

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 7400.9L, dated September 2, 2003, and effective September 16, 2003, is amended as follows:

* * * * *

Paragraph 6005 Class E Airspace Areas Extending Upward From 700 Feet or More Above the Surface of the Earth.

* * * * *

ACE NE E5 Cozad, NE

Cozad Municipal Airport, NE
(lat. 40°52'09" N., long. 100°00'15" W.)
Cozad VOR
(lat. 40°52'14" N., long. 100°00'13" W.)

That airspace extending upward from 700 feet above the surface within a 6.4-mile radius of Cozad Municipal Airport and within 2.6 miles each side of the 312° bearing from the Cozad VOR extending from the 6.4 mile radius of the airport to 7 miles northwest of the VOR.

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Issued in Kansas City, MO, on April 16, 2004.

Elizabeth S. Wallis,

Acting Manager, Air Traffic Division, Central Region.

[FR Doc. 04–9404 Filed 4–23–04; 8:45 am]

BILLING CODE 4910–13–M

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9122]

RIN 1545–BC28

Guidance Under Section 1502; Stock Basis After a Group Structure Change

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains final regulations under section 1502 providing guidance regarding the determination of basis in the stock of the former common parent following a group structure change. These final regulations affect corporations filing consolidated returns.

DATES: These regulations are effective April 26, 2004.

FOR FURTHER INFORMATION CONTACT: Ross Poulsen, (202) 622–7770 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) under section 1502 of the Internal Revenue Code of 1986 (Code), specifically § 1.1502–31, relating to the determination of the basis of stock in the former common parent after a group structure change. Section 1.1502–31 applies if one corporation (P) succeeds another corporation (T) under the principles of § 1.1502–75(d)(2) or (3) as the common parent of a consolidated group in a group structure change. Section 1.1502–31 provides that if a corporation acquires stock of the former common parent in a group structure change, the basis of the members in the former common parent's stock immediately after the group structure change is generally redetermined to

reflect the former common parent's net asset basis.

Because of a concern that the application of the net asset basis rule may produce inappropriate results on the disposition of stock acquired in a transaction in which, under generally applicable rules, the basis of the acquired stock would otherwise be determined by reference to the acquirer's cost, the IRS and Treasury Department issued regulations proposing to except from the application of the net asset basis rule stock acquired in a transaction in which gain or loss was recognized in whole. Those regulations were included in a notice of proposed rulemaking (REG–130262–03) published in the **Federal Register** (68 FR 40579 [technical correction published in 68 FR 52545]) on July 8, 2003.

No public hearing was requested or held regarding the proposed regulations. One written comment, however, was received. That comment urged the expeditious promulgation of the proposed regulations as final regulations.

This Treasury decision adopts the proposed regulations without substantive changes as final regulations. The final regulations apply to group structure changes that occur after April 26, 2004. With respect to group structure changes that occur on or before April 26, 2004, and in a consolidated return year beginning on or after January 1, 1995, these regulations apply at the election of the group.

Special Analyses

It has been determined that these regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It is hereby certified that these regulations do not have a significant impact on a substantial number of small entities. This certification is based on the fact that these regulations primarily will affect affiliated groups of corporations, which tend to be larger businesses. Moreover, the number of taxpayers affected is minimal and the regulations will simplify basis determinations. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact.

Drafting Information

The principal author of this regulation is Ross Poulsen, Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and 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 1.1502–31 is amended by revising paragraphs (b)(2), (d)(2)(ii), (g), and (h) to read as follows:

§ 1.1502–31 Stock basis after a group structure change.

* * * * *

(b) * * *

(2) *Stock acquisitions.* If a corporation acquires stock of the former common parent in a group structure change, the basis of the members in the former common parent's stock immediately after the group structure change (including any stock of the former common parent owned before the group structure change) that is, or would otherwise be, transferred basis property is redetermined in accordance with the results for an asset acquisition described in paragraph (b)(1) of this section. For example, if all of T's stock is contributed to P in a group structure change to which section 351 applies, P's basis in T's stock is T's net asset basis, rather than the amount determined under section 362. Similarly, if S merges into T in a group structure change described in section 368(a)(2)(E) and P acquires all of the T stock, P's basis in T's stock is the basis that P would have in S's stock under paragraph (b)(1) of this section if T had merged into S in a group structure change described in section 368(a)(2)(D).

* * * * *

(d) * * *

(2) * * *

(ii) *Stock acquisitions.* If less than all of the former common parent's stock is subject to the redetermination described in paragraph (b)(2) of this section, the percentage of the former common parent's net asset basis taken into account in the redetermination equals

the percentage (by fair market value) of the former common parent's stock subject to the redetermination. For example, if P owns less than all of the former common parent's stock immediately after the group structure change and such stock would otherwise be transferred basis property, only an allocable part of the basis determined under this section is reflected in the shares owned by P (and the amount allocable to shares owned by nonmembers has no effect on the basis of their shares). Alternatively, if P acquired 10 percent of the former common parent's stock in a transaction in which the stock basis was determined by P's cost, and P later acquires the remaining 90 percent of the former common parent's stock in a separate transaction that is described in paragraph (b)(2) of this section, P retains its cost basis in its original stock and the basis of P's newly acquired shares reflects only an allocable part of the former common parent's net asset basis.

* * * * *

(g) *Examples.* For purposes of the examples in this section, unless otherwise stated, all corporations have only one class of stock outstanding, the tax year of all persons is the calendar year, all persons use the accrual method of accounting, the facts set forth the only corporate activity, all transactions are between unrelated persons, and tax liabilities are disregarded. The principles of this section are illustrated by the following examples:

Example 1. Forward triangular merger. (i) *Facts.* P is the common parent of one group and T is the common parent of another. T has assets with an aggregate basis of \$60 and fair market value of \$100 and no liabilities. T's shareholders have an aggregate basis of \$50 in T's stock. In Year 1, pursuant to a plan, P forms S and T merges into S with the T shareholders receiving \$100 of P stock in exchange for their T stock. The transaction is a reorganization described in section 368(a)(2)(D). The transaction is also a reverse acquisition under § 1.1502–75(d)(3) because the T shareholders, as a result of owning T's stock, own more than 50% of the value of P's stock immediately after the transaction. Thus, the transaction is a group structure change under § 1.1502–33(f)(1), and P's earnings and profits are adjusted to reflect T's earnings and profits immediately before T ceases to be the common parent of the T group.

(ii) *Analysis.* Under paragraph (b)(1) of this section, P's basis in S's stock is adjusted to reflect T's net asset basis. Under paragraph (c) of this section, T's net asset basis is \$60, the basis T would have in the stock of a subsidiary under section 358 if T had transferred all of its assets and liabilities to the subsidiary in a transaction to which section 351 applies. Thus, P has a \$60 basis in S's stock.

(iii) *Pre-existing S.* The facts are the same as in paragraph (i) of this *Example 1*, except that P has owned the stock of S for several years and P has a \$50 basis in the S stock before the merger with T. Under paragraph (b)(1) of this section, P's \$50 basis in S's stock is adjusted to reflect T's net asset basis. Thus, P's basis in S's stock is \$110 (\$50 plus \$60).

(iv) *Excess loss account included in former common parent's net asset basis.* The facts are the same as in paragraph (i) of this *Example 1*, except that T has two assets, an operating asset with an \$80 basis and \$90 fair market value, and stock of a subsidiary with a \$20 excess loss account and \$10 fair market value. Under paragraph (c) of this section, T's net asset basis is \$60 (\$80 minus \$20). See sections 351 and 358, and § 1.1502–19. Consequently, P has a \$60 basis in S's stock. Under section 362 and § 1.1502–19, S has an \$80 basis in the operating asset and a \$20 excess loss account in the stock of the subsidiary.

(v) *Liabilities in excess of basis.* The facts are the same as in paragraph (i) of this *Example 1*, except that T's assets have a fair market value of \$170 (and \$60 basis) and are subject to \$70 of liabilities. Under paragraph (c) of this section, T's net asset basis is negative \$10 (\$60 minus \$70). See sections 351 and 358, and §§ 1.1502–19 and 1.1502–80(d). Thus, P has a \$10 excess loss account in S's stock. Under section 362, S has a \$60 basis in its assets (which are subject to \$70 of liabilities). (Under paragraph (a)(2) of this section, because the liabilities are taken into account in determining net asset basis under paragraph (c) of this section, the liabilities are not also taken into account as consideration not provided by P under paragraph (d)(1) of this section.)

(vi) *Consideration provided by S.* The facts are the same as in paragraph (i) of this *Example 1*, except that P forms S with a \$100 contribution at the beginning of Year 1, and during Year 6, pursuant to a plan, S purchases \$100 of P stock and T merges into S with the T shareholders receiving P stock in exchange for their T stock. Under paragraph (b)(1) of this section, P's \$100 basis in S's stock is increased by \$60 to reflect T's net asset basis. Under paragraph (d)(1) of this section, P's basis in S's stock is decreased by \$100 (the fair market value of the P stock) because the P stock purchased by S and used in the transaction is consideration not provided by P.

(vii) *Appreciated asset provided by S.* The facts are the same as in paragraph (i) of this *Example 1*, except that P has owned the stock of S for several years, and the shareholders of T receive \$60 of P stock and an asset of S with a \$30 adjusted basis and \$40 fair market value. S recognizes a \$10 gain from the asset under section 1001. Under paragraph (b)(1) of this section, P's basis in S's stock is increased by \$60 to reflect T's net asset basis. Under paragraph (d)(1) of this section, P's basis in S's stock is decreased by \$40 (the fair market value of the asset provided by S). In addition, P's basis in S's stock is increased under § 1.1502–32(b) by S's \$10 gain.

(viii) *Depreciated asset provided by S.* The facts are the same as in paragraph (i) of this

Example 1, except that P has owned the stock of S for several years, and the shareholders of T receive \$60 of P stock and an asset of S with a \$50 adjusted basis and \$40 fair market value. S recognizes a \$10 loss from the asset under section 1001. Under paragraph (b)(1) of this section, P's basis in S's stock is increased by \$60 to reflect T's net asset basis. Under paragraph (d)(1) of this section, P's basis in S's stock is decreased by \$40 (the fair market value of the asset provided by S). In addition, S's \$10 loss is taken into account under § 1.1502-32(b) in determining P's basis adjustments under that section.

Example 2. Stock acquisition. (i) *Facts.* P is the common parent of one group and T is the common parent of another. T has assets with an aggregate basis of \$60 and fair market value of \$100 and no liabilities. T's shareholders have an aggregate basis of \$50 in T's stock. Pursuant to a plan, P forms S and S acquires all of T's stock in exchange for P stock in a transaction described in section 368(a)(1)(B). The transaction is also a reverse acquisition under § 1.1502-75(d)(3). Thus, the transaction is a group structure change under § 1.1502-33(f)(1), and the earnings and profits of P and S are adjusted to reflect T's earnings and profits immediately before T ceases to be the common parent of the T group.

(ii) *Analysis.* Under paragraph (d)(4) of this section, although S is not the new common parent of the T group, adjustments must be made to S's basis in T's stock in accordance with the principles of this section. Although S's basis in T's stock would ordinarily be determined under section 362 by reference to the basis of T's shareholders in T's stock immediately before the group structure change, under the principles of paragraph (b)(2) of this section, S's basis in T's stock is determined by reference to T's net asset basis. Thus, S's basis in T's stock is \$60.

(iii) *Higher-tier adjustments.* Under paragraph (d)(4) of this section, P's basis in S's stock is increased by \$60 (to be consistent with the adjustment to S's basis in T's stock).

(iv) *Cross ownership.* 1 The facts are the same as in paragraph (i) of this Example 2, except S purchased 10% of T's stock from an unrelated person for cash. In an unrelated transaction, S acquires the remaining 90% of T's stock in exchange for P stock. S's basis in the initial 10% of T's stock is not redetermined under this section. However, S's basis in the additional 90% of T's stock is redetermined under this section. S's basis in that stock is adjusted to \$54 (90% of T's net asset basis).

(v) *Allocable share.* The facts are the same as in paragraph (i) of this Example 2, except that P owns only 90% of S's stock immediately after the group structure change. S's basis in T's stock is the same as in paragraph (ii) of this Example 2. Under paragraph (d)(2) of this section, P's basis in its S stock is increased by \$54 (90% of S's \$60 adjustment).

Example 3. Taxable stock acquisition. (i) *Facts.* P is the common parent of one group and T is the common parent of another. T has assets with an aggregate basis of \$60 and fair market value of \$100 and no liabilities. T's shareholders have an aggregate basis of \$50

in T's stock. Pursuant to a plan, P acquires all of T's stock in exchange for \$70 of P's stock and \$30 in a transaction that is a group structure change under § 1.1502-33(f)(1). P's acquired T stock is not transferred basis property. (Because of P's use of cash, the acquisition is not a transaction described in section 368(a)(1)(B).)

(ii) *Analysis.* The rules of this section do not apply to determine P's basis in T's stock. Therefore, P's basis in T's stock is \$100.

(h) *Effective dates—(1) General rule.* This section applies to group structure changes that occur after April 26, 2004. However, a group may apply this section to group structure changes that occurred on or before April 26, 2004, and in consolidated return years beginning on or after January 1, 1995.

(2) *Prior law.* For group structure changes that occur on or before April 26, 2004, and in consolidated return years beginning on or after January 1, 1995, with respect to which the group does not elect to apply the provisions of this section, see § 1.1502-31 as contained in the 26 CFR part 1 edition revised as of April 1, 2003. For group structure changes that occur in consolidated return years beginning before January 1, 1995, see § 1.1502-31T as contained in the 26 CFR part 1 edition revised as of April 1, 1994.

Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

Approved: April 14, 2004.

Gregory F. Jenner,
Acting Assistant Secretary of the Treasury.
[FR Doc. 04-9448 Filed 4-23-04; 8:45 am]

BILLING CODE 4830-01-P

POSTAL SERVICE

39 CFR Part 111

Machinable Parcel Testing Changes

AGENCY: Postal Service.

ACTION: Final rule.

SUMMARY: On February 20, 2004 (69 FR 7887), the Postal Service™ published a proposed rule amending the *Domestic Mail Manual* (DMM™) to centralize the processing of requests for parcel testing. Such testing is requested to determine if parcels can be successfully processed on bulk mail center (BMC) parcel sorters when they do not conform to the general machinability criteria in the DMM. The Postal Service proposed DMM changes specific to this issue. This notice announces the adoption of these changes, which support the Postal Service's goal of consistency in determining the machinability of parcels.

EFFECTIVE DATE: April 17, 2004.

FOR FURTHER INFORMATION CONTACT: Obataiye B. Akinwale, 703-292-3643.
SUPPLEMENTARY INFORMATION: On April 15, 2004, *Domestic Mail Manual* (DMM) changes will be adopted to implement the new requirements for testing parcel machinability. The Postal Service believes that systemwide consistency will be achieved if exception requests are processed at one central location rather than at each BMC. This change is in line with the Postal Service's obligation to ensure prompt, efficient, reliable responses to customer needs, and will ensure that customer expectations of consistency across postal operations are met.

Comments Received

The Postal Service received one comment in response to the February 20, 2004, proposed rule. The comment came from a professional mailer. The mailer supports the proposed rule as a means of creating more consistent rulings on machinable parcels. The mailer also encouraged the Postal Service to expedite the publication of a final rule implementing the new process.

For the reasons discussed above, the Postal Service hereby adopts the following amendments to the *Domestic Mail Manual* (DMM), which is incorporated by reference in the *Code of Federal Regulations* (see 39 CFR part 111).

List of Subjects in 39 CFR Part 111

Postal Service.

PART 111—[AMENDED]

■ 1. The authority citation for 39 CFR Part 111 continues to read as follows:

Authority: 5 U.S.C. 552(a); 39 U.S.C. 101, 401, 403, 404, 414, 3001-3011, 3201-3219, 3403-3406, 3621, 3626, 5001.

■ 2. Revise the following sections of the *Domestic Mail Manual* (DMM) as set forth below:

Domestic Mail Manual (DMM)

* * * * *

C Characteristics and Content

C000 General Information

C010 General Mailability Standards

* * * * *

[Delete 7.0, Mailing Test Packages.]

* * * * *

C050 Mail Processing Categories

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4.0 MACHINABLE PARCEL

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