).

Dated: July 24, 2007.

Michael J. Astrue,

Commissioner of Social Security.

[FR Doc. E7–14686 Filed 7–30–07; 8:45 am]

BILLING CODE 4191–02–P

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG–118719–07]

RIN 1545–BG65

Diversification Requirements for Variable Annuity, Endowment, and Life Insurance Contracts

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document proposes changes to the regulations concerning the diversification requirements of section 817(h) of the Internal Revenue Code (Code). The proposed changes would expand the list of holders whose beneficial interests in an investment company, partnership, or trust do not prevent a segregated asset account from looking through to the assets of the investment company, partnership, or trust, to satisfy the requirements of section 817(h). The proposed regulations also would remove the sentence in § 1.817–5(a)(2) that provides that the payment required to remedy an inadvertent diversification failure must be based on the tax that would have been owed by the policyholders if they were treated as receiving the income on the contract. These proposed regulations would affect insurance companies that issue variable contracts and would affect policyholders who purchase such contracts.

DATES: Written or electronic comments and requests for a public hearing must be received by October 29, 2007.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–118719–07), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–118719–07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC, or sent electronically, via the Federal eRulemaking Portal at *http://www.regulations.gov/* (IRS REG–118719–07).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, James Polfer, at (202) 622–3970 (not a toll-free number). Concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, e-mail *Richard A. Hurst@irscousel.treas.gov*.

SUPPLEMENTARY INFORMATION:

Background

Section 817(d) defines a variable contract for purposes of part I of subchapter L of the Code (sections 801–818). For a contract to be a variable contract, it must provide for the allocation of all or a part of the amounts received under the contract to an account that, pursuant to state law or regulation, is segregated from the general asset accounts of the issuing insurance company. In addition, for a life insurance contract to be a variable contract, it must qualify as a life insurance contract for Federal income tax purposes, and the amount of the death benefits (or the period of coverage) must be adjusted on the basis of the investment return and the market value of the segregated asset account; for an annuity contract to be a variable contract, it must provide for the payment of annuities, and the amounts paid in, or the amount paid out, must reflect the investment return and the market value of the segregated asset account; for a contract that provides funding of insurance on retired lives to be a variable contract, the amounts paid in, or the amounts paid out, must reflect the investment return and the market value of the segregated asset account.

Section 817(h)(1) provides that a variable contract that is based on a segregated asset account is not treated as an annuity, endowment, or life insurance contract unless the segregated asset account is adequately diversified in accordance with regulations prescribed by the Secretary. If a

segregated asset account is not adequately diversified for a calendar quarter, then the contracts supported by that segregated asset account are not treated as annuity, endowment, or life insurance contracts for that period and subsequent periods, even if the segregated asset account is adequately diversified in those subsequent periods. Under § 1.817–5(a), if a segregated asset account is not adequately diversified, income earned by that segregated asset account is treated as ordinary income received or accrued by the policyholders. Section 1.817–5(a)(2) provides conditions an issuer of a variable contract must satisfy in order to correct an inadvertent failure to diversify. Rev. Proc. 92–25, 1992–1 CB 741, see § 601.601(d)(2) of this chapter, sets forth in more detail the procedure by which an issuer may request the relief described in § 1.817–5(a)(2).

Congress enacted the diversification requirements of section 817(h) to ''discourage the use of tax-preferred variable annuity and variable life insurance primarily as investment vehicles.'' H.R. Conf. Rep. No. 98–861, at 1055 (1984). In section 817(h)(1), Congress granted the Secretary broad regulatory authority to develop rules to carry out this intent. Congress directed that these standards be imposed because ''by limiting a customer's ability to select specific investments underlying a variable contract, [adequate diversification] will help ensure that a customer's primary motivation in purchasing the contract is more likely to be the traditional economic protections provided by annuities and life insurance.'' S. Prt. 98–169, Vol. I at 546 (1984). A primary directive from Congress to Treasury in enacting the standards was to ''deny annuity or life insurance treatment for investments that are publicly available to investors.'' H.R. Conf. Rep. No. 98–861, at 1055 (1984).

Section 817(h)(4) provides a look-through rule under which taxpayers do not treat the interest in a regulated investment company (RIC) or trust as a single asset of the segregated asset account but rather apply the diversification tests by taking into account the assets of the RIC or trust. Section 817(h) further provides that the look-through rule applies only if all of the beneficial interests in a RIC or trust are held by one or more insurance companies (or affiliated companies) in their general account or segregated asset accounts, or by fund managers (or affiliated companies) in connection with the creation or management of the RIC or trust.

Under § 1.817–5(f)(1), if look-through treatment is available, a beneficial interest in a RIC, real estate investment trust, partnership, or trust that is treated under sections 671 through 679 as owned by the grantor or another person (''investment company, partnership or trust'') is not treated as a single investment of a segregated asset account for purposes of testing diversification. Instead, a pro rata portion of each asset of the investment company, partnership, or trust is treated as an asset of the segregated asset account. Section 1.817–5(f)(2)(i) provides that the look-through rule applies to any investment company, partnership, or trust if (1) All the beneficial interests in the investment company, partnership, or trust are held by one or more segregated asset accounts of one or more insurance companies; and (2) public access to the investment company, partnership, or trust is available exclusively through the purchase of a variable contract (except as otherwise permitted in § 1.817–5(f)(3)).

Under § 1.817–5(f)(3), look-through treatment is not prevented by reason of beneficial interests in an investment company, partnership, or trust that are:

(1) Held by the general account of a life insurance company or a corporation related to a life insurance company, but only if the return on such interests is computed in the same manner as the return on an interest held by a segregated asset account is computed, there is no intent to sell such interests to the public, and a segregated asset account of such life insurance company also holds or will hold a beneficial interest in the investment company, partnership, or trust;

(2) Held by the manager, or a corporation related to the manager, of the investment company, partnership or trust, but only if the holding of the interests is in connection with the creation or management of the investment company, partnership or trust, the return on such interest is computed in the same manner as the return on an interest held by a segregated asset account is computed, and there is no intent to sell such interests to the public;

(3) Held by the trustee of a qualified pension or retirement plan; or

(4) Held by the public, or treated as owned by the policyholders pursuant to Rev. Rul. 81–225, see § 601.601(d)(2) of this chapter, but only if (A) the investment company, partnership or trust was closed to the public in accordance with Rev. Rul. 82–55, 1982–1 CB 12, see § 601.601(d)(2) of this chapter, or (B) all the assets of the segregated asset account are attributable to premium payments made by policyholders before September 26, 1981, to premium payments made in connection with a qualified pension or retirement plan, or to any combination of such premium payments.

Explanation of Provisions

This document contains proposed amendments to 26 CFR part 1 under section 817(h).

The amendments would remove the sentence from § 1.817–5(a)(2) which provides that the amount required to be paid to remedy an inadvertent failure to diversify must be based on the tax that would have been owed by the policyholders if they were treated as receiving the income on the contract for the period or periods of nondiversification.

The amendments also would expand the list of permitted investors in § 1.817–5(f)(3) to include (i) Qualified tuition programs as defined in section 529, (ii) trustees of foreign pension plans established and maintained outside the United States, primarily for the benefit of individuals, substantially all of whom are nonresident aliens, and (iii) accounts that, pursuant to Puerto Rican law or regulation, are segregated from the general asset accounts of the life insurance companies that own the accounts, provided the requirements of section 817(d) and (h) are satisfied (without regard to the requirement the accounts be segregated pursuant to ''State'' law or regulation).

Reasons for Change

1. Proposed Amendment to § 1.817–5(a)(2) (Remedy for Inadvertent Nondiversification

The proposed regulations would remove the sentence in § 1.817–5(a)(2) that provides that the payment required to remedy an inadvertent diversification failure must be based on the tax that would have been owed by the policyholders if they were treated as receiving the income on the contract. In Notice 2007–15, 2007–7 I.R.B. 503 (February 12, 2007), the IRS requested comments on how various correction procedures, including those described in § 1.817–5(a)(2) and Rev. Proc. 92–25, may be improved. Section 5.03(e) and (f) of the Notice specifically requested comments on the computation of the amounts required to be paid under these correction procedures. Moreover, in the past, the provision in § 1.817–5(a)(2) of the amount required to be paid has caused confusion about the scope of the IRS's authority to provide for amounts that depart from the plain language of the regulation. See, for example, Notice 2000–9, 2000–1 C.B. 449 (reduced amount applied for a limited period of

time in the case of failures due to investments in U.S. Treasury securities). See § 601.601(d)(2) of this chapter.

Even with the proposed modification of § 1.817–5(a)(2), the amount required to be paid to remedy an inadvertent failure to diversify remains the amount set forth in Rev. Proc. 92–25, section 4.02. The modification of § 1.817–5(a)(2) will preserve flexibility, however, should the IRS choose to modify this amount by publication in the Internal Revenue Bulletin in response to comments on Notice 2007–15.

2. Expansion of List of Permitted Investors Under § 1.817–5(f)(3)

On July 30, 2003, the Treasury Department and the IRS published a notice of proposed rulemaking (REG–163974–02, 2003–2 CB 595) under section 817 in the **Federal Register** (68 FR 44689), proposing to remove a specific rule that applied to nonregistered partnerships for purposes of testing diversification. Written comments were received both on the proposed regulations and on the need for further guidance under section 817 more generally. Comments on the proposed regulations were taken into account in final regulations (T.D. 9185, 2005–1 CB 752) that were published March 1, 2005 in the **Federal Register** (70 FR 9869). Comments on section 817 more generally covered a broad range of issues. Two of those issues have since been addressed by revenue ruling. See Rev. Rul. 2005–7, 2005–1 CB 464 (concerning application of the look-through rule in the case of tiered regulated investment companies); Rev. Rul. 2007–7, 2007–7 I.R.B. 468 (February 12, 2007) (concluding that an interest held by a permitted investor is not treated as an interest held by the general public for purposes of Rev. Rul. 2003–92, 2003–2 CB 350).

These proposed regulations would expand the list of permitted investors in § 1.817–5(f)(3) to include two categories of holders that were the subject of comments in 2003: (i) Qualified tuition programs as defined in section 529, and (ii) trustees of pension or retirement plans established and maintained outside of the United States primarily for the benefit of individuals substantially all of whom are nonresident aliens.

Section 529 provides for the exemption from Federal income tax of qualified tuition programs. The term ''qualified tuition program'' means a program established and maintained by a state or agency or instrumentality thereof or by one or more eligible educational institutions (A) Under which a person (i) May purchase tuition credits or certificates on behalf of a designated beneficiary which entitle the beneficiary to the waiver or payment of qualified higher education expenses of the beneficiary, or (ii) in the case of a program established and maintained by a State or agency or instrumentality thereof, may make contributions to an account which is established for the purpose of meeting the qualified higher education expenses of the designated beneficiary of the account, and (B) which meets the other requirements of section 529(b).

The Treasury Department and the IRS agree with the 2003 commentators that permitting qualified tuition programs and certain trustees of foreign pension plans to own a beneficial interest in an investment company, partnership, or trust that is also owned by one or more segregated asset accounts would be consistent with the purpose and operation of section 817(h). In addition, neither qualified tuition programs nor the foreign pension plans that are described in the proposed regulations present the possibility of investment by the general public, as that term is used in Rev. Rul. 81–225, 1981–2 CB 12, and Rev. Rul. 2003–92. See also Rev. Rul. 2007–7. The inclusion of qualified tuition programs in the list of permitted investors in § 1.817–5(f)(3) does not relieve those programs of the need to satisfy all requirements of section 529 and the regulations under that section. In particular, the inclusion of such programs does not imply that an investment in a single investment company, partnership, or trust satisfying the minimum diversification requirements of § 1.817–5(b) would necessarily be treated as a permitted investment under section 529, whether as a ''broad-based investment strategy'' within the meaning of Notice 2001–55, 2001–2 C.B. 299 or otherwise. The Treasury Department and the IRS will continue to evaluate other comments received in this area for future guidance by publication in the Internal Revenue Bulletin.

Finally, the proposed regulations would expand the list of permitted investors in § 1.817–5(f)(3) to include investment by an account which, pursuant to Puerto Rican law or regulation, is segregated from the general asset accounts of the life insurance company that owns the account, provided the requirements of section 817(d) and (h) are satisfied (without regard to the requirement that the account be segregated pursuant to ''State'' law or regulation). The Treasury Department and the IRS have received a number of requests for guidance interpreting the term ''variable contract'' to include a contract issued by a Puerto Rican company, based on accounts that are segregated under Puerto Rican law or regulation. One reason for these requests is to ensure that a beneficial interest held by a Puerto Rican company in an investment company, partnership, or trust does not prevent look-through treatment for the other holders of an interest in the same investment, company, partnership, or trust under § 1.817–5(f)(2). The Treasury Department and the IRS believe that expanding the list of permitted investors as proposed would address this issue without implicating the interpretive question of what constitutes a ''State'' within the meaning of sections 817(d) and 7701(a)(10).

Proposed Effective Date

The Treasury Department and the IRS intend these regulations to be effective on the date the final regulations are published in the **Federal Register**.

Special Analyses

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

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are timely submitted to the IRS. In addition to comments on the proposed regulations more generally, the Treasury Department and the IRS specifically request comments on (i) the clarity of the proposed regulations and how they can be made easier to understand; and (ii) whether rules similar to those proposed to apply to accounts that are segregated pursuant to Puerto Rican law or regulation should apply to accounts that are segregated pursuant to the laws or regulations of other territories.

All comments will be available for public inspection and copying. A public hearing may be scheduled if requested

in writing by any person that timely submits written or electronic comments. If a public hearing is scheduled, notice of the date, time, and place for the hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these proposed regulations is James Polfer, Office of the Associate Chief Counsel (Financial Institutions and Products), Internal Revenue Service. However, personnel from other offices of the Treasury Department and the IRS participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAX

Paragraph 1. The authority citation for part 1 is amended by adding an entry in numerical order to read in part as follows:

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

Section 1.817–5 also issued under 26 U.S.C. 817(h). * * *

Par. 2. Section 1.817–5 is amended as follows:

1. The last sentence of paragraph (a)(2)(iii) is removed.

2. Paragraph (f)(3)(iii) is revised.

3. Paragraph (f)(3)(iv) is redesignated as paragraph (f)(3)(vii).

4. New paragraphs (f)(3)(iv) through (vi) are added.

The revisions and additions read as follows:

§ 1.817–5 Diversification requirements for variable annuity, endowment, and life insurance contracts.

* * * * *

(f) * * *

(3) * * *

(iii) Held by the trustee of a qualified pension or retirement plan;

(iv) Held by a qualified tuition program as defined in section 529;

(v) Held by the trustee of a pension plan established and maintained outside of the United States, as defined in section 7701(a)(9), primarily for the benefit of individuals substantially all of whom are nonresident aliens, as defined in section 7701(b)(1)(B);

(vi) Held by an account which, pursuant to Puerto Rican law or regulation, is segregated from the general asset accounts of the life insurance company that owns the account, provided the requirements of section 817(d) and (h) are satisfied. Solely for purposes of this paragraph (f)(3)(vi), the requirement under section 817(d)(1) that the account be segregated pursuant to State law or regulation shall be disregarded; or

* * * * *

Kevin M. Brown,

Deputy Commissioner for Services and Enforcement.

[FR Doc. E7–14620 Filed 7–30–07; 8:45 am]

BILLING CODE 4830–01–P

DEPARTMENT OF DEFENSE

Department of the Army; Corps of Engineers

33 CFR Part 334

Naval Restricted Area, Port Townsend, Indian Island, Walan Point, WA

AGENCY: U.S. Army Corps of Engineers, DoD.

ACTION: Notice of proposed rulemaking and request for comments.

SUMMARY: The U.S. Army Corps of Engineers (Corps) is proposing to amend its regulations for the restricted area established in the waters of Port Townsend Bay off Puget Sound adjacent to Naval Magazine Indian Island, Jefferson County, Washington. The amendments will enable the affected units of the United States military to enhance safety and security around an active military establishment. The regulations are necessary to safeguard military vessels and United States government facilities from sabotage and other subversive acts, accidents, or incidents of similar nature. The regulations are also necessary to protect the public from potentially hazardous conditions that may exist as a result of military use of the area.

DATES: Written comments must be submitted on or before August 30, 2007.

ADDRESSES: You may submit comments, identified by docket number COE–2007–0020, by any of the following methods:

Federal eRulemaking Portal: *http://www.regulations.gov.* Follow the instructions for submitting comments.

E-mail: david.b.olson@usace.army.mil. Include the docket number COE–2007–0020 in the subject line of the message.

Mail: U.S. Army Corps of Engineers, Attn: CECW–CO (David B. Olson), 441 G Street, NW., Washington, DC 20314–1000.

Hand Delivery/Courier: Due to security requirements, we cannot receive comments by hand delivery or courier.

Instructions: Direct your comments to docket number COE–2007–0020. All comments received will be included in the public docket without change and may be made available on-line at *http://www.regulations.gov,* including any personal information provided, unless the commenter indicates that the comment includes information claimed to be Confidential Business Information (CBI) or other information whose disclosure is restricted by statute. Do not submit information that you consider to be CBI, or otherwise protected, through *regulations.gov* or e-mail. The *regulations.gov* Web site is an anonymous access system, which means we will not know your identity or contact information unless you provide it in the body of your comment. If you send an e-mail directly to the Corps without going through *regulations.gov*, your e-mail address will be automatically captured and included as part of the comment that is placed in the public docket and made available on the Internet. If you submit an electronic comment, we recommend that you include your name and other contact information in the body of your comment and with any disk or CD–ROM you submit. If we cannot read your comment because of technical difficulties and cannot contact you for clarification, we may not be able to consider your comment. Electronic comments should avoid the use of any special characters, any form of encryption, and be free of any defects or viruses.

Docket: For access to the docket to read background documents or comments received, go to *www.regulations.gov.* All documents in the docket are listed. Although listed in the index, some information is not publicly available, such as CBI or other information whose disclosure is restricted by statute. Certain other material, such as copyrighted material, is not placed on the Internet and will be publicly available only in hard copy form.

Consideration will be given to all comments received within 30 days of the date of publication of this notice.

FOR FURTHER INFORMATION CONTACT: Mr. David Olson, Headquarters, Operations and Regulatory Community of Practice, Washington, DC at 202–761–4922; Ms. Michelle Walker, Regulatory Branch Chief, U.S. Army Corps of Engineers, Seattle District, Northwest Division, at 206–764–6915; or Ms. Koko Ekendiz of the Regulatory Branch, U.S. Army Corps