Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

NUCLEAR REGULATORY COMMISSION

10 CFR Parts 170 and 171

[Docket No. PRM–170–4]

American Mining Congress; Denial of Petition for Rulemaking

AGENCY: Nuclear Regulatory Commission.

ACTION: Denial of petition for rulemaking.

SUMMARY: The Nuclear Regulatory Commission (''NRC'' or ''Commission'') received a petition for rulemaking submitted by the American Mining Congress (''petitioner'') concerning the licensing, inspection and annual fees assessed by the NRC. The petitioner requested that the NRC amend its regulations to alleviate what the petitioner claimed are inequitable impacts of NRC user and annual fees on its members, specifically for uranium recovery sites with conventional mills that have ceased operations and are awaiting NRC approval of their reclamation plans. The petitioner claimed that there is a lack of a rational relationship between fees and regulatory services. The petitioner requested that the fee be waived for any licensed facility serving solely as a cost center and not generating revenues; that licensees be given the ability to review and have input into the NRC's budget and fee development and that annual fees only be increased in proportion to normal inflation rates; that time limits be established for NRC's processing of amendment requests and cost sheets showing sample charges be provided to licensees; that more detailed information be provided to support the bills for licensing and inspection services; and that the Department of Energy (DOE) be assessed costs for NRC review of DOE sites under the Uranium Mill Tailings Radiation Control Act (UMTRCA). After careful consideration, the Commission has decided to deny the petition for rulemaking but notes that (1) the NRC will continue its current practice of providing available backup data to support Part 170 licensing and inspection billings upon request by the licensee or applicant and (2) petitioner's request that DOE be assessed fees for its UMTRCA actions was implemented in the final fee rule for FY 1994.

ADDRESSES: Copies of the petition for rulemaking, the public comments received, and the NRC's letter to the petitioner are available for public inspection or copying in the NRC Public Document Room, 2120 L Street, NW. (Lower Level), Washington, DC 20555.

FOR FURTHER INFORMATION CONTACT: Glenda C. Jackson, Office of the Controller, U.S. Nuclear Regulatory Commission, Washington, DC 20555, Telephone 301–415–6057.

SUPPLEMENTARY INFORMATION:

I. Background

On February 4, 1993, the American Mining Congress petitioned the NRC to amend 10 CFR Parts 170 and 171 to alleviate what the petitioner claimed are inequitable NRC fees assessed its members. Because the petition involved Commission fee policy, the NRC announced receipt of and solicited public comment on the petition in its April 19, 1993 (58 FR 21116), **Federal Register** notice requesting public comment on the NRC's fee policy as required by the Energy Policy Act of 1992. The Energy Policy Act of 1992 directed the NRC to review its policy for assessment of annual fees, to solicit public comment on the need for changes to this policy, and to recommend to the Congress changes needed in existing law to prevent placing an unfair burden on NRC licensees.

The petitioner requested that the NRC take the following four actions to ensure that the fee schedule bears a reasonable relationship to the benefits provided by NRC oversight and regulation.

1. Waive the annual fee for any licensed facility in a standby status and not generating revenue from use of licensed material, i.e., those facilities in standby status which still possess licenses authorizing operation. The petitioner claimed that current NRC policy violates the principle that there must be a reasonable relationship between the cost of the NRC's regulatory program and the benefits derived from the regulatory services. The petitioner also stated that the annual fee does not reflect NRC involvement with Class I (conventional mill) uranium recovery sites, particularly those that have ceased operations and are awaiting NRC approval of reclamation plans or are in standby status. The petitioner suggested that the fee regulations should take into account the NRC's own failure to complete review as the only reason these sites are assessed annual fees and should adjust those fees accordingly.

2. Institute a system that allows NRC licensees to have some control over their fees. The petitioner suggested that a licensee review board be established to (i) review NRC fees annually; (ii) monitor NRC inspection activities to prevent regulatory abuse; and (iii) propose revisions to the fee system to eliminate inequitable treatment of licensees. The petitioner stated that its central concern with the NRC fee system is the absence of built-in safeguards to prevent overzealous imposition of fees or to ensure that the fee schedule bears a reasonable relationship to the benefits provided by NRC. The petitioner believes that the current system lacks accountability, oversight, and quality control, as well as a provision for licensees to object to unreasonable costs. The petitioner also indicated that the annual fee should be increased only in proportion to normal inflation rates and stated that NRC's hourly rate is excessive for NRC staff as compared to hourly charges of a senior consultant, principal or project manager at a nationally recognized consulting firm.

3. Develop a consistent method for applying charges by setting standards for services provided by the Commission. For example, the petitioner indicated that comparable amounts should be charged for similar types of work (i.e., amendment requests), regardless of which licensee submits the request or which particular NRC employee completes the work. NRC should develop and distribute to its licensees a cost sheet describing sample charges for different types of work, establish time limits for processing amendment requests, and distribute response times to all licensees. In addition, the 10 CFR Part 170 licensing and inspection bills should show not only hours worked and hourly charges, but also a description of the work performed, the name(s) of

individual(s) who performed the work, and the dates on which the work was done.

4. Assess fees to the Department of Energy (DOE) for NRC review of DOE sites under the Uranium Mill Tailings Radiation Control Act (UMTRCA). The petitioner stated that it is inequitable and improper for DOE to receive NRC oversight and review of DOE mill tailings site reclamation activities without contributing anything to the NRC budget.

Of the 566 comments received on the fee policy review, 21 specifically addressed the AMC petition. Others who provided comments on the fee policy review addressed some of the same issues raised by the petitioner, such as inequities in the fee systems and assessment of Part 170 fees to Federal agencies because these issues were included in the overall review of NRC fee policy. Of the 21 comments, four were from fuel facility licensees, applicants, or their representatives; three were from facility licensees; one was from an Agreement State; nine were from materials licensees or medical associations; one was from two uranium recovery licensees; one was from an industry group representing fuel fabrication facilities, conversion facilities, uranium enrichment plants, material processing facilities, transporters, and other related service facilities; one was from a company holding materials, export and import, distribution, and non-power reactor licenses; and one was from the petitioner, who represents the mining and milling industry.

A majority of the commenters supported all or portions of the petition. After careful consideration of the comments, the Commission has decided to deny the petition for rulemaking for reasons stated below.

II. Responses to Comments

1. *Comment:* Although commenters did not support a full waiver of the annual fee for facilities that are not operating, several agreed that some relief should be provided in the form of reduced fees. One commenter suggested a tiered fee system that would result in full fees for operating facilities, reduced fees for facilities in shutdown or standby status, and minimal fees for licenses who have shut down and have submitted a decommissioning plan. Another commenter indicated that although the fee should not be waived, the NRC should consider the licensee's ability to pass the costs of the NRC fees to its customers—''cost passthrough''—to determine the fee level for facilities that require minimal NRC participation.

Response: The Commission acknowledges the concern raised by the petitioner regarding non-operating facilities and has carefully evaluated the comments received on this issue. The Commission has considered a range of options: (a) continuing the current policy of charging operating mills and those in standby status annual fees; (b) only charging operating mills annual fees; and (c) charging operating mills, facilities in standby status, and those with possession-only licenses annual fees. The Commission has concluded that the current policy represents the fairest option available under current legislation and therefore has denied petitioner's request. The NRC will continue to assess annual fees based on whether a licensee holds a valid license with the NRC that authorizes possession and use of radioactive material, independent of whether the facility is actively operating or in a standby status. The basic premise for this policy is that the benefit the NRC provides a licensee is the authority to use licensed material. The choice of whether or not to exercise that authority is a business decision of the licensee.

Because of the mandate that NRC recover approximately 100 percent of its budget through fees, to refrain from charging annual fees to mills in a standby status would increase the annual fees for the other licensees in the class because the number of licensees assessed annual fees would decrease. Such an approach would raise fairness concerns.

The Commission recognizes that some may perceive it to be unfair to charge a licensee an annual fee when the facility in question is not generating revenue. However, the Commission has previously considered the extent to which a licensee's economic status and ability to ''pass through'' its costs to its customers should be considered in establishing fees, and the Commission has declined to do so. As stated in the final rule published July 20, 1993 (58 FR 38666), the Commission concluded, after full consideration of the ''cost passthrough'' question, that it cannot set fees using passthrough considerations with reasonable accuracy and at reasonable costs even for classes of licensees with few members. The Commission has no new information that would cause it to change this policy. The Commission is also unable to use factors such as the revenue earned by a licensee or the licensee's profit from the use of licensed material in developing the fees because OBRA–90 requires that annual charges must, to the maximum extent practicable, have a reasonable relationship to the cost of providing regulatory services.

The Commission decided that it would not be appropriate to charge facilities who have received a POL an annual fee. While the NRC incurs generic costs relating to the decommissioning/reclamation of facilities with POLs, many POL holders were induced to relinquish their authority to operate by the Commission's policy of not charging annual fees to holders of POLs (56 FR 31485, July 10, 1991). It would be unjust at this date to change this policy with respect to these facilities. Primarily for this reason, the Commission has also decided not to implement a tiered approach recommended by some commenters, in which all licensees would pay an annual fee, including those no longer authorized to operate. In sum, the NRC will continue to waive the fee for licensees who have voluntarily relinquished the authority to operate and have ceased operations. This includes licensees who have voluntarily relinquished their authority to operate, but must continue to be licensed to possess nuclear materials, that is, possession-only licenses (POLs). In articulating our policy, we emphasize that, contrary to the petitioner's statement, reclamation or decommissioning plans do not have to be approved for the annual fee to be waived for these licensees. Therefore, petitioner's argument that some sites are charged annual fees because of the NRC's failure to complete review of reclamation plans is fallacious. The Commission's fee policy with respect to operating, standby, and POL status is consistently applied to all classes of licensees, including uranium recovery, fuel fabrication, and power reactor licensees.

2. *Comment:* A majority of the commenters supported the petitioner's request that licensees be given the ability to oversee and have input into the NRC budget and to review NRC fees annually. Commenters suggested that a review board, with at least some members representing the regulated parties, be established to review NRC activities to control costs, to ensure that maximum benefits and effectiveness are achieved, and to monitor NRC activities to prevent the appearances of regulatory abuse. One commenter stated that such a review board could benefit NRC, citing as an example that the NRC incurred higher costs by using a government laboratory than the commenter incurred using a commercial laboratory for the same type of service. Another commenter suggested that the review board propose revisions to the fee

system and methods to eliminate inequities in the treatment of licensees. Another commenter sought a greater role in the development of regulatory programs that could have a substantial impact on the economic status of licensees or result in license termination. On the other hand, one commenter disagreed with the petitioner, stating that a scheme whereby licensees would directly control the agency's activities would be inappropriate for a regulatory program. Another commenter was skeptical that the petitioner's suggestions would simplify or otherwise lead to a more equitable allocation of Commission costs.

Several commenters agreed with the petitioner that the fees charged do not reflect the benefits derived and expressed concern with the fee amounts. One commenter stated that as fees increase and more licenses are terminated, it will create a disincentive for continuing their licensed activities, which include beneficial research. This commenter suggested that the fee be proportional to the number of pieces of equipment used, the small amounts of low energy radioisotopes in use, and the status of the licensee as a business or not-for-profit organization.

Other commenters maintained that the fee increases may be due to a lack of accountability by NRC; that the frequency and details covered in inspections is unnecessary and inefficient; and that a limited number of licensees are being billed to support NRC services to Federal agencies, Agreement States, and international organizations. Some commenters suggested that NRC's management structure be reviewed to streamline activities and reduce redundancy and unnecessary paperwork, that NRC review its mechanism for calculating fees, and that either costs be borne by the organization receiving the services or these costs should be recovered through tax dollars rather than fees.

Response: The Commission addressed many of these issues and similar comments regarding the NRC budget in the final rules published July 10, 1991 (56 FR 31482), July 23, 1992 (57 FR 32696), and July 20, 1993 (58 FR 38672). As stated in these final rules, the requirement for the NRC to recover 100 percent of its budget through fees does not exempt the NRC from the normal Government budget review and decisionmaking process. The Commission monitors and controls its operating costs and is tightening its financial operations by increasing the effectiveness and efficiency of its program financing. Notably, as a result of its initial efforts, the Commission proposed, and Congress approved, a $12.7 million recision to the original appropriation for FY 1994. The NRC is committed to making its regulatory programs more efficient wherever it can do so without diminishing its ability to protect the public health and safety.

In addition to its own rigorous budget review, the NRC must submit its budget to the Office of Management and Budget for review. The NRC budget is then sent to the Congress for approval. The bases for requested NRC resources are thoroughly addressed by the Congress through hearings and written submissions. This budget process, combined with the internal NRC review process, ensures that the approved budget resources are those necessary for NRC to implement its statutory responsibilities and to carry out an effective regulatory program. The fees established by NRC must be consistent with its annual budget in order to comply with OBRA–90. As in the past, the NRC will continue to base its fees on its Congressionally approved budget authority and provide the public and licensees with detailed supporting information concerning the bases for its fees. This information will continue to be available at the activity level, the lowest level for budgeting purposes.

As a result of the very extensive review of the NRC budget, the Commission opposes the establishment of a review board to oversee the NRC budget. In 1994 testimony before Congress on the NRC's fee policy review, Chairman Selin reiterated the Commission's position that it would be inappropriate to have the regulated community make recommendations which the NRC would have to accept or rebut on how it carries out its regulatory function. The Commission also believes that there are other avenues for licensees to communicate with the NRC concerning the efficiency of the NRC's regulatory program.

Additionally, the NRC complies with legislation such as the Paperwork Reduction Act of 1980 (44 U.S.C. 3501 *et seq.*) and the Regulatory Flexibility Act of 1980 (5 U.S.C. 601 *et seq.*) that require the agency to analyze the economic effects of new regulations on licensees. The NRC staff also prepares detailed cost-benefit analyses to justify any new regulatory requirements. These analyses are carefully reviewed by the Commission. The Commission has seen nothing either in the petition or comments on the petition that would lead it to change its approach in this area. The Commission would like to emphasize, however, that licensees are always welcome and expected to comment on and propose revisions to proposed rulemakings, including the accompanying cost-benefit analyses, and that such comments, along with the day-to-day interaction between licensees and the agency, in the Commission's view provide an adequate and successful method of keeping each group apprised of the other's concerns.

For the foregoing reasons, the Commission is denying the petitioner's request that a licensee review board be established to oversee and make recommendations about NRC's budget and fees.

The Commission has also carefully considered the petitioner's concerns and the comments received regarding the annual fee increases and the hourly rate, issues which have been raised by commenters in previous rulemakings. As previously stated in the Commission's response to commenters on the FY 1993 rule (58 FR 38674), the NRC is unable to use the CPI or other indices in the development of the hourly rate or fees charged under 10 CFR Part 170 and 171 because these increases may not allow the NRC to meet the statutory requirement of OBRA–90 to recover approximately 100 percent of the NRC budget authority through fees. The NRC's Congressionally-approved budget is determined on the basis of the resources needed to carry out the agency mission. The NRC professional hourly rate is established to recover approximately 100 percent of the budget authority, less the appropriation from the Nuclear Waste Fund, as required by OBRA–90. The method and budgeted costs used by NRC in the development of the hourly rate are discussed in Part IV, Section-by-Section Analysis, of 10 CFR 170.20 in each proposed and final fee rule. The NRC budgeted costs for salaries and benefits, administrative support, travel, and program support (excluding contract or other services in support of the line organization's direct program), less offsetting receipts, are allocated uniformly to the direct FTEs. The hourly rate is calculated by dividing the budget allocated to the direct FTEs by the number of direct FTEs and the number of productive hours in one year (1,744 hours) as indicated in OMB Circular A–76, ''Performance of Commercial Activities.'' The Commission continues to believe that this cost allocation is appropriate and represents a practical and equitable way of allocating these costs to NRC licensees and applicants in order to meet the 100 percent recovery requirement of OBRA–90.

The Commission has explained in the past why it does not believe that basing

fees on factors such as number of sources, the size of the facility, and market competitive positions, as suggested by commenters, would result in a fairer allocation of the 100 percent recovery requirement. (See FY 1991 Final Rule, 56 FR 31472; July 10, 1991, and Appendix A to that Final Rule; and Limited Revision of Fee Schedules, 57 FR 13625; April 17, 1992). The Commission has seen no evidence in the petition or comments on the petition which would lead it to change its current approach of charging fees by class of license.

3. *Comment:* Most commenters supported the petitioner's request that the NRC establish standards for its activities, such as a schedule for response intervals for processing licensing actions, and provide licensees with a cost sheet indicating these schedules in order to assure licensees that services will be provided in a reasonably stated time period. However, one commenter stated that licensees should not be in a position of dictating things such as time limits for processing applications. Several commenters also supported the petitioner's request that NRC provide more detailed information with the bills. Some commenters indicated that bills should be itemized to show hours spent, a description of the work performed (specifically work performed by contractors), the name(s) of the individual(s) who completed the work, and the dates on which the work was performed.

Response: The petitioner's requests that review standards be established, that cost sheets describing sample charges be developed, and that additional information be provided on the bills pertain to NRC practices and procedures which should not be codified in a rule. The Commission cannot establish fixed costs for completing licensing actions and inspections for major fuel cycle licensees since the cost varies for such activities. License and inspection fees, established by 10 CFR Part 170 under the authority of the Independent Offices Appropriation Act (IOAA) and the Atomic Energy Act (AEA), as amended, recover the NRC's cost of providing individually identifiable services to specific applicants and licensees. The NRC's principal concern is public health and safety and thus the NRC must spend the appropriate resources to accomplish this, not a predetermined amount. While the Commission is committed to the expeditious review of each application and uses all reasonable means of keeping costs as low as feasible, its responsibility for ensuring the public health and safety and environmental protection cannot be compromised. The Commission is committed to the effective use of its increasingly limited resources and therefore cannot afford to use these resources unwisely if it is to successfully perform its mission.

In response to the request for one standard fee for the same type of action, the Commission notes that full-cost recovery fees based on the actual professional staff hour and contractual services costs expended for the review were established in 1984 for the NRC's larger licensees (reactor and major fuel cycle facilities). Previously, the IOAA fees for amendment actions and inspections of these licensees were ''flat'' fees based on the average number of hours to process the same type of licensing action or to conduct similar inspection. Commenters on the fee system at that time complained about the inequities of such a fee system for larger licensees. They pointed out that NRC's response time for applications filed by licensees could vary significantly, depending upon the quality and completeness of the information submitted by the applicant or licensee and the extent and complexity of the licensing action requested. The NRC agreed with the commenters and changed its method of assessing fees for larger licensees based on the fact that there were differences in the types and complexity of the applications being filed and the fact that the NRC maintained a system whereby employees processing applications and conducting inspections reported, on a periodic basis, the professional time expended to process an application or to conduct an inspection.

To ensure that applications are processed in a timely and cost-effective manner, each NRC office in the licensing process develops and works in accordance with an approved operating plan. Upon receipt of applications, schedules are established and resources allocated for each review based on the amount of time and professional staff effort determined necessary to complete the particular type of application or activity. Because the total assigned workload must be completed with limited resources, management is continuously challenged and, indeed, evaluated on its ability to balance workload and assigned resources in the most efficient and effective manner. Similarly, management is expected to adhere to established review schedules, and changes are approved only with suitable justification. The NRC staff's success in meeting schedules is monitored continuously and critically by both NRC management and the Commission to ensure that projects are completed expeditiously and efficiently.

For the foregoing reasons, the Commission is denying the petitioner's request that standards be established, that costs sheets describing sample charges be developed for different types of work, and that response times be established by NRC and distributed to all licensees.

With regard to the petitioner's request that additional details be provided on the bills, the NRC believes that sufficient information is currently provided to licensees or applicants on which to base payment of the invoice. NRC's invoices for full-cost licensing actions and inspections currently contain information detailing the type of service for which the costs are being billed, the date or date range the service was performed, the number of professional staff-hours expended in providing the service, the hourly rate, and the contractual costs incurred. Additionally, the Inspection Report number is provided on inspection fee bills, and the date of the application, NRC's completion date, and the subject of the application or the amendment number, if appropriate, are provided on bills for licensing actions.

A licensee or applicant who does not understand the charges or who feels they need more information to understand a bill may request additional information from the NRC regarding the specific bill in question. The NRC will turn over all available data used to support the bill upon request of the licensee or applicant.[1] Additionally, if requested, the NRC program staff will provide a best estimate of the hours required to complete a specific licensing action, with the caveat that the actual hours expended may differ from that estimate. However, OMB Circular A–25, which provides guidelines for Federal agencies to assess fees for Government services, provides that new cost accounting systems need not be established solely for the purpose of determining or estimating full cost. Therefore, the NRC does not plan to develop additional systems solely to provide additional information on its fee invoices at this time.

4. *Comment:* Several commenters agreed with the petitioner that all Federal agencies should be assessed fees to recover their share of NRC's costs.

The Commission agrees that, where legally permissible, Federal agencies should pay for services rendered,

[1] At the request of uranium recovery industry representatives in a meeting with the NRC staff on October 24, 1994, this additional information will be provided with all Part 170 bills issued to uranium recovery licensees and applicants.

including the Department of Energy for NRC review of DOE sites under UMTRCA. However, as stated in response to similar comments (See FY 1992 Final Rule, 57 FR 32695) NRC is currently precluded under the Independent Offices Appropriation Act (IOAA) from assessing Part 170 fees to Federal agencies for specific services rendered. The NRC currently assesses annual fees under 10 CFR Part 171 to Federal agencies if those agencies have a license or approval/certificate from the NRC; however, OBRA–90 limits annual fee assessments to NRC *licensees*. In September 1993, DOE became a general licensee of the NRC because post-reclamation closure of the Spook, Wyoming, site had been achieved. Therefore, effective with the FY 1994 final rule published July 20, 1994, DOE is being assessed for costs associated with DOE facilities under the Uranium Mill Tailings Radiation Control Act of 1978 (UMTRCA). These costs were previously recovered from operating reactors because DOE was not an NRC licensee prior to September 1993 and therefore could not be billed under 10 CFR Part 171.

The Commission has recommended in its report submitted to Congress on February 23, 1994, that either OBRA–90 be modified to remove costs from the fee base for services to other Federal agencies or the Atomic Energy Act be modified to permit the NRC to assess application and other fees for specific services rendered to all Federal agencies.

For the reasons stated above, the NRC has denied this petition.

Dated at Rockville, Maryland, this 24th day of April, 1995.

For the Nuclear Regulatory Commission.

John C. Hoyle,

Secretary of the Commission.

[FR Doc. 95–10477 Filed 4–27–95; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[INTL–0065–93]

RIN 1545–AS46

Exceptions to Passive Income Characterization for Certain Foreign Banks and Securities Dealers

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document provides guidance concerning the application of the exceptions to passive income contained in section 1296(b) for foreign banks, securities dealers and brokers. This document affects persons who own direct or indirect interests in certain foreign corporations. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments must be received by August 10, 1995. Outlines of oral comments to be presented at the public hearing scheduled for August 31, 1995 at 10 a.m. must be received by August 10, 1995.

ADDRESSES: Send submissions to: CC:DOM:CORP:T:R (INTL–0065–93), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:T:R (INTL–0065–93), Courier's Desk, Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Ramon Camacho at (202) 622–3870; concerning submissions and the hearing, Ms. Christina Vasquez, (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

A passive foreign investment company (PFIC) is any foreign corporation that satisfies either the income test or asset test in section 1296(a) of the Internal Revenue Code (Code). Under the income test, a foreign corporation is a PFIC if 75 percent or more of its gross income for the year is passive income. Sec. 1296(a)(1). Alternatively, a foreign corporation is a PFIC if 50 percent or more of the average value of its assets for the taxable year produce passive income or are held for the production of passive income. Sec. 1296(a)(2). Under section 1296(b)(1), passive income is foreign personal holding company income as defined in section 954(c) of the Code, and includes dividends, interest, certain rents and royalties, and gain from certain property transactions, including gain from the sale of assets that produce passive income.

Under section 1296(b)(2)(A), income earned in the active conduct of a banking business by a foreign corporation licensed to do business as a bank in the United States and, to the extent provided in regulations, by other corporations engaged in the banking business is not passive. Notice 89–81, 1989–2 CB 399, (Notice) described rules to be incorporated into subsequent regulations that would expand this exception to certain foreign banks not licensed to do a banking business in the United States. The rules contained in § 1.1296–4 of the proposed regulations would implement section 1296(b)(2)(A) for banking activities conducted by foreign corporations.

In 1993, Congress added section 1296(b)(3)(A) to the Code, effective for taxable years beginning after September 30, 1993. See Omnibus Budget Reconciliation Act of 1993 (1993 Act), Pub. L. 103–66, section 13231(d), 107 Stat. 312, 499. The provision treats as nonpassive any income derived in the active conduct of a securities business by a controlled foreign corporation (CFC) if the CFC is a U.S. registered dealer or broker and, to the extent provided in regulations, a CFC not so registered. The rules contained in § 1.1296–6 would implement section 1296(b)(3)(A).

Section 956A, added by the 1993 Act, requires each U.S. shareholder of a CFC to include in income its pro rata share of the CFC's excess passive assets. Under section 956A(c)(2), a passive asset is any asset that produces passive income as defined in section 1296(b). An asset that generates nonpassive income under § 1.1296–4 or § 1.1296–6 of the proposed regulations will be nonpassive for purposes of section 956A.

Explanation of Provisions

I. Description of Proposed Rules for Foreign Banks

A. General Rule

Section 1.1296–4(a) of the proposed regulations provides generally that, for purposes of section 1296(a)(1), passive income does not include banking income earned by an active bank or by a qualified affiliate of such a bank. For this purpose, an active bank is either a corporation that possesses a license issued under federal or state law to do business as a bank in the United States, or a foreign corporation that meets the licensing, deposit-taking, and lending requirements of paragraphs (c), (d), and (e), respectively, of § 1.1296–4.

The proposed rules generally adopt the deposit, lending, and licensing standards contained in the Notice. These standards are consistent with the provisions of the Code that define a bank as an institution that accepts deposits from and makes loans to the public and is licensed under state or federal law to conduct banking activities. See e.g., sec. 581. The IRS and Treasury believe that Congress intended