

OPTION DESIGNATION CHECKLIST FOR OPTIONS ON PHYSICALS—Continued

Criteria	Applicable commission rule, 17 CFR	Standard	Met by exchange rule number
5. Option expiration.....	33.4(d)(1).....	Options expire not less than one business day before the earlier of the last trading day or the first notice day of any futures contract in the same or a related commodity, except for cash-settled futures contracts..	

(6) *Other required information.* As requested, a board of trade shall submit additional evidence, information, data or stipulations relating to whether a contract meets, initially or on a continuing basis, the public interest standard contained in section 5(g) of the Act, the economic purpose standard of § 33.4(a)(5)(i) of this chapter, or any other requirement for designation under the Act or Commission rules.

Issued in Washington, DC this 22nd day of January, 1992, by the Commodity Futures Trading Commission.

Jean A. Webb,

Secretary of the Commission.

[FR Doc. 92-1910 Filed 1-29-92; 8:45 am]

BILLING CODE 6351-01-M

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Food and Drug Administration

21 CFR Part 310

[Docket No. 89N-0525]

Status of Certain Over-the-Counter Drug Category II and III Active Ingredients; Technical Amendment

AGENCY: Food and Drug Administration, HHS.

ACTION: Final rule; technical amendment.

SUMMARY: The Food and Drug Administration (FDA) is amending the regulations regarding the status of certain over-the-counter (OTC) drug Category II and III active ingredients. This final rule makes nonsubstantive corrections to the final regulations that were published in the *Federal Register* of November 7, 1990 (55 FR 46914). That final rule listed the names of several active ingredients incorrectly. This document corrects those errors and provides clarification of the final rule for certain OTC drug products.

EFFECTIVE DATE: January 30, 1992.

FOR FURTHER INFORMATION CONTACT: William E. Gilbertson, Center for Drug Evaluation and Research (HFD-210), Food and Drug Administration, 5600 Fishers Lane, Rockville, MD 20857, 301-295-8000.

SUPPLEMENTARY INFORMATION: This document amends the final rule concerning drug products containing certain active ingredients offered OTC for certain uses in 21 CFR part 310 (as set forth in the *Federal Register* of November 7, 1990 (55 FR 46914)). That final rule lists several active ingredients incorrectly. This final rule corrects those errors in the regulations. As noted above, these amendments institute changes that are nonsubstantive in nature. Because the amendments are not controversial and because, when effective, they provide clarification of a final rule for OTC drug products, FDA finds that the usual notice and comment procedures are unnecessary.

List of Subjects in 21 CFR Part 310

Administrative practice and procedure, Drugs, Labeling, Medical devices, Reporting and recordkeeping requirements.

Therefore under the Federal Food, Drug, and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs, 21 CFR part 310 is amended as follows:

PART 310—NEW DRUGS

1. The authority citation for 21 CFR part 310 continues to read as follows:

Authority: Secs. 201, 301, 501, 502, 503, 505, 506, 507, 512-516, 520, 601(a), 701, 704, 705, 706 of the Federal Food, Drug, and Cosmetic Act (21 U.S.C. 321, 331, 351, 352, 353, 355, 356, 357, 360b-360f, 360j, 361(a), 371, 374, 375, 376); secs. 215, 301, 302(a), 351, 354-360F of the Public Health Service Act (42 U.S.C. 216, 241, 242(a), 262, 263b-263n).

§ 310.545 [Amended]

2. Section 310.545 *Drug products containing certain active ingredients offered over-the-counter (OTC) for certain uses* is amended in paragraph (a)(1) by removing the entry "Chlorhydroxyquinoline" and alphabetically adding the entry "Cloxyquin"; by removing from paragraph (a)(2) the entry "Acidulated sodium phosphate"; by removing from paragraphs (a)(6)(i) and (a)(6)(ii) the entry "Thenyldiamine" and adding in their place the entry "Thenyldiamine hydrochloride"; by removing from

paragraph (a)(7) the entries "Alkyl isoquinolinium", "Lauryl isoquinolinium", and "Methylbenzethonium" and adding in their place the entries "Alkyl isoquinolinium bromide", "Lauryl isoquinolinium bromide", and "Methylbenzethonium chloride", respectively; by removing from paragraph (a)(8) the entries "Dihydroxyaluminum", "Glutamic acid", and "Homatropine", and adding in their place the entries "Dihydroxyaluminum sodium carbonate", "Glutamic acid hydrochloride", and "Homatropine methylbromide", respectively; by removing from paragraph (a)(12)(iv) the entry "Prune concentrate" and adding in its place the entry "Prune concentrate dehydrate".

Dated: January 24, 1992.

Michael R. Taylor,

Deputy Commissioner for Policy.

[FR Doc. 92-2229 Filed 1-29-92; 8:45 am]

BILLING CODE 4160-01-M

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[T.D. 8394]

RIN 1545-A037

Proceeds of Bonds Used for Reimbursement

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide guidance as to when the allocation of bond proceeds to reimburse expenditures previously made by an issuer is treated as an expenditure of the bond proceeds. When bond proceeds are "spent," they are no longer subject to arbitrage rebate, arbitrage yield limitations, and certain other limitations. Changes to the applicable law were made by the Tax Reform Act of 1984 and the Tax Reform Act of 1986.

The regulations provide guidance to issuers of tax exempt bonds.

DATES: The regulations are effective for bonds issued after March 2, 1992.

FOR FURTHER INFORMATION CONTACT: William P. Cejudo, 202-566-3283 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this final regulation has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1980 (44 U.S.C. 3504(h)) under control number 1545-1226. The estimated average annual burden per recordkeeper is 2.4 hours. These estimates are an approximation of the average time expected to be necessary for a collection of information. They are based on such information as is available to the Internal Revenue Service. Individual recordkeepers may require greater or less time, depending on their particular circumstances.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer T:FP, Washington, DC, 20224, and to the Office of Management and Budget, Attention: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

Background

On April 25, 1991, the Internal Revenue Service published a notice of proposed rulemaking to provide guidance under sections 103 and 150 of the Internal Revenue Code with respect to reimbursement bonds (56 FR 19046 (1991)). The proposed regulations reflected amendments to section 103 and the addition of sections 141 through 150 to the Code by the Tax Reform Act of 1986 (Pub. L. 99-514, 100 Stat. 2602). The notice of proposed rulemaking proposed to add to the Income Tax Regulations (26 CFR part 1) provisions for determining when the use of bond proceeds to reimburse a previously paid expenditure is treated as an expenditure of the bond proceeds for purposes of sections 103 and 141 through 150 of the Code.

Written comments were received on the proposed regulations, and a public hearing was held on August 8, 1991. These written and oral comments requested many changes, including simplification of the regulations generally. After consideration of the comments, the proposed regulations are

adopted as revised by this Treasury decision.

Explanation of Provisions and Changes

A. General Purpose of the Regulations

These regulations provide rules for allocating proceeds of "reimbursement bonds." Reimbursement bonds are bonds the proceeds of which are allocated to reimburse expenditures paid prior to the date of issue of the bonds.

Proceeds of a bond generally cease to be treated as proceeds on the date they are spent. Moneys that cease to be treated as proceeds of a bond are no longer subject to arbitrage yield limitations, the arbitrage rebate requirement, and certain other restrictions imposed by sections 103 and 141-150 of the Code. Therefore, spending bond proceeds as soon as possible may reduce the amount of arbitrage rebate an issuer would otherwise pay and may free the issuer from complying with other significant requirements of the Code.

The early expenditure of bond proceeds as a means of avoiding or minimizing the amount of arbitrage rebate due the United States is encouraged by section 148(f)(4) of the Code, which generally treats an obligation as complying with the arbitrage rebate requirement if all gross proceeds of the obligation are spent within 6 months of the date of issue of the obligation (subject to certain exceptions) or in prescribed installments over a 2-year period (subject to certain exceptions and other requirements). Encouraging the early expenditure of bond proceeds furthers Federal tax policy by discouraging the issuance of bonds earlier than the bond proceeds are needed for governmental purposes. Deferring bond issuances reduces opportunities for earning arbitrage and lessens the burden on financial markets.

Because the applicability of many restrictions and requirements imposed by the Code ceases when bond proceeds are spent, proper administration of sections 103 and 141-150 requires a definition of what constitutes an expenditure of bond proceeds. In particular, it is important to define to what extent the allocation of bond proceeds to reimburse prior expenditures is considered an expenditure of the proceeds.

These regulations describe the circumstances in which an allocation of bond proceeds to reimburse a prior expenditure is treated as an expenditure of bond proceeds on the date of allocation. If reimbursements were not limited to expenditures made a

reasonable period of time prior to issuance of bonds, issuers could generally avoid compliance with sections 103 and 141-150 by simply allocating bond proceeds to capital expenditures paid long before, and without reliance on, the issuance of the bonds. In addition, the intent of these regulations is to limit the treatment of reimbursement allocations as expenditures of bond proceeds to situations in which economic circumstances justify the reimbursement. These regulations are not intended to permit or condone the use of reimbursement allocations to avoid arbitrage yield limitations, arbitrage rebate, or other tax limitations or restrictions.

B. General Requirements

An allocation of proceeds of governmental bonds, qualified 501(c)(3) bonds, and certain other private activity bonds to a previously paid expenditure must comply with § 1.103-18 to be an expenditure of bond proceeds. If a bond meets the requirements of these regulations, bond proceeds are deemed to be spent when they are allocated to reimburse a prior expenditure.

In the case of a governmental bond, a qualified 501(c)(3) bond, or a private activity bond the proceeds of which are used to finance a governmentally owned facility, three general requirements must be met in order for a reimbursement allocation of proceeds of those bonds to qualify as an expenditure of bond proceeds:

(1) On or before the date the expenditure that is being reimbursed is paid, the issuer (which, as defined, includes the borrower from a conduit issuer) must declare a reasonable official intent to reimburse the expenditure (the "official intent requirement").

(2) The allocation of reimbursement bond proceeds to an expenditure must take place by a required time (the "reimbursement period requirement"). The allocation must generally occur on or before the later of the date 1 year after the expenditure was paid or the date 1 year after the property was placed in service. Allocation may not occur before the date on which the expenditure was paid.

(3) The reimbursed expenditure must be a capital expenditure (the "capital expenditure requirement").

Under the "official intent period" requirement contained in the proposed regulations, official intent had to be declared no earlier than the date 2 years prior to the date of the expenditure. This requirement was not included in these

final regulations in an effort to simplify the regulations and in response to comments that the requirement was unnecessary in light of other requirements applicable to reimbursement allocations.

If proceeds of a private activity bond (other than a qualified 501(c)(3) bond) are allocated to reimburse a previously paid expenditure of the issuer, the allocation can qualify as an expenditure of the bond proceeds only if the bond complies with the requirements of § 1.103-8(a)(5) and does not violate the anti-abuse rules of § 1.103-18(k) (1) and (3) (ii) and (iii).

C. Official Intent Requirement

The purposes of the official intent requirement are to provide evidence that, on or prior to the date of payment, the issuer intended to reimburse the expenditure and to ensure that the reimbursement is not a device to avoid requirements imposed by the Code with respect to tax exempt bonds. In order to ensure that an issuer will consider its current financial and budgetary circumstances in connection with any declaration of official intent and that the reimbursement will be consistent with the issuer's financial and budgetary circumstances, the regulations require that the declaration of official intent (1) state that the issuer reasonably expects to reimburse the expenditure with proceeds of its debt, (2) specifically state that it is intended to be a declaration of official intent under these regulations, (3) contain a general functional description of the property to which the reimbursement relates or an identification of the fund or account from which the expenditure is to be paid and a general functional description of the purposes of the fund or account, (4) indicate the maximum principal amount of debt expected to be issued for reimbursement, and (5) be reasonably available for public inspection. The issuer may designate any person to act on its behalf in declaring official intent.

Unlike the proposed regulations, which required that the declaration of official intent state the issuer's intent to issue taxable or tax exempt debt to reimburse the prior expenditure, these regulations require only that the issuer declare its intent to issue debt to reimburse the expenditure. This change was made in response to comments expressing confusion over the language in the proposed regulations. The requirement that the declaration of official intent state that it is a declaration of official intent under these regulations was added in order to ensure appropriate evidence of intent to reimburse the expenditure. Without this

evidence, expenditure authorizations by issuers or conduit borrowers (which may also be legal authorizations to incur debt) are not treated as declarations of official intent for purposes of these regulations.

With respect to the proposed regulations, state and local financial officers commented that many larger issuers use a fund or account method to account for ongoing projects for which reimbursement financing may be used. These commentators pointed out that because of their use of fund accounting, the project-specific accounting requirements of the proposed regulations were burdensome. In response to these comments, these regulations permit declarations of official intent to describe identified funds or accounts in lieu of identified specific projects. Therefore, if a declaration of official intent both identifies the fund or account from which the expenditure to be reimbursed is paid and describes the general functional purpose of the fund or account, that declaration adequately describes the expenditure to be reimbursed for purposes of the official intent requirement.

Commentators requested clarification regarding the provision in the proposed regulations permitting "reasonable deviations" between the property described in the declaration of official intent and the actual property acquired. In response to these comments, these regulations permit reasonable deviations between the project described and the project acquired if "the actual project financed is reasonably related in function to the project described in the declaration of official intent." The intent of this change is to simplify compliance with the official intent requirement and to allow flexibility for changes within the same project.

In response to comments that the public availability requirement under the proposed regulations was burdensome, these regulations require only that the declaration of official intent be "reasonably available for public inspection within a reasonable period of time." Safe harbors are provided for declarations of official intent made available for public inspection in compliance with State or local law and for declarations of official intent made available within 30 days of the declaration of official intent. The intent of these changes is to simplify compliance with the public availability requirement while assuring that declarations of official intent are available for public inspection. Special

rules continue to apply to public availability of declarations of official intent with respect to conduit financings such as qualified 501(c)(3) bonds and other private activity bonds.

A declaration of official intent must be reasonable. The reasonableness requirement is intended to curb abuses that may otherwise arise when bond proceeds are allocated to reimburse expenditures primarily for the purpose of avoiding tax restrictions or requirements. The reasonableness requirement does not impose a requirement on an issuer that all other funds be exhausted. Instead, the requirement ensures that reimbursement of an expenditure is motivated by an intent to finance, on a long-term basis, an expenditure originally paid with moneys that were not available to fund the expenditure on a long-term basis.

Commentators asked for clarification of the concept of "available moneys" in the proposed regulations. In response to this request, these regulations clarify that moneys are taken into account for purposes of determining consistency with an issuer's budgetary and financial circumstances if, at the time of the declaration of official intent, they are, or are reasonably expected to be, allocated on a long-term basis, reserved, or otherwise set aside with respect to the expenditure to be reimbursed by the issuer or by any member of the same controlled group as the issuer. The application of the controlled group concept for purposes of determining available moneys should be easier for issuers to comply with since not all members of a controlled group need to be identified if it is clear that none of them could have available moneys with respect to the expenditure to be reimbursed by the issuer. A controlled group of entities is a group of entities controlled by the same entity or entities and is defined in new § 1.150-1(f). Because of these changes to the reasonableness requirement, the examples contained in the proposed regulations illustrating this principal were not included in these final regulations.

The reasonableness requirement is not intended to preclude an issuer from avoiding or minimizing arbitrage rebate or arbitrage yield limitations by intentionally delaying the issuance of a bond. For example, prior to the issuance of the bond, an issuer may pay expenditures with respect to a project with moneys that are not available on a long-term basis to finance the project. By delaying the bond issue, the issuer is able to reimburse itself for the prior expenditures with bond proceeds that

will be spent within the relevant 6-month or 2-year time period, thereby meeting an exception to arbitrage rebate. Delaying the issuance of obligations for this purpose furthers Federal tax policy and is encouraged.

The reasonableness requirement will not be applied to question the soundness or appropriateness of an issuer's budget or financial practices; rather it is meant to ensure that any intent to reimburse is consistent with an issuer's established budgetary and financial practices (provided that those practices are not adopted for tax avoidance purposes). In order to ensure that an issuer's actions reasonably conform to the issuer's declarations of official intent, under the reasonableness requirement the issuer must reasonably expect to reimburse the expenditure with proceeds of a borrowing (the "reasonable expectations test"). The determination of whether an expectation to reimburse is reasonable is based on all of the relevant facts and circumstances. For purposes of this determination, one important factor is whether an issuer has failed to reimburse expenditures which it has actually paid and for which it has declared official intent. The reasonable expectations test replaces the "pattern of failing to reimburse" rules of the proposed regulations. This change was made in part in response to comments that the "pattern of failing to reimburse" rules were burdensome.

D. Reimbursement Period Requirement

The purpose of the reimbursement period requirement is to provide assurance that the money originally used to pay for the expenditure that is to be reimbursed is not available with respect to the expenditure on a long-term basis. If an expenditure is not reimbursed within a relatively short period of time after its payment or after completion of the project, it is more likely that the money used to pay the expenditure is available with respect to that expenditure on a long-term basis.

Some commentators have suggested that reimbursement allocations be permitted on an unrestricted basis with respect to all expenditures paid within a certain period of time. For example, some commentators have suggested permitting unlimited reimbursement of all expenditures paid during the 3 fiscal years preceding the date of issue of the reimbursement bonds. These commentators have argued that such a rule would be simple and that significant abuse (e.g., reimbursement of expenditures incurred many years ago) would be curbed because of the time limitation. This provision was not

included in these regulations because of the potentially adverse effect that it would have on arbitrage rebate, arbitrage yield restriction, and other tax requirements and limitations applicable to tax exempt bonds. If reimbursement allocations were permitted for defined periods of time without further limitation, issuers could conceivably reimburse themselves for all expenditures paid during the defined time period whenever they issued debt regardless of their actual economic motivation for incurring the debt. Issuers could then use the proceeds of that reimbursement bond to pay for all or a portion of the project that they had not originally intended to finance with bond proceeds. By structuring the financing as a reimbursement bond rather than as a "new money" bond, the bond proceeds could be treated as "spent" and no longer subject to most tax limitations that would otherwise apply to a new money bond.

E. Capital Expenditure Requirement

The purpose of the capital expenditure requirement is to prohibit the reimbursement of day-to-day operating costs and similar "working capital" items. Comments on the proposed regulations requested clarification of the distinction between costs with a reasonably expected economic life of 1 year or more and those with a life of less than a year. In response to this request, the economic life requirement was changed to a capital expenditure requirement. For this purpose, a "capital expenditure" is defined in new § 1.150-1(h) as any cost of a type that is properly chargeable to capital account (or would be so chargeable with proper election such as an election under section 266) under general Federal income tax principles. Whether an expenditure is a capital expenditure is determined at the time the expenditure is paid with respect to the property. Future changes in law do not affect whether an expenditure is a capital expenditure.

For purposes of applying the "general Federal income tax principles" standard referred to in § 1.150-1(h), an issuer should generally be treated as if it were a corporation subject to taxation under subchapter C of chapter 1 of the Code. For example, costs that would be deducted as trade or business expenses under section 162 of the Code are expenditures for working capital and are not capital expenditures. On the other hand, costs incurred to acquire, construct, or improve land, buildings, and equipment generally are capital expenditures under section 263 of the Code. Costs properly allocable to the

issuance of the reimbursement bond are treated as capital expenditures.

F. Special Exception for Preliminary Expenditures and Abandonment Prior to Completion

Preliminary expenditures such as architectural, engineering, survey, reimbursement bond issuance, and similar costs (not exceeding in the aggregate 20 percent of the issue price of that portion of the issue that finances the project) generally are not subject to the official intent requirement. A separate exception also recognizes that projects may be abandoned prior to completion, and generally permits reimbursement of expenditures in this event. Under the proposed regulations, preliminary expenditures were excepted only from the official intent period requirement and were limited to 10 percent of the expected cost of the project. Changes to this provision were made in response to comments that the provision was insufficient to cover all ordinary preliminary expenditures.

G. Definition of Issuer

For purposes of these regulations, "issuer" means the actual issuer of an obligation. If the proceeds of a bond are loaned by the issuer to an entity (the "conduit borrower") that uses the bond proceeds to carry out the governmental purpose of the bond, "issuer" includes the conduit borrower. The actual issuer of the reimbursement bonds is not treated as the issuer with respect to proceeds loaned to a conduit borrower.

The proposed regulations defined issuer as including all entities that were members of the same controlled group. Comments were received indicating that application of the controlled group concept in all circumstances was burdensome. In response to these comments, the controlled group concept was deleted from the definition of issuer and was applied instead generally for purposes of determining available amounts under the reasonableness requirement.

H. Anti-Abuse Rule and Limitation on Scope of Reimbursement Regulations

In general, a reimbursement allocation is not treated as an expenditure of bond proceeds if any action or inaction of the issuer with respect to the allocation constitutes an artifice or device. This general anti-abuse rule was not contained in the proposed regulations and is added to these regulations to prevent abuse that may otherwise occur because of certain more liberal provisions contained in these regulations (e.g., more liberal definition

of issuer and a more narrow application of the reasonableness standard).

In addition to the general anti-abuse rule, a reimbursement allocation is not treated as an expenditure of bond proceeds if, absent that application, the bond proceeds are otherwise used directly or indirectly for one of the following prohibited uses: (1) Within 1 year of the allocation, to refund another issue of governmental obligations of the issuer within the meaning of section 148 of the Code, (2) within 1 year of the allocation, to create or increase the balance in a "sinking fund" (as defined in § 1.103-13(g)) with respect to any obligation of the issuer, or to replace funds that have been, are, or will be so used for sinking fund purposes, (3) within 1 year of the allocation, to create or increase the balance in a "reserve or replacement fund" (as defined in § 1.103-14(d)) with respect to any obligation of the issuer, or to replace funds that have been, are, or will be so used for reserve or replacement fund purposes, or (4) to reimburse any person (other than the issuer) for any expenditure or payment that was originally paid with proceeds of any obligation of the issuer. Any obligation that may arise when an issuer borrows from its own internal funds or from the funds of entities that are members of the same controlled group is not treated as an "obligation" as that term is used in subdivision (4) in the preceding sentence.

The purpose of the limitations on the use of reimbursement proceeds is to prohibit issuers from using a reimbursement allocation to earn otherwise prohibited arbitrage in certain transactions involving refundings, sinking funds, reserve and replacement funds, and previously-financed expenditures. Comments on the proposed regulations stated that the anti-abuse rule under the proposed regulations did not contain any time limit for "tracing" reimbursement bond proceeds to the prohibited uses, thereby making it difficult to determine when any use of moneys for the prohibited uses would be attributed to the reimbursement allocation. One-year time limitations were added to the prohibited use provisions in response to these comments. However, reimbursement proceeds intentionally used for these prohibited uses after the 1-year period are still subject to the general anti-abuse rule.

There are two exceptions to the limitations on uses of reimbursement proceeds. Under the first exception, the limitation does not apply if the issuer deposits the moneys from the

reimbursement allocation in a bona fide debt service fund (as defined in § 1.103-13(b)(12)) or otherwise uses these moneys to pay current debt service on any obligation of the issuer (other than the reimbursement bonds). Under the second exception, the limitations with respect to refundings and expenditures originally paid with proceeds of a borrowing do not apply if the financing proceeds originally used to pay the expenditure were not reasonably expected to be used to finance that expenditure.

Because of confusion over the application of the proposed regulations to refunding bonds and reimbursements made with taxable debt, these regulations clarify the treatment of those transactions. In the case of a tax exempt refunding of a taxable bond, if proceeds of the taxable bond were allocated to reimburse a previously paid expenditure, the proceeds of the taxable bond are not deemed to have been spent unless the reimbursement allocation complied with the Federal tax law and regulations applicable to reimbursement allocations of proceeds of tax exempt issues in effect as of the date of issue of the taxable bond. If the proceeds of the taxable bond are deemed to be unspent by application of the preceding sentence, the proceeds of the taxable bond are subject to "transfer" to the tax exempt bond issued to refund the taxable bond (directly or indirectly in a series of refundings) and therefore may become proceeds of the refunding bond. For purposes of these regulations, proceeds of the taxable bond are deemed to remain unspent until a reimbursement allocation of those proceeds is made that complies with these regulations or the taxable bond proceeds are otherwise spent. The purpose of this provision is to prevent the use of a combination of taxable and tax exempt debt to circumvent the requirements of these allocation rules.

Effective Date

These regulations apply to bonds issued after March 2, 1992.

Special Analyses

These rules are not major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. Although this Treasury decision was preceded by a notice of proposed rulemaking that solicited public comments, the notice was not required by section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) since the regulations proposed in that notice and adopted by this Treasury decision are interpretive. Therefore, a final Regulatory Flexibility

Analysis is not required by the Regulatory Flexibility Act (5 U.S.C. chapter 6). Pursuant to section 7805(f) of the Internal Revenue Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal authors of these regulations are David A. Walton, Office of Tax Legislative Counsel, Department of the Treasury, and formerly of the Office of Assistant Chief Counsel (Financial Institutions and Products), Internal Revenue Service and John J. Cross III, Office of Assistant Chief Counsel (Financial Institutions and Products), Internal Revenue Service. However, other personnel from the Service and Treasury Department participated in their development.

List of Subjects

26 CFR 1.101-1—1.133-1T

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES: TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority for part 1 continues to read in part:

Authority: Sec. 7805, 68A Stat. 917 (26 U.S.C. 7805) * * *

Par. 2. New § 1.103-18 is added to read as follows:

§ 1.103-18 Proceeds of bonds used for reimbursement.

(a) *Table of contents.* This table of contents contains a listing of the headings of § 1.103-18 (a) through (l).

- (a) Table of contents.
- (b) Scope of application.
- (c) Operating rules for governmental bonds and certain private activity bonds.
 - (1) Bonds subject to these operating rules.
 - (2) Operating rules.
 - (i) Official intent requirement.
 - (ii) Reimbursement period requirement.
 - (iii) Capital expenditure requirement.
 - (d) Operating rules for certain private activity bonds.
 - (e) Definitions of reimbursement bond and reimbursement allocation.
 - (1) Definition of reimbursement bond.
 - (2) Definition of reimbursement allocation.
 - (f) Procedure for declaring official intent.

- (1) Form of official intent.
- (2) General description of property to which reimbursement relates and maximum anticipated debt.
 - (i) In general.
 - (ii) Specificity of description.
 - (iii) Project.
- (3) Public availability of official intent.
- (4) Public availability requirement.
 - (i) Safe harbors.
 - (A) Time and location safe harbors.
 - (B) Compliance with State or local law.
- (5) Special rule for conduit and "on-behalf-of" borrowers.
- (6) Reasonableness requirement for declaring official intent.
 - (1) General rule.
 - (2) Consistency with budgetary and financial circumstances.
 - (3) Reasonable expectation to reimburse.
 - (i) Factors to be considered.
 - (A) General rule.
 - (B) Examples.
 - (ii) Failure to reimburse.
 - (h) Issuance costs treated as capital expenditures.
 - (i) Special exceptions.
 - (1) Exception for official intent declared subsequent to the payment of certain unforeseeable expenditures.
 - (i) Extension of time.
 - (ii) Example.
 - (2) Special exception for preliminary expenditures.
 - (i) General rule.
 - (ii) Definition of preliminary expenditures.
 - (3) Special rule for abandonment prior to completion.
 - (j) Definition of issuer.
 - (k) Anti-abuse rules.
 - (1) General rule.
 - (2) Reimbursement allocations of proceeds of refunded bonds.
 - (i) Operating rule.
 - (ii) Example.
 - (3) Limitations on uses of reimbursement amounts.
 - (4) Exception for bona fide debt service funds.
 - (5) Exception for certain previously financed expenditures.
 - (6) Examples.
 - (i) Effective date.
 - (1) In general.
 - (2) Transitional rule for certain expenditures.

(b) *Scope of application.* This section applies only to reimbursement allocations (as defined in paragraph (e)(2) of this section) of proceeds of any reimbursement bond (as defined in paragraph (e)(1) of this section). Except as provided in paragraph (d) of this section, the anti-abuse rules contained in paragraph (k) of this section do not apply to private activity bonds described in paragraph (d) of this section.

(c) *Operating rules for governmental bonds and certain private activity bonds—(1) Bonds subject to these operating rules.* The operating rules provided in this paragraph apply only to bonds that are—

(i) Not private activity bonds described in section 141(a) (except as otherwise provided in paragraphs (c)(1) (ii) and (iii) of this section).

(ii) Qualified 501(c)(3) bonds described in section 145, or

(iii) Private activity bonds the proceeds of which are used to finance a facility that is owed by a governmental unit (within the meaning of section 142).

(2) *Operating rules.* Except as provided in paragraph (i) of this section (relating to certain unforeseeable expenditures and certain preliminary expenditures) and in paragraph (k) (relating to anti-abuse rules) of this section, for purposes of applying section 103 and 141–150, a reimbursement allocation is treated as an expenditure of proceeds of the reimbursement bond on the date of the reimbursement allocation if each of the following requirements is met—

(i) *Official intent requirement.* On or before the date the expenditure is paid by the issuer, the issuer declares a reasonable intention to reimburse the expenditure with proceeds of a borrowing.

(ii) *Reimbursement period requirement.* The reimbursement allocation occurs not earlier than the date on which the expenditure is paid and not later than 1 year after the later of—

(A) The date on which the expenditure is paid, or

(B) The date on which the property is placed in service.

(iii) *Capital expenditure requirement.* The expenditure to be reimbursed is a capital expenditure (as defined in § 1.150–1(h)).

(d) *Operating rules for certain private activity bonds.* In the case of a reimbursement allocation of proceeds of an exempt facility bond under section 141(e)(1)(A) or a qualified small issue bond under section 141(e)(1)(D), a reimbursement allocation is treated as an expenditure of proceeds of the reimbursement bond on the date of the reimbursement allocation for purposes of applying section 103 and 141–150 if the property financed meets the requirements imposed under § 1.103–8(a)(5) and the reimbursement allocation does not violate the anti-abuse rules of paragraphs (k)(1) and (k)(3)(ii)–(iii) of this section.

(e) *Definitions of reimbursement bond and reimbursement allocation—(1) Definition of reimbursement bond.* For purposes of this section, "reimbursement bond" means the portion of an issue allocated to reimburse an expenditure that was paid prior to the date of issue. Thus, "reimbursement bond" does not include that portion of an issue

allocated to reimburse an expenditure that is paid on or after the date of issue of the bond issue.

(2) *Definition of reimbursement allocation.* For purposes of this section, the term "reimbursement allocation" means an allocation of proceeds of a reimbursement bond to pay an expenditure if—

(i) The allocation is evidenced by an entry on the books or records of the issuer maintained with respect to the bonds.

(ii) The allocation entry identifies either an actual prior expenditure to be reimbursed or, in the case of a reimbursement of a fund or an account, the fund or account from which the expenditure was paid, and

(iii) As a result of the allocation, the bond proceeds covered by the entry are relieved from any restrictions under the relevant legal documents and applicable state law that apply to unspent bond proceeds.

(f) *Procedure for declaring official intent—(1) Form of official intent.* For purposes of paragraph (c)(2)(i) of this section, an issuer declares an intention to reimburse an expenditure ("official intent") if—

(i) The issuer, or any person or entity designated by the issuer to declare official intent on behalf of the issuer, states that the issuer reasonably expects to reimburse the expenditure with proceeds of debt to be incurred by the issuer.

(ii) The statement of official intent specifically states that it is a declaration of official intent under this section.

(iii) The statement contains the other information required by paragraph (f)(2) of this section, and

(iv) The public availability requirements contained in paragraph (f)(3) of this section are satisfied.

(2) *General description of property to which reimbursement relates and maximum anticipated debt—(i) In general.* The declaration of official intent must contain, at minimum, a general functional description of the project (as defined in paragraph (f)(2)(iii) of this section) for which the expenditure to be reimbursed is paid (e.g., "highway capital improvement program," "hospital equipment acquisition," "school building renovation," etc.) and a statement of the maximum principal amount of debt expected to be issued for such purposes.

(ii) *Specificity of description.* A description of project is sufficient if it identifies the fund or account from which the expenditure to be reimbursed is paid and describes the general functional purpose of the fund or

account (e.g., "parks and recreation fund—recreational facility capital improvement program"). Reasonable deviations between a project described in a declaration of official intent and an actual project financed with a reimbursement bond do not invalidate an otherwise valid official intent if the actual project financed is reasonably related in function to the project described in the declaration of official intent. For example, reimbursement of an expenditure for hospital equipment is a reasonable deviation from a project described in a declaration of official intent as "hospital building improvements." In contrast, reimbursement of an expenditure for a rehabilitation of a city office building is not a reasonable deviation from a project described in the declaration of official intent as "highway improvements".

(iii) *Project*. For purposes of this section, "project" means a property, project, or program.

(3) *Public availability of official intent*—(i) *Public availability requirement*. The declaration of official intent must be reasonably available for public inspection within a reasonable period of time after the declaration of official intent.

(ii) *Safe harbors*. A declaration of official intent satisfies the public availability requirement set forth in paragraph (f)(3)(i) of this section if—

(A) *Time and location safe harbor*. Within 30 days after the date of the declaration, it is made available for public inspection at the main administrative office of the issuer or at the customary location of records of the issuer that are available to the general public and it remains available for public inspection on a reasonable basis until the date of issue of the reimbursement bonds, or

(B) *Compliance with State or local law*. The issuer complies with applicable State or local law governing the public availability of records of official acts of the actual issuer other than a law that was adopted for a purpose of avoiding or minimizing the public availability requirement of this paragraph (f)(3).

(4) *Special rule for conduit and "on-behalf-of" borrowers*. If, under paragraph (j) of this section, a conduit borrower (rather than the actual issuer) is treated as the issuer of the reimbursement bonds, or if the actual issuer issues on behalf of another entity (the "on-behalf-of unit"), any of the requirements of this paragraph (f) may be met by the conduit borrower, the actual issuer, or the on-behalf-of unit. For example, a declaration of official intent made available for public

inspection within 30 days after the date of the declaration either at the main administrative office of the conduit borrower or at the main administrative office or customary location of records of the governmental entity reasonably expected to issue the reimbursement bonds is reasonably available for public inspection for purposes of paragraph (f)(3)(ii)(A) of this section.

(g) *Reasonableness requirement for declaring official intent*—(1) *General rule*. A declaration of official intent to reimburse an expenditure is reasonable only if, as of the date of the declaration—

(i) It is consistent with the budgetary and financial circumstances of the issuer, and

(ii) The issuer reasonably expects to reimburse the expenditure with proceeds of a borrowing.

(2) *Consistency with budgetary and financial circumstances*. In general, a declaration of official intent is consistent with an issuer's budgetary and financial circumstances if no funds from sources other than the reimbursement bond issue are, or are reasonably expected to be, reserved, allocated on a long-term basis, or otherwise set aside by the issuer or by any member of the same controlled group as the issuer pursuant to their budget or financial policies with respect to the expenditure to be reimbursed. See § 1.150-1(f) for a definition of controlled group.

(3) *Reasonable expectation to reimburse*—(i) *Factors to be considered*—(A) *General rule*. The determination of whether, at the time of the declaration of official intent, an issuer reasonably expects to reimburse an expenditure with proceeds of a borrowing is based on all the relevant facts and circumstances, including the issuer's purposes for declaring official intent, its history of actual reimbursement of other expenditures for which official intent was declared and which were actually paid, and its actions taken toward reimbursement of the expenditures. Declarations of official intent that are made as a matter of course or are made for amounts of expenditures substantially in excess of amounts reasonably necessary for a described project (e.g., "blanket" declarations of official intent) do not meet the reasonable expectation requirement.

(B) *Examples*. The operation of this paragraph (g)(3)(i) is illustrated by the following examples.

Example 1. In order to preserve the option of reimbursing expenditures, an issuer declares official intent with respect to all expenditures it pays from cash on hand. A

declaration of official intent made under these circumstances does not meet the reasonable expectation requirement.

Example 2. An issuer is planning on making certain expenditures that it expects to reimburse only if an expected grant or other source of money is not received. There is a reasonable possibility that the grant or other source of money will not be received or will be received a significant period of time after the expenditure is paid. The issuer declares an official intent to reimburse the expenditures in the event the grant is not received or is substantially delayed. Under these circumstances, the declaration of official intent meets the reasonable expectation requirement.

(ii) *Failure to reimburse*. A pattern of failing to reimburse expenditures for which official intent was declared and that were actually paid by the issuer is one factor indicating that the issuer does not reasonably expect to reimburse the expenditure for which official intent is declared. To the extent that a failure to reimburse was due to extraordinary circumstances that were beyond the control of the issuer and that could not have been foreseen, failure to reimburse is not taken into account in determining the reasonable expectations of the issuer. Examples of extraordinary circumstances include unexpected significant increases in interest rates, unexpected reductions in creditworthiness of the issuer, unexpected judicial or legislative impediments that make the financing uneconomic or impractical, unexpected or emergency borrowing for other needs that cause the issuer to reach its borrowing limits, and unexpected significant increases in tax or other revenues (or significant reductions in expected expenditures) that make the reimbursement unnecessary because of the increase in available funds.

(h) *Issuance costs treated as capital expenditures*. For purposes of this section, costs of issuing a reimbursement bond paid out of proceeds of the issue that are properly allocable to the reimbursement are treated as capital expenditures.

(i) *Special exceptions*—(1) *Exception for official intent declared subsequent to the payment of certain unforeseeable expenditures*—(i) *Extension of time*. If an expenditure was not reasonably foreseeable at least 30 days before its payment, the date (described in paragraph (c)(2)(i) of this section) by which official intent must be declared is extended to the date 45 days after the payment was made.

(ii) *Example*. The operation of this paragraph (i)(1) is illustrated by the following example.

Example. On June 1, 1992, fire destroyed city B's data processing system. On June 5, 1992, B purchased replacement data processing equipment with moneys on hand in its general operating fund. On June 25, 1992, B declared official intent to reimburse the cost of the equipment. Because B could not have reasonably foreseen the destruction of the equipment, for purposes of paragraph (c)(2)(i) of this section, the period for declaring official intent to reimburse the expenditure is extended to July 20, 1992, and therefore B's intent was declared during the required period.

(2) *Special exception for preliminary expenditures*—(i) *General rule.* The official intent requirement of paragraph (c)(2)(i) of this section does not apply to preliminary expenditures (as defined in paragraph (i)(2)(ii) of this section) that are reimbursed with proceeds of a bond that finances all or a portion of the project with respect to which the preliminary expenses were incurred.

(ii) *Definition of preliminary expenditures.* For purposes of this paragraph, subject to the limitation in the following sentence, the term "preliminary expenditures" includes architectural, engineering, surveying, soil testing, reimbursement bond issuance, and similar costs that are incurred prior to commencement of construction, rehabilitation, or acquisition of a project, but does not include land-acquisition, site preparation, and similar costs incident to commencement of construction. Preliminary expenditures include only amounts that do not exceed in the aggregate 20 percent of the issue price of that portion of the issue or issues that finance the project with respect to which the preliminary expenditures were incurred. For purposes of the preceding sentence, issue price is determined in the same manner as under § 1.148-8T(c).

(3) *Special rule for abandonment prior to completion.* For a project abandoned prior to completion, the reimbursement period requirement of paragraph (c)(2)(ii) of this section is satisfied with respect to expenditures paid with respect to the abandoned project only if the reimbursement allocation for those expenditures is made by the later of—

(i) The date that is 1 year after the date that the project is abandoned, or

(ii) The date 2 years after the last payment of an expenditure with respect to the abandoned project that is not less than the lesser of \$25,000 or 5 percent of the cost of the project.

(j) *Definition of issuer.* For purposes of this section, "issuer" generally means the entity that actually issues the reimbursement bond (the "actual issuer"). If the proceeds of a reimbursement bond are provided to a

conduit borrower (as defined in § 1.150-1(g)), the term issuer generally means the conduit borrower and does not include the actual issuer.

(k) *Anti-abuse rules*—(1) *General rules.* A purported reimbursement allocation of bond proceeds is not treated as an expenditure of the bond proceeds if any action or inaction of the issuer with respect to the allocation is an artifice or device under § 1.103-13(j) or § 1.148-9T(g) to avoid, in whole or in part, arbitrage yield restrictions or arbitrage rebate requirements.

(2) *Reimbursement allocations of proceeds of refunded bonds*—(1) *Operating rule.* Amounts allocable to a taxable issue of bonds are treated as unspent proceeds of the taxable bonds (and thus are subject to "transfer" to a refunding issue of tax exempt bonds) if—

(A) The proceeds of the taxable bonds are allocated by the issuer to reimburse an expenditure that was paid by or on behalf of the issuer prior to the date of issue of the taxable bonds.

(B) If the taxable bonds were an issue of tax exempt bonds, the purported reimbursement would not be treated for Federal income tax purposes as an expenditure of the bond proceeds.

(C) The taxable issue is refunded directly or indirectly in a series of refundings by the tax exempt refunding issue, and

(D) The refunding issue is issued on or after March 2, 1992.

(ii) *Example.* The operation of this paragraph (k)(2) is illustrated by the following example.

Example. In 1999, city issues its tax exempt series 1999 bonds to refund its taxable series 1997 bonds (issued in 1997). The series 1997 bonds refunded the city's taxable series 1995 "new money" bonds. The proceeds of the series 1995 bonds were used to reimburse expenditures paid by the city prior to the date of issue of the series 1995 bonds. The principles of this paragraph (k)(2) apply to the original issue the proceeds of which were used to reimburse prior expenditures (the series 1995 bonds) to the extent that the proceeds of the series 1995 bonds would be treated as proceeds of the series 1999 bonds had all the bonds in the series of refundings been tax exempt. These unspent proceeds remain unspent either until a reimbursement allocation is made that complies with the relevant requirements of this section or the bond proceeds are otherwise spent.

(3) *Limitations on uses of reimbursement amounts.* Except as otherwise provided in this section, an allocation of bond proceeds to reimburse a previously paid expenditure is not treated as an expenditure of the bond proceeds if, but for the allocation, the bond proceeds are used directly or indirectly—

(i) Within 1 year of the date of the reimbursement allocation, to "refund" an issue of governmental obligations within the meaning of section 148,

(ii) Within 1 year of the date of the reimbursement allocation, to create or increase the balance in a "sinking fund" (within the meaning of § 1.103-13(g)) with respect to any obligation of the issuer, or to replace funds that have been, are being, or will be so used for sinking fund purposes,

(iii) Within 1 year of the date of the reimbursement allocation, to create or increase the balance in a "reserve or replacement fund" (within the meaning of § 1.103-14(d)) with respect to any obligation of the issuer, or to replace funds that have been, are being, or will be so used for reserve or replacement fund purposes, or

(iv) To reimburse any person (other than the issuer) for any expenditure or payment that was originally paid with proceeds of any obligation of the issuer (other than a borrowing by the issuer from one of its own funds or the funds of a member of the same controlled group).

(4) *Exception for bona fide debt service funds.* Paragraph (k)(3) of this section does not apply (and thus does not prevent a reimbursement allocation from being treated as an expenditure of bond proceeds) if the issuer deposits the moneys from the reimbursement allocation in a bona fide debt service fund (as defined in § 1.103-13(b)(12)) or otherwise uses these moneys to pay current debt service coming due within the next succeeding 1-year period on any obligation of the issuer (other than the reimbursement bonds).

(5) *Exception for certain previously financed expenditures.* Paragraphs (k)(3) (i) and (iv) of this section do not apply (and thus do not prevent a reimbursement allocation from being treated as an expenditure of bond proceeds) if, as of the date of issue of the bond originally used to pay the expenditure for which a reimbursement allocation is made (the "original financing"), the issuer did not reasonably expect to finance the expenditure with the proceeds of the original financing.

(6) *Examples.* The operation of this paragraph (k) is illustrated by the following examples.

Example 1. (i) City C issues \$10,000,000 principal amount of its taxable bonds on April 20, 1992 (the 1992 taxable bonds), and allocates all of the proceeds to reimburse expenditures it paid on March 1, 1988, for property that was immediately placed in service by C. The expenditures do not constitute preliminary expenditures as defined in paragraph (i) of this section. The

reimbursement allocation of the 1992 taxable bond proceeds is not treated as an expenditure of the 1992 taxable bond proceeds under this section because the allocation violates the reimbursement period requirement of paragraph (c)(2)(ii) of this section.

(ii) On November 12, 1992, C issues \$10,000,000 principal amount of its tax exempt refunding bonds and uses the proceeds to immediately redeem all of the outstanding 1992 taxable bonds. Because the reimbursement allocation of the 1992 taxable bond proceeds does not comply with the requirements of this section, under paragraph (k)(2) of this section, the proceeds of the 1992 taxable bonds are deemed to be unspent.

Example 2. County D issues reimbursement bonds with a yield of 7 percent per annum and reimburses a previously paid expenditure. D immediately uses the proceeds of the reimbursement bond to create a sinking fund with respect to an issue of its outstanding tax exempt bonds. The outstanding tax exempt bonds have a yield of 9 percent per annum. As a sinking fund of the outstanding 9 percent bonds, the reimbursement moneys are restricted to a yield of 9 percent per annum. If D had issued bonds to advance refund the outstanding 9 percent bonds and the advance refunding bonds had a yield of 7 percent per annum, the refunding escrow created with the proceeds of the advance refunding bonds would be restricted to a yield of 7 percent per annum. Thus, D's use of the reimbursement proceeds is the equivalent of a refunding for purposes of section 148 of the Code, and the creation of a sinking fund violates § 1.103-18(k)(3)(ii). In addition, this transaction violates the arbitrage yield limitations imposed by section 148(a).

Example 3. On April 20, 1992, City E borrows \$30,000 from a bank (tax exempt) and immediately purchases 2 police cars with the loan proceeds. On September 12, 1992, E issues general obligation bonds and proposes to use \$30,000 of the bond proceeds to reimburse itself for the police cars. Because the police cars were financed with proceeds of an obligation incurred for the purpose of financing the police cars, the allocation of bond proceeds to reimburse the expenditure for the police cars is not treated as an expenditure of the bond proceeds. Even if the \$30,000 bank loan were not outstanding at the time of E's issuance of the general obligation bonds on September 12, 1992, the results of this example would be the same.

Example 4. The facts are the same as in Example 3 except that instead of borrowing \$30,000 from the bank, E finances the purchase of the police cars by using \$30,000 of proceeds of its tax exempt general obligation bonds issued on February 5, 1992. On February 5, 1992, E reasonably expects to use the proceeds of the general obligation bonds to finance the renovation of city hall and not to finance police cars. The \$30,000 expenditure is eligible for a reimbursement allocation if it meets the other relevant requirements of this section.

(l) **Effective date—(1) In general.** The provisions of this section apply to all allocations of proceeds of

reimbursement bonds issued after March 2, 1992.

(2) **Transitional rule for certain expenditures.** The requirement of paragraph (c)(2)(i) of this section (concerning official intent) with respect to an expenditure paid by the issuer does not apply if—

(i) The expenditure was paid by the issuer after September 8, 1989, and before March 2, 1992,

(ii) There is objective evidence that, at the time the expenditure was paid, the issuer expected to reimburse the expenditure with proceeds of a borrowing (taxable or tax exempt), and

(iii) That expectation was reasonable as defined in paragraph (g) of this section.

Par. 3. The following new section 1.150-1 is added to read as follows:

§ 1.150-1 Definitions and special rules relating to tax exempt bond requirements in general.

(a) through (e) [Reserved]

(f) **Controlled group.** A controlled group of entities is a group of entities controlled directly or indirectly by the same entity or group of entities within the meaning of paragraphs (f)(1) or (f)(2) of this section.

(1) **Direct control.** The determination of direct control is made on the basis of all the relevant facts and circumstances. However, generally one entity or group of entities (the "controlling entity") controls another entity or group of entities (the "controlled entity") for purposes of this paragraph if the controlling entity possesses simultaneously at least two of the following rights or powers and the rights or powers are discretionary and non-ministerial—

(i) The right or power to remove or cause to be removed without cause a controlling portion of the governing body of the controlled entity,

(ii) The right or power to select, approve of, or disapprove of a controlling portion of the governing body of the controlled entity,

(iii) The right or power to determine the budget of the controlled entity or to require the use of funds or assets of the controlled entity for any purpose of the controlling entity, or

(iv) The right or power to approve, disapprove, or prevent the issuance of debt obligations by the controlled entity.

(2) **Indirect control.** If a controlling entity controls a controlled entity under the test in paragraph (f)(1) of this section, then the controlling entity also controls all entities controlled, directly or indirectly, by the controlled entity or entities.

(3) **Example.** The operation of this paragraph (f) is illustrated by the following example.

Example. State law prohibits authority A from issuing bonds unless city C approves the issue. C, however, is required by state law to approve A's bond issues if the bonds meet certain objective criteria. C does not control, directly or indirectly, the establishment of the bond approval criteria. C possesses a purely ministerial or non-discretionary right or power with respect to A.

(g) **Conduit borrower.** The term "conduit borrower" means the obligor on a purpose investment (as defined in § 1.148-8T(e)(10)). For example, if an issuer invests proceeds in a purpose investment in the form of a loan, lease, installment sale obligation or similar obligation, to another entity (the obligor on the purpose investment) and the obligor uses the proceeds to carry out the governmental purpose of the issue, the obligor is a conduit borrower.

(h) **Capital expenditure.** The term "capital expenditure" means any cost of a type that is properly chargeable to capital account (or would be so chargeable with a proper election) under general Federal income tax principles. Whether an expenditure is a capital expenditure is determined at the time the expenditure is paid with respect to the property. Future changes in law do not affect whether an expenditure is a capital expenditure. For example, costs incurred to acquire, construct, or improve land, buildings, and equipment generally are capital expenditures. Capital expenditures do not include expenditures for items of current operating expense that are not properly chargeable to capital account (so called "working capital items").

(1) **Effective date—(1) [Reserved]**

(2) **Effective dates for definitions of control, conduit borrower, and capital expenditure.** The definitions contained in § 1.150-1 (f), (g), and (h) apply to bonds issued after March 2, 1992.

PART 602—OMB CONTROL NUMBER UNDER THE PAPERWORK REDUCTION ACT

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

Authority: 26 U.S.C. 7805.

§ 602.101 [Amended]

Par. 5. Section 602.101(c) is amended by adding the following entry in the table:

"§ 1.103-18..... 1545-1226".

Michael J. Murphy,

Acting Commissioner of Internal Revenue.

Approved: December 24, 1991.

Kenneth W. Gideon,

Assistant Secretary of the Treasury.

[FR Doc. 92-2023 Filed 1-27-92; 8:45 am]

BILLING CODE 4830-01-M

26 CFR Part 301

[T.D. 8392]

RIN 1545-AM75

Civil Cause of Action for Unauthorized Collection Actions

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide guidance relating to the civil cause of action under section 7433 of the Internal Revenue Code of 1986 (the "Code") for certain unauthorized collection actions. The cause of action for unauthorized collection actions was created by section 6241 of the Technical and Miscellaneous Revenue Act of 1988. The regulations define certain key terms in the underlying statute and create an administrative remedy that must be exhausted prior to the filing of a cause of action. The regulations are needed to provide taxpayers with guidance and to create an administrative remedy in connection with this cause of action.

EFFECTIVE DATE: These regulations are effective with respect to actions filed after January 30, 1992.

FOR FURTHER INFORMATION CONTACT: Kevin B. Connelly, 202-535-9682 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

Background

This document contains final regulations amending the Procedure and Administration Regulations (26 CFR part 301) pursuant to section 7433 of the Internal Revenue Code. The regulations reflect the addition of section 7433 to the Internal Revenue Code by section 6241 of the Technical and Miscellaneous Revenue Act of 1988 (Pub. L. No. 100-647).

Explanation of Provisions

The Internal Revenue Service published a notice of proposed rulemaking in the *Federal Register* on May 25, 1991 [26 FR 28842], providing rules under section 7433 of the Code. The final regulations adopt the rules

contained in the notice of proposed rulemaking without change.

Section 6241 of the Technical and Miscellaneous Revenue Act of 1988 (Pub. L. No. 100-647, 102 Stat. 3342) added section 7433 to the Code. Section 7433 gives taxpayers the right to bring an action for damages in federal district court if, in connection with the collection of a federal tax, any officer or employee of the Internal Revenue Service recklessly or intentionally disregards any provision of the Internal Revenue Code or any regulation promulgated under the Internal Revenue Code. The taxpayer has a duty to mitigate damages, and the total amount of damages recoverable under section 7433 is the lesser of \$100,000, or the sum of (i) the actual, direct economic damages sustained as a proximate result in the internal revenue officer's or employee's wrongful conduct, and (ii) costs of the action. No action may be filed in federal district court until the taxpayer exhausts administrative remedies available within the Internal Revenue Service.

The regulations define actual, direct economic damages as actual pecuniary damages sustained by a taxpayer as a proximate result of reckless or intentional actions of an internal revenue officer or employee. Injuries such as inconvenience, emotional distress and loss of reputation are compensable only to the extent that they result in actual pecuniary damages. Litigation and administrative costs are not recoverable under the regulations as actual, direct economic damages.

The Internal Revenue Service received only one comment concerning the proposed regulations. That comment proposed to include administrative costs in the definition of actual, direct economic damages. This issue was considered at length during the drafting of the proposed regulations, and for the reasons discussed below the final regulations adopt without change the definition of actual, direct economic damages contained in the proposed regulations.

According to the common law "American Rule", damages do not include any costs incurred by parties in seeking relief. Generally, each party must pay its own costs. If the right to receive costs from an opposing party exists at all, the right exists only by virtue of a contract or specific statutory authority.

While section 7433 does provide for the recovery of certain costs, recovery is limited specifically to costs of the civil action in federal district court. The final regulations thus define costs of the action recoverable under section

7433(b)(2) as: (1) Fees of the clerk and marshal; (2) fees of the court reporter for all or any part of the stenographic transcript necessarily obtained for use in the case; (3) fees and disbursements for printing and witnesses; (4) fees for exemplification and copies of papers necessarily obtained for use in the case; (5) docket fees; and (6) compensation of court appointed experts and interpreters. Costs of the action do not include any costs other than those costs specifically enumerated in the regulations. Therefore, administrative costs are not recoverable as economic damages or as costs of the action.

In addition, costs of the action do not include attorneys fees. Under the common law "American Rule", the term "costs of the action" in a statute is not ordinarily interpreted to include attorney's fees. In other contexts, where Congress intended to provide for the recovery of attorney's fees, Congress specifically provided that attorney's fees are recoverable in addition to or together with costs of the action. See section 6110(i)(2)(B) of the Code.

Reasonable litigation costs, including attorney's fees (generally limited to \$75 per hour), not recoverable under section 7433 may be recoverable under section 7430. If following the Internal Revenue Service's denial of an administrative claim on the grounds that the Internal Revenue Service did not violate section 7433(a), a taxpayer brings a civil action for damages in a district court of the United States, and establishes entitlement to damages under this section, substantially prevails with respect to the amount of damages in controversy and meets the requirements of section 7430(c)(4)(A)(iii) (relating to notice and net worth requirements), the taxpayer will be considered a "prevailing party" for purposes of section 7430. Such taxpayer, therefore, will generally be entitled to attorney's fees and other reasonable litigation costs not recoverable under section 7433.

Administrative costs, including attorney's fees incurred pursuing an administrative claim for damages under section 7433, are not recoverable under section 7430. Section 7430(c)(2) provides that recoverable administrative costs include only those costs incurred on or after the earlier of (1) the date of the receipt by the taxpayer of the notice of a decision by the Internal Revenue Service Office of Appeals, and (2) the date of the notice of deficiency. The legislative history to the Technical and Miscellaneous Revenue Act of 1988 indicates that this limitation is intended to prevent recovery of administrative

costs incurred in a collection action. H.R. Conf. Rep. No. 1104, 100th Cong., 2d Sess. 226 (1988).

The regulations provide that an action may not be maintained in federal district court under section 7433 unless the taxpayer first files an administrative claim for damages with the Internal Revenue Service. The claim must be made in writing to the district director (marked for the attention of Chief, Special Procedures Function) of the district in which the taxpayer currently resides. The claim must include: (1) The name, current address, current home and work telephone numbers and any convenient times to be contacted, and taxpayer identification number of the taxpayer making the claim; (2) the grounds, in detail, for the claim; (3) a description of the damages incurred by the taxpayer; (4) the dollar amount of the claim, including an estimate of damages that have not yet been incurred, but that are reasonably foreseeable; and (5) the signature of the taxpayer or duly authorized representative. A taxpayer is precluded from maintaining a civil action for an amount greater than the amount (already incurred and estimated) specified in the administrative claim, except where the increased amount is based upon newly discovered evidence not reasonably discoverable at the time the administrative claim was filed, or upon allegation and proof of intervening facts relating to the amount of the claim.

The regulations provide that, after an administrative claim has been filed, an action may not be filed in federal district court until the earlier of (1) the time a decision is rendered on the claim or (2) six months from the date the administrative claim is filed. A taxpayer, however, must file an action in federal district court within two years after a cause of action accrues. Thus, if an administrative claim is filed in the last six months before the two-year limitation period expires, the taxpayer may file an action in federal district court any time after the administrative claim is filed and before the expiration of the two-year limitation period. A cause of action accrues under this section when the taxpayer has had a reasonable opportunity to discover all essential elements of a possible cause of action.

For purposes of the recovery of litigation costs under section 7430, if the Internal Revenue Service does not respond on the merits to an administrative claim for damages within six months after the claim is filed, the Internal Revenue Service's failure to respond will be considered a denial of

the claim on the grounds that Internal Revenue Service did not violate section 7433(a).

Special Analyses

It has been determined that these final regulations are not major rules as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, an initial Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking for the regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comments on their impact on small business.

Drafting Information

The principal author of these regulations is Kevin B. Connelly, Office of Assistant Chief Counsel (General Litigation), Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 301

Administrative practice and procedure, Alimony, Bankruptcy, Child support, Continental shelf, Courts, Crime, Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Investigations, Law enforcement, Oil pollution, Penalties, Pensions, Reporting and recordkeeping requirements, Statistics, Taxes.

Adoption of Addition to the Regulations

Accordingly, title 26, part 301 of the Code of Federal Regulations is amended as follows.

PART 301—[AMENDED]

Paragraph 1. The authority citation for part 301 continues to read in part:

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

Par. 2. Section 301.7433-1 is added under "Proceedings by Taxpayers and Third Parties" to read as follows:

§ 301.7433-1 Civil cause of action for certain unauthorized collection actions.

(a) *In general.* If, in connection with the collection of a federal tax with respect to a taxpayer, an officer or an employee of the Internal Revenue Service recklessly or intentionally disregards any provision of the Internal Revenue Code or any regulation promulgated under the Internal Revenue

Code, such taxpayer may bring a civil action for damages against the United States in federal district court. The taxpayer has a duty to mitigate damages. The total amount of damages recoverable is the lesser of \$100,000, or the sum of:

(1) The actual, direct economic damages sustained as a proximate result of the reckless or intentional actions of the officer or employee; and

(2) Costs of the action. An action for damages filed in federal district court may not be maintained unless the taxpayer has filed an administrative claim pursuant to paragraph (e) of this section, and has waited for the period required under paragraph (d) of this section.

(b) *Actual, direct economic damages—(1) Definition.* Actual, direct economic damages are actual pecuniary damages sustained by the taxpayer as the proximate result of the reckless or intentional actions of an officer or an employee of the Internal Revenue Service. Injuries such as inconvenience, emotional distress and loss of reputation are compensable only to the extent that they result in actual pecuniary damages.

(2) *Litigation costs and administrative costs not recoverable.* Litigation costs and administrative costs are not recoverable as actual, direct economic damages. Litigation costs may be recoverable under section 7430 (see paragraph (h) of this section) or, solely to the extent described in paragraph (c) of this section, as costs of the action.

(i) *Litigation costs.* For purposes of this paragraph, litigation costs are any costs incurred pursuing litigation for relief from the action taken by the officer or employee of the Internal Revenue Service, including costs incurred pursuing a civil action in federal district court under paragraph (a) of this section. The term litigation costs includes the following:

(A) Court costs;
(B) Expenses of expert witnesses in connection with a court proceeding;
(C) Cost of any study, analysis, engineering report, test, or project prepared for a court proceeding; and
(D) Fees paid or incurred for the services of attorneys, or other individuals authorized to practice before the court, in connection with a court proceeding.

(ii) *Administrative costs.* For purposes of this section, administrative costs are any costs incurred pursuing administrative relief from the action taken by an officer or employee of the Internal Revenue Service, including costs incurred pursuing an administrative claim for damages under

paragraph (e) of this section. The term administrative costs includes:

(A) Any administrative fees or similar charges imposed by the Internal Revenue Service; and

(B) Expenses, costs, and fees described in paragraph (b)(2)(i) of this section incurred pursuing administrative relief.

(c) *Costs of the action.* Costs of the action recoverable as damages under this section are limited to the following costs:

(1) Fees of the clerk and marshal;

(2) Fees of the court reporter for all or any part of the stenographic transcript necessarily obtained for use in the case;

(3) Fees and disbursements for printing and witnesses;

(4) Fees for exemplification and copies of paper necessarily obtained for use in the case;

(5) Docket fees; and

(6) Compensation of court appointed experts and interpreters.

(d) *No civil action in federal district court prior to filing an administrative claim*—(1) Except as provided in paragraph (d)(2) of this section, no action under paragraph (a) of this section shall be maintained in any federal district court before the earlier of the following dates:

(i) The date the decision is rendered on a claim filed in accordance with paragraph (e) of this section; or

(ii) The date six months after the date an administrative claim is filed in accordance with paragraph (e) of this section.

(2) If an administrative claim is filed in accordance with paragraph (e) of this section during the last six months of the period of limitations described in paragraph (g) of this section, the taxpayer may file an action in federal district court any time after the administrative claim is filed and before the expiration of the period of limitations.

(e) *Procedures for an administrative claim*—(1) *Manner.* An administrative claim for the lesser of \$100,000 or actual, direct economic damages as defined in paragraph (b) of this section shall be sent in writing to the district director (marked for the attention of the Chief, Special Procedures Function) of the district in which the taxpayer currently resides.

(2) *Form.* The administrative claim shall include:

(i) The name, current address, current home and work telephone numbers and any convenient times to be contacted, and taxpayer identification number of the taxpayer making the claim;

(ii) The grounds, in reasonable detail, for the claim (include copies of any

available substantiating documentation or correspondence with the Internal Revenue Service);

(iii) A description of the injuries incurred by the taxpayer filing the claim (include copies of any available substantiating documentation or evidence);

(iv) The dollar amount of the claim, including any damages that have not yet been incurred but which are reasonably foreseeable (include copies of any available substantiating documentation or evidence); and

(v) The signature of the taxpayer or duly authorized representative. For purposes of this paragraph, a duly authorized representative is any attorney, certified public accountant, enrolled actuary, or any other person permitted to represent the taxpayer before the Internal Revenue Service who is not disbarred or suspended from practice before the Internal Revenue Service and who has a written power of attorney executed by the taxpayer.

(f) *No action in federal district court for any sum in excess of the dollar amount sought in the administrative claim.* No action for actual, direct economic damages under paragraph (a) of this section shall be instituted in federal district court for any sum in excess of the amount (already incurred and estimated) of the administrative claim filed under paragraph (e) of this section, except where the increased amount is based upon newly discovered evidence not reasonably discoverable at the time the administrative claim was filed, or upon allegation and proof of intervening facts relating to the amount of the claim.

(g) *Period of limitations*—(1) *Time for filing.* A civil action under paragraph (a) of this section must be brought in federal district court within 2 years after the date the cause of action accrues.

(2) *Right of action accrues.* A cause of action under paragraph (a) of this section accrues when the taxpayer has had a reasonable opportunity to discover all essential elements of a possible cause of action.

(h) *Recovery of costs under section 7430.* Reasonable litigation costs, including attorney's fees, not recoverable under this section may be recoverable under section 7430. If following the Internal Revenue Service's denial of an administrative claim on the grounds that the Internal Revenue Service did not violate section 7433(a), a taxpayer brings a civil action for damages in a district court of the United States, and establishes entitlement to damages under this section, substantially prevails with respect to the amount of damages in controversy and

meets the requirements of section 7430(c)(4)(A)(iii) (relating to notice and net worth requirements), the taxpayer will be considered a "prevailing party" for purposes of section 7430. Such taxpayer, therefore, will generally be entitled to attorney's fees and other reasonable litigation costs not recoverable under this section. For purposes of this paragraph, if the Internal Revenue Service does not respond on the merits to an administrative claim for damages within six months after the claim is filed, the Internal Revenue Service's failure to respond shall be considered a denial of the claim on the grounds that the Internal Revenue Service did not violate section 7432(a). Administrative costs, including attorney's fees incurred pursuing an administrative claim under paragraph (e) of this section, are not recoverable under section 7430.

(i) *Effective date.* This section applies with respect to civil actions under section 7433 filed after January 30, 1992.

Fred T. Goldberg, Jr.,

Commissioner of Internal Revenue.

Approved: December 31, 1991.

Kenneth W. Gideon,

Assistant Secretary of the Treasury.

[FR Doc. 92-2024 Filed 1-29-92; 8:45 am]

BILLING CODE 4830-01-M

26 CFR Part 301

[T.D. 8393]

RIN 1545-AM63

Civil Cause of Action for Failure to Release a Lien Under I.R.C. Section 6325

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations that provide guidance relating to the civil cause of action under section 7432 of the Internal Revenue Code of 1986 (the "Code") for the knowing or negligent failure to release a lien under section 6325 of the Code. The cause of action for the failure to release a lien was created by section 6240 of the Technical and Miscellaneous Revenue Act of 1988. The regulations define certain key terms in the underlying statute, provide procedures for a taxpayer to notify the Internal Revenue Service of the failure to release a lien and create an administrative remedy that must be exhausted prior to the filing of a cause of action. The regulations are needed to provide taxpayers with guidance and to create