

**§ 1.6154-5 Definition of estimated tax.**

For taxable years beginning after December 31, 1976, the term "estimated tax" means the excess of—

(a) The amount which the corporation estimates as its income tax liability for the taxable year under section 11 or 1201(a), or subchapter L of chapter 1 of the Code, whichever is applicable, over

(b) The sum of—

(1) Any estimated credits against tax provided by part IV of subchapter A of chapter 1 of the Code, plus

(2) For taxable years ending after February 29, 1980, the amount which the corporation estimates will be the amount of such corporation's overpayment of windfall profit tax imposed by section 4988 of the Code for the taxable year. For this purpose, the amount of such overpayment is the amount by which such corporation's aggregate windfall profit tax liability for the taxable year as a producer of crude oil is reasonably expected to be exceeded by withholding of windfall profit tax for the taxable year.

**Par. 4. Section 1.6654-1 is amended as follows:**

1. By removing, in paragraph (a)(4)(iii), the words "and also minus" and inserting, in their place, the word "minus".

2. By removing, in paragraph (a)(4)(iv), the words "[relating to the credit for tax withheld from wages on account of qualified State individual income taxes]," and inserting, in their place, the words "[relating to the credit for tax withheld from wages on account of qualified State individual income taxes], and minus".

3. By adding a new paragraph (a)(4)(v) immediately after paragraph (a)(4)(iv) as set forth below.

**§ 1.6654-1 Addition to the tax in the case of an individual.**

(a) *In general.* \* \* \*

(4) \* \* \*

(v) For taxable years ending after February 29, 1980, the individual's overpayment of windfall profit tax imposed by section 4986 of the Code for the taxable year. For this purpose, the amount of such overpayment is the sum of (A) the amount by which such individual's aggregate windfall profit tax liability for the taxable year as producer of crude oil is exceeded by withholding of windfall profit tax for the taxable year, and (B) any amount treated under section 6429 or 6430 as an overpayment of windfall profit tax for crude oil removed during the taxable year. The deemed payment date in section 4995(a)(4)(B) for the amount of windfall profit tax withheld with respect to payments for crude oil shall have no effect in the determination of the overpayment of windfall profit tax.

profit tax withheld with respect to payment for crude oil shall have no effect in the determination of the overpayment of windfall profit tax.

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Par. 5. Section 1.6654-2 is amended as follows:

1. By removing, in paragraph (b)(1)(iii), the words "estimated tax, and also minus" and inserting, in their place, the words "estimated tax, minus".

2. By removing, in paragraph (b)(1)(iv), the words "[relating to the credit for tax withheld from wages on account of qualified State individual income taxes]," and inserting, in their place, the words "[relating to the credit for tax withheld from wages on account of qualified State individual income taxes], and minus".

3. By adding a new paragraph (b)(1)(v) immediately after paragraph (b)(1)(iv) as set forth below.

**§ 1.6654-2 Exceptions to imposition of the addition to the tax in the case of individuals.**

(b) *Meaning of terms.* \* \* \*

(1) \* \* \*

(v) For taxable years ending after February 29, 1980, the individual's overpayment of windfall profit tax imposed by section 4986 of the Code for the taxable year. For this purpose, the amount of such overpayment is the sum of (A) the amount by which such individual's aggregate windfall profit tax liability for the taxable year as producer of crude oil is exceeded by withholding of windfall profit tax for the taxable year, and (B) any amount treated under section 6429 or 6430 as an overpayment of windfall profit tax for crude oil removed during the taxable year. The deemed payment date in section 4995(a)(4)(B) for the amount of windfall profit tax withheld with respect to payments for crude oil shall have no effect in the determination of the overpayment of windfall profit tax.

\* \* \* \* \*

Par. 6. Paragraph (b)(5)(ii)(B) of proposed § 1.6655-1 is revised to read as follows:

**§ 1.6655-1 Addition to the tax in the case of a corporation.**

(b) *Amount of underpayment.* \* \* \*

\* \* \* \* \*

(5) *Definition of the term "tax."* \* \* \*

(ii) \* \* \*

(B) For taxable years ending after February 29, 1980, the corporation's overpayment of windfall profit tax imposed by section 4986 of the Code for the taxable year. For this purpose, the amount of such overpayment is the amount by which such corporation's

aggregate windfall profit tax liability for the taxable year as a producer of crude oil is exceeded by withholding of windfall profit tax for the taxable year. The deemed payment date in section 4995(a)(4)(B) for the amount of windfall profit tax withheld with respect to payments for crude oil shall have no effect in the determination of the overpayment of windfall profit tax.

\* \* \* \* \*

Par. 7. Paragraph (c)(1)(ii)(B) of proposed § 1.6655-2 is revised to read as follows:

**§ 1.6655-2 Exceptions to imposition of the addition to the tax in the case of corporations.**

(c) *Meaning of terms.* \* \* \*

(1) *Meaning of term "tax."* \* \* \*

(ii) \* \* \*

(B) For taxable years ending after February 29, 1980, the corporation's overpayment of windfall profit tax imposed by section 4986 of the Code from the taxable year. For this purpose, the amount of such overpayment is the amount by which such corporation's aggregate windfall profit tax liability for the taxable year as a producer of crude oil is exceeded by withholding of windfall profit tax for the taxable year. The deemed payment date in section 4995(a)(4)(B) for the amount of windfall profit tax withheld with respect to payment for crude oil shall have no effect in the determination of the overpayment of windfall profit tax.

\* \* \* \* \*

Roscoe L. Egger, Jr.,

*Commissioner of Internal Revenue.*

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BILLING CODE 4830-01-M

**26 CFR Part 51**

[LR-38-82]

**Net Profits Interests; Proposed Rulemaking**

**AGENCY:** Internal Revenue Service, Treasury.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** This document contains proposed regulations relating to the rules applicable to net profits interests for purposes of the windfall profit tax on domestic crude oil imposed by title I of the Crude Oil Windfall Profit Tax Act of 1980. Changes to the applicable law were made by sections 201(h) and 203(c) of the Technical Corrections Act of 1982. The regulations would provide guidance for determining the portion of crude oil produced from the property attributable

to the holder of a new profits interest. These regulations would supersede § 150.4996-1(b)(3) of the Temporary Excise Tax Regulations Under the Crude Oil Windfall Profit Tax Act of 1980, 26 CFR Part 150, for those net profits interests for which these regulations would be effective. Those temporary regulations remain in effect for those net profits interests for which these regulations would not be effective (e.g., a net profits interest established by an agreement entered into before April 1, 1982, which is held by a profit making corporation).

**DATES:** Written comments and requests for a public hearing must be delivered or mailed by October 29, 1984. The amendments are proposed to be effective generally with respect to net profits agreements entered into (or renewed) after March 31, 1982. However, in the case of a 90 percent or more net profits interest held by an exempt charity or exempt governmental interest, these amendments are proposed to be effective with respect to crude oil removed after February 29, 1980.

**ADDRESS:** Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-38-82), Washington, D.C. 20224.

**FOR FURTHER INFORMATION CONTACT:** Douglas W. Charnas of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297).

#### SUPPLEMENTARY INFORMATION:

##### Background

On November 5, 1982, the Federal Register published final regulations (47 FR 50215) under sections 4986, 4987, 4988, 4989, 4991, 4922, 4993, 4994, 4995, 4996, 4997, 6050C, 6076, 6081 and 6402 of the Internal Revenue Code of 1954. Those regulations were required to implement various sections of the Crude Oil Windfall Profits Tax Act of 1980. In general, those regulations superseded Temporary Excise Tax Regulations under the Crude Oil Windfall Tax Act of 1980. However, paragraph (b)(3) of § 51.4996-1, relating to net profits interests, was reserved in the final regulations. The final regulations did not supersede paragraph (b)(3) of § 150.4996-1. These proposed amendments are to be issued under the authority of Code section 4997(b), which grants the Secretary of the Treasury or his delegate authority to prescribe regulations necessary or appropriate to carry out the purpose of the windfall profit tax (including changes in the

application of the energy regulations), sections 4996(a)(1)(B) and 4996(h)(2), and under the more general regulatory authority contained in section 7805(b).

#### Explanation of Provisions

The windfall profit tax imposes a tax on the producer of domestic crude oil except exempt oil. Section 4996(a)(1)(A) provides that the term "producer" generally means the holder of an economic interest with respect to the crude oil. The holder of a net profits interest in a property is generally considered to hold an economic interest with respect to the crude oil. Under § 150.4996-1(b)(3) of the temporary regulations (promulgated before enactment of the Technical Corrections Act of 1982), the holder of a net profits interest is treated as the producer of the number of barrels of crude oil equal to the net profits interest holder's share of net profits divided by the removal price of the crude oil. For example, if X receives \$120 of his share of net profits and the removal price of the crude oil is \$30 per barrel, X is treated as the producer of four barrels of crude oil.

Section 201(h) of the Technical Corrections Act of 1982 amends the definition of "producer" in section 4996(a) to provide special rules for producers subject to a net profits interest agreement. These special rules provide that for windfall profit tax purposes the amount of crude oil equal in value to the cost of operating the property (cost recovery oil) will be treated as produced by the net profits interest holder and the person holding the interest burdened by the net profits interest in the same proportion as their respective shares of net profits. Section 201(h) of the Act also amends section 4988(b) by adding a new paragraph (6) which provides that for purposes of the net income limitation the expenses of producing the crude oil will be allocated in the same manner as the cost recovery oil. Thus, the holder of a 10 percent net profits interest essentially will be treated as the producer of 10 percent of the barrels of crude oil produced and will be attributed 10 percent of the expenses of producing that crude oil.

#### As if Cost Depletion

Section 4988(b)(6) provides that for net income limitation purposes, if any person is treated as the producer of a portion of cost recovery oil covered by a net profits agreement, such person (and only such person) shall include in its gross income from the property the gross income from such portion and the qualified costs allocable to such portion shall be treated as paid or incurred by such person. Section 51.4988-2(c)(4) of

the proposed regulations makes clear that this rule applies for purposes of determining "as if" cost depletion under § 51.4988-2(b)(3). This position is consistent with Congressional intent as indicated in the following statement from the Senate report: "Thus the net income limitation treatment of depletion and intangible drilling costs, for example, will be determined in accordance with the new allocation rules [section 4988(b)(6)] for the windfall profit tax and not under the usual income tax rules." S. Rep. No. 97-592, 97th Cong., 2d Sess. 43 (1982).

#### Specified Amounts

There may be situations in which the person with the working interest transfers that interest while retaining an overriding royalty interest with certain conditions. For example, the agreement may provide that the person holding the overriding royalty interest will not receive an amount in excess of a specified percentage of net profits (e.g., the overriding royalty interest is entitled to the proceeds from  $\frac{1}{4}$  of the production except that such amount shall not exceed 90 percent of net profits). The proposed regulations treat this type of limited overriding royalty interest as a net profits interest in those cases in which the proceeds from the specified share of production exceed the specified percentage of net profits.

There may be situations in which the person with the working interest transfers that interest while retaining an interest that entitles such person to the greater of a specified percentage of net profits or a specified amount (e.g., 90 percent of net profits or \$200, whichever is greater). The proposed regulations do not treat this type of interest as a net profits interest in those cases in which the specified amount exceeds the specified percentage of net profits. If the share of net profits exceeds the specified amount, the excess of the amount received over the specified amount, rather than the entire amount received, is treated as attributable to a net profits interest. The amount received equal to the specified amount is treated as attributable to a royalty interest or production payment, depending on the particular situation.

#### Allocation of Cost Recovery Oil

Section 4996(h)(2) defines "cost recovery oil" as crude oil produced from a property that is allocated to a person as reimbursement for qualified costs paid or incurred with respect to the production of crude oil from the property. That section also provides that the Secretary shall by regulations

prescribe rules for allocating the cost recovery oil to the oil produced from the property. Proposed § 51.4996-1(b)(3)(iv) provides that if a property produces crude oil of different categories, cost recovery oil shall be allocated among such categories in proportion to the production from that property in each such category that was removed from the premises during the immediately preceding calendar quarter. For this purpose, the categories of crude oil are tier 1, tier 2, newly discovered oil, tier 3 oil other than newly discovered oil, and exempt oil. Proposed § 51.4996-1(b)(3)(iv) also provides that if a net profits agreement provides that net profits are determined from proceeds other than proceeds solely from the production of crude oil, "cost recovery oil" shall be deemed to exist to the extent that, based on all the facts and circumstances, the expenses paid or incurred in producing the net profits are attributable to the production of crude oil.

#### Qualified Costs

Section 4996(h)(3) defines "qualified costs" as any amount paid or incurred for exploring for, or developing or producing, one or more oil or gas wells on the property. The proposed regulations provide that this term includes any amounts paid or incurred for overhead or indirect costs that are attributable to the activities described in the preceding sentence. The proposed regulations also provide that the term "qualified costs" does not include any amount that is paid or incurred with respect to the tax imposed by chapter 45.

#### Comments and Requests for Public Hearing

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is to be held, notice of the time and place will be published in the *Federal Register*.

#### Special Analysis

The Commissioner of the Internal Revenue has determined that these proposed rules are not major rules as defined in Executive Order 12291 and the Treasury-OMB agreement dated April 29, 1983, implementing that order. Accordingly, a Regulatory Impact Analysis is not required.

Although this document is a notice of proposed rulemaking which solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

#### Drafting Information

The principal author of these proposed regulations is Douglas W. Charnas 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 these regulations, both on matters of substance and style.

#### List of Subjects in 26 CFR Part 51

Excise tax, Petroleum, Crude Oil Windfall Profit Tax Act of 1980.

#### Proposed Amendments to the Regulations

The proposed amendments to 26 CFR Part 51 are as follows:

Paragraph 1. Paragraph (c) of § 51.4988-2 is amended by redesignating paragraphs (c)(4), (5), and (6) as (5), (6), and (7), respectively, and by inserting a new paragraph (c)(4) to read as set forth below.

#### § 51.4988-2 Net income limitation on windfall profit.

##### (c) Special rules. \*

(4) *Certain net profits interests.* (i) For purposes of determining the net income limitation under this section in the case of any person treated under paragraph (b)(3) of § 51.4996-1 (relating to net profits interests) as the producer of any portion of cost recovery oil (within the meaning of § 51.4996-1(b)(3)(iv)) covered by a net profits agreement (within the meaning of § 51.4996-1(b)(3)(iii))—

(A) Such person (and only such person) shall include in its gross income from the property the gross income from such portion, and

(B) The qualified costs (within the meaning of § 51.4996-1(b)(3)(v)) allocable to such portion (and only by such person).

The determination of cost depletion under paragraph (b)(3) of this section shall be made with regard to the principles of paragraph (b)(3) of § 51.4996-1. Thus, a person treated under

that paragraph as the producer of any portion of cost recovery oil covered by a net profits agreement computes the cost depletion deduction allowable under paragraph (b)(3) of this section by using as the number of units sold that number of units which such person would have used for income tax purposes of such person's gross income from the property had included the gross income attributable to that portion of the cost recovery oil of which such person is treated as the producer.

(ii) *Example.* B owns 100 percent of the working interest in Whiteacre. B's working interest is burdened by a 75 percent net profits interest held by C. The net profits agreement provides that the amount of net profits is determined by subtracting from gross income from the sale of Crude oil or gas production from Whiteacre all payments to royalty holders and all operating expenses except the windfall profit tax. Whiteacre produces only taxable crude oil. For the taxable year, 20,000 barrels of crude oil are produced from Whiteacre and sold for \$40 per barrel for a total of \$800,000. Of this amount, \$100,000 is paid to D for his 1/4 royalty interest ( $\$40 \times (20,000 \times \frac{1}{4})$ ). The operating expenses attributable to the production of the taxable crude oil are \$100,000. The net profits for the year are \$600,000 ( $\$800,000$  (gross income) —  $(\$100,000$  (royalty payment) +  $\$100,000$  (expenses))). C is entitled to \$450,000 ( $\$600,000 \times .75$ ). Under § 51.4996-1(b)(3) C is treated as the producer of 13,125 barrels of crude oil ( $20,000 \times \frac{1}{4} \times .75$ ). Thus, for purposes of determining C's hypothetical cost depletion deduction allowable for the taxable year under paragraph (b)(3) of § 51.4988-2, C would use the 13,125 barrels as his number of units sold and would attribute \$75,000 of the costs ( $\$100,000 \times .75$ ) to that production for purposes of calculating the net income limitation.

Par. 2. Paragraph (b)(3) of § 51.4996-1 is revised to read as follows:

#### § 51.4996-1 Definitions.

##### (b) Producer. \*

(3) *Certain net profits interests*—(i) *In general.* In the case of any property (within the meaning of paragraph (i) of this section), all cost recovery oil (within the meaning of paragraph (b)(3)(iv) of this section) covered by a net profits agreement (within the meaning of paragraph (b)(3)(iii) of this section) shall be treated as produced by the parties to such agreement in proportion to the respective shares (determined after reduction for such cost recovery oil) of the production of the crude oil covered by such agreement. An economic interest in crude oil in place in the ground which is not a working interest (within the meaning of paragraph (d)(2)

of § 51.4992-1) without regard to this subparagraph shall not be considered a working interest by reason of the allocation of costs to a holder of a net profits interest under this subparagraph.

(ii) *General rule inapplicable before payout.* In the case of any property, the provisions of paragraph (b)(3)(i) of this section only shall apply for—

(A) The first taxable period in which, under the agreement with respect to such property, one or more persons receive a share described in paragraph (b)(3)(iii)(B) of this section, and

(B) All subsequent taxable periods to which such agreement applies.

(iii) *Net profits agreement defined.* The term "net profits agreement" means an agreement entered into [or renewed] after March 31, 1982, that provides for sharing part or all of the production of crude oil from a property where—

(A) One or more persons are to be reimbursed for qualified costs (within the meaning of paragraph (b)(3)(v) of this section) by the allocation of cost recovery oil, and

(B) One or more persons are to receive a share of any production of crude oil from the property remaining after reduction for the cost recovery oil referred to in paragraph (b)(3)(iii)(A) of this section.

The term "net profits agreement" shall include an agreement that provides that a party to the agreement is entitled to the greater or lesser of a specified share of production of crude oil from the property remaining after reduction for cost recovery oil or some other amount (such as a specified share of total production or a maximum or minimum amount) provided the requirements of paragraphs (b)(3)(iii)(A) and (B) of this section are satisfied. If a party to an agreement described in the preceding sentence receives a share of production other than the specified share of production of crude oil from the property remaining after reduction for cost recovery oil, such party shall be treated as receiving a share of production of crude oil from the property remaining after reduction for cost recovery oil in certain situations. If such party receives a maximum or minimum amount with respect to any crude oil production instead of a specified share of production, such party shall not be treated as receiving a share of production remaining after reduction for cost recovery oil with respect to such crude oil production. However, if such party is entitled to receive the greater of a specified share of production or a specified amount and receives the specified share of production remaining after reduction for cost recovery oil

instead of the specified amount, such party shall be treated as receiving a share of production remaining after reduction for cost recovery oil to the extent that the amount of the share received exceeds the specified amount. See example (4) of paragraph (b)(3)(viii) of this section.

(iv) *Cost recovery oil defined.* The term "cost recovery oil" means crude oil produced from the property that is allocated to a person as reimbursement for qualified costs paid or incurred with respect to the property. If the property produces crude oil of different categories, cost recovery oil shall be allocated among such categories in proportion to the production from that property in each such category that was removed from the premises during the immediately preceding calendar quarter. For purposes of the preceding sentence, the categories of crude oil are tier 1, tier 2, newly discovered oil, tier 3 oil other than newly discovered oil, and exempt oil. If a new profits agreement provides that net profits are determined from proceeds other than proceeds solely from the production of crude oil, cost recovery oil shall be deemed to exist to the extent that, based on all the facts and circumstances, the expenses paid or incurred in producing the net profits are attributable to the production of crude oil. See example (7) of paragraph (b)(3)(viii) of this section.

(v) *Qualified costs.* The term "qualified costs" means any amount paid or incurred for exploring, developing, or producing natural gas or crude oil from a reservoir on the property. The term includes any overhead or indirect costs paid or incurred that are attributable to the activities described in the preceding sentence. The term does not include any amount that is paid or incurred with respect to the tax imposed by chapter 45.

(vi) *Scope of agreement.* A net profits agreement shall be treated as covering only shares of production of crude oil held by persons who hold economic interests in the property (determined without regard to paragraph (b)(3)(i) of this section).

(vii) *Effective date for certain governmental entities and certain charities.* If 90 percent or more of the remaining production referred to in paragraph (b)(3)(iii)(B) of this section is to be received by holders of a qualified governmental interest (within the meaning of section 4994(a)) or holders of a qualified charitable interest (within the meaning of section 4994(b)), or both, that do not share in the costs referred to on paragraph (b)(3)(iii)(A) of this section, then the requirement of

paragraph (b)(3)(iii) that the agreement be entered into [or renewed] after March 31, 1982, shall not apply. Accordingly, the applicability of the provisions of this subparagraph is determined without regard to the date on which the net profits agreement was entered into.

(viii) The principles of this subparagraph may be illustrated by the following examples:

*Example (1).* A, an independent producer, holds the working interest in property X which produces tier 1 oil. A's interest is burdened by a 95 percent net profits interest held by B who is neither an independent producer nor an exempt producer. The agreement between A and B provides that the amount of net profits is determined by subtracting from gross income all operating expenses except windfall profit taxes. Property X produces 400 barrels of crude oil during the month of May, each of which is sold for \$35. The operating expenses for May are \$6,300. Of the 400 barrels produced during May, 180 are attributed to A under the agreement to cover operating expenses (\$6,300 ÷ \$35). Of the 220 barrels remaining, 11 are attributed to A (5% of 220) and 209 are attributed to B (95% of 220) under the agreement. For windfall profit tax purposes, the 180 barrels are treated as cost recovery oil. Under § 51.4996-1(b)(3)(i), 171 barrels of the cost recovery oil are allocated to B (95% of 180). Thus, for windfall profit tax purposes, A and B are treated as producers of 20 barrels and 380 barrels, respectively, for May.

*Example (2).* C, an independent producer, owns an oil and gas property that is burdened by an overriding royalty interest held by D. The overriding royalty agreement provides that D is entitled to the lesser of the proceeds from 1/4 of the production from the property or 50 percent of the net profits from the property for a calendar quarter. The property produced 1,000 barrels at \$30 per barrel for a calendar quarter and had net profits of \$1,400. The proceeds from 1/4 of the production for the quarter exceeded 50 percent of the net profits. D is treated as the holder of a 50 percent net profits interest with respect to those barrels of crude oil for which D's share of the proceeds from production is determined by reference to 50 percent of net profits. D is treated as the producer of 500 barrels.

*Example (3).* E, an independent producer, owns an oil and gas property that is burdened by a net profits interest (determined before any reduction of the net profits for chapter 45 taxes) held by F. F is entitled to 10 percent of the net profits or \$2,200 (or revenue from total production if revenue from production is \$2,200 or less per calendar quarter) for a calendar quarter, whichever is greater. For a calendar quarter gross income from the property is \$26,010 (867 barrels at \$30 each) and expenses are \$4,800. F's share of net profits is \$2,121  $([\$26,010 - \$4,800] \times 10\%)$ . F receives \$2,200 because this amount exceeds 10 percent of net profits. F is treated as the holder of an 8.45829% royalty interest  $(\$2,200 \div \$26,010)$ , and is treated as the producer of 73.33337

barrels of crude oil ( $867 \times 8.45829\%$ ) with respect to that royalty interest.

**Example (4).** Assume the same facts as example (3) except that the expenses are \$1,200. F's share of net profits is \$2,481 ( $(\$26,010 - \$1,200) \times 10\%$ ). F is treated as the holder of an 8.45829% royalty interest ( $\$2,200 \div \$26,010$ ) because F is entitled to the \$2,200 without regard to net profits. F is also treated as the holder of a 1.24281% net profits interest because \$281 ( $\$2,481 - \$2,200$ ) are determined by reference to net profits to net profits from production ( $\$281 \div \$26,010 \times \$1,200 + \$2,200$ ). F is treated as the producer of 84,10853 barrels of crude oil. Of this amount, 73,3337 barrels are attributable to the royalty interest ( $867 \times 8.45829\%$ ) and 10,77516 barrels are attributable to the net profits interest ( $867 \times 1.24281\%$ ). F is treated as the producer of 1.24281% of the cost recovery oil, and, accordingly, is allocated \$14,91372 of expenses ( $1.24281\% \times \$1,200$ ) for purposes of the net income limitation.

**Example (5).** On January 1, 1983, G and H enter into an agreement which provides for the following: (1) G will incur all expenses of exploring for and developing property Y. (2) G will receive all production from Y until G has recovered all expenses for exploration and development, and (3) after G has recovered all expenses for exploration and development, G and H will share equally the production remaining after G has recovered operating costs (determined without regard to the tax imposed by chapter 45). Y begins producing crude oil on July 1, 1983. G recovers all expenses for exploration and development as of December 31, 1983, and on January 1, 1984, G and H begin sharing the production from Y remaining after G has recovered operating expenses. For purposes of paragraph (b)(3)(ii)(A) of this section, H is not treated as receiving a share described in paragraph (b)(3)(iii)(B) of this section until January 1, 1984.

**Example (6).** Assume the same facts as example (5) except that the agreement provides that after G has recovered all expenses for exploration and development, G and H will share equally the revenue and expenses of production from Y. The agreement between G and H is not a net profits agreement because H's share of production after G has recovered all expenses for exploration and development is burdened by the expenses of such production.

**Example (7).** J, an independent producer, owns property Z which produces tier 1 and tier 2 oil. J's interest is burdened by a 95 percent net profits interest held by K whose interest is a qualified charitable interest. The net profits agreement between J and K provides that the amount of net profits is determined by subtracting from gross income from the sale of crude oil and natural gas production from property Z all operating expenses except the windfall profit tax. The agreement also provides that the proceeds from the production of natural gas shall be used to reimburse J for all operating expenses for the production of crude oil and natural gas from property Z. Fifty percent of the gross income from property Z is attributable to the

production of crude oil and 50 percent is attributable to the production of natural gas. However, 80 percent of the operating expenses of property Z are attributable to the production of crude oil while only 20 percent are attributable to the production of natural gas. During January of 1984, property Z produces 900 barrels of crude oil which sell for \$27,000 (\$30 per barrel) and 10,000 MCF of natural gas which also sell for \$27,000. The operating expenses of property Z for that month are \$4,500, \$3,600 of which are attributable to the production of crude oil and \$900 of which are attributable to the production of natural gas. Because 80 percent of the operating expenses are attributable to the production of crude oil, cost recovery oil shall be deemed to exist to the extent of 80 percent of the operating expenses. Accordingly, there are 120 barrels of cost recovery oil (\$3,600 (operating expenses attributable to crude oil)  $\div$  \$30 (removal price of each barrel of crude oil)). During the immediately preceding calendar quarter, 50 percent of the crude oil removed from the premises was tier 1 and 50 percent was tier 2. Accordingly, of the 120 barrels of cost recovery oil, 60 barrels are treated as tier 1 and 60 barrels are treated as tier 2.

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Roscoe L. Egger, Jr.,  
Commissioner of Internal Revenue.  
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## 26 CFR Part 301

[LR-149-84]

### Requirement to Maintain Lists of Investors in Potentially Abusive Tax Shelters

**AGENCY:** Internal Revenue Service, Treasury.

**ACTION:** Notice of proposed rulemaking by cross-reference to temporary regulations.

**SUMMARY:** In the Rules and Regulations portion of this issue of the *Federal Register*, the Internal Revenue Service is issuing temporary regulations relating to the requirement to maintain a list of investors in potentially abusive tax shelters. The text of the temporary regulations also serves as the comment document for this notice of proposed rulemaking.

**DATES:** Written comments and requests for a public hearing must be delivered or mailed by October 29, 1984. The regulations are proposed to apply to any interest in a potential abusive tax shelter other than an interest that was acquired by an investor before September 1, 1984.

**ADDRESS:** Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-149-84), Washington, D.C. 20224.

**FOR FURTHER INFORMATION CONTACT:** Alice M. Bennett of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., NW, Washington, D.C. 20224 (Attention: CC:LR:T), (202) 566-3918 (not a toll-free call).

### SUPPLEMENTARY INFORMATION

#### Background

The temporary regulations in the Rules and Regulations section of this issue of the *Federal Register* amend the Procedure and Administration Regulations (26 CFR Part 301) to provide rules under sections 6112 and 6708 of the Internal Revenue Code of 1954. The text of those temporary regulations serves as the comment document for this notice of proposed rulemaking.

Section 6112 provides that any person who organizes, or sells any interest in, a potential abusive tax shelter must maintain a list of investors in that tax shelter. Any person who is required to maintain a list under section 6112 must make the list available for inspection upon request of the Secretary, and generally must retain any information required to be included on the list for 7 years.

Section 6708 provides that any person who fails to meet any requirement under section 6112 shall be subject to a penalty of \$50 for each person with respect to whom there is such a failure, unless it is shown that the failure is due to reasonable cause and not to willful neglect. The penalty imposed by section 6708 on a person who fails to meet the requirements of section 6112 shall not exceed \$50,000 for any calendar year. The penalty imposed by section 6708 is in addition to any other penalty provided by law.

The regulations under sections 6112 and 6708 are to be issued under the authority contained in sections 6112 and 7805 of the Internal Revenue Code of 1954 (98 Stat. 681, 68A Stat. 917; 26 U.S.C. 6112, 7805). For the text of the temporary regulations, see FR Doc. 84-22939 (T.D. 7969) published in the Rules and Regulations section of this issue of the *Federal Register*.

#### Special Analyses

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed

herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

#### Comments and Request for a Public Hearing

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the **Federal Register**.

The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB also to send copies of the comments to the Service.

#### Drafting Information

The principal author of these proposed regulations is Alice M. Bennett 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, on matters of both substance and style.

#### List of Subjects in 26 CFR Part 301

Administrative practice and procedure, Bankruptcy, Courts, Crime, Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Investigations, Law enforcement, Penalties, Pensions, Statistics, Taxes, Disclosure of information, Filing requirements.

Roscoe L. Egger, Jr.

Commissioner of Internal Revenue.

[FR Doc. 84-22938 Filed 8-24-84; 3:31 pm]

BILLING CODE 4830-10-M

#### ENVIRONMENTAL PROTECTION AGENCY

##### 40 CFR Part 52

[A-5-FRL-2661-4]

#### Approval and Promulgation of Implementation Plans; Ohio

**AGENCY:** U.S. Environmental Protection Agency (U.S. EPA).

**ACTION:** Notice announcing extension of public comment period.

**SUMMARY:** On July 17, 1984, (49 FR 28888) the U.S. EPA proposed to change the sulfur dioxide designation for Columbiana and portions of Summit Counties in Ohio from nonattainment to attainment of the National Ambient Air Quality Standard (NAAQS). In addition U.S. EPA proposed to deny the State of Ohio's request for the redesignation of Clermont, Coshocton, Cuyahoga, Lake, Lorain, Morgan, Washington and portions of Summit Counties. In that notice U.S. EPA also proposed to take no action on the redesignation request for Gallia, Lucas and Jefferson Counties.

A 30-day comment period was provided which was scheduled to end on August 16, 1984. In response to a commenter's request to extend the comment period an additional 30 days, the public comment period is being extended to September 17, 1984.

**DATE:** Comments must be received on or before September 17, 1984.

**ADDRESSES:** Comments should be submitted to: Gary Gulezian, Chief, Regulatory Analysis Section, Air and Radiation Branch, Region V, U.S. Environmental Protection Agency (5AR-26), 230 S. Dearborn Street, Chicago, Illinois 60604.

**FOR FURTHER INFORMATION CONTACT:** Debra Marcantonio (312) 886-6088.

Dated: August 15, 1984.

Alan Levin,

Acting Regional Administrator.

[FR Doc. 84-22904 Filed 8-28-84; 8:45 am]

BILLING CODE 6560-50-M

##### 40 CFR Part 180

[OPP-300096; FRL-2661-5]

#### Methyl Esters of Higher Fatty Acids; Proposed Exemptions From the Requirement of a Tolerance

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Proposed rule.

**SUMMARY:** This document proposes to expand the exemption for methyl esters of higher fatty acids from the

requirement of a tolerance when used as a surfactant in pesticide formulations. This proposed regulation was requested by Domain, Inc.

**DATE:** Written comments must be received on or before September 28, 1984.

**ADDRESS:** By mail, submit written comments identified by the document control number [OPP-300091] to: Information Services Section (TS-757C), Program Management and Support Division, Office of Pesticide Programs, Environmental Protection Agency, 401 M St., SW., Washington, D.C. 20460.

In person, bring comments to: Registration Support and Emergency Response Branch, Registration Division (TS-767), Environmental Protection Agency, Rm. 724A, CM#2, 1921 Jefferson Davis Highway, Arlington, VA 22202.

Information submitted as a comment concerning this notice may be claimed confidential by marking any part or all of that information as "Confidential Business Information" (CBI). Information so marked will not be disclosed except in accordance with procedures set forth in 40 CFR Part 2. A copy of the comment that does not contain CBI must be submitted for inclusion in the public record.

Information not marked "confidential" may be disclosed publicly by EPA without prior notice to the submitter. All written comments will be available for public inspection in Rm. 236 at the address given above from 8 a.m. to 4 p.m., Monday through Friday, excluding legal holidays.

#### FOR FURTHER INFORMATION CONTACT:

By mail: N. Bhushan Mandava, Registration Support and Emergency Response Branch (TS-767C), Environmental Protection Agency, 401 M St., SW., Washington, D.C. 20460. Office location and telephone number: Rm. 716, CM #2, 1921 Jefferson Davis Highway, Arlington, VA 22202, (703-557-7700).

**SUPPLEMENTARY INFORMATION:** At the request of Domain, Inc., the Administrator proposes amending 40 CFR 180.1001(c) by expanding the existing exemption from the requirement of a tolerance for methyl esters of higher fatty acids for the additional use as a surfactant in pesticide formulations. A separate entry is not necessary in order to reflect this change.

Inert ingredients are all ingredients which are not active ingredients as defined in 40 CFR 162.3(c), and include, but are not limited to, the following types of ingredients (except when they have a pesticidal efficacy of their own): solvents such as water; baits such as sugar, starches, and meat scraps; dust