

(23 U.S.C. 315; 49 CFR 1.48(b))

Issued on December 9, 1983.

L. P. Lamm,

Deputy Administrator, Federal Highway Administration.

[FR Doc. 83-33483 Filed 12-15-83; 8:45 am]

BILLING CODE 4910-22-M

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[T.D. 7928; LR-57-81]

Source of Income From Certain Leased Aircraft, Vessels, and Spacecraft

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document amends the Income Tax Regulations under section 861(e) of the Internal Revenue Code of 1954, relating to the source of income with respect to certain aircraft, vessels, and spacecraft that are or have been leased to a United States person. This amendment conforms the regulations to the amendment of section 861(e) by the Miscellaneous Revenue Act of 1980. This amendment will affect owners of such craft that are used outside the United States.

DATE: This amendment is effective for income with respect to craft that are first leased after December 28, 1980.

FOR FURTHER INFORMATION CONTACT: Mary Frances Pearson of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3289, not a toll-free call.

SUPPLEMENTARY INFORMATION:

Background

On May 5, 1983, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 861 of the Internal Revenue Code of 1954 (48 FR 20244). These amendments were proposed to conform the regulations to changes made to section 861(e) by section 104 of the Miscellaneous Revenue Act of 1980 (94 Stat. 3523). There were no written comments or requests for a public hearing. Therefore, the regulations are being published as they appeared in the notice of proposed rulemaking except for minor clarifying changes.

Section 861(e), as amended, provides that income with respect to aircraft,

vessels, and spacecraft that are section 38 property (as defined in section 48) and that are manufactured or constructed in the United States will be treated as income from sources within the United States after the craft is leased to a United States person. Income with respect to a craft includes payments for use of the craft and gain on the sale or exchange of the craft. Section 861(e) alters the general statutory rules that (1) payments under a lease of personal property are considered to be from sources within the United States only if the leased property is used within the United States and (2) gain or loss on the sale or exchange of personal property is treated as from sources within the country in which the transfer of title takes place. Thus, this provision modifies the rules for determining the source of income with respect to certain craft that are used or sold outside the United States.

Section 861(e) does not apply if the lessor and the lessee are members of the same controlled group of corporations. For purposes of this section, if either the lessor or the lessee is a partnership at least 80 percent of which is owned by members of a controlled group of corporations, that partnership is considered to be member of the controlled group.

Prior law applies to the income with respect to aircraft and vessels first leased on or before December 28, 1980. Those rules allowed taxpayers to elect to treat the subject income as from sources within the United States. The Miscellaneous Revenue Act of 1980 changed this treatment from elective to mandatory and expanded the scope of the provision to include spacecraft. The statutory source rule was made mandatory to insure that the lease payments from a United States person to the lessor were subject to income taxation by some country. In this regard, see H.R. Rep. No. 96-1278, 96th Cong., 2d Sess. 24 (1980); S. Rep. No. 96-1036, 96th Cong., 2d Sess. 16-17 (1980).

The regulations describe the craft covered by section 861(e) in § 1.861-9A(b). The craft must be section 38 property, that is, property for which an investment tax credit is available. The regulations treat a craft as manufactured or constructed within the United States if at least 50 percent of the basis of the craft on the date it is leased to a United States person is attributable to value added within the United States.

The regulations require that later income with respect to a craft be treated as U.S. source income even after the craft is no longer leased to a United States person or the property ceases to be section 38 property. Under § 1.861-

9A(e) this treatment as U.S. source income also continues when the craft is transferred or distributed if the basis of the craft in the hands of the recipient is determined by reference to the basis it had in the hands of the transferor or distributor.

Drafting Information

The principal author of these regulations is Mary Frances Pearson of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

Regulatory Flexibility Act and Executive Order 12291

These regulations are not subject to the Regulatory Flexibility Act because they are interpretative and thus the notice and public comment procedure requirements of 5 U.S.C. 553 do not apply. The Commissioner of Internal Revenue has determined that these regulations are not subject to Executive Order 12291.

List of Subjects

26 CFR 1.861-1 through 1.997-1

Income taxes, Aliens, Exports, DISC, Foreign investment in U.S., Foreign tax credit, Sources of income, United States investments abroad.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 1 is amended as follows:

PART 1—[AMENDED]

Paragraph 1. Section 1.861-1(a)(4) is revised to read as follows:

§ 1.861-1 Income from sources within the United States.

(a) *Categories of income.* * * *

(4) *Exceptions.* An owner of certain aircraft or vessels first leased on or before December 28, 1980, may elect to treat income in respect of these aircraft or vessels as income from sources within the United States for purposes of sections 861(a) and 862(a). See § 1.861-9. An owner of certain aircraft, vessels, or spacecraft first leased after December 28, 1980, must treat income in respect of these craft as income from sources within the United States for purposes of sections 861(a) and 862(a). See § 1.861-9A.

* * * * *

Par. 2. Section § 1.861-9 is amended as follows:

1. The title of the section is revised to read "Income from certain aircraft or vessels first leased on or before December 28, 1980."

2. The second sentence of paragraph (a) is amended by adding after the word "date", the phrase "of aircraft or vessels first leased by the taxpayer on or before December 28, 1980."

3. A new paragraph (g)(6) is added immediately after paragraph (g)(5), the new paragraph to read as follows:

(g) * * *

(6) *Revocation or termination after December 28, 1980.* The rules in paragraph (g)(1) through (g)(5) continue to apply with respect to any election made pursuant to this section even through the revocation or termination may occur after December 28, 1980.

Par. 3. Section 1.861-9A is added immediately after § 1.861-9, to read as follows:

§ 1.861-9A. *Income from certain craft first leased after December 28, 1980.*

(a) *General rule.* If a taxpayer—

(1) Owns a qualified craft (as defined in paragraph (b) of this section).

(2) Leases such qualified craft after December 28, 1980, to a United States person that is not a member of the same controlled group of corporations as the taxpayer, and

(3) The lease is the taxpayer's first lease of the craft and the taxpayer is not considered to have made an election with respect to the craft under § 1.861-9(e)(2),

then the taxpayer shall treat all amounts includible in gross income with respect to the qualified craft as income from sources within the United States for each taxable year ending after commencement of the lease. If this section applies to income with respect to a craft, it applies to all such amounts that are includible in the taxpayer's gross income, whether or not includible during or after the period of a lease to a United States person. Amounts derived by the taxpayer with respect to the qualified craft include any gain from the sale, exchange, or other disposition of the qualified craft. If this section applies to income with respect to a craft and there is a loss with respect to that craft (either due to the allowance of expenses and other deductions or due to a sale, exchange, or other disposition of the qualified craft), such loss is treated as allocable or apportionable to sources within the United States. The fact that a craft ceases to be section 38 property, ceases to be leased by the taxpayer to a United States person, or is leased or

subleased for any period of time to a person who is not a United States person will not terminate the application of this section.

(b) *Qualified craft.*—(1) *In general.* A qualified craft is a vessel, aircraft, or spacecraft that—

(i) Is section 38 property (or would be section 38 property but for section 48(a)(5), relating to use by governmental units), and

(ii) Is manufactured or constructed in the United States.

(2) *Vessel.* The term "vessel" includes every type of watercraft capable of being used as a means of transportation on water, and any items of property that are affixed in a permanent fashion or are integral to the vessel. A vessel that is used predominately outside the United States must be described in section 48(a)(2)(B)(iii) and § 1.48-1(g)(2)(iii), relating to vessels documented for use in the foreign or domestic commerce of the United States, to be a qualified craft.

(3) *Aircraft.* An aircraft used predominantly outside the United States must be described in section 48(a)(2)(B)(i) and § 1.48-1(g)(2)(i), relating to aircraft registered by the Administrator of the Federal Aviation Agency, and operated to and from the United States or operated under contract with the United States, to be a qualified craft.

(4) *Spacecraft.* A spacecraft must be described in section 48(a)(2)(B)(viii) and § 1.48-1(g)(2)(viii), relating to communications satellites, or any interest therein, of a United States person, to be a qualified craft.

(5) *United States manufacture or construction.* A craft will be considered to be manufactured or constructed in the United States if 50 percent or more of the basis of the craft on the date of the lease to a United States person is attributable to value added within the United States.

(c) *United States person.* For purposes of this section, the term "United States person" includes those persons described in section 7701(a)(30) and individuals with respect to whom an election under section 6013 (g) or (h) (relating to nonresident alien individuals married to United States citizens or residents) is in effect.

(d) *Controlled group.* For purposes of paragraph (a)(2) of this section, whether a taxpayer and a United States person are members of the same controlled group of corporations is determined under section 1563. Solely for purposes of this section, if at least 80% of the capital interest, or the profits interest, in a partnership is owned, directly or indirectly, by a member or members of a

controlled group of corporations, then the partnership shall be considered a member of that controlled group of corporations. In addition, if at least 80% of the capital interest, or the profits interest, in a partnership is owned, directly or indirectly, by a corporation, then the partnership and that corporation shall be considered members of a controlled group of corporations.

(e) *Certain transfers and distributions.*—(1) *Transfers and distributions involving carryover of basis.* If—

(i) The income with respect to a craft is subject to this section,

(ii) The taxpayer transfers or distributes such craft, and

(iii) The basis of such craft in the hands of the transferee or distributee is determined by reference to its basis in the hands of the transferor or distributor,

then this section will apply to the income with respect to the craft includible in the gross income of the transferee or distributee. This paragraph (e)(1) applies even though the transferor or distributor recognizes an amount of gain that increases basis in the hands of the transferee or distributee and even though the transferee or distributee is a nonresident alien or foreign corporation. For example, if a corporation distributes a craft the income of which is subject to this section to its parent corporation in a complete liquidation described in section 332(b), the parent corporation will be treated as if it satisfied the requirements of paragraph (a) of this section with respect to such craft if the basis of the property in the hands of the parent corporation is determined under section 334(b) (relating to the general rule on carryover of basis in liquidations). In further illustration, if a corporation distributes a craft the income of which is subject to this section, in a distribution to which section 301(a) applies, the distributee will be treated as if it satisfied the requirements of paragraph (a) of this section with respect to such craft if its basis is determined under section 301(d)(2) (relating to basis of corporate distributees) even though the basis may be the fair market value of the craft under section 301(d)(2)(A).

(2) *Partnerships.* If a partnership satisfies the requirements of paragraph (a) (1), (2), and (3) of this section, each partner shall treat all amounts includible in gross income with respect to the craft as income from sources within the United States for any taxable year of the partnership ending after commencement of the lease. In addition,

if a partnership distributes a craft the income of which is subject to this section, to a partner, the partner will be treated as if he or she satisfied the requirements of paragraph (a) of this section with respect to such craft.

(3) *Affiliated groups.* If a member of a group of corporations that files a consolidated return transfers a craft, the income of which is subject to this section, to another member of that same group, the transferee will be treated as if it satisfied the requirements of paragraph (a) of this section with respect to the craft.

Par. 4. Section 1.862-1(c) is revised to read as follows:

§ 1.862-1 Income specifically from sources without the United States.

(c) *Income from certain property.* For provisions permitting a taxpayer to elect to treat amounts of gross income attributable to certain aircraft or vessels first leased on or before December 28, 1980, as income from sources within the United States which would otherwise be treated as income from sources without the United States under paragraph (a) of this section, see § 1.861-9. For provisions requiring amounts of gross income attributable to certain aircraft, vessels, or spacecraft first leased by the taxpayer after December 28, 1980, to be treated as income from sources within the United States which would otherwise be treated as income from sources without the United States under paragraph (a) of this section, see § 1.861-9A.

This Treasury decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved:
John E. Chapoton,
Assistant Secretary of the Treasury.

[FR Doc. 83-33537 Filed 12-15-83; 8:45 am]
BILLING CODE 4830-01-M

26 CFR Part 1

[T. D. 7926]

Income Tax; Taxable Years Beginning After December 31, 1953; Income Tax—Return Regarding Corporate Liquidation Within One Calendar Month

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations eliminating a requirement

that additional information be included in the information return of a corporation liquidating within one calendar month. The burden of the requirement is not justified by the use that is made of the additional information.

DATES: These regulations are effective as of December 16, 1983.

FOR FURTHER INFORMATION CONTACT: Charles W. Culmer of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attn: CC:LR:T) (202-566-4336; not a toll-free number).

SUPPLEMENTARY INFORMATION:

Explanation of Provisions

This document contains final amendments to the Income Tax Regulations (26 CFR Part 1) under section 6043(a)(1) of the Internal Revenue Code of 1954. The amendments eliminate paragraph (b)(2) from § 1.6043-1. Paragraph (b)(2) specifies additional information required to be included in the section 6043(a)(1) information return of a corporation liquidating pursuant to section 333 (Form 966). The amendments will permit the deletion of Item 11 from the existing Form 966.

The Internal Revenue Service has determined that paragraph (b)(2) imposes a burden on taxpayers which is not justified by the use which the Service makes of the additional information.

Omission of Notice

Issuance of these regulations was not preceded by publication in the *Federal Register* of a notice of proposed rulemaking and request for comments. These steps were dispensed with as unnecessary because it is believed that these regulations, which liberalize existing requirements, are beneficial to all interested parties.

Executive Order 12291 and Regulatory Flexibility Act

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The Internal Revenue Service has concluded that the regulations contained herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

Drafting Information

The principal author of this Treasury decision is Charles W. Culmer of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in drafting this Treasury decision, both on matters of substance and style.

List of Subjects in 26 CFR 1.6001-1-1.6109-2

Income taxes, Administration and procedure, Filing requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 1 is amended as follows:

PART 1—[AMENDED]

§ 1.6043-1 [Amended]

Section 1.6043-1 is amended by removing paragraph (b)(2) and renumbering paragraph (b)(3) as paragraph (b)(2).

This Treasury decision liberalizes existing rules with respect to information required to be included in the section 6043(a)(1) information return of a corporation liquidating pursuant to section 333. This change does not affect the tax liability of any taxpayer and is considered to be beneficial to all interested parties. For these reasons, it is found unnecessary to issue this Treasury decision with notice and public procedure under 5 U.S.C. 553.

This Treasury decision is issued under the authority contained in Code sections 6043(a)(1) (68A Stat. 746, 26 U.S.C. 6043(a)(1)) and 7805 (68A Stat. 917, 26 U.S.C. 7805).

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved: December 2, 1983.
John E. Chapoton,
Assistant Secretary of the Treasury.
[FR Doc. 83-33541 Filed 12-15-83; 8:45 am]
BILLING CODE 4830-01-M

26 CFR Parts 1 and 15b

[T.D. 7927]

Income Tax; Taxable Years Beginning After December 31, 1953; Amortization of Reforestation Expenditures

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to an election under which taxpayers may amortize up to \$10,000 of qualified reforestation expenditures over a seven-year period. Changes to the applicable tax law were made by the Recreational Boating Safety and Facilities Improvement Act of 1980 and the Subchapter S Revision Act of 1982. These regulations provide guidance to taxpayers who make expenditures to pay for planting or seeding areas for forestation or reforestation purposes. In addition, a clerical change is being made to the regulations under section 121 of the Internal Revenue Code of 1954 (Code), relating to the exclusion of gain on the sale of a personal residence.

DATES: Generally, the regulations are effective for qualifying reforestation expenditures added to capital accounts after December 31, 1979. The amendments made by the Subchapter S Revision Act of 1982 are effective for taxable years beginning after December 31, 1982.

FOR FURTHER INFORMATION CONTACT: Robert B. Coplan of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention CC:LR:T) 202-566-3287, not a toll-free call.

SUPPLEMENTARY INFORMATION:

Background

On March 15, 1983, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under sections 48, 62, 194, and 1245 of the Code (48 FR 10860). The proposed regulations included as a portion thereof, temporary regulations which were published in the Rules and Regulations portion of the same issue of the Federal Register (48 FR 10816). The amendments were proposed to conform the regulations to section 301 of the Recreational Boating Safety and Facilities Improvement Act of 1980 (94 Stat. 1989). The amendments contained in this document also conform the regulations to section 3(g) (1) and (2) of the Subchapter S Revision Act of 1982 (96 Stat. 1689). After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

Changes in Regulations in Response to Comments

The proposed regulations have been clarified in three areas in response to a comment. First, § 1.48-1(p) has been clarified to provide that if a taxpayer incurs more than \$10,000 of qualifying

reforestation expenditures in connection with more than one qualified timber property, and an election to amortize such costs under section 194 is made, the allocation of the \$10,000 limitation among such properties which is selected by the taxpayer under § 1.194-2(b)(2) shall be controlling for purposes of determining which expenditures are eligible for the investment credit. Section 1.48-1(p) also provides that if the taxpayer does not elect to amortize reforestation costs under section 194, for purposes of the investment credit, the taxpayer may select the timber properties to which the \$10,000 limitation is to be allocated.

Second, § 1.48-3(d)(2) is revised to clarify that, for purposes of the investment credit, qualified reforestation expenditures will be considered to be in a condition or state of readiness and availability for a specifically assigned function (*i.e.*, placed in service) in the year in which the expenditures are incurred. This rule will eliminate any question as to when such property is considered to have been placed in service in those cases in which the taxpayer does not elect to amortize costs under section 194.

Finally, the example is § 1.1245-4(h)(2) is expanded in the final regulations to clarify how long a taxpayer must wait to dispose of timber property in order to avoid recapturing the amortization deductions claimed under section 194. The example, as revised, provides that amortization deductions attributable to reforestation expenditures incurred in 1981 will not be recaptured under section 1245 so long as the property to which the expenditures are attributable is not disposed of prior to 1992.

S Corporations

Section 1.194-2(b)(6) of the final regulations clarifies that, for taxable years beginning after December 31, 1982, the rules limiting both a partnership and each partner to \$10,000 in amortizable expenditures each year, apply to S Corporations and their shareholders, as well.

Clerical Amendment

A clerical amendment is being made to § 1.121-4(c) of the regulations (relating to the exclusion of gain on the sale of a residence), in order to provide that the statement filed under such section may be filed with either the Internal Revenue Service Center with which the original election was filed, the Service Center nearest the taxpayer, or the taxpayer's local Internal Revenue office. This liberalizing change conforms the regulations to previously published IRS publications. This change applies to

sales or exchanges after July 26, 1978, in taxable years ending after such date.

Special Analyses

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although a notice of proposed rulemaking which solicited public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirement of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

Paperwork Reduction Act

The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved at OMB.

Drafting Information

The principal author of this regulation is Robert B. Coplan of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations both on matters of substance and style.

List of Subjects

26 CFR 1.0-1.58-8

Income taxes, Tax liability, Tax rates, Credits.

26 CFR 1.61-1-1.281-4

Income taxes, Taxable income, Deductions, Exemptions.

26 CFR 1.1201-1.1252-2

Income taxes, Capital gains and losses, Recapture.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Parts 1 and 15b are amended as follows:

PART 1—[AMENDED]

Paragraph 1. Section 1.48-3 is amended by adding a new paragraph (d) (2)(iv) immediately after paragraph (d) (2)(iii) thereof, and by revising paragraph (e)(4) to read as follows:

§ 1.46-3 Qualified investment.

(d) * * *

(2) * * *

(iv) Reforestation expenditures (as defined in § 1.194-3(c)) are incurred during the taxable year in connection with qualified timber property (as defined in § 1.194-3(a)).

(e) *Estimated useful life*—* * *

(4) *Useful life of property subject to amortization*—(i) *In general.* In the case of property with respect to which amortization in lieu of depreciation is allowable, the term over which amortization deductions are taken shall be considered as the estimated useful life of such property.

(ii) *Qualified timber property.* In the case of qualified timber property (within the meaning of section 194(c)(1)), the normal growing period of such property shall be considered its estimated useful life.

Par. 2. Section 1.48-1 is amended by revising the first sentence of paragraph (b)(1) and by adding a new paragraph (p) in the appropriate place as follows:

§ 1.48-1 Definition of section 38 property.(b) *Depreciation allowable.* (1)

Property (with the exception of property described in section 48(a)(1)(F) and paragraph (p) of this section) is not section 38 property unless a deduction for depreciation (or amortization in lieu of depreciation) with respect to such property is allowable to the taxpayer for the taxable year. * * *

(p) *Qualified timber property.* (1)

Qualified timber property (within the meaning of section 194(c)(1)) shall be treated as section 38 property to the extent of the portion of the basis of such property which is the amortizable basis (as defined in § 1.194-3(b)) acquired during the taxable year and taken into account under section 194 (after applying the limitation of section 194(b)(1)). Such amortizable basis shall qualify as section 38 property whether or not an election is made under section 194. However, any portion of such amortizable basis which is attributable to property which otherwise qualifies as section 38 property shall not be treated as section 38 property under section 48(a)(1)(F) and this paragraph. For example, amortizable basis attributable to depreciation on equipment would not qualify as section 38 property under this paragraph if such equipment qualifies as section 38 property under sections 48(a)(1) (A) or (B). In determining the

portion of amortizable basis which qualifies as section 38 property under this paragraph, the reduction in amortizable basis to account for depreciation sustained with respect to property used in the reforestation process (which otherwise qualifies as section 38 property) shall be applied before the \$10,000 limitation on eligible costs under section 194(b)(1). For example, if in a taxable year a taxpayer incurs qualifying reforestation cost resulting in \$12,000 of amortizable basis with respect to property for which an election is in effect, and \$2,000 of these costs are attributable to depreciation of the taxpayer's equipment, such \$12,000 would first be reduced by the \$2,000 of depreciation, and the \$10,000 limitation under section 194(b)(1) would be applied following such reduction.

(2) If a taxpayer makes an election to amortize reforestation expenditures under section 194, and allocates the \$10,000 limitation among more than one property under § 1.194-2(b)(2), then such allocation shall apply for purposes of determining the amortizable basis that qualifies as section 38 property under paragraph (p)(1) of this section. If no election is made under section 194, the taxpayer may select the manner in which the \$10,000 limitation is to be allocated among the qualified timber properties.

Par. 3. Section 1.62-1(c) is amended by changing the periods at the end of paragraphs (c) (15) and (16) to semicolons, and by adding a new paragraph (c)(17) to read as set forth below:

§ 1.62-1 Adjusted gross income.

(c) * * *

(17) The deduction allowed by section 194 for the amortization of reforestation expenditures.

Par. 4. The third sentence of § 1.121-4 (c) is amended by removing the phrase "the district director with whom the election was filed", and inserting in lieu thereof, "either the Internal Revenue Service Center with which the election was filed, the Internal Revenue Service Center nearest the taxpayer at the time the statement is filed, or the taxpayer's local Internal Revenue office".

Par. 5. New §§ 1.194-1 through 1.194-4 are added in the appropriate place to read as follows:

§ 1.194-1 Amortization of reforestation expenditures.

(a) *In general.* Section 194 allows a taxpayer to elect to amortize over an 84-month period, up to \$10,000 of reforestation expenditures as defined in § 1.194-3(c) incurred by the taxpayer in

a taxable year in connection with qualified timber property (as defined in § 1.194-3(a)). The election is not available to trusts. Only those reforestation expenditures which result in additions to capital accounts after December 31, 1979 are eligible for this special amortization.

(b) *Determination of amortization period.* The amortization period must begin on the first day of the first month of the last half of the taxable year during which the taxpayer incurs the reforestation expenditures. For example, the 84-month amortization period begins on July 1 of a taxable year for a calendar year taxpayer, regardless of whether the reforestation expenditures are incurred in January or December of that taxable year. Therefore, a taxpayer will be allowed to claim amortization deductions for only six months of each of the first and eighth taxable years of the period over which the reforestation expenditures will be amortized.

(c) *Recapture.* If a taxpayer disposes of qualified timber property within ten years of the year in which the amortizable basis was created and the taxpayer has claimed amortization deductions under section 194, part or all of any gain on the disposition may be recaptured as ordinary income. See section 1245.

§ 1.194-2 Amount of deduction allowable.

(a) *General rule.* The allowable monthly deduction with respect to reforestation expenditures made in a taxable year is determined by dividing the amount of reforestation expenditures made in such taxable year (after applying the limitations of paragraph (b) of this section) by 84. In order to determine the total allowable amortization deduction for a given month, a taxpayer should add the monthly amortization deductions computed under the preceding sentence for qualifying expenditures made by the taxpayer in the taxable year and the preceding seven taxable years.

(b) *Dollar limitation*—(1) *Maximum amount subject to election.* A taxpayer may elect to amortize up to \$10,000 of qualifying reforestation expenditures each year under section 194. However, the maximum amortizable amount is \$5,000 in the case of a married individual (as defined in section 143) filing a separate return. No carryover or carryback of expenditures in excess of \$10,000 is permitted. The maximum annual amortization deduction for expenditures incurred in any taxable year is \$1,428.57 (\$10,000/7). The maximum deduction in the first and eighth taxable years of the amortization

period is one-half that amount, or \$714.29, because of the half-year convention provided in § 1.194-1(b). Total deductions for any one year under this section will reach \$10,000 only if a taxpayer incurs and elects to amortize the maximum \$10,000 of expenditures each year over an 8-year period.

(2) *Allocation of amortizable basis among taxpayer's timber properties.* The limit of \$10,000 on amortizable reforestation expenditures applies to expenditures paid or incurred during a taxable year on all of the taxpayer's timber properties. A taxpayer who incurs more than \$10,000 in qualifying expenditures in connection with more than one qualified timber property during a taxable year may select the properties for which section 194 amortization will be elected as well as the manner in which the \$10,000 limitation on amortizable basis is allocated among such properties. For example, A incurred \$10,000 of qualifying reforestation expenditures on each of four properties in 1981. A may elect under section 194 to amortize \$2,500 of the amount spent on each property, \$5,000 of the amount spent on any two properties, the entire \$10,000 spent on any one property, or A may allocate the \$10,000 maximum amortizable basis among some or all of the properties in any other manner.

(3) *Basis—(i) In general.* Except as provided in paragraph (b)(3)(ii) of this section, the basis of a taxpayer's interest in qualified timber property for which an election is made under section 194 shall be adjusted to reflect the amount of the section 194 amortization deduction allowable to the taxpayer.

(ii) *Special rule for trusts.* Although a trust may be a partner of a partnership, income beneficiary of an estate, or (for taxable years beginning after December 31, 1982) shareholder of an S corporation, it may not deduct its allocable share of a section 194 amortization deduction allowable to such a partnership, estate, or S corporation. In addition, the basis of the interest held by the partnership, estate, or S corporation in the qualified timber property shall not be adjusted to reflect the portion of the section 194 amortization deduction that is allocable to the trust.

(4) *Allocation of amortizable basis among component members of a controlled group.* Component members of a controlled group (as defined in § 1.194-3(d)) on a December 31 shall be treated as one taxpayer in applying the \$10,000 limitation of paragraph (b)(1) of this section. The amortizable basis may be allocated to any one such member or allocated (for the taxable year of each

such member which includes such December 31) among the several members in any manner, provided that the amount of amortizable basis allocated to any member does not exceed the amount of amortizable basis actually acquired by the member in the taxable year. The allocation is to be made (1) by the common parent corporation if a consolidated return is filed for all component members of the group, or (2) in accordance with an agreement entered into by the members of the group if separate returns are filed. If a consolidated return is filed by some component members of the group and separate returns are filed by other component members, then the common parent of the group filing the consolidated return shall enter into an agreement with those members who do not join in filing the consolidated return allocating the amount between the group filing the return and the other component members of the controlled group who do not join in filing the consolidated return. If a consolidated return is filed, the common parent corporation shall file a separate statement attached to the income tax return on which an election is made to amortize reforestation costs under section 194. See § 1.194-4. If separate returns are filed by some or all component members of the group, each component member to which is allocated any part of the deduction under section 194 shall file a separate statement attached to the income tax return in which an election is made to amortize reforestation expenditures. See § 1.194-4. Such statement shall include the name, address, employer identification number, and the taxable year of each component member of the controlled group, a copy of the allocation agreement signed by persons duly authorized to act on behalf of those members who file separate returns, and a description of the manner in which the deduction under section 194 has been divided among them.

(5) *Partnerships—(i) Election to be made by partnership.* A partnership makes the election to amortize qualified reforestation expenditures of the partnership. See section 703(b).

(ii) *Dollar limitations applicable to partnerships.* The dollar limitations of section 194 apply to the partnership as well as to each partner. Thus, a partnership may not elect to amortize more than \$10,000 of reforestation expenditures under section 194 in any taxable year.

(iii) *Partner's share of amortizable basis.* Section 704 and the regulations thereunder shall govern the determination of a partner's share of a

partnership's amortizable reforestation expenditures for any taxable year.

(iv) *Dollar limitation applicable to partners.* A partner shall in no event be entitled in any taxable year to claim a deduction for amortization based on more than \$10,000 (\$5,000 in the case of a married taxpayer who files a separate return) of amortizable basis acquired in such taxable year regardless of the source of the amortizable basis. In the case of a partner who is a member of two or more partnerships that elect under section 194, the partner's aggregate share of partnership amortizable basis may not exceed \$10,000 or \$5,000, whichever is applicable. In the case of a member of a partnership that elects under section 194 who also has separately acquired qualified timber property, the aggregate of the member's partnership and non-partnership amortizable basis may not exceed \$10,000 or \$5,000 whichever is applicable.

(6) *S corporations.* For taxable years beginning after December 31, 1982, rules similar to those contained in paragraph (b)(5) (ii) and (iv) of this section shall apply in the case of S corporations (as defined in section 1361(a)) and their shareholders.

(7) *Estates.* Estates may elect to amortize in each taxable year up to a maximum of \$10,000 of qualifying reforestation expenditures under section 194. Any amortizable basis acquired by an estate shall be apportioned between the estate and the income beneficiary on the basis of the income of the estate allocable to each. The amount of amortizable basis apportioned from an estate to a beneficiary shall be taken into account in determining the \$10,000 (or \$5,000) amount of amortizable basis allowable to such beneficiary under this section.

(c) *Life tenant and remainderman.* If property is held by one person for life with remainder to another person, the life tenant is entitled to the full benefit of any amortization allowable under section 194 on qualifying expenditures he or she makes. Any remainder interest in the property is ignored for this purpose.

[Approved by the Office of Management and Budget under control number 1545-0735.]

§ 1.194-3 Definitions.

(a) *Qualified timber property.* The term "qualified timber property" means property located in the United States which will contain trees in significant commercial quantities. The property may be a woodlot or other site but must consist of at least one acre which is

planted with tree seedlings in the manner normally used in forestation or reforestation. The property must be held by the taxpayer for the growing and cutting of timber which will either be sold for use in, or used by the taxpayer in, the commercial production of timber products. A taxpayer does not have to own the property in order to be eligible to elect to amortize costs attributable to it under section 194. Thus, a taxpayer may elect to amortize qualifying reforestation expenditures incurred by such taxpayer on leased qualified timber property. Qualified timber property does not include property on which the taxpayer has planted shelter belts (for which current deductions are allowed under section 175) or ornamental trees, such as Christmas trees.

(b) *Amortizable basis.* The term "amortizable basis" means that portion of the basis of qualified timber property which is attributable to reforestation expenditures.

(c) *Reforestation expenditures—(1) In general.* The term "reforestation expenditures" means direct costs incurred to plant or seed for forestation or reforestation purposes. Qualifying expenditures include amounts spent for site preparation, seed or seedlings, and labor and tool costs, including depreciation on equipment used in planting or seeding. Only those costs which must be capitalized and are included in the adjusted basis of the property qualify as reforestation expenditures. Costs which are currently deductible do not qualify.

(2) *Cost-sharing programs.* Any expenditures for which the taxpayer has been reimbursed under any governmental reforestation cost-sharing program do not qualify as reforestation expenditures unless the amounts reimbursed have been included in the gross income of the taxpayer.

(d) *Definitions of controlled group of corporations and component member of controlled group.* For purposes of section 194, the terms "control group of corporations" and "component member" of a controlled group of corporations shall have the same meaning assigned to those terms in section 1583 (a) and (b), except that the phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in section 1583(a)(1).

§ 1.194-4 Time and manner of making election.

(a) *In general.* Except as provided in paragraph (b) of this section, an election to amortize reforestation expenditures under section 194 shall be made by entering the amortization deduction

claimed at the appropriate place on the taxpayer's income tax return for the year in which the expenditures were incurred, and by attaching a statement to such return. The statement should state the amounts of the expenditures, describe the nature of the expenditures, and give the date on which each was incurred. The statement should also state the type of timber being grown and the purpose for which it is being grown. A separate statement must be included for each property for which reforestation expenditures are being amortized under section 194. The election may only be made on a timely return (taking into account extensions of the time for filing) for the taxable year in which the amortizable expenditures were made.

(b) *Special rule.* With respect to any return filed before March 15, 1984, on which a taxpayer was eligible to, but did not make an election under section 194, the election to amortize reforestation expenditures under section 194 may be made by a statement on, or attached to, the income tax return (or an amended return) for the taxable year, indicating that an election is being made under section 194 and setting forth the information required under paragraph (a) of this section. An election made under the provisions of this paragraph (b) must be made not later than,

(1) The time prescribed by law (including extensions thereof) for filing the income tax return for the year in which the reforestation expenditures were made, or

(2) March 15, 1984, whichever is later. Nothing in this paragraph shall be construed as extending the time specified in section 6511 within which a claim for credit or refund may be filed.

(c) *Revocation.* An application for consent to revoke an election under section 194 shall be in writing and shall be addressed to the Commissioner of Internal Revenue, Washington, D.C. 20224. The application shall set forth the name and address of the taxpayer, state the taxable years for which the election was in effect, and state the reason for revoking the election. The application shall be signed by the taxpayer or a duly authorized representative of the taxpayer and shall be filed at least 90 days prior to the time prescribed by law (without regard to extensions thereof) for filing the income tax return for the first taxable year for which the election is to terminate. Ordinarily, the request for consent to revoke the election will not be granted if it appears from all the facts and circumstances that the only reason for the desired change is to obtain a tax advantage.

[Approved by the Office of Management and Budget under control number 1545-0735.]

Part 6. Section 1.1245-4 is amended by adding new paragraphs (g) and (h) at the end thereof to read as follows:

§ 1.1245-4 Exceptions and limitations.

(g) [Reserved]

(h) *Timber property subject to amortization under section 194—(1) In general.* For purposes of section 1245(a)(2), in determining the recomputed basis of property with respect to which a deduction under section 194 was allowed for any taxable year, a taxpayer shall not take into account amortization deductions claimed under section 194 to the extent such deductions are attributable to the amortizable basis (within the meaning of section 194(c)(2)) of the taxpayer acquired before the tenth taxable year preceding the taxable year in which gain with respect to the property is recognized.

(2) *Example.* The principles of paragraph (h)(1) of this section are illustrated by the following example:

Example. Assume A owns qualified timber property (as defined in section 194(c)(1)) with a basis of \$30,000. In 1981, A incurs \$12,000 of qualifying reforestation expenditures and elects to amortize the maximum \$10,000 of such expenses under section 194. The \$10,000 of deductions are taken during the 8-year period from 1981 to 1988. If A sells the property in 1990 for \$60,000 a gain of \$28,000 (\$60,000—adjusted basis of \$32,000) is recognized on the sale. Since the sale took place within 10 years of the taxable year in which the reforestation expenditures were made, \$10,000 of the gain is treated as ordinary income, and the remaining \$18,000 of gain would be capital gain, if it otherwise qualifies for capital gain treatment. In order to avoid ordinary income treatment of the gain attributable to the reforestation expenditures incurred in 1981, A would have to wait until 1992 to dispose of the property.

PART 15b—[REMOVED]

Par. 7. 26 CFR Part 15b is removed.

This Treasury decision is issued under the authority contained in sections 194 (94 Stat. 1989; 26 U.S.C. 194) and 7805 (68A Stat. 917; 26 U.S.C. 7805) of the Internal Revenue Code of 1954.

Roscoe L. Egger, Jr.,

Commissioner of Internal Revenue.

Approved: December 2, 1983.

John E. Chapoton,

Assistant Secretary of the Treasury.

[FR Doc. 83-33539 Filed 12-15-83; 8:43 am]

BILLING CODE 4830-01-M