document will be published subsequently in the Order.

The Direct Final Rule Procedure

The FAA anticipates that this regulation will not result in adverse or negative comment and, therefore, is issuing it as a direct final rule. Previous actions of this nature have not been controversial and have not resulted in adverse comments or objections. The amendment will enhance safety for all flight operations by designating an area where VFR pilots may anticipate the presence of IFR aircraft at lower altitudes, especially during inclement weather conditions. A greater degree of safety is achieved by depicting the area on aeronautical charts. unless a written adverse or negative comment, or a written notice of intent to submit an adverse or negative comment is received within the comment period, the regulation will become effective on the date specified above. After the close of the comment period, the FAA will publish a document in the **Federal Register** indicating that no adverse or negative comments were received and confirming the date on which the final rule will become effective. If the FAA does receive, within the comment period, an adverse or negative comment, or written notice of intent to submit such a comment, a document withdrawing the direct final rule will be published in the **Federal Register**, and a notice of proposed rulemaking may be published with a new comment period.

Comments Invited

Although this action is in the form of a final rule and was not preceded by a notice of proposed rulemaking, comments are invited on this rule. Interested persons are invited to comment on this rule by submitting such written data, views, or arguments as they may desire. Communications should identify the Rules Docket number and be submitted in triplicate to the address specified under the caption **ADDRESSES**. All communications received on or before the closing date for comments will be considered, and this rule may be amended or withdrawn in light of the comments received. Factual information that supports the commenter's ideas and suggestions is extremely helpful in evaluating the effectiveness of this action and determining whether additional rulemaking action would be needed.

Comments are specifically invited on the overall regulatory, economic, environmental, and energy-related aspects of the rule that might suggest a need to modify the rule. All comments submitted will be available, both before and after the closing date for comments, in the Rules Docket for examination by interested persons. A report that summarizes each FAA-public contact concerned with the substance of this action will be filed in the Rules Docket.

Commenters wishing the FAA to acknowledge receipt of their comments submitted in response to this rule must submit a self-addressed, stamped postcard on which the following statement is made: ''Comments to Docket No. 00–ACE–5.'' The postcard will be date stamped and returned to the commenter.

Agency Findings

The regulations adopted herein will not have a substantial direct effect on the States, on the relationship between the national Government and the States, or on the distribution of power and responsibilities among the various levels of government. Therefore, it is determined that this final rule does not have federalism implications under Executive Order 13132.

The FAA has determined that this regulation is noncontroversial and unlikely to result in adverse or negative comments. For the reasons discussed in the preamble, I certify that this regulation (1) Is not a ''significant regulatory action'' under Executive Order 12866; (2) Is not a ''significant rule'' under Department of Transportation (DOT) Regulatory Policies and Procedures (44 FR 11034, February 26, 1979); and (3) If promulgated, will not have a significant economic impact, positive or negative, on a substantial number of small entities under the criteria of the Regulatory Flexibility Act.

List of Subjects in 14 CFR Part 71

Airspace, Incorporation by reference, Navigation (air).

Adoption of the Amendment

Accordingly, the Federal Aviation Administration amends 14 CFR part 71 as follows:

PART 71—DESIGNATION OF CLASS A, CLASS B, CLASS C, CLASS D, AND CLASS E AIRSPACE AREAS; AIRWAYS; ROUTES; AND REPORTING POINTS

1. The authority citation for part 71 continues to read as follows:

Authority: 49 U.S.C. 106(g), 40103, 40113, 40120; E.O. 10854, 24 FR 9565, 3 CFR, 1959–1963 Comp., p. 389.

§ 71.1 [Amended]

2. The incorporation by reference in 14 CFR 71.1 of Federal Aviation Administration Order 7400.9G, Airspace Designations and Reporting Points, dated September 10, 1999, and effective September 16, 1999, is amended as follows:

Paragraph 6005 Class E airspace areas extending upward from 700 feet or more above the surface of the earth.

* * * * *

ACE IA E5 Monticello, IA [Revised]

Monticello Regional Airport, IA
(Lat. 42°13′34″N., long. 91°10′02″W.)
Monticello NDB
(Lat. 42°12′02″N., long. 91°08′14″W.)

That airspace extending upward from 700 feet above the surface within a 6.4-mile radius of Monticello Regional Airport and within 2.6 miles each side of the 141° bearing from the Monticello NDB extending from the 6.4-mile radius to 9.2 miles southeast of the airport.

* * * * *

Issued in Kansas City, MO, on January 26, 2000.

Herman J. Lyons, Jr.,

Manager, Air Traffic Division, Central Region.

[FR Doc. 00–2672 Filed 2–4–00; 8:45 am]

BILLING CODE 4910–13–M

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 8874]

RIN 1545–AW10

Travel and Tour Activities of Tax-Exempt Organizations

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations clarifying when the travel and tour activities of tax-exempt organizations are substantially related to the purposes for which exemption was granted. This action provides needed guidance for tax-exempt organizations concerning when travel tour activities may be subject to tax as an unrelated trade or business. This action affects tax-exempt organizations that engage in travel tour activities.

DATES: *Effective Date:*

These regulations are effective on February 7, 2000.

Applicability Date: These regulations are applicable for taxable years beginning after February 7, 2000.

FOR FURTHER INFORMATION CONTACT: Robin Ehrenberg, (202) 622–6080 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

On April 23, 1998, the IRS published in the **Federal Register** (63 FR 20156) a notice of proposed rulemaking under section 513 to clarify when the travel and tour activities of tax-exempt organizations are substantially related to the purposes for which exemption was granted. The notice of proposed rulemaking added Treas. Reg. § 1.513–7, which provides that whether travel tour activities are substantially related to an organization's exempt purposes is determined by examining all the relevant facts and circumstances. The proposed regulations also contain examples applying the facts and circumstances test in four situations.

The notice of proposed rulemaking solicited comments from the public. Nineteen commentators submitted written comments. A public hearing was held on February 10, 1999, at which eight speakers presented testimony. After consideration of all the comments, the proposed regulations under section 513 are adopted as revised by this Treasury Decision. The comments and revisions are discussed below.

Explanation of Provisions and Summary of Comments

Many of the commentators welcomed the proposed regulations as workable guidance that will promote tax compliance. Commentators differed on the approach that the IRS should adopt in final regulations. Some commentators suggested that the final regulations should adopt specific, weighted standards to be used in evaluating relatedness to exempt purpose. Other commentators recommended against adopting specific standards, arguing that no single set of standards would be appropriate given the broad range of tax-exempt organizations. One commentator suggested that the final regulations adopt a set of specific standards that would apply to test relatedness of tours in the educational context and a more general consistency standard that would evaluate whether the marketing, location, and execution of a tour are consistent with the organization's core exempt activities.

Section 513(a) generally defines an unrelated trade or business as any trade or business the conduct of which is not substantially related to the exercise or performance by the organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501(a). *See also United States* v. *American Bar Endowment,* 477 U.S. 105, 109–110 (1986). Treas Reg. § 1.513–1(d)(2) provides that, for the conduct of a trade or business to be substantially related to the purposes for which exemption was granted, the production or distribution of the goods or the performance of services must contribute importantly to the accomplishment of those purposes. Whether activities generating gross income contribute importantly to accomplishing any purpose for which an organization was granted exemption depends in each case upon the particular facts and circumstances. *Id.* This rule applies to travel tours.

Organizations exempt from tax under section 501(a) have diverse exempt purposes (for example: charities; social welfare organizations; labor, agricultural and horticultural organizations; business leagues; fraternal beneficiary societies). Accordingly, no one set of factors could be sufficiently comprehensive as to define relatedness for the variety of exempt organizations to which these travel tour regulations apply. Even among exempt organizations that share a common exempt purpose, such as education, the methods of accomplishing that purpose vary considerably. For this reason, the final regulations do not enumerate any specific factors that determine relatedness of travel tour activities to exempt purposes. The final regulations adopt the general facts and circumstances approach of the proposed regulations. *See e.g, Hi-Plains Hospital* v. *United States,* 670 F.2d 528 (5th Cir. 1982) (need for case-by-case analysis identifying exempt purpose and analysis of how activity in each case contributes to exempt purpose); *Louisiana Credit Union League* v. *United States,* 693 F.2d 525, 534 (5th Cir. 1982) (resolution of the substantial relationship test requires ''an examination of the relationship between the business activities that generate the income in question* * * and the accomplishment of the organization's exempt purposes''). However, as discussed below, the final regulations include new examples that provide additional guidance regarding the application of this facts and circumstances approach in both educational and noneducational contexts.

Another commentator suggested that the final regulations should clarify that the manner in which an organization develops and promotes a tour is relevant to determining whether the tour activity is substantially related to exempt purposes. The development, promotion and operation of a tour are all indicators of whether an organization's offering of a tour is related or unrelated to its exempt purpose. *See International Postgraduate Medical Found.* v. *Commissioner,* 1989–36 T.C. Memo., 56 T.C.M. (CCH) 1140 (1989) (brochures promoting the trips emphasized recreational sightseeing activity and omitted educational course descriptions). Language has been added to the final regulations stating that relevant facts and circumstances include (but are not limited to) how a travel tour is developed, promoted and operated. Examples in the final regulations also illustrate the relevance of these factors.

Many commentators requested more examples addressing specific areas. As noted above, examples have been added that further illustrate the application of the facts and circumstances rule. Some commentators raised concerns regarding the number of hours of related activities a travel tour must offer. Examples in the final regulation clarify that the number of hours spent on any related travel tour activity is only one factor in determining relatedness of the tour as a whole to exempt purposes and is not by itself determinative. Examples in the final regulation clarify that the nature of the related activities, and the practicalities of engaging in such activities (for example, the hours during which the activity normally would be conducted), must also be taken into account.

One commentator suggested adding an example addressing whether income from travel tour activity is a royalty under section 512(b)(2) where the exempt organization does not operate the tour, but provides member names to a for-profit tour operator. Section 512(b)(2) excludes royalties from the computation of unrelated business taxable income. The question of what constitutes a royalty is beyond the scope of these regulations. For guidance as to whether income received by a tax-exempt organization from travel tour activities is excludable from unrelated business taxable income as a royalty, *see generally* Treas. Reg. § 1.512(b)–1(b) and *Sierra Club* v. *Commissioner,* 86 F.3d 1526 (9th Cir. 1996).

Some commentators suggested that the final regulations should contain provisions that prevent tax-exempt organizations from competing unfairly with taxable travel businesses. However, the test under section 513 is substantial relatedness to exempt purposes, not the presence or absence of unfair competition. Section 513 was enacted to prevent unfair competition between exempt organizations and taxable businesses. H.R. Rep. No. 2319, 81st Cong., 2d Sess. (1950), *reprinted in* 1950–2 C.B. 380, 409; S. Rep. No. 2375, 81st Cong., 2d Sess. (1950), *reprinted in* 1950–2 C.B. 483, 504; *Portland Golf*

Club v. *Commissioner,* 497 U.S. 154, 161–162, fn. 12 (1990); Treas. Reg. § 1.513–1(b). Nevertheless, ''Congress did not force exempt organizations to abandon all commercial ventures'', but rather imposed a tax on ventures that are not substantially related to an organization's exempt purposes. *United States* v. *American College of Physicians,* 475 U.S. 834, 838 (1986). *See also Louisiana Credit Union League* v. *United States,* 693 F.2d 525, 541 (5th Cir. 1982). Following this approach, the section 513(a) regulations, published in 1967, state that ''any activity of a section 511 organization which is carried on for the production of income and which otherwise possesses the characteristics required to constitute 'trade or business' within the meaning of section 162—and which, in addition, is not substantially related to the performance of exempt functions—presents sufficient likelihood of unfair competition to be within the policy of the tax [imposed by section 511(a)].'' Treas. Reg. § 1.513–1(b). In expanding the categories of organizations subject to unrelated business income tax in 1969, Congress revisited the unfair competition issue. ''[A] business competing with taxpaying organizations should not be granted an unfair competitive advantage by operating tax free *unless* the business contributes importantly to the exempt function.'' H.R. Rep. No. 413 (Part 1), 91st Cong., 1st Sess., 44, 50 (1969), *reprinted in* 1969 U.S.C.C.A.N. 1645, 1689, 1695 (emphasis added). If an organization's trade or business is substantially related to its exempt purposes, the tax under section 511 is not imposed, regardless of the existence of competition with taxable entities. Accordingly, the final regulations continue to focus on relatedness to exempt purposes, as required by section 513.

The preamble to the proposed regulations requested comments on whether the final regulations should include documentation and recordkeeping requirements specific to travel tours. Commentators split on the preferred approach. Some commentators requested general guidance as to the types of records that an organization should keep to establish a tour's purpose, but did not want the IRS to mandate specific recordkeeping requirements. Other commentators asked that the IRS specify what documentation is required. Section 6001 authorizes the Secretary to prescribe regulations that require taxpayers to keep records sufficient to establish whether a taxpayer is liable for any tax imposed under the Code. Currently, any person subject to tax under subtitle A of the Code, including the tax imposed under section 511, or required to file a return of information with respect to income, must keep permanent books or records sufficient to establish the amount of gross income, deductions, credits or other matters required to be shown by such person in any return of tax or information. *See* Treas. Reg. § 1.6001–1(a). In addition, every organization exempt from tax under section 501(a) must keep permanent books of account or records sufficient to show specifically items of gross income, receipts and disbursements, and to substantiate the information required by section 6033. *See* Treas. Reg. § 1.6001–1(c).

The IRS and Treasury Department believe that, with respect to travel tours, it is unnecessary to supplement the existing recordkeeping requirements under sections 6001 and 6033. Therefore, the final regulations do not impose additional recordkeeping requirements. However, in response to commentators' suggestions, examples in the final regulations illustrate that contemporaneous documentation showing how an organization develops, promotes and operates the travel tour is relevant to the facts and circumstances analysis.

Special Analyses

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

Drafting Information

The principal author of these regulations is Robin Ehrenberg, Office of Associate Chief Counsel (Employee Benefits and Exempt Organizations). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

Par. 2. Section 1.513–7 is added to read as follows:

§ 1.513–7 Travel and tour activities of tax exempt organizations.

(a) Travel tour activities that constitute a trade or business, as defined in § 1.513–1(b), and that are not substantially related to the purposes for which exemption has been granted to the organization constitute an unrelated trade or business with respect to that organization. Whether travel tour activities conducted by an organization are substantially related to the organization's exempt purpose is determined by looking at all relevant facts and circumstances, including, but not limited to, how a travel tour is developed, promoted and operated. Section 513(c) and § 1.513–1(b) also apply to travel tour activity. Application of the rules of section 513(c) and § 1.513–1(b) may result in different treatment for individual tours within an organization's travel tour program.

(b) *Examples.* The provisions of this section are illustrated by the following examples. In all of these examples, the travel tours are priced to produce a profit for the exempt organization. The examples are as follows:

Example 1. O, a university alumni association, is exempt from federal income tax under section 501(a) as an educational organization described in section 501(c)(3). As part of its activities, O operates a travel tour program. The program is open to all current members of O and their guests. O works with travel agencies to schedule approximately 10 tours annually to various destinations around the world. Members of O pay $x to the organizing travel agency to participate in a tour. The travel agency pays O a per person fee for each participant. Although the literature advertising the tours encourages O's members to continue their lifelong learning by joining the tours, and a faculty member of O's related university frequently joins the tour as a guest of the alumni association, none of the tours includes any scheduled instruction or curriculum related to the destinations being visited. The travel tours made available to O's members do not contribute importantly to the accomplishment of O's educational purpose. Rather, O's program is designed to generate revenues for O by regularly offering its members travel services. Accordingly, O's tour program is an unrelated trade or

business within the meaning of section 513(a).

Example 2. N is an organization formed for the purpose of educating individuals about the geography and culture of the United States. It is exempt from federal income tax under section 501(a) as an educational and cultural organization described in section 501(c)(3). N engages in a number of activities to accomplish its purposes, including offering courses and publishing periodicals and books. As one of its activities, N conducts study tours to national parks and other locations within the United States. The study tours are conducted by teachers and other personnel certified by the Board of Education of the State of P. The tours are directed toward students enrolled in degree programs at educational institutions in P, as reflected in the promotional materials, but are open to all who agree to participate in the required study program. Each tour's study program consists of instruction on subjects related to the location being visited on the tour. During the tour, five or six hours per day are devoted to organized study, preparation of reports, lectures, instruction and recitation by the students. Each tour group brings along a library of material related to the subject being studied on the tour. Examinations are given at the end of each tour and the P State Board of Education awards academic credit for tour participation. Because the tours offered by N include a substantial amount of required study, lectures, report preparation, examinations and qualify for academic credit, the tours are substantially related to N's educational purpose. Accordingly, N's tour program is not an unrelated trade or business within the meaning of section 513(a).

Example 3. R is a section 501(c)(4) social welfare organization devoted to advocacy on a particular issue. On a regular basis throughout the year, R organizes travel tours for its members to Washington, DC. While in Washington, the members follow a schedule according to which they spend substantially all of their time during normal business hours over several days attending meetings with legislators and government officials and receiving briefings on policy developments related to the issue that is R's focus. Members do have some time on their own in the evenings to engage in recreational or social activities of their own choosing. Bringing members to Washington to participate in advocacy on behalf of the organization and learn about developments relating to the organization's principal focus is substantially related to R's social welfare purpose. Therefore, R's operation of the travel tours does not constitute an unrelated trade or business within the meaning of section 513(a).

Example 4. S is a membership organization formed to foster cultural unity and to educate X Americans about X, their country of origin. It is exempt from federal income tax under section 501(a) and is described in section 501(c)(3) as an educational and cultural organization. Membership in S is open to all Americans interested in the X heritage. As part of its activities, S sponsors a program of travel tours to X. The tours are divided into two categories. Category A tours are trips to X that are designed to immerse participants in the X history, culture and language. Substantially all of the daily itinerary includes scheduled instruction on the X language, history and cultural heritage, and visits to destinations selected because of their historical or cultural significance or because of instructional resources they offer. Category B tours are also trips to X, but rather than offering scheduled instruction, participants are given the option of taking guided tours of various X locations included in their itinerary. Other than the optional guided tours, Category B tours offer no instruction or curriculum. Destinations of principally recreational interest, rather than historical or cultural interest, are regularly included on Category B tour itineraries. Based on the facts and circumstances, sponsoring Category A tours is an activity substantially related to S's exempt purposes, and does not constitute an unrelated trade or business within the meaning of section 513(a). However, sponsoring Category B tours does not contribute importantly to S's accomplishment of its exempt purposes and, thus, constitutes an unrelated trade or business within the meaning of section 513(a).

Example 5. T is a scientific organization engaged in environmental research. T is exempt from federal income tax under section 501(a) as an organization described in section 501(c)(3). T is engaged in a long-term study of how agricultural pesticide and fertilizer use affects the populations of various bird species. T collects data at several bases located in an important agricultural region of country U. The minutes of a meeting of T's Board of Directors state that, after study, the Board has determined that non-scientists can reliably perform needed data collection in the field, under supervision of T's biologists. The Board minutes reflect that the Board approved offering one-week trips to T's bases in U, where participants will assist T's biologists in collecting data for the study. Tour participants collect data during the same hours as T's biologists. Normally, data collection occurs during the early morning and evening hours, although the work schedule varies by season. Each base has rustic accommodations and few amenities, but country U is renowned for its beautiful scenery and abundant wildlife. T promotes the trips in its newsletter and on its Internet site and through various conservation organizations. The promotional materials describe the work schedule and emphasize the valuable contribution made by trip participants to T's research activities. Based on the facts and circumstances, sponsoring trips to T's bases in country U is an activity substantially related to T's exempt purpose, and, thus, does not constitute an unrelated trade or business within the meaning of section 513(a).

Example 6. V is an educational organization devoted to the study of ancient history and cultures and is exempt from federal income tax under section 501(a) as an organization described in section 501(c)(3). In connection with its educational activities, V conducts archaeological expeditions around the world, including in the Y region of country Z. In cooperation with the National Museum of Z, V recently presented an exhibit on ancient civilizations of the Y region of Z, including artifacts from the collection of the Z National Museum. V instituted a program of travel tours to V's archaeological sites located in the Y region. The tours were initially proposed by V staff members as a means of educating the public about ongoing field research conducted by V. V engaged a travel agency to handle logistics such as accommodations and transportation arrangements. In preparation for the tours, V developed educational materials relating to each archaeological site to be visited on the tour, describing in detail the layout of the site, the methods used by V's researchers in exploring the site, the discoveries made at the site, and their historical significance. V also arranged special guided tours of its exhibit on the Y region for individuals registered for the travel tours. Two archaeologists from V (both of whom had participated in prior archaeological expeditions in the Y region) accompanied the tours. These experts led guided tours of each site and explained the significance of the sites to tour participants. At several of the sites, tour participants also met with a working team of archaeologists from V and the National Museum of Z, who shared their experiences. V prepared promotional materials describing the educational nature of the tours, including the daily trips to V's archaeological sites and the educational background of the tour leaders, and providing a recommended reading list. The promotional materials do not refer to any particular recreational or sightseeing activities. Based on the facts and circumstances, sponsoring trips to the Y region is an activity substantially related to V's exempt purposes. The scheduled activities, which include tours of archaeological sites led by experts, are part of a coordinated educational program designed to educate tour participants about the ancient history of the Y region of Z and V's ongoing field research. Therefore, V's tour program does not constitute an unrelated trade or business within the meaning of section 513(a).

Example 7. W is an educational organization devoted to the study of the performing arts and is exempt from federal income tax under section 501(a) as an organization described in section 501(c)(3). In connection with its educational activities, W presents public performances of musical and theatrical works. Individuals become members of W by making an annual contribution to W of q dollars. Each year, W offers members an opportunity to travel as a group to one or more major cities in the United States or abroad. In each city, tour participants are provided tickets to attend a public performance of a play, concert or dance program each evening. W also arranges a sightseeing tour of each city and provides evening receptions for tour participants. W views its tour program as an important means to develop and strengthen bonds between W and its members, and to increase their financial and volunteer support of W. W engaged a travel agency to handle logistics

such as accommodations and transportation arrangements. No educational materials are prepared by W or provided to tour participants in connection with the tours. Apart from attendance at the evening cultural events, the tours offer no scheduled instruction, organized study or group discussion. Although several members of W's administrative staff accompany each tour group, their role is to facilitate member interaction. The staff members have no special expertise in the performing arts and play no educational role in the tours. W prepared promotional materials describing the sightseeing opportunities on the tours and emphasizing the opportunity for members to socialize informally and interact with one another and with W staff members, while pursuing shared interests. Although W's tour program may foster goodwill among W members, it does not contribute importantly to W's educational purposes. W's tour program is primarily social and recreational in nature. The scheduled activities, which include sightseeing and attendance at various cultural events, are not part of a coordinated educational program. Therefore, W's tour program is an unrelated trade or business within the meaning of section 513(a).

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: January 21, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury.

[FR Doc. 00–2154 Filed 2–4–00; 8:45 am]

BILLING CODE 4830–01–P

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 8872]

RIN 1545–AW93

Certain Asset Transfers to Regulated Investment Companies [RICs] and Real Estate Investment Trusts [REITs]

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations that apply with respect to the net built-in gain of C corporation assets that become assets of a Regulated Investment Company [RIC] or Real Estate Investment Trust [REIT] by the qualification of a C corporation as a RIC or REIT or by the transfer of assets of a C corporation to a RIC or REIT in a carryover basis transaction. The regulations generally require the corporation to recognize gain as if it had sold the assets transferred or converted to RIC or REIT assets at fair market value and immediately liquidated. The regulations permit the transferee RIC or REIT to elect, in lieu of liquidation treatment, to be subject to the rules of section 1374 of the Internal Revenue Code and the regulations thereunder. The text of the temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section of this issue of the **Federal Register**.

DATES: *Effective Date:* These regulations are effective February 4, 2000.

Applicability Dates: For dates of applicability, see the Effective Dates portion of the preamble under **SUPPLEMENTARY INFORMATION.**

FOR FURTHER INFORMATION CONTACT: Christopher W. Schoen, (202) 622–7750 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

These regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. section 553). For this reason, the collection of information contained in these regulations has been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545–1672. Responses to this collection of information are required to obtain a benefit, *i.e.*, to elect to be subject to section 1374 of the Internal Revenue Code (Code) and the regulations thereunder.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden, and suggestions as to reducing this burden, please refer to the preamble to the cross-referencing notice of proposed rulemaking published in the Proposed Rules section of this issue of the **Federal Register**.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. section 6103.

Background

Sections 631 and 633 of the Tax Reform Act of 1986 (the 1986 Act) (Public Law 99–514), as amended by sections 1006(e) and (g) of the Technical and Miscellaneous Revenue Act of 1988 (the 1988 Act) (Public Law 100–647), amended the Code to repeal the *General Utilities* doctrine. The 1986 Act amended sections 336 and 337 of the Code, generally requiring corporations to recognize gain when appreciated property is distributed in connection with a complete liquidation. Section 337(d) directs the Secretary to prescribe regulations as may be necessary to carry out the purposes of *General Utilities* repeal, including rules to ''ensure that such purposes shall not be circumvented * * * through the use of a regulated investment company [RIC], a real estate investment trust [REIT], or a tax exempt entity * * *.'' The transfer of the assets of a C corporation to a RIC or REIT could result in permanently removing the built-in gain inherent in those assets from the reach of the corporate income tax because RIC and REIT income is not subject to a corporate-level income tax if such income is distributed to the RIC or REIT shareholders.

Accordingly, on February 4, 1988, the IRS issued Notice 88–19 (1988–1 C.B. 486). Notice 88–19 announced that the IRS intended to promulgate regulations under the authority of section 337(d) with respect to transactions or events that result in the ownership of C corporation assets by a RIC or REIT with a basis determined by reference to the corporation's basis (a carryover basis). Notice 88–19 served as an ''administrative pronouncement,'' and could be relied upon to the same extent as a revenue ruling or revenue procedure. Notice 88–19 also indicated that the regulations would be applicable retroactively to June 10, 1987. See also Notice 88–96 (1988–2 C.B. 420).

As a result of the issuance of Notice 88–19, many taxpayers have become uncertain about the current law applicable to their transactions, as well as the proper method of making a valid election to be subject to the rules of section 1374 and the regulations thereunder. In order to resolve this uncertainty and to provide taxpayers with guidance, the IRS and Treasury are issuing these temporary regulations.

Explanation of Provisions

These regulations implement Notice 88–19 by providing that when a C corporation (1) qualifies to be taxed as a RIC or REIT, or (2) transfers assets to a RIC or REIT in a carryover basis transaction, the C corporation is treated as if it sold all of its assets at their respective fair market values and immediately liquidated, unless the RIC or REIT elects to be subject to tax under