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This section of the FEDERAL REGISTER contains regulatory documents having general applicability and legal effect, most of which are keyed to and codified in the Code of Federal Regulations, which is published under 50 titles pursuant to 44 U.S.C. 1510.

The Code of Federal Regulations is sold by the Superintendent of Documents.

DEPARTMENT OF AGRICULTURE

Commodity Credit Corporation

7 CFR Part 1485

RIN 0551–AA97

Market Access Program

AGENCY: Commodity Credit Corporation and Foreign Agricultural Service, USDA.

ACTION: Final rule.

SUMMARY: The Commodity Credit Corporation (CCC) is revising the Market Access Program (MAP) regulations to eliminate the 5-year limit on participation by branded products in the program, as required in the Agriculture Improvement Act of 2018, and to incorporate changes that conform the operation of the program to the requirements in the Uniform Guidance and Federal grant-making best practices.

DATES: This rule is effective on January 13, 2020.

FOR FURTHER INFORMATION CONTACT: Curt Alt, (202) 690–4784, *curt.alt@usda.gov.*

SUPPLEMENTARY INFORMATION:

Background

The MAP is authorized under Section 203 of the Agricultural Trade Act of 1978 (7 U.S.C. 5623), as amended. The MAP program regulations appear at 7 CFR part 1485. The Agriculture Improvement Act of 2018 (Pub. L. 115–334), which reauthorized the program for fiscal years 2019–2023, increased the program's flexibility and usefulness to stakeholders by eliminating the 5-year limit on participation by branded products in the program and making minor legislative changes to the program. In addition, FAS is updating the regulations to bring the operation of the program into conformance with the requirements in the Uniform Guidance. Additional changes, such as the flexibility to announce program funding opportunities on the *Grants.gov* portal and edits to bring more consistency between the Market Access Program (MAP) and the Foreign Market Development (FMD) program, are desirable to bring the administration of the program into line with current best practices in Federal grant-making.

Notice and Comment

This rule is being issued as a final rule without prior notice and opportunity for comment. The Administrative Procedure Act (5 U.S.C. 553) exempts rules ''relating . . . to public property, loans, grants, benefits, or contracts'' from the statutory requirements for prior notice and opportunity for comment and publication of the rule not less than 30 days before its effective date (5 U.S.C. 553(a)(2)). Accordingly, this final rule is effective when published in the **Federal Register**.

Catalog of Federal Domestic Assistance

The program covered by this regulation is listed in the Catalog of Federal Domestic Assistance (CFDA) under the following FAS CFDA number: 10.601, Market Access Program.

E-Government Act Compliance

FAS is committed to complying with the E-Government Act of 2002 (44 U.S.C. chapter 36), to promote the use of the internet and other information technologies to provide increased opportunities for citizens' access to Government information and services, and for other purposes.

Executive Order 12988

This rule has been reviewed in accordance with Executive Order 12988, ''Civil Justice Reform.'' This rule does not preempt State or local laws, regulations, or policies unless they present an irreconcilable conflict with this rule. This rule will not be retroactive.

Executive Order 12372

Executive Order 12372, ''Intergovernmental Review of Federal Programs,'' requires consultation with officials of State and local governments that would be directly affected by the proposed Federal financial assistance. The objectives of the Executive Order are to foster an intergovernmental partnership and a strengthened federalism by relying on State and local processes for the State and local government coordination and review of proposed Federal financial assistance and direct Federal development. This rule will not directly affect State or local governments, and, for this reason, it is excluded from the scope of Executive Order 12372.

Executive Order 12866 and 13563

Executive Orders 12866 and 13563 direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This final rule has been determined to be not significant and was not reviewed by the Office of Management and Budget (OMB) in conformance with Executive Order 12866.

Congressional Review Act

Pursuant to the Congressional Review Act (5 U.S.C. 801 *et seq.*), the Office of Information and Regulatory Affairs has designated this rule as not a major rule, as defined by 5 U.S.C. 804(2).

Executive Order 13175

This rule has been reviewed for compliance with Executive Order 13175, ''Consultation and Coordination with Indian Tribal Governments.'' Executive Order 13175 requires Federal agencies to consult and coordinate with tribes on a government-to-government basis on policies that have tribal implications, including regulations, legislative comments, proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes or on the distribution of power and responsibilities between the Federal Government and Indian tribes. FAS has assessed the impact of this rule on Indian tribes and determined that this rule does not, to the knowledge of FAS, have tribal implications that require tribal consultation under Executive Order 13175. If a tribe requests consultation, FAS will work with USDA Office of Tribal Relations to ensure

meaningful consultation is provided where changes, additions, and modifications identified herein are not expressly mandated by Congress.

Executive Order 13771

Executive Order 13771 directs agencies to reduce regulation and control regulatory costs and provides that for every new regulation issued, at least two prior regulations be identified for elimination, and that the cost of planned regulations be prudently managed and controlled through a budgeting process. This rule is not an Executive Order 13771 regulatory action because this rule is not significant under Executive Order 12866.

List of Subjects in 7 CFR Part 1485

Agricultural commodities, Exports.

For the reasons discussed in the preamble, CCC revises 7 CFR part 1485 to read as follows:

PART 1485—GRANT AGREEMENTS FOR THE DEVELOPMENT OF FOREIGN MARKETS FOR U.S. AGRICULTURAL COMMODITIES

Subpart A—[Reserved]

Subpart B—Market Access Program

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Authority: 7 U.S.C. 5623, 5662–5663

Subpart A—[Reserved]

Subpart B—Market Access Program

§ 1485.10 General purpose and scope.

(a) This subpart sets forth the general terms and conditions governing the Commodity Credit Corporation's (CCC) operation of the Market Access Program (MAP).

(b)(1) The Office of Management and Budget (OMB) issued guidance on Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards in 2 CFR part 200. In 2 CFR 400.1, the U.S. Department of Agriculture (USDA) adopted OMB's guidance in subparts A through F of 2 CFR part 200, as supplemented by 2 CFR part 400, as USDA policies and procedures for uniform administrative requirements, cost principles, and audit requirements for Federal awards.

(2) The OMB guidance at 2 CFR part 200, as supplemented by 2 CFR part 400 and this subpart, applies to the Market Access Program (MAP) Program.

(3) In addition to the provisions of this subpart, other regulations that are generally applicable to grants and cooperative agreements of USDA, including the applicable regulations set forth in 2 CFR chapters I, II, and IV, also apply to the MAP, to the extent that these regulations do not directly conflict with the provisions of this subpart. The provisions of the CCC Charter Act (15 U.S.C. 714 *et seq.*) and any other statutory or regulatory provisions that are generally applicable to CCC also apply to the MAP.

(c) Under the MAP, CCC may provide grants to eligible U.S. entities to conduct certain marketing and promotion activities aimed at developing, maintaining, or expanding commercial export markets for U.S. agricultural commodities. MAP Participants may receive assistance for either generic or brand promotion activities. While activities generally take place overseas, reimbursable activities may also take place in the United States. CCC expects all activities that occur in the United States for which MAP reimbursement is sought to develop, maintain, or expand the commercial export market for the relevant U.S. agricultural commodity in accordance with the MAP Participant's approved MAP program.

(d) The MAP generally operates on a reimbursement basis.

(e) CCC's policy is to ensure that benefits generated by MAP agreements are broadly available throughout the relevant agricultural sector and that no single entity gains an undue advantage or sole benefit from program activities. CCC also endeavors to enter into MAP agreements covering a broad array of agricultural commodity sectors. The MAP is administered by the Foreign Agricultural Service (FAS) acting on behalf of CCC.

§ 1485.11 Definitions.

For purposes of this subpart the following definitions apply:

Activity means a specific foreign market development effort undertaken by a MAP Participant.

Administrative expenses or costs means expenses or costs of administering, directing, and controlling an organization that is a MAP Participant. Generally, this would include expenses or costs such as those related to:

(1) Maintaining a physical office (including, but not limited to: Rent, office equipment, office supplies, office décor, office furniture, computer hardware and software, maintenance, extermination, parking, and business cards);

(2) Personnel (including, but not limited to: Salaries, benefits, payroll taxes, individual insurance, and training);

(3) Communications (including, but not limited to: Phone expenses, internet, mobile phones, personal digital assistants, email, mobile email devices, postage, courier services, television, radio, and walkie talkies);

(4) Management of an organization or unit of an organization (including, but not limited to: Planning, supervision, supervisory travel, teambuilding, recruiting, and hiring);

(5) Utilities (including, but not limited to: Sewer, water, and energy);

(6) Professional services (including, but not limited to: Accounting expenses, financial services, and investigatory services).

Affiliate means any partnership, association, company, corporation, trust, or any other such party in which the Participant has an investment, other than a mutual fund.

Agreement means a legally binding grant entered into between CCC and a MAP applicant setting forth the terms and conditions to implement approved activities under the MAP program, including any subsequent amendments to such agreement.

Approval letter means a document by which CCC informs an applicant that its MAP application for a program year has been approved for funding. This letter may also approve specific activities and contain terms and conditions in addition to the agreement. This letter requires a countersignature by the MAP Participant before it becomes effective.

Attaché/Counselor means the FAS employee representing USDA interests in the foreign country in which promotional activities are conducted.

Brand participant means a small-sized U.S. for-profit entity or a U.S. agricultural cooperative that owns the brand(s) of the eligible commodity to be promoted or has the exclusive rights to use such brand(s) and that is participating in the MAP brand promotion program of another MAP Participant. This definition does not include any U.S. agricultural cooperatives that are MAP Participants that apply for MAP funds to implement their own brand programs.

Brand promotion means an activity that involves the exclusive or predominant use of a single U.S. company name, or the logo or brand name of a single U.S. company, or the brand of a U.S. agricultural cooperative, or any activity undertaken by a MAP Participant in the brand program.

Constraint means a condition in a particular country or region that needs to be addressed in order to develop, expand, or maintain exports of a specific eligible commodity.

Contribution means the funds, *e.g.,* money, personnel, materials, services, facilities, or supplies, provided by a MAP Participant, State agency or entities in the MAP Participant's industry (''U.S. industry'') in support of a MAP Participant's generic promotion program as well as funds provided by the MAP Participant, U.S. industry, or State agency in support of related promotion activities in the markets covered by the MAP Participant's agreement.

Cost share means the funds, *e.g.,* money, personnel, materials, services, facilities, or supplies, provided by a MAP Participant, entities in the MAP Participant's industry, or State agency in support of an approved activity.

Credit memo means a commercial document, also known as a credit memorandum, issued by the MAP Participant to a commercial entity that owes the MAP Participant a certain sum. A credit memo is used when the MAP Participant owes the commercial entity a sum less than the amount the entity owes the Participant. The credit memo reflects an offset of the amount the MAP Participant owes the entity against the amount the entity owes to the MAP Participant.

Demonstration projects means activities involving the erection or construction of a structure or facility or the installation of equipment.

Eligible commodity means any agricultural commodity or product thereof, excluding tobacco, that is comprised of at least 50 percent by weight, exclusive of added water, of agricultural commodities grown or raised in the United States.

Expenditure means either payment via the transfer of funds or offset reflected in a credit memo in lieu of a transfer of funds.

FAS website means a website maintained by FAS providing information on the MAP. It is currently accessible at *www.fas.usda.gov/programs/market-access-program-map.*

Foreign subrecipient means a foreign entity that a MAP Participant works with, in accordance with this subpart, to promote the export of an eligible commodity under the MAP program.

Generic promotion means an activity that is not a brand promotion but, rather, promotes an eligible commodity generally. A generic promotion activity may include the promotion of a foreign brand (*i.e.,* a brand owned primarily by foreign interests and being used to market a commodity or product in a foreign market), if the foreign brand uses the promoted eligible commodity or product from multiple U.S. suppliers. A generic promotion activity may also involve the use of specific U.S. company names, logos, or brand names. However, in that case, the MAP Participant must ensure that all U.S. companies seeking to promote such eligible commodity in the market have an equal opportunity to participate in the activity and that at least two U.S. companies participate. In addition, an activity that promotes separate items from multiple U.S. companies will be considered a generic promotion only if the promotion of the separate items maintains a unified theme (*i.e.,* a dominant idea or motif) and style and is subordinate to the promotion of the generic theme.

MAP is the acronym for the Market Access Program.

MAP Participant or Participant means an entity that has entered into an agreement with CCC.

Market means a country or region targeted by an activity.

Notification means a document from the MAP Participant by which the MAP Participant proposes to CCC changes to the activities and/or funding levels in an approved agreement and/or approval letter.

Product samples means a representative part of a larger whole promoted commodity or group of promoted commodities. Product samples include all forms of a promoted commodity (*e.g.,* fresh or processed), independent of the ultimate utilization of the sample. Product samples might be used in support of international marketing activities including, but not limited to: Displays, food process testing, cooking demonstrations, or trade and consumer tastings.

Program notice means documents that CCC issues for informational purposes. These notices are currently made available electronically through the FAS website. These notices have no legal effect. They are intended to alert MAP Participants of various aspects of CCC's current administration of the MAP program. For example, CCC issues notices to alert Participants of applicable Federal pay scale rates and lists of economic and trade sanctions against certain foreign countries.

Program year means, unless otherwise agreed to in writing between CCC and a MAP Participant, a 12-month period during which a MAP Participant can undertake activities consistent with this subpart and its agreement and approval letter with CCC. This is also known as a project period, which in multiple year awards will be divided into budget periods.

Promoted commodity means an eligible commodity the sale of which is the intended result of a promotional activity under the MAP.

Sales and trade relations expenditures (STRE) means expenditures made on breakfast, lunch, dinner, receptions, and refreshments at approved activities; miscellaneous courtesies such as checkroom fees, taxi fares, and tips for approved activities; and decorations for a special promotional occasion that is part of an approved activity.

Sales team means a group of individuals engaged in an approved activity intended to result in specific sales.

Small-sized entity means a U.S. commercial entity that meets the small business size standards published at 13 CFR part 121, Small Business Size Regulations.

SRTG is the acronym for State Regional Trade Group. An SRTG is a nonprofit association of state-funded agricultural promotion agencies.

Supergrade means a salary level above the reimbursable salary range generally allowable under the MAP, which CCC may approve on a case by case basis. This salary level is available only for certain non-U.S. employees who direct MAP Participants' overseas offices.

Temporary contractor means a contractor, typically a consultant or other highly paid professional, that is hired on a short-term basis to assist in the performance of an activity.

Trade team means a group of individuals engaged in an approved

activity intended to promote the interests of an entire agricultural sector rather than to result in specific sales by any of its members.

Unified Export Strategy (UES) means a holistic marketing plan that outlines an applicant's proposed foreign market development activities and requested funding under each of the FAS market development programs.

Unified Export Strategy (UES) system means an online internet system maintained by FAS through which applicants may currently apply to the MAP and other FAS market development programs. The system is currently accessible at *https://apps.fas.usda.gov/ues/webapp/.* FAS may prescribe a different system through which applicants may apply to MAP and will announce such system in the applicable Notice of Funding Opportunity (NOFO).

U.S. agricultural commodity means any agricultural commodity of U.S. origin, including food, feed, fiber, forestry product, livestock, insects, and fish harvested from a U.S. aquaculture farm or harvested by a vessel (as defined in Title 46 of the United States Code) in waters that are not waters (including the territorial sea) of a foreign country, and any product thereof.

U.S. for-profit entity means an organized or incorporated firm, association, or other entity that is located and doing business for profit in the United States and is engaged in the export or sale of an eligible commodity.

§ 1485.12 Participation eligibility.

(a) To participate in the MAP, an entity shall be:

(1) A nonprofit U.S agricultural trade organization;

(2) A nonprofit SRTG;

(3) A U.S. agricultural cooperative; or

(4) A State agency.

(b) CCC will enter into an agreement only for the promotion of an eligible commodity.

(c) FAS may set forth specific eligibility information, including any factors or priorities that will affect the eligibility of an applicant or application for selection, in the full text of the applicable NOFO posted on the U.S. Government website for grant opportunities.

§ 1485.13 Application process.

(a) *General application requirements.* CCC will periodically announce through a NOFO that it is accepting applications for participation in the MAP for a specified program year. This announcement will be posted on the U.S. Government website for grant opportunities. Applications shall be submitted in accordance with the terms and requirements specified in the announcement and in this part. Currently, applicants are encouraged to submit applications through the UES system but are not required to do so. Applicants may apply to conduct a generic promotion program and/or a brand promotion program that provides MAP funds to brand participants for branded promotion. An applicant that is a U.S. agricultural cooperative may also apply for funds to conduct its own brand promotion program.

(b) *Universal identifier and System for Award Management (SAM).* In accordance with 2 CFR part 25, each entity that applies to the MAP program and does not qualify for an exemption under 2 CFR 25.110 must:

(1) Be registered in the SAM prior to submitting an application or plan;

(2) Maintain an active SAM registration with current information at all times during which it has an active Federal award or an application or plan under consideration by CCC; and

(3) Provide its DUNS number, or a unique identifier designated as a DUNS replacement, in each application or plan it submits to CCC.

(c) *Reporting subaward and executive compensation information.* In accordance with 2 CFR part 170, each entity that applies to the MAP program and does not qualify for an exception under 2 CFR 170.110(b) must ensure it has the necessary processes and systems in place to comply with the applicable reporting requirements of 2 CFR part 170 should it receive MAP funding.

§ 1485.14 Application review and formation of agreements.

(a) *General.* (1) CCC will, subject to the availability of funds, approve those applications that it considers to present the best opportunity for developing, maintaining, or expanding export markets for U.S. agricultural commodities. CCC will review all proposals for eligibility and completeness. CCC will evaluate and score each proposal against the factors described in the NOFO. The purpose of this review is to identify meritorious proposals, recommend an appropriate funding level for each proposal, and submit the proposals and funding recommendations to appropriate officials for decision. CCC may, when appropriate to the subject matter of the proposal, request the assistance of other U.S. Government experts in evaluating the merits of a proposal.

(2) When considering eligible nonprofit U.S. trade organizations, CCC may weigh which organizations have the broadest producer representation and affiliated industry participation of the commodity being promoted. CCC may require that an applicant participate in the MAP through another MAP Participant or applicant. All reviewers will be required to sign a conflict of interest form, and when conflicts of interests are identified the reviewer will be recused from the objective review process.

(b) *Application review criteria.* CCC follows results-oriented management principles and considers the following criteria when assessing the likelihood of success of the applications it receives, determining which applications to recommend for approval, and developing preliminary recommended funding levels:

(1) Strategic planning (25%);

(2) Program implementation (25%); and

(3) Program results and evaluation (50%).

(c) *Allocation factors.* CCC determines final funding levels after allocating available funds to approved applications on the basis of criteria that will be fully described in each program year's MAP announcement. Generally, extensions will not be allowable.

(d) *Approval decision*—(1) *Approval decision.* CCC will approve those applications that it determines best satisfy the criteria and factors specified in paragraphs (a), (b), and (c) of this section.

(2) *Notification of decision.* CCC will notify each applicant in writing of the final disposition of its application. CCC will send an agreement, an approval letter, and a signature card to each approved applicant. The agreement and the approval letter will outline which activities and budgets are approved and will specify any special terms and conditions applicable to a MAP Participant's program, including any requirements with respect to contribution, cost share and program evaluations. An applicant that decides to accept the terms and conditions contained in the agreement and the approval letter must so indicate by having its Chief Executive Officer (CEO) or designee sign the agreement and the approval letter and submit these to CCC. Final agreement shall occur when the agreement and the approval letter are signed by both parties. The agreement, approval letter, and this subpart shall establish the terms and conditions of a MAP agreement between CCC and the approved applicant.

(e) *Signature cards.* The MAP Participant shall designate at least two individuals in its organization to sign agreements and amendments, approval letters, reimbursement claims, and

advance requests. The MAP Participant shall submit the signature card signed by those designated individuals and by the MAP Participant's CEO to CCC prior to the start of the program year. The Participant shall immediately notify CCC of any changes in signatories (*e.g.,* removal or addition of individuals, name changes, etc.), and shall submit a revised signature card accordingly.

(f) *UES ID and passwords.* CCC will provide each MAP Participant with IDs and passwords for the UES system, as necessary. MAP Participants shall protect these IDs and passwords in accordance with USDA's information technology policies. MAP Participants shall immediately notify CCC whenever a person who possesses the ID and password information no longer needs such information or a person who is not authorized gains such information.

(g) *Annual size certification.* A MAP Participant through which small-sized U.S. for-profit entities and/or U.S. agricultural cooperatives are participating in the MAP program shall obtain annual certifications from all such entities that they are small-sized U.S. entities or U.S. agricultural cooperatives as defined in these regulations. The Participant shall retain these certifications in accordance with the recordkeeping requirements of this subpart.

(h) *Changes to activities and funding*—(1) *Adding a new activity.* (i) A MAP Participant may not conduct a new activity without first obtaining an approved activity budget for such change. To request approval of such activity budget, the MAP Participant shall submit a notification to CCC.

(ii) A notification for a new activity shall provide an activity justification and identify any related adjustments to the approved strategic plan, including changes in the market, constraint, or opportunity that the activity proposes to address. The notification shall contain the activity description, the proposed budget, and a justification for the transfer of funds.

(iii) After receipt of the notification, CCC will inform the MAP Participant via the UES system whether the requested budget is approved.

(2) *Modifying existing activities and their funding levels.* (i) A MAP Participant desiring to increase the funding level for existing, approved activities addressing a single constraint or opportunity by more than $25,000 or 25 percent of the approved funding level, whichever is greater, must first submit a notification explaining the adjustment to CCC before making such change.

(ii) A MAP Participant may make significant adjustments below that threshold to the funding levels for existing, approved activities without prior notification to CCC, but only if it submits a notification explaining the adjustments to CCC no later than 30 calendar days after the change. Minor adjustments to existing, approved activities and/or funding levels do not require notification.

(iii) Notifications shall describe the activity and any changes to the activity, the existing funding level, or the proposed funding level and shall include a justification for the transfer of funds, if applicable.

§ 1485.15 Operational procedures for brand programs.

(a) Where CCC approves an application by a MAP Participant to run a brand promotion program that will include brand participants, the MAP Participant shall establish brand program operational procedures. The MAP Participant annually shall submit to CCC for approval its proposed brand program operational procedures for such program year. CCC will notify all new and existing MAP Participants in writing in each Participant's approval letter and through the FAS website as to applicable submission dates for brand program operation procedures. Such procedures shall include, at a minimum, a brand program application, application procedures, application review criteria, brand participant eligibility requirements, a participation agreement, reimbursement requirements, compliance requirements, reporting and recordkeeping requirements, employment practices, financial management requirements, contracting procedures, and evaluation requirements.

(b) The MAP Participant shall not enter into any participation agreements with brand participants nor shall it implement any MAP brand activities for the applicable program year unless and until CCC has communicated in writing its approval of the proposed operational procedures to the MAP Participant.

(c) Participation agreements between MAP Participants and brand participants. Where CCC approves a MAP Participant's application to run a brand promotion program that will include brand participants, the MAP Participant shall enter into participation agreements with brand participants. These agreements must:

(1) Specify a time period for such brand promotion and require that all brand promotion expenditures be made within the MAP Participant's approved program year;

(2) Make no allowance for extension or renewal;

(3) Limit reimbursable expenditures to those made in countries and for activities approved in the brand participant's activity plan;

(4) Specify the percentage of promotion expenditures that will be reimbursed, reimbursement procedures, and documentation requirements;

(5) Include a written certification by the brand participant that it either owns the brand of the product it will promote or has exclusive rights to promote the brand in each of the countries in which promotion activities will occur;

(6) Require: That all product labels, promotional material, and advertising will identify the origin of the eligible commodity as ''American,'' ''Product of the United States of America,'' ''Product of the U.S.,'' ''Product of the U.S.A.,'' ''Product of America,'' ''Grown in the United States of America,'' ''Grown in the U.S.,'' ''Grown in the U.S.A.,'' ''Grown in America,'' ''Made in the United States of America,'' ''Made in the U.S.,'' ''Made in the U.S.A.,'' ''Made in America,'' or product of, grown in, or made in any state or territory of the United States of America spelled out in its entirety, or other U.S. regional designation if approved in advance by CCC; that such origin identification will be conspicuously displayed in a manner easily observed as identifying the origin of the product; and that such origin identification will conform, to the extent possible, to the U.S. standard of 1/6 inch (.42 centimeters) in height based on the lower case letter ''o.'' The use of these terms as a descriptor or in the name of the product (*e.g.,* Texas style chili, Bob's American Pizza) does not satisfy the product origin requirement. Phrases ''product of,'' ''grown in,'' or ''made in'' are encouraged, but not required. A MAP Participant may request an exemption from this requirement on a case by case basis. All such requests shall be in writing and include justification satisfactory to CCC that this labeling requirement would hinder a MAP Participant's promotional efforts. CCC will determine, on a case by case basis, whether sufficient justification exists to grant an exemption from the labeling requirement. In addition, CCC may temporarily waive this requirement where CCC has determined that such labeling will likely harm sales rather than help them. Such determinations will be announced to MAP Participants via a program notice issued on FAS' website;

(7) Include a written certification by the brand participant that it is either a small–sized entity as defined in this

subpart or a U.S. agricultural cooperative;

(8) Require that the brand participant submit to the MAP Participant a statement certifying that any Federal funds received will supplement, but not supplant, any private or third–party funds or other contribution or cost share to program activities; and

(9) Require the brand participant to maintain all original records and documents relating to program activities for five calendar years following the end of the applicable program year and make such records and documents available upon request to authorized officials of the U.S. Government.

§ 1485.16 Contribution and cost share rules.

(a) A MAP Participant implementing a MAP generic promotion program shall make contributions equal to at least 10 percent of the total amount reimbursed by CCC for all approved generic promotion activities undertaken by the MAP Participant. The contribution amount will be reflected in the award budget.

(b) A MAP Participant conducting its own brand promotion or a brand participant that is participating in the MAP brand promotion program of another MAP Participant shall provide funds for the branded activity in an amount that is at least equivalent to the amount of assistance they get from MAP for that activity.

(c) A MAP Participant must use its own funds and may not use MAP funds to pay any administrative costs of the MAP Participant's U.S. office(s), including legal fees, except as set forth in this subpart. Where the MAP Participant uses its own funds to pay for administrative costs, such costs may be counted in calculating the amount of contribution or cost share the MAP Participant contributes to MAP generic or brand promotion programs.

(d)(1) In calculating the amount of contribution or cost share that it will make, and the contribution or cost share that the U.S. industry (including expenditures to be made by entities in the applicant's industry in support of the entities' related promotion activities in the markets covered by the applicant's application) or State or local agency will make, the MAP applicant may include the costs (or such prorated costs) listed under paragraph (d)(2) of this section if:

(i) Expenditures are necessary and reasonable for accomplishment of an approved activity;

(ii) Expenditures are not included as cost share for any other Federal award;

(iii) Expenditures are not paid by the Federal Government under another Federal award, except where the Federal statute authorizing a program specifically provides that Federal funds made available for such program can be applied to matching or cost sharing requirements of other Federal programs; and

(iv) The contribution or cost share is made during the period covered by the agreement.

(2) Subject to paragraph (d)(1) of this section, as well as the cost principles in 2 CFR part 200 to the extent these principles do not directly conflict with the provisions of this subpart, the following are eligible contribution or cost share:

(i) Cash;

(ii) Compensation paid to personnel;

(iii) The cost of acquiring materials, supplies, or services;

(iv) The cost of office space, including legal fees;

(v) A reasonable and justifiable proportion of general administrative costs and overhead;

(vi) Payments for indemnity and fidelity bond expenses;

(vii) The cost of business cards that target a foreign audience;

(viii) Fees for office parking;

(ix) The cost of subscriptions that are of a technical, economic, or marketing nature and that are relevant to the approved activities of the MAP Participant;

(x) The cost of activities conducted overseas;

(xi) Credit card fees;

(xii) The cost of any independent evaluation or audit that is not required by CCC to ensure compliance with agreement or regulatory requirements;

(xiii) The cost of giveaways, awards, prizes, and gifts;

(xiv) The cost of product samples;

(xv) Fees for participating in U.S. Government sponsored or endorsed export promotion activities;

(xvi) The cost of air and local travel in the United States related to a foreign market development effort;

(xvii) Transportation and shipping costs;

(xviii) The cost of displays and promotional materials;

(xix) Advertising costs;

(xx) Reasonable travel costs and expenses related to undertaking a foreign market development activity;

(xxi) The costs associated with trade shows, seminars, and STRE conducted in the United States, and costs associated with entertainment conducted in the United States where such entertainment costs have a programmatic purpose and are authorized in the agreement and/or the approval letter or are authorized by prior written approval of CCC;

(xxii) Product research that is undertaken to benefit an industry and has a specific export application;

(xxiii) Other administrative expenses (*e.g.,* supervisory travel from the U.S. to an overseas office); and

(xxiv) The cost of any activity expressly listed as reimbursable in this subpart.

(3) The following are not eligible contribution or cost share:

(i) Any portion of salary or compensation of an individual who is the target of a promotional activity;

(ii) Any expenditure, including that portion of salary and time spent, related to promoting membership in the Participant's organization;

(iii) Any land costs other than allowable costs for office space;

(iv) The cost of refreshments and related equipment provided to office staff;

(v) The cost of insuring articles owned by private individuals;

(vi) The cost of any arrangement that has the effect of reducing the selling price of a U.S. agricultural commodity;

(vii) The cost of product development, product modifications, or product research;

(viii) Slotting fees or similar sales expenditures;

(ix) Funds, services, capital goods, or personnel provided by any U.S. Government agency;

(x) The value of any services generated by a MAP Participant or third party that involve no expenditure by the MAP Participant or third party, *e.g.,* free publicity;

(xi) Membership fees in clubs and social organizations; and

(xii) Any expenditure for an activity prior to CCC's approval of that activity.

(4) CCC shall determine, at CCC's discretion, whether any cost not expressly listed in this section may be included by the MAP Participant as an eligible contribution or cost share.

§ 1485.17 Reimbursement rules.

(a) A MAP Participant may seek reimbursement for an eligible expenditure if:

(1) The expenditure was necessary and reasonable for the performance of an approved activity; and

(2) The Participant has not been and will not be reimbursed for such expenditure by any other source.

(b) Subject to paragraphs (a) and (d) of this section, as well as the cost principles in 2 CFR 200 to the extent these principles do not directly conflict with the provisions of this subpart, for

either brand or generic promotion activities, CCC will reimburse, in whole or in part, the cost of:

(1) Production and placement of advertising, including in print, electronic media, billboards, or posters, which may include advertising the availability of price discounts, except that advertising associated with a coupon or price discount for the MAP-promoted product is not reimbursable. If advertising is related to both coupons or price discounts for products other than the MAP Participant's promoted products as well as for MAP-promoted products, expenditures for such advertising will not be reimbursed in whole or in part (*e.g.,* expenditures may not be prorated and submitted for reimbursement). Electronic media includes, but is not limited to, radio, television, electronic mail, internet, telephone, text messaging, and podcasting;

(2) Production and distribution of banners, recipe cards, table tents, shelf talkers, and other similar point of sale materials;

(3) Direct mail advertising;

(4) In-store and food service promotions, product demonstrations to the trade and to consumers, and distribution of product samples (but not the purchase of the product samples), including shipment of samples or other program materials from the United States to foreign countries;

(5) Temporary displays and rental of space for temporary displays;

(6) Expenditures, other than travel expenditures, associated with seminars and educational training, whether conducted in the United States or outside the United States, including space rental, equipment rental, and duplication of seminar materials;

(7) Subject to paragraph (b)(18) of this section, non-travel expenditures, including participation fees, booth construction, transportation of related materials, rental of space and equipment, and duplication of related printed materials, associated with retail, trade, and consumer exhibits and shows, whether held outside or inside the United States. However, non-travel expenditures associated with retail, trade, and consumer exhibits and shows held inside the United States are reimbursable only if the exhibit or show is included on the list of approved U.S. exhibits and shows announced via a program notice issued on FAS' website and the exhibit or show is one that the MAP Participant has not participated in within the last three years using funds from a source other than the MAP. Retail, trade, and consumer exhibits and shows held inside the United States may be considered for inclusion on the list of approved exhibits and shows if they are:

(i) A food or agricultural exhibit or show with no less than 30% of exhibitors selling food or agricultural products; and

(ii) An international exhibit or show that targets buyers, distributors, and the like from more than one foreign country and no less than 15% of its visitors are from countries other than the host country;

(8) Subject to paragraph (b)(18) of this section, international travel expenditures (with airfare limited to the full fare economy rate), including per diem and any fees for passports, visas, inoculations, and modifying the originally purchased airline ticket, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), for no more than two representatives of a single brand participant (or MAP Participant directly running its own brand program) to exhibit their company's (or cooperative's) products at a retail, trade, or consumer exhibit or show held outside the United States. Representatives may include employees and board members of private companies, employees or members of cooperatives, or any broker, consultant, or marketing representative contracted by the company or cooperative to represent the company or cooperative in sales transactions;

(9) Subscriptions that are of a technical, economic, or marketing nature and that are relevant to the approved activities of the MAP Participant;

(10) Demonstrators, interpreters, translators, receptionists, and similar temporary workers who help with the implementation of individual promotional activities, such as trade shows, in-store promotions, food service promotions, and trade seminars;

(11) Giveaways, awards, prizes, gifts, and other similar promotional materials, subject to such reimbursement limitation as CCC may determine and announce in writing to MAP Participants via a program notice issued on FAS' website. Reimbursement is available only when:

(i) The items are described in detail with a per unit cost in an approved strategic plan; and

(ii) Distribution of the promotional item is not contingent upon the consumer, or other target audience, purchasing a good or service to receive the promotional item;

(12) The design and production of packaging, labeling, or origin identification to be used during the program year in which the expenditure is made, if such packaging, labeling, or origin identification is necessary to meet the importing requirements of a foreign country;

(13) The design, production, and distribution of coupons for products other than the MAP Participant's promoted products. If such activities include both coupons or price discounts for products other than the MAP Participant's promoted products as well as for MAP-promoted products, expenditures for such activities will not be reimbursed in whole or in part (*e.g.,* expenditures may not be prorated and submitted for reimbursement);

(14) An audit of a MAP Participant as required by 2 CFR part 200, subpart F if the MAP is the MAP Participant's largest source of Federal funding;

(15) The translation of written materials as necessary to carry out approved activities;

(16) Expenditures associated with developing, updating, and servicing websites on the internet that clearly target a foreign audience;

(17) International travel expenditures (with airfare limited to the full fare economy rate), including per diem and any fees for passports, visas, inoculations, and modifying the originally purchased airline ticket, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), incurred for a foreign trade mission conducted outside the United States that is an activity under an approved branded program and that has met the following conditions:

(i) Trade mission travel for company (or cooperative) representatives was identified as a separate approved activity in the MAP Participant's UES;

(ii) The trade mission included representatives, as defined in paragraph (b)(8) of this section, from a minimum of five different companies (or cooperatives), and no more than two representatives from each participating company (or cooperative);

(iii) The appropriate FAS overseas office supported the trade mission by dedicating meaningful funding or other resources (such as facilities or staff time) to the activity; and

(iv)(A) The MAP Participant with the approved brand program produced an itinerary or agenda for the trade mission that demonstrated that company (or cooperative) representatives would be engaged for a minimum of 6 hours per day (except for the first and last days of the mission) in trade mission activities that include, at a minimum, each of the following:

(*1*) A product showcase where the FAS overseas office approved an invitation list of qualified buyers;

(*2*) Pre-arranged one-on-one business meetings; and

(*3*) Evaluation and feedback sessions with FAS staff and trade mission sponsors.

(B) Reimbursement is conditional on the MAP Participant having notified in writing the Attaché/Counselor in the destination country in advance of the travel;

(18) Where USDA has sponsored or endorsed a U.S. pavilion at a retail, trade, or consumer exhibit or show, whether held outside or inside the United States, MAP funds may be used to reimburse the travel and/or non-travel expenditures of only those MAP Participants located within the U.S. pavilion. Such expenditures must also adhere to the standard terms and conditions of the U.S. pavilion organizer. Upon written request, CCC may temporarily waive this subsection, on a case by case basis, where the trade show is segregated into product pavilions or a company's distributor or importer is located outside the U.S. pavilion. Such waiver will be provided to the MAP Participant in writing; and

(19) Contracts with U.S.-based organizations when the only contracted service such organizations provide to a MAP Participant is carrying out a specific market promotion activity in the United States directed to a foreign audience (*e.g.,* a trade mission of foreign buyers coming to the United States to visit U.S. exporters). Such contracts may be reimbursable as a direct promotional expense. If a U.S.-based organization provides administrative services to the MAP Participant's domestic home office during a program year, any direct promotional services such organization provides to the Participant, whether for the Participant's domestic or overseas offices, during the same program year are not reimbursable.

(c) Subject to paragraphs (a) and (d) of this section, as well as the cost principles in 2 CFR part 200 to the extent these principles do not directly conflict with the provisions of this subpart, but for generic promotion activities only, CCC will also reimburse, in whole or in part, the cost of:

(1) Compensation and allowances for housing, educational tuition, and cost of living adjustments paid to a U.S. citizen employee or a U.S. citizen contractor stationed overseas, provided such benefits are granted under established written policies, except CCC will not reimburse that portion of:

(i) The total of compensation and allowances that exceed 125 percent of the level of a GS-15 Step 10 salary for U.S. Government employees; or

(ii) Allowances that exceed the rate authorized for U.S. Embassy personnel.

(2) Approved Supergrade salaries for non-U.S. citizen employees and non-U.S. contractors stationed overseas;

(3) Compensation of non-U.S. citizen staff employees or non-U.S. contractors stationed overseas, subject to the following limitations:

(i) Where there is a local U.S. Embassy Foreign Service National (FSN) salary plan, CCC will not reimburse any portion of such compensation that exceeds the compensation prescribed for the most comparable position in the FSN salary plan, except for approved Supergrades; or

(ii) Where an FSN salary plan does not exist, CCC will not reimburse any portion of such compensation that exceeds locally prevailing levels, which the MAP Participant shall document by a salary survey or other means, except for approved Supergrades;

(4) A retroactive salary adjustment for non-U.S. citizen staff employees or non-U.S. contractors stationed overseas that conforms to a change in FSN salary plans, effective as of the date of such change;

(5) Accrued annual leave as of the time employment is terminated or as of such time as required by local law;

(6) Overtime paid to clerical staff of approved MAP-funded overseas offices;

(7) Temporary contractor fees for contractors stationed overseas, except CCC will not reimburse any portion of any such fee that exceeds the daily gross GS-15, Step 10 salary for U.S. Government employees in effect on the date the fee is earned, unless a bidding process reveals that such a contractor is not available at or below that salary rate;

(8)(i) Subject to paragraph (b)(18) of this section, international travel expenditures, including per diem and any fees for passports, visas, inoculations, and modifying the originally purchased airline ticket, for activities held outside the United States or in the United States, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), except that if the activity is participation in a retail, trade, or consumer exhibit or show held inside the United States, international travel expenditures are reimbursable only if the exhibit or show is included on the list of approved U.S. exhibits and shows announced via a program notice issued on FAS' website and the exhibit or show is one that the Participant has not participated in within the last three years using funds from a source other than the MAP. Retail, trade, and consumer exhibits and shows held inside the United States may be considered for inclusion on the list of approved exhibits and shows if they are:

(A) A food or agricultural exhibit or show with no less than 30% of exhibitors selling food or agricultural products; and

(B) An international exhibit or show that targets buyers, distributors, and the like from more than one foreign country and no less than 15% of its visitors are from countries other than the host country.

(ii) CCC generally will not reimburse any portion of air travel, including any fees for modifying the originally purchased ticket, in excess of the full fare economy rate. If a traveler flies in business class or a different premium class, the basis for reimbursement will be the full fare economy class rate for the same flight and the MAP Participant shall provide documentation establishing such full fare economy class rate to support its reimbursement claim. If economy class is not offered for the same flight or if the traveler flies on a charter flight, the basis for reimbursement will be the average of the full fare economy class rate for flights offered by three different airlines between the same points on the same date and the MAP Participant shall provide documentation establishing such average of the full fare economy class rates to support its reimbursement claim.

(iii) In very limited circumstances, the MAP Participant may be reimbursed for air travel up to the business class rate (*i.e.,* a premium class rate other than the first class rate). Such circumstances are:

(A) Regularly scheduled flights between the origin and destination points do not offer economy class (or equivalent) airfare and the MAP Participant receives written documentation to that effect at the time the tickets are purchased;

(B) Business class air travel is necessary to accommodate an eligible traveler's disability. Such disability must be substantiated in writing by a physician; or

(C) An eligible traveler's origin and/or destination are outside of the continental United States and the scheduled flight time, beginning with the scheduled departure time and ending with the scheduled arrival time, including stopovers and changes of planes, exceeds 14 hours. In such cases, per diem and other allowable expenses will also be reimbursable for the day of arrival. However, no expenses will be reimbursable for a rest period or for any non-work days (*e.g.,* weekends, holidays, personal leave, etc.)

immediately following the date of arrival. A stopover is the time a traveler spends at an airport, other than the originating or destination airport, which is a normally scheduled part of a flight. A change of planes is the time a traveler spends at an airport, other than the originating or destination airport, to disembark from one flight and embark on another. All travel should follow a direct or usually traveled route. Under no circumstances should a traveler select flights in a manner that extends the scheduled flight time to beyond 14 hours in part to secure eligibility for reimbursement of business class travel;

(iv) Alternatively, in lieu of reimbursing up to the business class rate in such circumstances, CCC will reimburse economy class airfare plus per diem and other allowable travel expenses related to a rest period of up to 24 hours, either en route or upon arrival at the destination. For a trip with multiple destinations, each origin/destination combination will be considered separately when applying the 14-hour rule for eligibility of reimbursement of business class travel or rest period expenses;

(9) Automobile mileage at the local U.S. Embassy rate or rental cars while in travel status;

(10) Other allowable expenditures while in travel status as authorized by the U.S. Federal Travel Regulations (41 CFR parts 300 through 304);

(11) Organization costs for overseas offices approved in agreements. Such costs include incorporation fees, brokers' fees, fees to attorneys, accountants, or investment counselors, whether or not employees of the organization, incurred in connection with the establishment or reorganization of the overseas office, and rent, utilities, communications originating overseas, office supplies, accident liability insurance premiums (provided the types and extent and cost of coverage are in accordance with the MAP Participant's policy and sound business practice), and routine accounting and legal services required to maintain the overseas office;

(12) With prior CCC approval, the purchase, lease, or repair of, or insurance premiums for, capital goods that have an expected useful life of at least one year, such as furniture, equipment, machinery, removable fixtures, draperies, blinds, floor coverings, computer hardware and software, and portable electronic communications devices (including mobile phones, wireless email devices, and personal digital assistants);

(13) Such premiums for health or accident insurance and other benefits for foreign national employees that the employer is required by law to pay, provided that such benefits are granted under established written policies;

(14) Accident liability insurance premiums for facilities used jointly with third-party participants for MAP activities or for MAP-funded travel of third-party participants, provided the types and extent and cost of coverage are in accordance with the MAP Participant's policy and sound business practice;

(15) Market research, including research to determine the types of products that are desired in a market;

(16) Independent evaluations and audits, if not otherwise required by CCC, to ensure compliance with program requirements;

(17) Legal fees to obtain advice on the host country's labor laws;

(18) Employment agency fees;

(19) STRE incurred outside of the United States, and STRE incurred in conjunction with an approved activity taking place within the United States with prior written approval from CCC. MAP Participants are required to use the appropriate American Embassy representational funding guidelines for breakfasts, lunches, dinners, and receptions. MAP Participants may exceed Embassy guidelines only when they have received written authorization from the FAS Attaché/Counselor at the Embassy. The amount of unauthorized STRE expenses that exceed the guidelines will not be reimbursed. MAP Participants must pay the difference between the total cost of STRE events and the appropriate amount as determined by the guidelines. For STRE incurred in the United States, the MAP Participant should provide, in its request for approval, the basis for determining its proposed expenses;

(20) Evacuation payments (safe haven) and shipment and storage of household goods and motor vehicles for relocations lasting at least 12 months;

(21) U.S. office(s) administrative support expenses for the National Association of State Departments of Agriculture, the SRTGs, and the Intertribal Agriculture Council;

(22) Non-travel expenditures associated with conducting international staff conferences held either in or outside the United States;

(23) Subject to paragraph (b)(18) of this section, domestic travel expenditures, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), for international retail, trade, and consumer exhibits and shows conducted in the United States. Domestic travel expenses to such a show or exhibit are covered only if the exhibit or show is included on the list of approved U.S. exhibits and shows announced via a program notice issued on FAS' website and the exhibit or show is one that the Participant has not participated in within the last three years using funds from a source other than the MAP. Retail and trade exhibits and shows held inside the United States may be considered for inclusion on the list of approved exhibits and shows if they are:

(i) A food or agricultural exhibit or show with no less than 30% of exhibitors selling food or agricultural products; and

(ii) An international exhibit or show that targets buyers, distributors, and the like from more than one foreign country and no less than 15% of its visitors are from countries other than the host country;

(24) Domestic travel expenditures, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), for seminars and educational training conducted in the United States;

(25) Domestic travel expenditures, as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304), for one home office MAP Participant employee, one MAP Participant board member, or a state department of agriculture employee paid by the MAP Participant, when such individual accompanies foreign trade missions or technical teams while traveling in the United States where the following conditions are met:

(i) Such trade missions or technical team visits are identified in the MAP Participant's UES;

(ii) Such trade missions or technical team visits have been approved by CCC; and

(iii) The MAP-sponsored traveler submits a follow-up trip report to CCC that includes the following:

(A) Purpose for the individual's participation;

(B) Any pre-arranged business meetings;

(C) Itinerary and/or agenda for the trip; and

(D) Feedback from sponsors and trade mission/technical team members on the success of the trip.

(26) Approved demonstration projects;

(27) Expenditures related to copyright, trademark, or patent registration, including attorney fees;

(28) Rental or lease expenditures for storage space for program-related materials;

(29) Business cards that target a foreign audience;

(30) Expenditures associated with developing, updating, and servicing

websites on the internet that: Contain a message related to exporting or international trade, include a discernible ''link'' to the FAS/Washington homepage or an FAS overseas homepage, and have been specifically approved by FAS. Expenditures related to websites or portions of websites that are accessible only to an organization's members are not reimbursable. Reimbursement claims for websites that include any sort of ''members only'' sections must be prorated to exclude the costs associated with those areas subject to restricted access;

(31) Expenditures not otherwise prohibited from reimbursement that are associated with activities held in the United States or abroad designed to improve market access by specifically addressing temporary, permanent, or impending technical barriers to trade that prohibit or threaten U.S. exports of agricultural commodities;

(32) Membership fees in professional, industry-related organizations;

(33) Travel costs for dependents, as allowed in 2 CFR part 200 (*e.g.,* for travel of duration of six months or more with prior approval of CCC);

(34) That portion of airtime for wireless phones that is devoted to program activities and monthly service fees prorated at the proportion of program-related airtime to total airtime; and

(35) Production and distribution of publications.

(d) CCC will not reimburse any cost of:

(1) Forward year financial obligations, such as severance pay, attributable to employment of foreign nationals;

(2) Expenses, fines, settlements, judgments, or payments relating to legal suits, challenges, or disputes, except as otherwise allowed in 2 CFR part 200;

(3) The design and production of packaging, labeling, or origin identification, except as specifically allowed in this subpart;

(4) Product development, product modification, or product research;

(5) Product samples;

(6) Slotting fees or similar sales expenditures;

(7) The purchase, construction, or lease of space for permanent, non-mobile displays, *i.e.,* displays that are constructed to remain permanently in the same location beyond one program year. However, CCC may, at its discretion, reimburse the construction or purchase of permanent displays on a case by case basis, if the Participant sought and received prior written approval from CCC of such construction or purchase;

(8) Rental, lease, or purchase of warehouse space, except for storage space for program-related material;

(9) Coupon redemption or price discounts of the promoted commodity;

(10) Refundable deposits or advances;

(11) Giveaways, awards, prizes, gifts, and other similar promotional materials in excess of the limitation that CCC will determine. Such determination will be announced in writing via a program notice issued on FAS' website;

(12) Alcoholic beverages that are not a promoted commodity and part of an approved promotional activity;

(13) The purchase, lease (except for use in authorized travel status), or repair of motor vehicles;

(14) Travel of applicants for employment interviews;

(15) Unused non-refundable airline tickets or associated penalty fees, except where travel was restricted by U.S. Government action or advisory;

(16) Independent evaluations or audits, including evaluations or audits of the activities of a subcontractor, if CCC determines that such a review is needed in order to confirm past or to ensure future agreement or regulatory compliance;

(17) Any arrangement that has the effect of reducing the selling price of an agricultural commodity;

(18) Goods, services, and salaries of personnel provided by a third party;

(19) Membership fees in clubs and social organizations;

(20) Indemnity and fidelity bonds, except as otherwise allowed in 2 CFR part 200;

(21) Fees for participating in U.S. Government sponsored activities, other than trade fairs, shows, and exhibits;

(22) Business cards that target a U.S. domestic audience;

(23) Seasonal greeting cards;

(24) Office parking fees;

(25) Subscriptions to publications that are not of a technical, economic, or marketing nature or that are not relevant to the approved activities of the MAP Participant;

(26) U.S. office(s) administrative expenses, including communication costs, except as noted in paragraph (c)(21) of this section and except that usage costs for communications devices incurred while on reimbursable international or domestic travel for approved MAP brand or generic promotion activities are reimbursable as eligible travel expenditures as allowed under the U.S. Federal Travel Regulations (41 CFR parts 300 through 304);

(27) Any expenditure on an activity that includes any derogatory reference or comparison to other U.S. agricultural commodities;

(28) Payment of U.S. and foreign employees' or contractors' share of personal taxes, except where a foreign country's laws require the MAP Participant to pay such employees' or contractors' share;

(29) Any expenditure made for an activity prior to CCC's approval of that activity;

(30) Contributions to a contingency reserve or any similar provision made for events the occurrence of which cannot be foretold with certainty as to time, intensity, or with an assurance of their happening;

(31) Credit card fees;

(32) Entertainment, *e.g.,* amusements, diversions, cover charges, personal gifts, or tickets to theatrical or sporting events;

(33) Refreshments, or related equipment, for office staff; and

(34) Expenditures associated with a MAP Participant's creation or review of their fraud prevention program, contracting procedures, or brand program operational procedures.

(e) Paragraphs (e)(1) through (4) of this section shall apply to the approval of Supergrades.

(1) With respect to individuals who are not U.S. citizens and who are hired by MAP Participants either as employees or contractors acting as employees, CCC will not ordinarily reimburse any portion of such individual's compensation that exceeds the compensation prescribed for the most comparable position in the FSN salary plan applicable to the country in which the employee or contractor works. However, a MAP Participant may seek a higher level of reimbursement for a non-U.S. citizen employee or contractor who will be employed as a country director or regional director by requesting that CCC approve that employee or contractor as a Supergrade.

(2) To request approval of a Supergrade, the MAP Participant shall provide CCC with a detailed description of both the duties and responsibilities of the position and the qualifications and background of the employee or contractor concerned. The Participant shall also justify why the comparable FSN salary level is insufficient.

(3) Where a non-U.S. citizen employee or contractor will be employed as a country director, the MAP Participant may request approval for a ''Supergrade I'' salary level, equivalent to a single grade increase over the existing top grade of the FSN salary plan. The Supergrade I and its step increases are calculated by increasing each of the steps in the top FSN grade by the percentage difference between the second highest and the

highest grade in the FSN salary plan. Where the non-U.S. citizen employee or contractor will be employed as a regional director, with responsibility for activities and/or offices in more than one country, the MAP Participant may request approval for a ''Supergrade II'' salary level, which is calculated relative to a Supergrade I in the same way the latter is calculated relative to the highest grade in the FSN salary plan.

(4) A U.S. citizen with dual citizenship with another foreign country or countries shall not be considered a non-U.S. citizen.

(f) For a brand promotion activity, CCC will reimburse no more than 50 percent of the total eligible expenditures made on that activity.

(g) CCC will reimburse for expenditures made after the conclusion of a MAP Participant's program year provided:

(1) The activity was approved by CCC prior to the end of the program year;

(2) The activity was completed within 30 calendar days following the end of the program year; and

(3) All expenditures were made for the activity within 6 months following the end of the program year.

(h) A MAP Participant shall not use MAP funds for any activity, or any expenses incurred by the MAP Participant prior to the date specified in the approval letter or after the date the agreement is suspended or terminated, except as otherwise permitted by CCC.

(i) Except as otherwise provided in this subpart, MAP-funded travel shall conform to the U.S. Federal Travel Regulations (41 CFR parts 300 through 304) and 2 CFR part 200, and MAP-funded air travel shall conform to the requirements of the Fly America Act (49 U.S.C. 40118). The MAP Participant shall notify the Attaché/Counselor in the destination country(ies) in writing in advance of any proposed travel. The timing of such notice should be far enough in advance to enable the Attaché/Counselor to schedule appointments, make preparations, or otherwise provide any assistance being requested. Failure to provide advance notification of travel generally will result in disallowance of the expenses related to the travel, unless CCC determines it was impractical to provide such notification.

(j) CCC may determine, at CCC's discretion, whether any cost not expressly listed in this section will be reimbursed.

§ 1485.18 Reimbursement procedures.

(a) Following the implementation of a project for which CCC has agreed to provide funding, a Participant may submit claims for reimbursement of eligible expenses incurred in implementing MAP activities, to the extent that CCC has agreed to pay such expenses. Any changes to approved activities must be approved in writing by CCC before any reimbursable expenses associated with the change can be incurred. A Participant will be reimbursed after CCC reviews the claim and determines that it is complete.

(b) All claims for reimbursement shall be submitted by the MAP Participant's U.S. office to CCC. CCC will make all payments to Participants in U.S. dollars. FAS will initiate payment within 30 days after receipt of the billing, unless the billing is improper.

(c) Participants will be authorized to submit requests for reimbursement or advance at least monthly when electronic fund transfers (EFTs) are not used, and as frequently as desired when electronic transfers are used, in accordance with the provisions of the Electronic Fund Transfer Act (15 U.S.C. 1693–1693r).

(d) CCC will not reimburse claims submitted later than 6 months after the end of a MAP Participant's program year.

(e) If CCC overpays a reimbursement claim, the MAP Participant shall repay CCC within 30 calendar days of such overpayment the amount of the overpayment either by submitting a check payable to CCC or by offsetting its next reimbursement claim. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC.

(f) If a MAP Participant receives a reimbursement or offsets an advanced payment which is later disallowed, the MAP Participant shall repay CCC within 30 calendar days of such disallowance the amount disallowed either by submitting a check payable to CCC or by offsetting its next reimbursement claim. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC.

(g) MAP funds may be expended by MAP Participants only on legitimate, approved activities as set forth in the agreement and approval letter. If a MAP Participant discovers that MAP funds have not been properly spent, it shall notify CCC and shall within 30 calendar days of its discovery repay CCC the amount owed either by submitting a check payable to CCC or by offsetting its next reimbursement claim. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC.

(h) The MAP Participant shall report any actions that may have a bearing on the propriety of any claims for reimbursement in writing to the appropriate Attaché/Counselor and its U.S. office shall report such actions in writing to the appropriate FAS Division Director.

§ 1485.19 Advances.

(a) *Policy.* In general, CCC operates the MAP on a reimbursable basis.

(b) *Exception.* A MAP Participant may request an advance of MAP funds from CCC for generic promotion activities, provided the MAP Participant meets the criteria for advance payments in 2 CFR part 200. CCC will not approve any request for an advance submitted after the end of a MAP Participant's program year. At any given time, total payments advanced shall not exceed 40 percent of a MAP Participant's total approved generic activity budget for the program year. CCC will not advance funds to a MAP Participant for brand promotion activities. When approving a request for an advance, CCC may require the MAP Participant to carry adequate fidelity bond coverage when the absence of such coverage is considered to create an unacceptable risk to the interests of the MAP. Whether an ''unacceptable risk'' exists in a particular situation will depend on a number of factors, such as, for example, the Participant's history of performance in the MAP, the Participant's perceived financial stability and resources, and any other factors presented in the particular situation that may reflect on the Participant's responsibility or the riskiness of its activities.

(c) *Interest.* A MAP Participant shall deposit and maintain all funds advanced by CCC in an insured account in the United States. The account shall be interest-bearing, unless the exceptions in 2 CFR part 200 apply. Interest earned by the MAP Participant on funds advanced by CCC is not program income. Up to $500 of interest earned per year may be retained by the MAP Participant for administrative expenses. Any additional interest earned on MAP advances shall be remitted annually to the appropriate entity as required in 2 CFR part 200.

(d) *Refunds due CCC.* A MAP Participant shall fully expend all advances on approved generic promotion activities within 90 calendar days after the date of disbursement by CCC. By the end of the 90 calendar days, the MAP Participant must submit reimbursement claims to offset the advance and submit a check made payable to CCC for any unexpended balance. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC.

§ 1485.20 Employment practices.

(a) A MAP Participant shall enter into written contracts with all overseas employees who are paid in whole or in part with MAP funds and shall ensure that all terms, conditions, and related formalities of such contracts conform to governing local law.

(b) A MAP Participant shall, in its overseas offices, conform its office hours, work week, and holidays to local law and to the custom generally observed by U.S. commercial entities in the local business community.

(c) A MAP Participant may pay salaries or fees in any currency (U.S. or foreign) in conformance with contract specifications. Participants should consult local laws regarding currency restrictions.

§ 1485.21 Financial management.

(a) A MAP Participant shall implement and maintain a financial management system that conforms to generally accepted accounting principles and complies with the standards in 2 CFR part 200.

(b) A MAP Participant shall institute internal controls and provide written guidance to commercial entities participating in its activities to ensure their compliance with these regulations.

(c) A MAP Participant shall retain all records concerning a MAP program transaction for a period of five years after completion of the transaction and permit authorized officials of the U.S. Government to have full and complete access, for such five-year period, to such records. These records shall include all documents related to employment of any employees whose salaries are reimbursed in whole or in part with MAP funds, whether such employees are based in the United States or overseas, such as employment applications, contracts, position descriptions, leave records, salary changes, and all records pertaining to contractors.

(d) A MAP Participant shall also maintain adequate documentation related to the proper disposition of all personal property having a useful life of more than one year and an acquisition cost of $500 or more purchased by the Participant and for which the Participant is reimbursed, in whole or in part, with MAP funds.

(e) A MAP Participant shall maintain its records of expenditures, contributions, and cost share in a manner that allows it to provide information by program year, activity plan, country or region (as applicable), activity number, and cost category. Such records shall include copies of:

(1) Receipts for all STRE (actual vendor invoices or restaurant checks, rather than credit card receipts);

(2) Receipts for any other program-related expenditure in excess of a minimum level that CCC shall determine and announce in writing to all MAP Participants via a program notice issued on the FAS website. Receipts for all actual M&IE reimbursements must be maintained, regardless of the amount;

(3) The exchange rate used to calculate the dollar equivalent of expenditures made in a foreign currency and the basis for such calculation;

(4) Reimbursement claims;

(5) An itemized list of claims charged to each of the MAP Participant's MAP accounts;

(6) Documentation, with accompanying English translation, supporting each reimbursement claim, including evidence to support the financial transactions, such as canceled checks, receipted paid bills, contracts, purchase orders, per diem calculations, travel vouchers, and credit memos; and

(7)(i) Each MAP Participant must keep records documenting all claimed contributions and cost share, to include:

(A) Copies of invoices or receipts for expenses paid by the U.S. industry or State agency and not reimbursed by the MAP Participant for the joint activity, or

(B) If invoices are not available, an itemized statement from the U.S. industry or State agency as to what costs it incurred pursuant to the joint activity, or

(C) If neither of the foregoing is available, a statement from the U.S. industry or State agency as to what goods and services it provided, or

(D) If none of the foregoing are available, a memo to the files of the MAP Participant's estimate of what contribution or cost share was made by the U.S. industry or State agency, item by item, and the method used to assign a value to each.

(ii) The documentation required in paragraph (e)(7)(i) of this section must include the dates, purpose, and location of the activity for which the cash or in-kind items were claimed as a contribution or cost share, who conducted the activity, the participating groups or individuals, and the method of computing the claimed contribution or cost share. MAP Participants must retain and make available for compliance reviews and audits documentation related to claimed contribution or cost share.

(f) Upon request, a MAP Participant shall provide documents supporting reimbursement claims to CCC. CCC may deny a claim for reimbursement if the claim is not supported by adequate documentation.

§ 1485.22 Reports.

(a) Participants are required to submit regular financial and performance reports in accordance with their agreement. Reporting requirements and formats for the required financial and performance reports will be specified in the agreement between CCC and the Participant.

(b)(1) In addition to the information required in 2 CFR 200.328(b)(2), a Participant's performance reports must include pertinent information regarding the Participant's progress, measured against established indicators, baselines, and targets, towards achieving the expected results specified in the agreement. This reporting must include, for each performance indicator, a comparison of actual accomplishments with the baseline and the targets established for the period. When actual accomplishments deviate significantly from targeted goals, the Participant must provide an explanation in the report.

(2) A Participant must ensure the accuracy and reliability of the performance data submitted to FAS in performance reports. At any time during the period of performance of the agreement, FAS may review the Participant's performance data to determine whether it is accurate and reliable. The Participant must comply with all requests made by FAS or an entity designated by FAS in relation to such reviews.

(c) All final performance reports will be made available to the public.

(d) Not later than 45 calendar days after the completion of travel (other than local travel), a MAP Participant shall submit a trip report. The report must be submitted to the appropriate Attaché/Counselor(s) and must include the name(s) of the traveler(s), purpose of travel, itinerary, names and affiliations of contacts, and a brief summary of findings, conclusions, recommendations, and specific accomplishments.

(e) Not later than 90 calendar days after the end of its program year, a MAP Participant shall submit a report on any research conducted pursuant to the approved MAP program.

(f) If requested by FAS, a Participant must provide to FAS additional information or reports relating to the agreement.

(g) If a Participant requires an extension of a reporting deadline, it must ensure that FAS receives an extension request at least five business days prior to the reporting deadline. FAS may decline to consider a request

for an extension that it receives after this time period. FAS will consider requests for reporting deadline extensions on a case by case basis and will make a decision based on the merits of each request. FAS will consider factors such as unforeseen or extenuating circumstances and past performance history when evaluating requests for extensions.

§ 1485.23 Evaluation.

(a)(1) The Government Performance and Results Act (GPRA) of 1993 (5 U.S.C. 306; 31 U.S.C. 1105, 1115–1119, 3515, 9703–9704) requires performance measurement of Federal programs, including the MAP. Evaluation of the MAP's effectiveness will depend on a clear statement by Participants of the constraints and opportunities facing U.S. exports, goals to be met within a specified time, schedule of measurable milestones for gauging success, plan for achievement, and assessment of results of activities at regular intervals. The overall goal of the MAP and of individual Participants' programming is to achieve or maintain sales that would not have occurred in the absence of MAP funding. A MAP Participant that can demonstrate such sales, taking into account extenuating factors beyond the Participant's control, will have met the overall objective of the GPRA and the need for evaluation.

(2) Evaluation is an integral element of program planning and implementation, providing the basis for the strategic plan. The evaluation results guide the development and scope of a MAP Participant's program, contribute to program accountability, and provide evidence of program effectiveness.

(b) A MAP Participant shall complete at least one program evaluation each year. A program evaluation is a review of the MAP Participant's entire program, or an appropriate portion of the program as agreed to by the MAP Participant and CCC, to determine the effectiveness of the MAP Participant's strategy in meeting specified goals. The actual scope and timing of the program evaluation shall be determined by the MAP Participant and CCC and specified in the approval letter. A MAP Participant may contract with an independent evaluator to satisfy this requirement, although CCC reserves the right to have direct input and control over the design, scope, and methodology of any such evaluation, including direct contact with and provision of guidance to the independent evaluator. A MAP Participant shall submit, via a cover letter to CCC, an executive summary that assesses the program evaluation's findings and recommendations and proposed changes in program strategy or design as a result of the evaluation. In addition to the requirements set forth in 2 CFR part 200, a program evaluation shall contain:

(1) The name of the party conducting the evaluation;

(2) The scope of the evaluation;

(3) A concise statement of the market constraint(s)/opportunity(ies) and the goals specified in the approved strategic plan;

(4) A description of the evaluation methodology;

(5) A description of additional export sales achieved, including the ratio of additional export sales in relation to the MAP Participant's program funding received;

(6) A summary of the findings, including an analysis of the strengths and weaknesses of the program(s); and

(7) Recommendations for future programs.

(c) MAP Participants conducting a branded program must also complete a brand promotion evaluation. A brand promotion evaluation is a review of the U.S. and foreign commercial entities' export sales to determine whether the activity achieved the goals specified in the approved MAP program. This evaluation shall be completed and submitted to CCC no later than 6 months following the end of the Participant's program year.

(d) On an annual basis, or more often when appropriate or required by CCC, a MAP Participant shall complete and submit program success stories. CCC will announce to all MAP Participants the detailed requirements for completing and submitting program success stories.

§ 1485.24 Compliance reviews and notices.

(a) USDA staff may conduct compliance reviews of the Participant's activities under this program to ensure compliance with this subpart, applicable Federal laws and regulations, and the terms of the agreements and approval letters. Participants shall cooperate fully with relevant USDA staff conducting compliance reviews and shall comply with all requests from USDA staff to facilitate the conduct of such reviews. Program funds spent inappropriately or on unapproved activities must be returned to CCC.

(b) Any project or activity funded under the program is subject to review or audit at any time during the course of implementation or after the completion of the project.

(c) Upon conclusion of the compliance review, USDA staff will provide a written compliance report to the Participant. The compliance report will detail any instances where it appears that the Participant is not complying with any of the terms or conditions of the agreement, approval letter, or the applicable laws and regulations. The report will also specify if it appears that CCC may be entitled to recover funds from the Participant and will explain the basis for any recovery of funds from the Participant. If, as a result of a compliance review, CCC determines that further review is needed in order to ensure compliance with the requirements of the program, CCC may require the Participant to contract for an independent audit.

(d) In addition, CCC may notify a Participant in writing at any time if CCC determines that CCC may be entitled to recover funds from the Participant. CCC will explain the basis for any recovery of funds from the Participant in the written notice. The Participant shall, within 30 calendar days of the date of the notice, repay CCC the amount owed either by submitting a check payable to CCC or by offsetting its next reimbursement claim. The Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC. If, however, a Participant notifies CCC within 30 calendar days of the date of the written notice that the Participant intends to file an appeal pursuant to the provisions of this subpart, the amount owed to CCC by the Participant is not due until the appeal procedures are concluded and CCC has made a final determination as to the amount owed.

(e) The fact that a compliance review has been conducted by USDA staff does not signify that a Participant is in full compliance with its agreement, approval letter, and/or applicable laws and regulations.

(f) For a Participant response to compliance report:

(1) A Participant shall, within 60 calendar days of the date of the issuance of a compliance report, submit a written response to CCC. The response may include additional documentation for consideration or a request for reconsideration of any finding along with supporting justification. If the Participant does not wish to contest the compliance report, the response shall include any money owed to CCC, which may be returned by submitting a check payable to CCC or by offsetting a reimbursement claim. The Participant shall make any payments in U.S. dollars, unless otherwise approved in advance by CCC. CCC, at its discretion, may extend the period for response.

(2) After reviewing the response, CCC shall determine whether the Participant owes any funds to CCC and will inform the Participant in writing of the basis for the determination. CCC may initiate action to collect such amount by providing the Participant a written demand for payment of the debt pursuant to debt settlement policies and procedures, 7 CFR part 1403.

(g) For Participant appeals of CCC determinations:

(1) Within 30 calendar days of the date of the issuance of a determination, the Participant may appeal the determination by making a request in writing that includes the basis for such reconsideration. The Participant may also request a hearing.

(2) If the Participant requests a hearing, CCC will set a date and time for the hearing. The hearing will be an informal proceeding. A transcript will not ordinarily be prepared unless the Participant bears the cost of a transcript; however, CCC may, at its discretion, have a transcript prepared at CCC's expense.

(3) CCC will base its final determination upon information contained in the administrative record. The Participant must exhaust all administrative remedies contained in this section before pursuing judicial review of a determination by CCC.

§ 1485.25 Failure to make required contribution or cost share.

A MAP Participant's required contribution or cost share will be specified in the approval letter. If the MAP Participant's required contribution or cost share is specified as a dollar amount and the MAP Participant does not make the required contribution or cost share, the MAP Participant shall pay to CCC in dollars the difference between the amount actually contributed and the amount specified in the approval letter. If the MAP Participant's required contribution or cost share is specified as a percentage of the total amount reimbursed by CCC, the MAP Participant may either return to CCC the necessary amount of funds reimbursed by CCC to increase its actual contribution or cost share percentage to the required level or pay to CCC in dollars the difference between the amount actually contributed and the amount of funds necessary to increase its actual contribution or cost share percentage to the required level. A MAP Participant shall remit such payment within six months after the end of its program year. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC.

§ 1485.26 Submissions.

For all permissible methods of delivery, submissions required by this subpart shall be deemed submitted as of the date received by CCC.

§ 1485.27 Disclosure of program information.

(a) Documents submitted to CCC by MAP Participants are subject to the provisions of the Freedom of Information Act (FOIA), 5 U.S.C. 552, 7 CFR part 1, subpart A, and specifically 7 CFR 1.12.

(b) Upon request, a Participant shall provide to any person a copy of any document in its possession or control containing market information developed and produced under the terms of its agreement. The Participant may charge a fee not to exceed the costs for assembling, duplicating, and distributing the materials.

(c) Any research conducted by a MAP Participant pursuant to an agreement and/or approval letter shall be subject to the provisions relating to intangible property in 2 CFR part 200.

§ 1485.28 Ethical conduct.

(a) A MAP Participant shall conduct its business in accordance with the laws and regulations of the country(s) in which an activity is carried out and in accordance with applicable U.S. Federal, state, and local laws and regulations. A MAP Participant shall conduct its business in the United States in accordance with applicable Federal, state, and local laws and regulations.

(b) Except for a U.S. agricultural cooperative or a U.S. for-profit entity, neither a MAP Participant nor its affiliates shall make export sales of eligible commodities covered under the terms of the applicable MAP agreement. Nor shall such entities charge a fee for facilitating an export sale. A MAP Participant may, however, collect check-off funds and membership fees that are required for membership in the MAP Participant's organization.

(c) A MAP Participant shall not limit participation in its MAP activities to members of its organization. Participants shall ensure that their MAP-funded programs and activities are open to all otherwise qualified individuals and entities on an equal basis and without regard to any non-merit factors. The MAP Participant shall publicize its program and make participation possible for commercial entities throughout the relevant commodity sector or, in the case of SRTGs, throughout the corresponding region. This includes providing to such commercial entities, upon request, a copy of any document in its possession or control containing market information developed and produced under the terms of its MAP agreement. The Participant may charge a fee not to exceed the costs for assembling, duplicating, and distributing the materials. This paragraph does not apply to U.S. agricultural cooperatives when implementing their own brand program.

(d) A MAP Participant shall select U.S. agricultural industry representatives to participate in generic MAP activities such as trade teams, sales teams, and trade fairs based on criteria that ensure participation on an equitable basis by a broad cross section of the U.S. industry. If requested by CCC, a MAP Participant shall submit such selection criteria to CCC for approval.

(e) All MAP Participants should endeavor to ensure fair and accurate fact-based advertising. Deceptive or misleading promotions may result in cancellation or termination of a MAP Participant's agreement and the recovery of CCC funds related to such promotions from the Participant.

(f) The MAP Participant must report any actions or circumstances that may have a bearing on the propriety of its MAP program to the appropriate Attaché/Counselor, and its U.S. office shall report such actions or circumstances in writing to CCC.

§ 1485.29 Subawarding procedures.

(a) MAP Participants have full and sole responsibility for the legal sufficiency of all contracts and assume financial liability for any costs or claims resulting from suits, challenges, or other disputes based on contracts entered into by the MAP Participant. Neither CCC nor any other agency of the U.S. Government nor any official or employee of CCC, FAS, USDA, or the U.S. Government has any obligation or responsibility with respect to MAP Participant contracts with third parties.

(b) A MAP Participant shall comply with the procurement standards set forth below and in 2 CFR part 200 when procuring goods and services and when engaging in construction to implement agreements.

(c) Each MAP Participant shall establish open, fair, and competitive contracting procedures for contracts that are funded, in whole or in part, with MAP funds.

(d) Each MAP Participant shall submit to CCC, for CCC approval, written contracting guidelines for contracts that are funded, in whole or in part, with MAP funds. CCC will notify all new and existing MAP Participants in writing in

each Participant's approval letter and through the FAS website as to applicable submission dates for and dates for approvals of contracting guidelines. CCC's approval of such contracting guidelines will remain in place until CCC retracts its approval in writing, or until new guidelines are approved that supersede them. Once approved by CCC, these contracting guidelines shall govern all of a Participant's MAP-funded contracting involving contracts with an annual minimum value that CCC shall determine and announce in writing to all MAP Participants via a program notice issued on the FAS website. The guidelines shall indicate the method for evaluating proposals received for all contract competitions, the method for monitoring and evaluating performance under contracts, and the method for initiating corrective action for unsatisfactory performance under contracts. The MAP Participant may modify and resubmit these guidelines for re-approval at any time. In addition to the requirements in 2 CFR part 200, these guidelines shall include, at a minimum, the following:

(1) Procedures for developing and publicizing requests for proposals, invitations for bids, and similar documents that solicit third party offers to provide goods or services. Solicitations for professional and technical services shall be based on clear and accurate descriptions of and requirements related to the services to be procured. Such procedures must include a conflict of interest provision that states that no employee, officer, board member, or agent thereof of the MAP Participant will participate in the review, selection, award, or administration of a contract if a real or apparent conflict of interest would arise. Such a conflict would arise when an employee, official, board member, agent, or the employee's, officer's, board member's, or agent's family, partners, or an organization that employs or is about to employ any of these parties or their affiliates has a financial or other interest in the contract. Procedures shall provide that officers, employees, board members, and agents thereof shall neither solicit nor accept gratuities, favors, or anything of monetary value from contractors or subcontractors. Procedures shall also provide for disciplinary actions to be applied for violations of such standards by officers, employees, board members, or agents thereof;

(2) Procedures for reviewing proposals, bids, or other offers to provide goods and services. Separate procedures shall be developed for various situations, including, but not limited to: solicitations for highly technical services; solicitations for services that are not common in a specific market; sole source contracts; solicitations that yield receipt of three or more bids; or solicitations that yield receipt of fewer than three bids;

(3) Requirements to conduct all contracting in an openly competitive manner. Individuals who develop or draft specifications, requirements, statements of work, invitations for bids, and/or requests for proposals for procurement of any goods or services, and such individuals' families or partners, or an organization that employs or is about to employ any of the aforementioned, shall be excluded from competition for such procurement. MAP Participants' written contracting guidelines may detail special situations where the prohibitions in this subparagraph do not apply, such as in situations involving highly specialized technical services or situations where the services are not commonly offered in a specific market;

(4) Requirements to perform and document in the procurement files some form of price or cost analysis, such as a comparison of price quotations to market prices or other price indicia, to determine the reasonableness of the offered prices in connection with every procurement action that is governed by the contracting guidelines;

(5) Requirements to conduct an appropriate form of competition every 3 years on all multi-year contracts that are governed by the contracting guidelines. However, contracts for in-country representation are not required to be re-competed after the initial reward. Instead, the performance of in-country representation must be evaluated and documented by the MAP Participant annually to ensure that the terms of the contract are being met in a satisfactory manner; and

(6) Requirements for written contracts with each provider of goods, services, or construction work. Such contracts shall require such providers to maintain adequate records to account for funds provided to them by the MAP Participant.

(e) A MAP Participant may undertake MAP promotional activities directly or through a domestic or foreign subrecipient. However, the MAP Participant shall remain responsible and accountable to CCC for all MAP promotional activities and related expenditures undertaken by such subrecipient and shall be responsible for reimbursing CCC for any funds that CCC determines should be refunded to CCC in relation to such subrecipient's promotional activities and expenditures.

§ 1485.30 Property standards.

(a) A Participant shall maintain an inventory of all personal property having a useful life of more than one year and an acquisition cost of $500 or more that was acquired in furtherance of program activities. The inventory shall list and number each item and include the date of purchase or acquisition, cost of purchase, replacement value, serial number, make, model, and electrical requirements, as applicable.

(b) The Participant shall insure all real property and equipment that was acquired, in whole or in part, with MAP funds at a level minimally equal to the equivalent insurance coverage for property owned by the Participant. The Participant shall safeguard such property and equipment against theft, damage, and unauthorized use. The Participant shall promptly report any loss, theft, or damage of such property and equipment to the insurance company.

(c) Personal property having a useful life of more than one year and an acquisition cost of $500 or more purchased by the Participant, and for which the Participant is reimbursed, in whole or in part, with MAP funds, that is unusable, unserviceable, or no longer needed for project purposes shall be disposed of in one of the following ways. The Participant may:

(1) Exchange or sell the property, provided that it applies any exchange allowance, insurance proceeds, or sales proceeds toward the purchase of other property needed in the project;

(2) With CCC approval, transfer the property to other Participants for their activities, or to a foreign entity; or

(3) Upon Attaché/Counselor approval, donate the property to a local charity, or convey the property to the Attaché/Counselor, along with an itemized inventory list and any documents of title.

(d) The Participant is responsible for reimbursing CCC for the value of any uninsured property at the time of the loss or theft of the property.

§ 1485.31 Anti-fraud requirements.

(a) *All MAP Participants.* (1) All MAP Participants annually shall submit to CCC for approval a detailed fraud prevention program. CCC will notify all new and existing MAP Participants in writing in each Participant's approval letter and through the FAS website as to applicable submission dates for and dates for approvals of fraud prevention programs. MAP Participants should review their fraud prevention programs

annually. The fraud prevention program shall, at a minimum, include an annual review of physical controls and weaknesses, a standard process for investigating and remediation of suspected fraud cases, and training in risk management and fraud detection for all current and future employees. The MAP Participant shall not conduct or permit any MAP promotion activities to occur unless and until CCC has communicated in writing approval of the MAP Participant's fraud prevention program.

(2) The MAP Participant, within five business days of receiving an allegation or information giving rise to a reasonable suspicion of misrepresentation or fraud that could give rise to a claim by CCC, shall report such allegation or information in writing to such USDA personnel as specified in the Participant's agreement and/or approval letter. The MAP Participant shall cooperate fully in any USDA investigation of such allegation or occurrence of misrepresentation or fraud and shall comply with any directives given by CCC or USDA to the MAP Participant for the prompt investigation of such allegation or occurrence.

(b) *MAP Participants with brand programs.* (1) The MAP Participant may charge a fee to brand participants to cover the cost of the fraud prevention program.

(2) The MAP Participant shall repay to CCC funds paid to a brand participant through the MAP Participant on claims that the MAP Participant or CCC subsequently determines are unauthorized or otherwise non-reimbursable expenses within 30 calendar days of the MAP Participant's determination or CCC's disallowance. The MAP Participant shall repay CCC by submitting a check to CCC or by offsetting the MAP Participant's next reimbursement claim. The MAP Participant shall make such payment in U.S. dollars, unless otherwise approved in advance by CCC. A MAP Participant operating a brand program in strict accordance with an approved fraud prevention program, however, will not be liable to reimburse CCC for MAP funds paid on such claims if the claims were based on misrepresentations or fraud of the brand participant, its employees, or agents, unless CCC determines that the MAP Participant was grossly negligent in the operation of the brand program regarding such claims. CCC shall communicate any such determination to the MAP Participant in writing.

§ 1485.32 Program income.

Program income is gross income earned by the non-Federal entity that is directly generated by a supported activity or earned as a result of the Federal award during the period of performance. Any income generated from an activity, the expenditures for which have been wholly or partially reimbursed with MAP funds, shall be used by the MAP Participant in furtherance of its approved MAP activities in the program year during which the MAP funds are available for obligation by the MAP Participant, or must be returned to CCC. The use of such income shall be governed by this subpart. Interest earned on funds advanced by CCC is not program income. Reasonable activity fees or registration fees, if identified as such in a project budget, may be charged for approved activities. The intent to charge a fee must be part of the original proposal, along with an explanation of how such fees are to be used. Any activity fees charged must be used to offset activity expenses or returned to FAS. Such fees may not be used as profit or counted as contribution or cost share.

§ 1485.33 Amendments.

An agreement may be amended in writing with the consent of CCC and the MAP Participant. All requests for program amendments must be submitted to CCC in writing and contain a justification for why the amendment is necessary. All amendment requests must be reviewed and approved by CCC before an amendment can be issued.

§ 1485.34 Subrecipients.

(a) A Participant may utilize the services of a subrecipient to implement activities under the agreement if this is provided for in the agreement. The subrecipient may receive CCC-provided funds, program income, or other resources from the Participant for this purpose. The Participant must enter in to a written subaward with the subrecipient and comply with the applicable provisions of 2 CFR 200.331 and/or the Federal Acquisition Regulation (FAR), if applicable. If required by the agreement, the Participant must provide a copy of such subaward to FAS, in the manner set forth in the agreement, prior to the transfer of CCC-provided funds or program income to the subrecipient.

(b) A Participant must include the following requirements in a subaward:

(1) The subrecipient is required to comply with the applicable provisions of this part and 2 CFR parts 200 and 400 and/or the FAR, if applicable. The applicable provisions are those that relate specifically to subrecipients, as well as those relating to non-Federal entities that impose requirements that would be reasonable to pass through to a subrecipient because they directly concern the implementation by the subrecipient of one or more activities under the agreement. If there is a question about whether a particular provision is applicable, FAS will make the determination.

(2) The subrecipient must pay to the Participant the value of CCC-provided funds, interest, or program income that are not used in accordance with the subaward, or that are lost, damaged, or misused as a result of the subrecipient's failure to exercise reasonable care.

(3) In accordance with 2 CFR 200.501(h), subawards must include a description of the applicable compliance requirements and the subrecipient's compliance responsibility. Methods to ensure compliance may include pre-award audits, monitoring during the agreement, and post-award audits.

(c) A Participant must monitor the actions of a subrecipient as necessary to ensure that CCC-provided funds and program income provided to the subrecipient are used for authorized purposes in compliance with applicable U.S. Federal laws and regulations and the subaward and that performance indicator targets are achieved for both activities and results under the agreement.

§ 1485.35 Audit requirements.

(a) Subpart F of 2 CFR part 200 applies to all Participants and subrecipients under this part other than those that are for-profit entities, foreign public entities, or foreign organizations.

(b) A Participant or subrecipient that is a for-profit entity or a subrecipient that is a foreign organization and that expends, during its fiscal year, a total of at least the audit requirement threshold in 2 CFR 200.501 in Federal awards, is required to obtain an audit. Such a Participant or subrecipient has the following two options to satisfy this requirement:

(1)(i) A financial audit of the agreement or subaward, in accordance with the Government Auditing Standards issued by the United States Government Accountability Office (GAO), if the Participant or subrecipient expends Federal awards under only one FAS program during such fiscal year; or

(ii) A financial audit of all Federal awards from FAS, in accordance with GAO's Government Auditing Standards, if the Participant or subrecipient expends Federal awards under multiple

FAS programs during such fiscal year; or

(2) An audit that meets the requirements contained in subpart F of 2 CFR part 200.

(c) A Participant or subrecipient that is a for-profit entity or a subrecipient that is a foreign organization and that expends, during its fiscal year, a total that is less than the audit requirement threshold in 2 CFR 200.501 in Federal awards, is exempt from requirements under this section for an audit for that year, except as provided in paragraphs (d) and (f) of this section, but it must make records available for review by appropriate officials of Federal agencies.

(d) FAS may require an annual financial audit of an agreement or subaward when the audit requirement threshold in 2 CFR 200.501 is not met. In that case, FAS must provide funds under the agreement for this purpose, and the Participant or subrecipient, as applicable, must arrange for such audit and submit it to FAS.

(e) When a Participant or subrecipient that is a for-profit entity or a subrecipiet that is a foreign organization is required to obtain a financial audit under this section, it must provide a copy of the audit to FAS within 60 days after the end of its fiscal year.

(f) FAS, the USDA Office of Inspector General, or GAO may conduct or arrange for additional audits of any Participants or subrecipients, including for-profit entities and foreign organizations. Participants and subrecipients must promptly comply with all requests related to such audits. If FAS conducts or arranges for an additional audit, such as an audit with respect to a particular agreement, FAS will fund the full cost of such an audit, in accordance with 2 CFR 200.503(d).

§ 1485.36 Suspension and termination of agreements.

(a) An agreement or subaward may be suspended or terminated in accordance with 2 CFR 200.338 or 200.339. FAS may suspend or terminate an agreement if it determines that:

(1) One of the bases in 2 CFR 200.338 or 200.339 for termination or suspension by FAS has been satisfied; or

(2) The continuation of the assistance provided under the agreement is no longer necessary or desirable.

(b) If an agreement is terminated, the Participant:

(1) Is responsible for using or returning any CCC-provided funds, interest, or program income that have not been disbursed, as agreed to by FAS; and

(2) Must comply with any closeout and post-closeout procedures specified in the agreement and 2 CFR 200.343 and 200.344.

§ 1485.37 Noncompliance with an agreement.

(a) If a MAP Participant fails to comply with any term in its agreement or approval letter, CCC may take one or more of the enforcement actions in 2 CFR part 200 and, if appropriate, initiate a claim against the MAP Participant, following the procedures set forth in this subpart. CCC may also initiate a claim against a MAP Participant if program income or CCC-provided funds are lost due to an action or omission of the MAP Participant. If any MAP Participant has engaged in fraud with respect to the MAP, or has otherwise violated program requirements under this subpart, CCC may:

(1) Hold such MAP Participant liable for any and all losses to CCC resulting from such fraud or violation;

(2) Require a refund of any assistance provided to such MAP Participant plus interest as determined by FAS; and

(3) Collect liquidated damages from such MAP Participant in an amount determined appropriate by FAS.

(b) The provisions of this section shall be without prejudice to any other remedy that is available under any other provision of law.

§ 1485.38 Paperwork reduction requirements.

The paperwork and recordkeeping requirements imposed by this subpart have been approved by OMB under the Paperwork Reduction Act of 1980. OMB has assigned control number 0551–0026 for this information collection.

Dated: December 6, 2019.

Robert Stephenson,

Executive Vice President, Commodity Credit Corporation.

In concurrence with:

Dated: December 6, 2019.

Ken Isley,

Administrator, Foreign Agricultural Service.

[FR Doc. 2019–27965 Filed 1–10–20; 8:45 am]

BILLING CODE 3410–10–P

DEPARTMENT OF TRANSPORTATION

Office of the Secretary

14 CFR Parts 11, 300, and 302

49 CFR Parts 1, 5, 7, 106, 211, 389, 553, and 601

RIN 2105–AE84

Administrative Rulemaking, Guidance, and Enforcement Procedures

Correction

In rule document 2019–26672, appearing on pages 71714 through 71734, in the issue of Friday, December 27, 2019 make the following correction:

§ 5.25 General.

On page 71726, in the second column, in the footnotes, footnote 8 should read, ''[8] See Appendix A to ''Memorandum on the Review and Clearance of Guidance Documents,'' available at *https://cms.dot.gov/sites/dot.gov/files/docs/regulations/328566/gen-counsel-mem-guidance-documentssigned-122018.pdf.*''

[FR Doc. C1–2019–26672 Filed 1–10–20; 8:45 am]

BILLING CODE 1301–01–D

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 143

RIN 3038–AE82

Annual Adjustment of Civil Monetary Penalties To Reflect Inflation—2020

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission (Commission) is amending its rule governing the maximum amount of civil monetary penalties to adjust for inflation. This rule sets forth the maximum, inflation-adjusted dollar amount for civil monetary penalties (CMPs) assessable for violations of the Commodity Exchange Act (CEA) and Commission rules, regulations, and orders thereunder. The rule, as amended, implements the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended.

DATES: This rule is effective on January 13, 2020 and is applicable to penalties assessed after January 15, 2020.

FOR FURTHER INFORMATION CONTACT: Edward J. Riccobene, Associate Chief Counsel, Division of Enforcement, at (202) 418–5327 or *ericcobene@cftc.gov,*

Commodity Futures Trading Commission, 1155 21st Street NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

The Federal Civil Penalties Inflation Adjustment Act of 1990 (FCPIAA) [1] requires the head of each Federal agency to periodically adjust for inflation the minimum and maximum amount of CMPs provided by law within the jurisdiction of that agency.[2] A 2015 amendment to the FCPIAA [3] required agencies to make an initial ''catch-up'' adjustment to its civil monetary penalties effective no later than August 1, 2016.[4] For every year thereafter effective not later than January 15, the FCPIAA, as amended, requires agencies to make annual adjustments for inflation, with guidance from the Director of the Office of Management and Budget.[5]

II. Commodity Exchange Act Civil Monetary Penalties

The following sections of the CEA provide for CMPs that meet the FCPIAA definition [6] and these CMPs are, therefore, subject to the inflation adjustment: Sections 6(c), 6b, and 6c of the CEA.[7]

III. Annual Inflation Adjustment for Commodity Exchange Act Civil Monetary Penalties

A. Methodology

The FCPIAA annual inflation adjustment, in the context of the CFTC's CMPs, is determined by increasing the maximum penalty by a ''cost-of-living adjustment'', rounded to the nearest multiple of one dollar.[8] Annual inflation adjustments are based on the percent change between the October Consumer Price Index for all Urban Consumers (CPI–U) preceding the date of the adjustment, and the prior year's October CPI–U.[9] In this case, the October 2019 CPI–U (257.346)/October 2018 CPI–U (252.885) = 1.01764.[10] In order to complete the 2020 annual adjustment, the CFTC must multiply each of its most recent CMP amounts by the multiplier, 1.01764, and round to the nearest dollar.[11]

B. Civil Monetary Penalty Adjustments

Applying the FCPIAA annual inflation adjustment methodology results in the following amended CMPs:

U.S. Code citation	Civil monetary penalty description		Violations occurring on or after 11/02/2015		
			Penalty amount in 2019 final rule [12]	CPI–U multiplier	New adjusted penalty amount
Civil Monetary Penalty Imposed By The Commission In An Administrative Action					
7 U.S.C. 9 (Section 6(c) of the Commodity Exchange Act).	For any person other than a registered entity [1].	Non-Manipulation or Attempted Manipulation.	$165,227	1.01764	$168,142
	For any person other than a registered entity [1].	Manipulation or Attempted Manipulation.	1,191,842	1.01764	1,212,866
7 U.S.C. 13a (Section 6b of the Commodity Exchange Act).	For a registered entity [1] or any of its directors, officers or employees.	Non-Manipulation or Attempted Manipulation.	910,158	1.01764	926,213
	For a registered entity [1] or any of its directors, officers or employees.	Manipulation or Attempted Manipulation.	1,191,842	1.01764	1,212,866
Civil Monetary Penalty Imposed By A Federal District Court In A Civil Injunctive Action					
7 U.S.C. 13a–1 (Section 6c of the Commodity Exchange Act).	Any Person	Non-Manipulation or Attempted Manipulation.	182,031	1.01764	185,242
	Any Person	Manipulation or Attempted Manipulation.	1,191,842	1.01764	1,212,866

[1] The term ''Registered Entity'' is defined in 7 U.S.C. 1a (Section 1a of the Commodity Exchange Act).

[1] The FCPIAA, Pub. L. 101–410 (1990), as amended, is codified at 28 U.S.C. 2461 note. The FCPIAA states that the purpose of the FCPIAA is to establish a mechanism that (1) allows for regular adjustment for inflation of civil monetary penalties; (2) maintains the deterrent effect of civil monetary penalties and promote compliance with the law; and (3) improves the collection by the Federal Government of civil monetary penalties.

[2] For the relevant CMPs within the Commission's jurisdiction, the Act provides only for maximum amounts that can be assessed for each violation of the Act or the rules, regulations and orders promulgated thereunder; the Act does not set forth any minimum penalties. Therefore, the remainder of this release will refer only to CMP maximums.

[3] Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015, Public Law 114–74, 129 Stat. 584 (2015) (2015 Act), title VII, Section 701.

[4] FCPIAA Sections 4 and 5. See also, Adjustment of Civil Monetary Penalties for Inflation, 81 FR 41435 (June 27, 2016).

[5] FCPIAA Sections 4 and 5. See also, Executive Office of the President, Office of Management and Budget Memorandum, M–20–05, Implementation of Penalty Inflation Adjustments for 2020, Pursuant to the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (Dec. 16, 2019) (2019 OMB Guidance) (*https://www.whitehouse.gov/wp-content/uploads/2019/12/M-20-05.pdf*).

[6] FCPIAA Section 3(2).

[7] 7 U.S.C. 9, 13a-1, 13b. Criminal authorities may also seek fines for criminal violations of the CEA (see 7 U.S.C. 13, 13(c), 13(d), 13(e), and 13b). The FCPIA does not affect the amounts of these criminal penalties.

[8] FCPIAA Sections 4 and 5.

[9] FCPIAA Section 5(b)(1).

[10] The CPI–U is published by the Department of Labor. Interested parties may find the relevant Consumer Price Index on the internet. To access this information, go to the Consumer Price Index Home Page at: *http://www.bls.gov/cpi/*. Click the ''CPI Data/Databases'' heading, and select ''All Urban Consumers (Current Series)'', ''Top Picks.'' Then check the box for ''U.S. city average, All items—CUUR0000SA0'', and click the ''Retrieve data'' button.

[11] 2019 OMB Guidance at 3.

[12] 84 FR 3103.

The FCPIAA provides that any increase under the FCPIAA in a civil monetary penalty shall apply only to civil monetary penalties, including those whose associated violation predated such increase, which are assessed after the date the increase takes effect.[13] Thus, the new CMP amounts established by this rulemaking shall apply to penalties assessed after January 15, 2020, for violations that occurred on or after November 2, 2015, the effective date of the FCPIAA amendment requiring annual adjustments, the 2015 Act.

IV. Administrative Compliance

A. Notice Requirement

The FCPIAA specifically exempted from the Administrative Procedure Act (APA) the rulemakings required to implement annual inflation adjustments.[14] ''This means that the public procedure the APA generally requires-notice, an opportunity for comment, and a delay in effective date-is not required for agencies to issue regulations implementing the annual adjustment.'' [15] The Commission further notes that the notice and comment procedures of the APA do not apply to this rulemaking because the Commission is acting herein pursuant to statutory language that mandates that the Commission act in a nondiscretionary matter.[16]

B. Regulatory Flexibility Act

The Regulatory Flexibility Act [17] requires agencies with rulemaking authority to consider the impact of certain of their rules on small businesses. A regulatory flexibility analysis is only required for rules for which the agency publishes a general notice of proposed rulemaking pursuant to section 553(b) or any other law.[18] Because, as discussed above, the Commission is not obligated by section 553(b) or any other law to publish a general notice of proposed rulemaking with respect to the revisions being made to Rule § 143.8, the Commission additionally is not obligated to conduct a regulatory flexibility analysis.

C. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA),[19] which imposes certain requirements on Federal agencies, including the Commission, in connection with their conducting or sponsoring any collection of information as defined by the PRA, does not apply to this rule. This rule amendment does not contain information collection requirements that require the approval of the Office of Management and Budget.

D. Consideration of Costs and Benefits

Section 15(a) of the CEA [20] requires the Commission to consider the costs and benefits of its action before issuing a new regulation. Section 15(a) of the CEA further specifies that costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.

The Commission believes that benefits of this rulemaking greatly outweigh the costs, if any. As the Commission understands, the statutory provisions by which it is making cost-of-living adjustments to the CMPs in Rule § 143.8 were enacted to ensure that CMPs do not lose their deterrence value because of inflation. An analysis of the costs and benefits of these adjustments were made before enactment of the statutory provisions under which the Commission is operating, and limit the discretion of the Commission to the extent that there are no regulatory choices the Commission could make that would supersede the pre-enactment analysis with respect to the five factors enumerated in Section 15(a) of the CEA, or any other factors.

List of Subjects in 17 CFR Part 143

Civil monetary penalties, Claims.

For the reasons set forth in the preamble, the Commodity Futures Trading Commission amends part 143 of chapter I of title 17 of the Code of Federal Regulations as follows:

PART 143—COLLECTION OF CLAIMS OWED THE UNITED STATES ARISING FROM ACTIVITIES UNDER THE COMMISSION'S JURISDICTION

■ 1. The authority citation for part 143 continues to read as follows:

Authority: 7 U.S.C. 9, 15, 9a, 12a(5), 13a, 13a–1(d), 13(a), 13b; 31 U.S.C. 3701–3720E; 28 U.S.C. 2461 note.

■ 2. Revise § 143.8(b) to read as follows:

§ 143.8 Inflation-adjusted civil monetary penalties.

* * * * *

(b) *2020 Inflation adjustment.* The maximum amount of each civil monetary penalty in the following charts applies to penalties assessed after January 15, 2020:

(1) For non-manipulation or attempted manipulation violations:

TABLE 1 TO PARAGRAPH (b)(1)

U.S. Code citation	Civil monetary penalty description	Date of violation and corresponding penalty			
		10/23/2004 through 10/22/2008	10/23/2008 through 10/22/2012	10/23/2012 through 11/01/2015	11/02/2015 to present
Civil Monetary Penalty Imposed by the Commission in an Administrative Action					
7 U.S.C. 9 (Section 6(c) of the Commodity Exchange Act).	For any person other than a registered entity[1].	$130,000	$130,000	$140,000	$168,142
7 U.S.C. 13a (Section 6b of the Commodity Exchange Act).	For a registered entity[1] or any of its directors, officers or employees.	625,000	675,000	700,000	926,213
Civil Monetary Penalty Imposed by a Federal District Court in a Civil Injunctive Action					
7 U.S.C. 13a–1 (Section 6c of the Commodity Exchange Act).	Any Person	130,000	140,000	140,000	185,242

[1] The term ''Registered Entity'' is defined in 7 U.S.C. 1a (Section 1a of the Commodity Exchange Act).

[13] FCPIAA Section 6.

[14] FCPIAA Section 4(b)(2).

[15] 2019 OMB Guidance at 4.

[16] *Lake Carriers' Ass'n* v. *E.P.A.,* 652 F.3d 1, 10 (DC Cir. 2011).

[17] 5 U.S.C. 601–612.

[18] 5 U.S.C. 603(a).

[19] 44 U.S.C. 3507(d).

[20] 7 U.S.C. 19(a).

(2) For manipulation or attempted manipulation violations:

TABLE 1 TO PARAGRAPH (b)(2)

U.S. Code citation	Civil monetary penalty description	Date of violation and corresponding penalty			
		10/23/2004 through 5/21/2008	05/22/2008 through 8/14/2011	08//15/2011 through 11/01/2015	11/02/2015 to present
Civil Monetary Penalty Imposed by the Commission in an Administrative Action					
7 U.S.C. 9 (Section 6(c) of the Commodity Exchange Act).	For any person other than a registered entity[1].	$130,000	$1,000,000	$1,025,000	$1,212,866
7 U.S.C. 13a (Section 6b of the Commodity Exchange Act).	For a registered entity[1] or any of its directors, officers or employees.	625,000	1,000,000	1,025,000	1,212,866
Civil Monetary Penalty Imposed by a Federal District Court in a Civil Injunctive Action					
7 U.S.C. 13a-1 (Section 6c of the Commodity Exchange Act).	Any Person	$130,000	$1,000,000	$1,025,000	$1,212,866

[1] The term "Registered Entity" is defined in 7 U.S.C. 1a (Section 1a of the Commodity Exchange Act).

Issued in Washington, DC on January 8, 2020, by the Commission.

Robert Sidman,

Deputy Secretary of the Commission.

Note: The following appendix will not appear in the Code of Federal Regulations.

Appendix to Adjustment of Civil Monetary Penalties for Inflation—2020—Commission Voting Summary

On this matter, Chairman Tarbert and Commissioners Quintenz, Behnam, Stump, and Berkovitz voted in the affirmative. No Commissioner voted in the negative.

[FR Doc. 2020–00313 Filed 1–10–20; 8:45 am]

BILLING CODE 6351–01–P

POSTAL SERVICE

39 CFR Part 111

New Mailing Standards for Domestic Mailing Services Products

AGENCY: Postal Service™.

ACTION: Final rule.

SUMMARY: On October 9, 2019, the Postal Service™ filed a notice of mailing services price adjustments with the Postal Regulatory Commission (PRC), effective January 26, 2020. This final rule contains the revisions to *Mailing Standards of the United States Postal Service,* Domestic Mail Manual (DMM®) to implement the changes coincident with the price adjustments and other minor DMM changes.

DATES: *Effective* January 26, 2020.

FOR FURTHER INFORMATION CONTACT: Jacqueline Erwin at (202) 268–2158, or Dale Kennedy at (202) 268–6592.

SUPPLEMENTARY INFORMATION: On December 20, 2019, the Postal Regulatory Commission (PRC) found that the price adjustments proposed by the Postal Service may take effect as planned. The price adjustments and DMM revisions are scheduled to become effective on January 26, 2020. Final prices are available under Docket No. R2020–1 (Order No.5373) on the Postal Regulatory Commission's website at *www.prc.gov.*

USPS did not receive any comments on the proposed changes.

List of Subjects in 39 CFR Part 111

Administrative practice and procedure, Postal Service.

The Postal Service adopts the following changes to *Mailing Standards of the United States Postal Service,* Domestic Mail Manual (DMM), incorporated by reference in the *Code of Federal Regulations.* See 39 CFR 111.1.

Accordingly, 39 CFR part 111 is amended as follows:

PART 111—[AMENDED]

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

Authority: 5 U.S.C. 552(a); 13 U.S.C. 301–307; 18 U.S.C. 1692–1737; 39 U.S.C. 101, 401, 403, 404, 414, 416, 3001–3011, 3201–3219, 3403–3406, 3621, 3622, 3626, 3632, 3633, and 5001.

■ 2. Revise the *Mailing Standards of the United States Postal Service,* Domestic Mail Manual (DMM) as follows:

Mailing Standards of the United States Postal Service, Domestic Mail Manual (DMM)

* * * * *

200 Commercial Mail

* * * * *

230 First-Class Mail

233 Prices and Eligibility

1.0 Prices and Fees

* * * * *

1.5 Presort Mailing Fee

[Revise the second sentence of 1.5; to read as follows:]

* * * Payment of this fee does not apply to qualified full-service mailings (under 705.23.3.1a).* * *

* * * * *

240 Commercial Mail USPS Marketing Mail

243 Prices and Eligibility

1.0 Prices and Fees

* * * * *

1.4 Fees

1.4.1 Presort Mailing Fee

[Revise the second sentence of 1.4.1; to read as follows:]

* * * Payment of this fee does not apply to mailers who present qualified full-service mailings (under 705.23.3.1a).* * *

* * * * *

260 Commercial Mail Bound Printed Matter

263 Prices and Eligibility

1.0 Prices and Fees

* * * * *

1.2 Presorted and Carrier Route Bound Printed Matter

* * * * *

1.2.5 Destination Entry Mailing Fee

[Revise the last sentence of 1.2.5; to read as follows:]

* * * Payment of this fee does not apply to mailers who present only qualified full-service flat-size mailings (under 705.23.3.1a).

* * * * *

500 Additional Services

* * * * *

508 Recipient Services

* * * * *

4.0 Post Office Box Service

* * * * *

4.4 Basis of Fees and Payment

* * * * *

4.4.2 Fee Changes

[Revise the second sentence of 4.4.2; to read as follows:]

* * * In addition, the USPS may assign a fee group to a new ZIP Code, may reassign one or more 5-digit ZIP Codes to the next higher or lower fee group based on the ZIP Codes' cost and market characteristics, or may regroup 5-digit ZIP Codes.* * *

* * * * *

5.0 Caller Service

* * * * *

5.5 Basis of Fees and Payment

* * * * *

5.5.3 Fee Changes

[Revise the text of 5.5.3 by adding new last sentence; to read as follows:]

* * * In addition, the USPS may assign a fee group to a new ZIP Code, may reassign one or more 5-digit ZIP Codes to the next higher or lower fee group based on the ZIP Codes' cost and market characteristics, or may regroup 5-digit ZIP Codes.

* * * * *

700 Special Standards

* * * * *

705 Advanced Preparation and Special Postage Payment Systems

* * * * *

22.0 Seamless Acceptance Program

* * * * *

22.3 Basic Standards

[Revise the introductory text of 22.3, by adding new second and third sentences to read as follows:]

* * * Any permits used in a Seamless acceptance mailing will not prevent that mailing from being finalized regardless of if an annual fee is due on that permit. However, the first time the permit is used for a non-seamless mailing the mailer will have to pay the permit fee if they do not meet the requirements for a fee waiver.* * *

* * * * *

23.0 Full-Service Automation Option

* * * * *

23.2 General Eligibility Standards

[Revise the first sentence of the introductory text of 23.2; to read as follows:]

First-Class Mail (FCM), Periodicals, and USPS Marketing Mail, cards (FCM only), letters (except letters using simplified address format) and flats meeting eligibility requirements for automation or carrier route prices (except for USPS Marketing Mail ECR saturation flats), and Bound Printed Matter presorted or carrier route barcoded flats, are potentially eligible for full-service incentives.* * *

23.3 Fees

[Revise the title of 23.3.1; to read as follows:]

23.3.1 Eligibility for Exception to Payment of Annual Fees and Waiver of Deposit of Permit Imprint Mail Restrictions

[Revise the introductory text of 23.3.1; to read as follows:]

Mailers who present automation or presort mailings (of First-Class Mail cards, letters, and flats, USPS Marketing Mail letters and flats, or Bound Printed Matter flats) that contain 90 percent or more full-service eligible mail as full-service, and 75 percent of their total mail is eligible for full-service incentives, are eligible for the following exception to standards:

[Revise the text of item 23.3.1a; to read as follows:]

a. Annual presort mailing or destination entry fees, as applicable, do not apply to mailings entered by mailers who meet both the 90 percent and 75 percent full-service thresholds, for qualified full-service mailings, as specified in 23.3.1.* * *

* * * * *

Notice 123 (Price List)

[Revise prices as applicable.]

* * * * *

We will publish an appropriate amendment to 39 CFR part 111 to reflect these changes.

Joshua J. Hofer,

Attorney, Federal Compliance.

[FR Doc. 2019–28488 Filed 1–10–20; 8:45 am]

BILLING CODE 7710–12–P

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 19

[FRL–10003–77–OECA]

Civil Monetary Penalty Inflation Adjustment

AGENCY: Environmental Protection Agency (EPA).

ACTION: Final rule.

SUMMARY: The Environmental Protection Agency (EPA) is promulgating this final rule to adjust the level of the maximum (and minimum) statutory civil monetary penalty amounts under the statutes the EPA administers. This action is mandated by the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended through the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (''the 2015 Act''). The 2015 Act prescribes a formula for annually adjusting the statutory maximum (and minimum) amount of civil penalties to reflect inflation, maintain the deterrent effect of statutory civil penalties, and promote compliance with the law. The rule does not necessarily revise the penalty amounts that the EPA chooses to seek pursuant to its civil penalty policies in a particular case. The EPA's civil penalty policies, which guide enforcement personnel on how to exercise the EPA's statutory penalty authorities, take into account a number of fact-specific considerations, *e.g.,* the seriousness of the violation, the violator's good faith efforts to comply, any economic benefit gained by the violator as a result of its noncompliance, and a violator's ability to pay.

DATES: This final rule is effective January 13, 2020.

FOR FURTHER INFORMATION CONTACT: David Smith-Watts, Office of Civil Enforcement, Office of Enforcement and Compliance Assurance, Mail Code 2241A, Environmental Protection Agency, 1200 Pennsylvania Avenue NW, Washington, DC 20460, telephone number: (202) 564–4083; *smith-watts.david@epa.gov.*

SUPPLEMENTARY INFORMATION:

I. Background

Since 1996, Federal agencies have been required to issue regulations adjusting for inflation the statutory civil penalties [1] that can be imposed under

[1] The Federal Civil Penalties Inflation Adjustment Act of 1990, Public Law 101–410, 28 U.S.C. 2461 note, defines ''civil monetary penalty'' as any penalty, fine, or other sanction that—(1)(i) is for a

Continued

the laws administered by that agency. The Federal Civil Penalties Inflation Adjustment Act of 1990, as amended by the Debt Collection Improvement Act of 1996 (DCIA), required agencies to review their statutory civil penalties every 4 years, and to adjust the statutory civil penalty amounts for inflation if the increase met the DCIA's adjustment methodology. In accordance with the DCIA, the EPA reviewed and, as appropriate, adjusted the civil penalty levels under each of the statutes the agency implements in 1996 (61 FR 69360), 2004 (69 FR 7121), 2008 (73 FR 75340), and 2013 (78 FR 66643).

The 2015 Act [2] required each Federal agency to adjust the level of statutory civil penalties under the laws implemented by that agency with an initial ''catch-up'' adjustment through an interim final rulemaking. The 2015 Act also required Federal agencies, beginning on January 15, 2017, to make subsequent annual adjustments for inflation. Section 4 of the 2015 Act requires each Federal agency to publish these annual adjustments by January 15 of each year. The purpose of the 2015 Act is to maintain the deterrent effect of civil penalties by translating originally enacted statutory civil penalty amounts to today's dollars and rounding statutory civil penalties to the nearest dollar.

As required by the 2015 Act, the EPA issued a catch-up rule on July 1, 2016, which was effective August 1, 2016 (81 FR 43091). The EPA made its first annual adjustment on January 12, 2017, which was effective on January 15, 2017 (82 FR 3633). The EPA made its second annual adjustment on January 10, 2018, which was effective on January 15, 2018 (83 FR 1190). The EPA made its third annual adjustment on February 6, 2019 (84 FR 2056) and issued a subsequent correction on February 25, 2019 (84 FR 5955). This rule implements the fourth annual adjustment mandated by the 2015 Act.

The 2015 Act provides a formula for calculating the adjustments. Each statutory maximum and minimum [3] civil monetary penalty as currently adjusted is multiplied by the cost-of-living adjustment multiplier, which is the percentage by which the Consumer Price Index for all Urban Consumers (CPI–U) for the month of October 2019 exceeds the CPI–U for the month of October 2018.[4]

With this rule, the new statutory maximum and minimum penalty levels listed in the third column of Table 1 of 40 CFR 19.4 will apply to all civil penalties assessed on or after January 13, 2020, for violations that occurred after November 2, 2015, the date the 2015 Act was enacted. The former maximum and minimum statutory civil penalty levels, which are in the fourth column of Table 1 to 40 CFR 19.4, will now apply only to violations that occurred after November 2, 2015, where the penalties were assessed on or after February 6, 2019, but before January 13, 2020. The statutory civil penalty levels that apply to violations that occurred on or before November 2, 2015, are codified at Table 2 to 40 CFR 19.4.[5] The fifth column of Table 1 and the seventh column of Table 2 display the statutory civil penalty levels as originally enacted.

The formula for determining the cost-of-living or inflation adjustment to statutory civil penalties consists of the following steps:

Step 1: The cost-of-living adjustment multiplier for 2020 is the percentage by which the CPI–U of October 2019 (257.346) exceeds the CPI–U for the month of October 2018 (252.885), which is 1.01764.[6] Multiply 1.01764 by the current penalty amount. This is the raw adjusted penalty value.

Step 2: Round the raw adjusted penalty value. Section 5 of the 2015 Act states that any adjustment shall be rounded to the nearest multiple of $1. The result is the final penalty value for the year.

II. The 2015 Act Requires Federal Agencies To Publish Annual Penalty Inflation Adjustments Notwithstanding Section 553 of the Administrative Procedures Act

Pursuant to section 4 of the 2015 Act, each Federal agency is required to publish annual adjustments no later than January 15 each year. In accordance with section 553 of the Administrative Procedures Act (APA), most rules are subject to notice and comment and are effective no earlier than 30 days after publication in the **Federal Register**. However, Section 4(b)(2) of the 2015 Act provides that each agency shall make the annual inflation adjustments ''notwithstanding section 553'' of the APA. Consistent with the language of the 2015 Act, this rule is not subject to notice and an opportunity for public comment and will be effective on January 13, 2020.

III. Statutory and Executive Order Reviews

Additional information about these statutes and Executive orders can be found at *https://www.epa.gov/laws-regulations/laws-and-executive-orders.*

A. Executive Order 12866: Regulatory Planning and Review and Executive Order 13563: Improving Regulation and Regulatory Review

This action is not a significant regulatory action and was therefore not submitted to OMB for review.

B. Executive Order 13771: Reducing Regulations and Controlling Regulatory Costs

This action is not an Executive Order 13771 regulatory action because this action is not significant under Executive Order 12866.

C. Paperwork Reduction Act (PRA)

This action does not impose an information collection burden under the PRA. This rule merely increases the level of statutory civil penalties that can be imposed in the context of a Federal civil administrative enforcement action or civil judicial case for violations of EPA-administered statutes and their implementing regulations.

specific monetary amount as provided by Federal law; or (ii) has a maximum amount provided for by Federal law; and (2) is assessed or enforced by an agency pursuant to Federal law; and (3) is assessed or enforced pursuant to an administrative proceeding or a civil action in the Federal courts.

[2] The Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (Section 701 of Pub. L. 114–74) was signed into law on Nov. 2, 2015, and further amended the Federal Civil Penalties Inflation Adjustment Act of 1990.

[3] Under Section 3(2)(A) of the 2015 Act, ''civil monetary penalty'' means ''a specific monetary amount as provided by Federal law''; or ''has a maximum amount provided for by Federal law.'' EPA-administered statutes generally refer to statutory maximum penalties, with the following exceptions: Section 311(b)(7)(D) of the Clean Water Act, 33 U.S.C. 1321(b)(7)(D), refers to a minimum penalty of ''not less than $100,000 . . .''; Section 104B(d)(1) of the Marine Protection, Research, and Sanctuaries Act, 33 U.S.C. 1414b(d)(1), refers to an exact penalty of $600 ''[f]or each dry ton (or equivalent) of sewage sludge or industrial waste dumped or transported by the person in violation of this subsection in calendar year 1992 . . .''; and Section 325(d)(1) of the Emergency Planning and Community Right-to-Know Act, 42 U.S.C. 11045(d)(1), refers to an exact civil penalty of $25,000 for each frivolous trade secret claim.

[4] Current and historical CPI–U's can be found on the Bureau of Labor Statistics' website here: *https://www.bls.gov/cpi/tables/supplemental-files/historical-cpi-u-201910.pdf.*

[5] With this rule, for ease of reference, the order of the Tables and the columns within each Table are now presented in reverse chronological order.

[6] Section 5(b) of the 2015 Act provides that the term ''cost-of-living adjustment'' means the percentage (if any) for each civil monetary penalty by which—

(1) the Consumer Price Index for the month of October preceding the date of the adjustment, exceeds

(2) the Consumer Price Index for the month of October 1 year before the month of October referred to in paragraph (2).

Because the CPI–U for October 2019 is 257.346 and the CPI–U for October 2018 is 252.885, the cost-of-living multiplier is 1.01764 (257.346 divided by 252.885).

D. Regulatory Flexibility Act (RFA)

This action is not subject to the RFA. The RFA applies only to rules subject to notice and comment rulemaking requirements under the APA, 5 U.S.C. 553, or any other statute. Because the 2015 Act directs Federal agencies to publish this rule notwithstanding section 553 of the APA, this rule is not subject to notice and comment requirements or the RFA.

E. Unfunded Mandates Reform Act (UMRA)

This action does not contain any unfunded mandate as described in UMRA, 2 U.S.C. 1531–1538, and does not significantly or uniquely affect small governments. This action is required by the 2015 Act, without the exercise of any policy discretion by the EPA. This action also imposes no enforceable duty on any state, local or tribal governments or the private sector. Because the calculation of any increase is formula-driven pursuant to the 2015 Act, the EPA has no policy discretion to vary the amount of the adjustment.

F. Executive Order 13132: Federalism

This action does not have federalism implications. It 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.

G. Executive Order 13175: Consultation and Coordination With Indian Tribal Governments

This action does not have tribal implications as specified in Executive Order 13175.

This rule merely reconciles the real value of current statutory civil penalty levels to reflect and keep pace with the levels originally set by Congress when the statutes were enacted. The calculation of the increases is formula-driven and prescribed by statute, and the EPA has no discretion to vary the amount of the adjustment to reflect any views or suggestions provided by commenters. Accordingly, this rule will not have a substantial direct effect on tribal governments, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes.

Thus, Executive Order 13175 does not apply to this action.

H. Executive Order 13045: Protection of Children From Environmental Health Risks and Safety Risks

The EPA interprets Executive Order 13045 as applying only to those regulatory actions that concern environmental health or safety risks that the EPA has reason to believe may disproportionately affect children, per the definition of ''covered regulatory action'' in section 2–202 of the Executive order. This action is not subject to Executive Order 13045 because it does not concern an environmental health risk or safety risk.

I. Executive Order 13211: Actions That Significantly Affect Energy Supply, Distribution, or Use

This action is not subject to Executive Order 13211, because it is not a significant regulatory action under Executive Order 12866.

J. National Technology Transfer and Advancement Act (NTTAA)

The rulemaking does not involve technical standards.

K. Executive Order 12898: Federal Actions To Address Environmental Justice in Minority Populations and Low-Income Populations

The EPA believes that this action is not subject to Executive Order 12898 (59 FR 7629, February 16, 1994) because it does not establish an environmental health or safety standard. Rather, this action is mandated by the 2015 Act, which prescribes a formula for adjusting statutory civil penalties on an annual basis to reflect inflation.

L. Congressional Review Act (CRA)

This action is subject to the CRA, and the EPA will submit a rule report to each House of the Congress and to the Comptroller General of the United States. The CRA allows the issuing agency to make a rule effective sooner than otherwise provided by the CRA if the agency makes a good cause finding that notice and comment rulemaking procedures are impracticable, unnecessary or contrary to the public interest (5 U.S.C. 808(2)). The EPA finds that the APA's notice and comment rulemaking procedures are unnecessary because the 2015 Act directs Federal agencies to publish their annual penalty inflation adjustments ''notwithstanding section 553 [of the APA].''

List of Subjects in 40 CFR Part 19

Environmental protection, Administrative practice and procedure, Penalties.

Dated: December 19, 2019.

Andrew R. Wheeler,

Administrator.

For the reasons set out in the preamble, the EPA amends title 40, chapter I, part 19 of the Code of Federal Regulations as follows:

PART 19—ADJUSTMENT OF CIVIL MONETARY PENALTIES FOR INFLATION

■ 1. The authority citation for part 19 continues to read as follows:

Authority: Pub. L. 101–410, Oct. 5, 1990, 104 Stat. 890, as amended by Pub. L. 104–134, title III, sec. 31001(s)(1), Apr. 26, 1996, 110 Stat. 1321–373; Pub. L. 105–362, title XIII, sec. 1301(a), Nov. 10, 1998, 112 Stat. 3293; Pub. L. 114–74, title VII, sec. 701(b), Nov. 2, 2015, 129 Stat. 599.

■ 2. Revise § 19.2 to read as follows:

§ 19.2 Effective date.

(a) The statutory civil penalty levels set forth in the third column of Table 1 of § 19.4 apply to all violations which occur or occurred after November 2, 2015, where the penalties are assessed on or after January 13, 2020. The statutory civil penalty levels set forth in the fourth column of Table 1 of § 19.4 apply to all violations which occurred after November 2, 2015, where the penalties were assessed on or after February 6, 2019 but before January 13, 2020.

(b) The statutory penalty levels in the third column of Table 2 to § 19.4 apply to all violations which occurred after December 6, 2013 through November 2, 2015, and to violations occurring after November 2, 2015, where penalties were assessed before August 1, 2016. The statutory civil penalty levels set forth in the fourth column of Table 2 of § 19.4 apply to all violations which occurred after January 12, 2009 through December 6, 2013. The statutory civil penalty levels set forth in the fifth column of Table 2 of § 19.4 apply to all violations which occurred after March 15, 2004 through January 12, 2009. The statutory civil penalty levels set forth in the sixth column of Table 2 of § 19.4 apply to all violations which occurred after January 30, 1997 through March 15, 2004.

■ 3. Revise § 19.4 to read as follows:

§ 19.4 Statutory civil penalties, as adjusted for inflation, and tables.

Table 1 of this section sets out the statutory civil penalty provisions of statutes administered by the EPA, with the third column setting out the latest operative statutory civil penalty levels for violations that occur or occurred after November 2, 2015, where penalties

are assessed on or after January 13, 2020. The fourth column displays the operative statutory civil penalty levels where penalties were assessed on or after February 6, 2019, but before January 13, 2020. Table 2 of this section sets out the statutory civil penalty provision of statutes administered by the EPA, with the operative statutory civil penalty levels, as adjusted for inflation, for violations that occurred on or before November 2, 2015, and for violations that occurred after November 2, 2015, where penalties were assessed before August 1, 2016.

TABLE 1 OF § 19.4—CIVIL MONETARY PENALTY INFLATION ADJUSTMENTS

U.S. Code citation	Environmental statute	Statutory civil penalties for violations that occurred after November 2, 2015, where penalties are assessed on or after January 13, 2020	Statutory civil penalties for violations that occurred after November 2, 2015, where penalties were assessed on or after February 6, 2019 but before January 13, 2020	Statutory civil penalties, as enacted
7 U.S.C. 136*l*(a)(1)	FEDERAL INSECTICIDE, FUNGICIDE, AND RODENTICIDE ACT (FIFRA).	$20,288	$19,936	$5,000
7 U.S.C. 136*l*(a)(2) [1]	FIFRA	2,976/1,917/2,976	2,924/1,884/2,924	1,000/500/1,000
15 U.S.C. 2615(a)(1)	TOXIC SUBSTANCES CONTROL ACT (TSCA).	40,576	39,873	25,000
15 U.S.C. 2647(a)	TSCA	11,665	11,463	5,000
15 U.S.C. 2647(g)	TSCA	9,639	9,472	5,000
31 U.S.C. 3802(a)(1)	PROGRAM FRAUD CIVIL REMEDIES ACT (PFCRA).	11,665	11,463	5,000
31 U.S.C. 3802(a)(2)	PFCRA	11,665	11,463	5,000
33 U.S.C. 1319(d)	CLEAN WATER ACT (CWA)	55,800	54,833	25,000
33 U.S.C. 1319(g)(2)(A)	CWA	22,320/55,800	21,933/54,833	10,000/25,000
33 U.S.C. 1319(g)(2)(B)	CWA	22,320/278,995	21,933/274,159	10,000/125,000
33 U.S.C. 1321(b)(6)(B)(i)	CWA	19,277/48,192	18,943/47,357	10,000/25,000
33 U.S.C. 1321(b)(6)(B)(ii)	CWA	19,277/240,960	18,943/236,783	10,000/125,000
33 U.S.C. 1321(b)(7)(A)	CWA	48,192/1,928	47,357/1,895	25,000/1,000
33 U.S.C. 1321(b)(7)(B)	CWA	48,192	47,357	25,000
33 U.S.C. 1321(b)(7)(C)	CWA	48,192	47,357	25,000
33 U.S.C. 1321(b)(7)(D)	CWA	192,768/5,783	189,427/5,683	100,000/3,000
33 U.S.C. 1414b(d)(1)	MARINE PROTECTION, RESEARCH, AND SANCTUARIES ACT (MPRSA).	1,284	1,262	600
33 U.S.C. 1415(a)	MPRSA	202,878/267,621	199,361/262,982	50,000/125,000
33 U.S.C. 1901 note (*see* 1409(a)(2)(A)).	CERTAIN ALASKAN CRUISE SHIP OPERATIONS (CACSO).	14,791/36,975	14,535/36,334	10,000/25,000
33 U.S.C. 1901 note (*see* 1409(a)(2)(B)).	CACSO	14,791/184,874	14,535/181,669	10,000/125,000
33 U.S.C. 1901 note (*see* 1409(b)(1)).	CACSO	36,975	36,334	25,000
33 U.S.C. 1908(b)(1)	ACT TO PREVENT POLLUTION FROM SHIPS (APPS).	75,867	74,552	25,000
33 U.S.C. 1908(b)(2)	APPS	15,173	14,910	5,000
42 U.S.C. 300g–3(b)	SAFE DRINKING WATER ACT (SDWA).	58,328	57,317	25,000
42 U.S.C. 300g–3(g)(3)(A)	SDWA	58,328	57,317	25,000
42 U.S.C. 300g–3(g)(3)(B)	SDWA	11,665/40,640	11,463/39,936	5,000/25,000
42 U.S.C. 300g–3(g)(3)(C)	SDWA	40,640	39,936	25,000
42 U.S.C. 300h–2(b)(1)	SDWA	58,328	57,317	25,000
42 U.S.C. 300h–2(c)(1)	SDWA	23,331/291,641	22,927/286,586	10,000/125,000
42 U.S.C. 300h–2(c)(2)	SDWA	11,665/291,641	11,463/286,586	5,000/125,000
42 U.S.C. 300h–3(c)	SDWA	20,288/43,280	19,936/42,530	5,000/10,000
42 U.S.C. 300i(b)	SDWA	24,386	23,963	15,000
42 U.S.C. 300i–1(c)	SDWA	141,943/1,419,442	139,483/1,394,837	100,000/1,000,000
42 U.S.C. 300j(e)(2)	SDWA	10,143	9,967	2,500
42 U.S.C. 300j–4(c)	SDWA	58,328	57,317	25,000
42 U.S.C. 300j–6(b)(2)	SDWA	40,640	39,936	25,000
42 U.S.C. 300j–23(d)	SDWA	10,705/107,050	10,519/105,194	5,000/50,000
42 U.S.C. 4852d(b)(5)	RESIDENTIAL LEAD-BASED PAINT HAZARD REDUCTION ACT OF 1992.	18,149	17,834	10,000
42 U.S.C. 4910(a)(2)	NOISE CONTROL ACT OF 1972.	38,352	37,687	10,000
42 U.S.C. 6928(a)(3)	RESOURCE CONSERVATION AND RECOVERY ACT (RCRA).	101,439	99,681	25,000

TABLE 1 OF § 19.4—CIVIL MONETARY PENALTY INFLATION ADJUSTMENTS—Continued

U.S. Code citation	Environmental statute	Statutory civil penalties for violations that occurred after November 2, 2015, where penalties are assessed on or after January 13, 2020	Statutory civil penalties for violations that occurred after November 2, 2015, where penalties were assessed on or after February 6, 2019 but before January 13, 2020	Statutory civil penalties, as enacted
42 U.S.C. 6928(c)	RCRA	61,098	60,039	25,000
42 U.S.C. 6928(g)	RCRA	75,867	74,552	25,000
42 U.S.C. 6928(h)(2)	RCRA	61,098	60,039	25,000
42 U.S.C. 6934(e)	RCRA	15,173	14,910	5,000
42 U.S.C. 6973(b)	RCRA	15,173	14,910	5,000
42 U.S.C. 6991e(a)(3)	RCRA	61,098	60,039	25,000
42 U.S.C. 6991e(d)(1)	RCRA	24,441	24,017	10,000
42 U.S.C. 6991e(d)(2)	RCRA	24,441	24,017	10,000
42 U.S.C. 7413(b)	CLEAN AIR ACT (CAA)	101,439	99,681	25,000
42 U.S.C. 7413(d)(1)	CAA	48,192/385,535	47,357/378,852	25,000/200,000
42 U.S.C. 7413(d)(3)	CAA	9,639	9,472	5,000
42 U.S.C. 7524(a)	CAA	48,192/4,819	47,357/4,735	25,000/2,500
42 U.S.C. 7524(c)(1)	CAA	385,535	378,852	200,000
42 U.S.C. 7545(d)(1)	CAA	48,192	47,357	25,000
42 U.S.C. 9604(e)(5)(B)	COMPREHENSIVE ENVIRONMENTAL RESPONSE, COMPENSATION, AND LIABILITY ACT (CERCLA).	58,328	57,317	25,000
42 U.S.C. 9606(b)(1)	CERCLA	58,328	57,317	25,000
42 U.S.C. 9609(a)(1)	CERCLA	58,328	57,317	25,000
42 U.S.C. 9609(b)	CERCLA	58,328/174,985	57,317/171,952	25,000/75,000
42 U.S.C. 9609(c)	CERCLA	58,328/174,985	57,317/171,952	25,000/75,000
42 U.S.C. 11045(a)	EMERGENCY PLANNING AND COMMUNITY RIGHT-TO-KNOW ACT (EPCRA).	58,328	57,317	25,000
42 U.S.C. 11045(b)(1)(A)	EPCRA	58,328	57,317	25,000
42 U.S.C. 11045(b)(2)	EPCRA	58,328/174,985	57,317/171,952	25,000/75,000
42 U.S.C. 11045(b)(3)	EPCRA	58,328/174,985	57,317/171,952	25,000/75,000
42 U.S.C. 11045(c)(1)	EPCRA	58,328	57,317	25,000
42 U.S.C. 11045(c)(2)	EPCRA	23,331	22,927	10,000
42 U.S.C. 11045(d)(1)	EPCRA	58,328	57,317	25,000
42 U.S.C. 14304(a)(1)	MERCURY-CONTAINING AND RECHARGEABLE BATTERY MANAGEMENT ACT (BATTERY ACT).	16,258	15,976	10,000
42 U.S.C. 14304(g)	BATTERY ACT	16,258	15,976	10,000

[1] Note that 7 U.S.C. 136*l*(a)(2) contains three separate statutory maximum civil penalty provisions. The first mention of $1,000 and the $500 statutory maximum civil penalty amount were originally enacted in 1978 (Pub. L. 95–396), and the second mention of $1,000 was enacted in 1972 (Pub. L. 92–516).

TABLE 2 OF § 19.4—CIVIL MONETARY PENALTY INFLATION ADJUSTMENTS

U.S. Code citation	Environmental statute	Statutory civil penalties for violations after December 6, 2013 through November 2, 2015, or assessed before August 1, 2016	Statutory civil penalties for violations after January 12, 2009 through December 6, 2013	Statutory civil penalties for violations after March 15, 2004 through January 12, 2009	Statutory civil penalties for violations after January 30, 1997 through March 15, 2004	Statutory civil penalties, as enacted
7 U.S.C. 136*l*(a)(1)	FEDERAL INSECTICIDE, FUNGICIDE, AND RODENTICIDE ACT (FIFRA).	$7,500	$7,500	$6,500	$5,500	$5,000
7 U.S.C. 136*l*(a)(2)	FIFRA	750/1,100	750/1,100	650/1,100	550/1,000	500/1,000
15 U.S.C. 2615(a)(1)	TOXIC SUBSTANCES CONTROL ACT (TSCA).	37,500	37,500	32,500	27,500	25,000
15 U.S.C. 2647(a)	TSCA	7,500	7,500	6,500	5,500	5,000
15 U.S.C. 2647(g)	TSCA	7,500	7,500	5,500	5,000	5,000
31 U.S.C. 3802(a)(1)	PROGRAM FRAUD CIVIL REMEDIES ACT (PFCRA).	7,500	7,500	6,500	5,500	5,000

TABLE 2 OF § 19.4—CIVIL MONETARY PENALTY INFLATION ADJUSTMENTS—Continued

U.S. Code citation	Environmental statute	Statutory civil penalties for violations after December 6, 2013 through November 2, 2015, or assessed before August 1, 2016	Statutory civil penalties for violations after January 12, 2009 through December 6, 2013	Statutory civil penalties for violations after March 15, 2004 through January 12, 2009	Statutory civil penalties for violations after January 30, 1997 through March 15, 2004	Statutory civil penalties, as enacted
31 U.S.C. 3802(a)(2)	PFCRA	7,500	7,500	6,500	5,500	5,000
33 U.S.C. 1319(d)	CLEAN WATER ACT (CWA).	37,500	37,500	32,500	27,500	25,000
33 U.S.C. 1319(g)(2)(A)	CWA	16,000/37,500	16,000/37,500	11,000/32,500	11,000/27,500	10,000/25,000
33 U.S.C. 1319(g)(2)(B)	CWA	16,000/187,500	16,000/177,500	11,000/157,500	11,000/137,500	10,000/125,000
33 U.S.C. 1321(b)(6)(B)(i)	CWA	16,000/37,500	16,000/37,500	11,000/32,500	11,000/27,500	10,000/25,000
33 U.S.C. 1321(b)(6)(B)(ii)	CWA	16,000/187,500	16,000/177,500	11,000/157,500	11,000/137,500	10,000/125,000
33 U.S.C. 1321(b)(7)(A)	CWA	37,500/2,100	37,500/1,100	32,500/1,100	27,500/1,100	25,000/1,000
33 U.S.C. 1321(b)(7)(B)	CWA	37,500	37,500	32,500	27,500	25,000
33 U.S.C. 1321(b)(7)(C)	CWA	37,500	37,500	32,500	27,500	25,000
33 U.S.C. 1321(b)(7)(D)	CWA	150,000/5,300	140,000/4,300	130,000/4,300	110,000/3,300	100,000/3,000
33 U.S.C. 1414b(d)(1) [1]	MARINE PROTECTION, RESEARCH, AND SANCTUARIES ACT (MPRSA).	860	860	760	660	600
33 U.S.C. 1415(a)	MPRSA	75,000/187,500	70,000/177,500	65,000/157,500	55,000/137,500	50,000/125,000
33 U.S.C. 1901 note (*see* 1409(a)(2)(A)).	CERTAIN ALASKAN CRUISE SHIP OPERATIONS (CACSO).	11,000/27,500	11,000/27,500	10,000/25,000	10,000/[2] 25,000	10,000/25,000
33 U.S.C. 1901 note (*see* 1409(a)(2)(B)).	CACSO	11,000/147,500	11,000/137,500	10,000/125,000	10,000/125,000	10,000/125,000
33 U.S.C. 1901 note (*see* 1409(b)(1)).	CACSO	27,500	27,500	25,000	25,000	25,000
42 U.S.C. 300g–3(b)	SAFE DRINKING WATER ACT (SDWA).	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 300g–3(g)(3)(A)	SDWA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 300g–3(g)(3)(B)	SDWA	7,000/32,500	7,000/32,500	6,000/27,500	5,000/25,000	5,000/25,000
42 U.S.C. 300g–3(g)(3)(C)	SDWA	32,500	32,500	27,500	25,000	25,000
42 U.S.C. 300h–2(b)(1)	SDWA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 300h–2(c)(1)	SDWA	16,000/187,500	16,000/177,500	11,000/157,500	11,000/137,500	10,000/125,000
42 U.S.C. 300h–2(c)(2)	SDWA	7,500/187,500	7,500/177,500	6,500/157,500	5,500/137,500	5,000/125,000
42 U.S.C. 300h–3(c)	SDWA	7,500/16,000	7,500/16,000	6,500/11,000	5,500/11,000	5,000/10,000
42 U.S.C. 300i(b)	SDWA	21,500	16,500	16,500	15,000	15,000
42 U.S.C. 300i–1(c)	SDWA	120,000/1,150,000	110,000/1,100,000	100,000/1,000,000	22,000/[3] 55,000	20,000/50,000
42 U.S.C. 300j(e)(2)	SDWA	3,750	3,750	2,750	2,750	2,500
42 U.S.C. 300j–4(c)	SDWA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 300j–6(b)(2)	SDWA	32,500	32,500	27,500	25,000	25,000
42 U.S.C. 300j–23(d)	SDWA	7,500/75,000	7,500/70,000	6,500/65,000	5,500/55,000	5,000/50,000
42 U.S.C. 4852d(b)(5)	RESIDENTIAL LEAD–BASED PAINT HAZARD REDUCTION ACT OF 1992.	16,000	16,000	11,000	11,000	10,000
42 U.S.C. 4910(a)(2)	NOISE CONTROL ACT OF 1972.	16,000	16,000	11,000	11,000	10,000
42 U.S.C. 6928(a)(3)	RESOURCE CONSERVATION AND RECOVERY ACT (RCRA).	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 6928(c)	RCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 6928(g)	RCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 6928(h)(2)	RCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 6934(e)	RCRA	7,500	7,500	6,500	5,500	5,000
42 U.S.C. 6973(b)	RCRA	7,500	7,500	6,500	5,500	5,000
42 U.S.C. 6991e(a)(3)	RCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 6991e(d)(1)	RCRA	16,000	16,000	11,000	11,000	10,000
42 U.S.C. 6991e(d)(2)	RCRA	16,000	16,000	11,000	11,000	10,000
42 U.S.C. 7413(b)	CLEAN AIR ACT (CAA)	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 7413(d)(1)	CAA	37,500/320,000	37,500/295,000	32,500/270,000	27,500/220,000	25,000/200,000
42 U.S.C. 7413(d)(3)	CAA	7,500	7,500	6,500	5,500	5,000

TABLE 2 OF § 19.4—CIVIL MONETARY PENALTY INFLATION ADJUSTMENTS—Continued

U.S. Code citation	Environmental statute	Statutory civil penalties for violations after December 6, 2013 through November 2, 2015, or assessed before August 1, 2016	Statutory civil penalties for violations after January 12, 2009 through December 6, 2013	Statutory civil penalties for violations after March 15, 2004 through January 12, 2009	Statutory civil penalties for violations after January 30, 1997 through March 15, 2004	Statutory civil penalties, as enacted
42 U.S.C. 7524(a)	CAA	3,750/37,500	3,750/37,500	2,750/32,500	2,750/27,500	2,500/25,000
42 U.S.C. 7524(c)(1)	CAA	320,000	295,000	270,000	220,000	200,000
42 U.S.C. 7545(d)(1)	CAA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 9604(e)(5)(B)	COMPREHENSIVE ENVIRONMENTAL RESPONSE, COMPENSATION, AND LIABILITY ACT (CERCLA).	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 9606(b)(1)	CERCLA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 9609(a)(1)	CERCLA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 9609(b)	CERCLA	37,500/117,500	37,500/107,500	32,500/97,500	27,500/82,500	25,000/75,000
42 U.S.C. 9609(c)	CERCLA	37,500/117,500	37,500/107,500	32,500/97,500	27,500/82,500	25,000/75,000
42 U.S.C. 11045(a)	EMERGENCY PLANNING AND COMMUNITY RIGHT–TO–KNOW ACT (EPCRA).	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 11045(b)(1)(A) [4]	EPCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 11045(b)(2)	EPCRA	37,500/117,500	37,500/107,500	32,500/97,500	27,500/82,500	25,000/75,000
42 U.S.C. 11045(b)(3)	EPCRA	37,500/117,500	37,500/107,500	32,500/97,500	27,500/82,500	25,000/75,000
42 U.S.C. 11045(c)(1)	EPCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 11045(c)(2)	EPCRA	16,000	16,000	11,000	11,000	10,000
42 U.S.C. 11045(d)(1)	EPCRA	37,500	37,500	32,500	27,500	25,000
42 U.S.C. 14304(a)(1)	MERCURY–CONTAINING AND RECHARGEABLE BATTERY MANAGEMENT ACT (BATTERY ACT).	16,000	16,000	11,000	10,000	10,000
42 U.S.C. 14304(g)	BATTERY ACT	16,000	16,000	11,000	10,000	10,000

[1] Note that 33 U.S.C. 1414b (d)(1)(B) contains additional penalty escalation provisions that must be applied to the penalty amounts set forth in this Table 2. The amounts set forth in this Table 2 reflect an inflation adjustment to the calendar year 1992 penalty amount expressed in section 104B(d)(1)(A), which is used to calculate the applicable penalty amount under MPRSA section 104B(d)(1)(B) for violations that occur in any subsequent calendar year.

[2] CACSO was passed on December 21, 2000 as part of Title XIV of the Consolidated Appropriations Act of 2001, Public Law 106–554, 33 U.S.C. 1901 note.

[3] The original statutory penalty amounts of $20,000 and $50,000 under section 1432(c) of the SDWA, 42 U.S.C. 300i–1(c), were subsequently increased by Congress pursuant to section 403 of the Public Health Security and Bioterrorism Preparedness and Response Act of 2002, Public Law 107–188 (June 12, 2002), to $100,000 and $1,000,000, respectively. The EPA did not adjust these new penalty amounts in its 2004 Civil Monetary Penalty Inflation Adjustment Rule ("2004 Rule"), published on February 13, 2004, because they had gone into effect less than two years prior to the 2004 Rule.

[4] Consistent with how the EPA's other penalty authorities are displayed under this section, this Table 2 now delineates, on a subpart-by-subpart basis, the penalty authorities enumerated under section 325(b) of EPCRA, 42 U.S.C. 11045(b) (*i.e.,* 42 U.S.C. 11045(b)(1)(A), (b)(2), and (b)(3)).

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BILLING CODE 6560–50–P

NATIONAL FOUNDATION ON THE ARTS AND THE HUMANITIES

National Endowment for the Arts

45 CFR Parts 1149 and 1158

RIN 3135–AA33

Civil Penalties Adjustment for 2020

AGENCY: National Endowment for the Arts, National Foundation on the Arts and the Humanities.

ACTION: Final rule.

SUMMARY: The National Endowment for the Arts (NEA) is adjusting the maximum civil monetary penalties (CMPs) that may be imposed for violations of the Program Fraud Civil Remedies Act (PFCRA) and the NEA's Restrictions on Lobbying to reflect the requirements of the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (the 2015 Act). The 2015 Act further amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (the Inflation Adjustment Act) to improve the

effectiveness of civil monetary penalties and to maintain their deterrent effect. This final rule provides the 2020 annual inflation adjustments to the initial ''catch-up'' adjustments made on June 15, 2017, and reflects all other inflation adjustments made in the interim.

DATES: *Effective date:* This rule is effective January 13, 2020.

FOR FURTHER INFORMATION CONTACT: Daniel Fishman, Assistant General Counsel, National Endowment for the Arts, 400 7th St. SW, Washington, DC 20506, Telephone: 202–682–5418.

SUPPLEMENTARY INFORMATION:

1. Background

On December 12, 2017 the NEA issued a final rule entitled ''Federal Civil Penalties Adjustments'' which finalized the NEA's June 15, 2017 interim final rule entitled ''Implementing the Federal Civil Penalties Adjustment Act Improvements Act'', implementing the 2015 Act (section 701 of Pub. L. 114–74), which amended the Inflation Adjustment Act (28 U.S.C. 2461 note) requiring catch-up and annual adjustments to the NEA's CMPs. The 2015 Act requires agencies make annual adjustments to its CMPs for inflation.

A CMP is defined in the Inflation Adjustment Act as any penalty, fine, or other sanction that is (1) for a specific monetary amount as provided by Federal law, or has a maximum amount provided for by Federal law; (2) assessed or enforced by an agency pursuant to Federal law; and (3) assessed or enforced pursuant to an administrative proceeding or a civil action in the Federal courts.

These annual inflation adjustments are based on the percentage change in the Consumer Price Index for all Urban Consumers (CPI–U) for the month of October preceding the date of the adjustment, relative to the October CPI–U in the year of the previous adjustment. The formula for the amount of a CMP inflation adjustment is prescribed by law, as explained in OMB Memorandum M–16–06 (February 24, 2016), and therefore the amount of the adjustment is not subject to the exercise of discretion by the Chairman of the National Endowment for the Arts (Chairman).

The Office of Management and Budget has issued guidance on implementing and calculating the 2020 adjustment under the 2015 Act.[1] Per this guidance, the CPI–U adjustment multiplier for this annual adjustment is 1.01764. In its prior rules, the NEA identified two CMPs, which require adjustment: The penalty for false statements under the PFCRA and the penalty for violations of the NEA's Restrictions on Lobbying. With this rule, the NEA is adjusting the amount of those CMPs accordingly.

2. Dates of Applicability

The inflation adjustments contained in this rule shall apply to any violations assessed after January 15, 2020.

3. Adjustments

Two CMPs in NEA regulations require adjustment in accordance with the 2015 Act: (1) The penalty associated with the Program Fraud Civil Remedies Act (45 CFR 1149.9) and (2) the penalty associated with Restrictions on Lobbying (45 CFR 1158.400; 45 CFR part 1158, app. A).

A. Adjustments to Penalties Under the NEA's Program Fraud Civil Remedies Act Regulations.

The current maximum penalty under the PFCRA for false claims and statements is currently set at $11,462. The post-adjustment penalty or range is obtained by multiplying the pre-adjustment penalty or range by the percent change in the CPI–U over the relevant time period and rounding to the nearest dollar. Between October 2018 and October 2019, the CPI–U increased by 101.764 percent. Therefore, the new post-adjustment maximum penalty under the PFCRA for false statements is $11,462 × 1.01764 = $11,664.19 which rounds to $11,664. Therefore, the maximum penalty under the PFCRA for false claims and statements will be $11,664.

B. Adjustments to Penalties Under the NEA's Restrictions on Lobbying Regulations

The penalty for violations of the Restrictions on Lobbying is currently set at a range of a minimum of $20,134 and a maximum of $201,340. The post-adjustment penalty or range is obtained by multiplying the pre-adjustment penalty or range by the percent change in the CPI–U over the relevant time period and rounding to the nearest dollar. Between October 2018 and October 2019, the CPI–U increased by 101.764 percent. Therefore, the new post-adjustment minimum penalty under the Restrictions on Lobbying is $20,134 × 1.01764 = $20,478.16, which rounds to $20,478, and the maximum penalty under the Restrictions on Lobbying is $201,340 × 1.01764 = $204,891.64, which rounds to $204,892. Therefore, the range of penalties under the law on the Restrictions on Lobbying shall be between $20,478 and $204,891.64.

Administrative Procedure Act

Section 553 of the Administrative Procedure Act requires agencies to provide an opportunity for notice and comment on rulemaking and also requires agencies to delay a rule's effective date for 30 days following the date of publication in the **Federal Register** unless an agency finds good cause to forgo these requirements. However, section 4(b)(2) of the 2015 Act requires agencies to adjust civil monetary penalties notwithstanding section 553 of the Administrative Procedure Act (APA) and publish annual inflation adjustments in the **Federal Register**. ''This means that the public procedure the APA generally requires . . . is not required for agencies to issue regulations implementing the annual adjustment.'' OMB Memorandum M–18–03.

Even if the 2015 Act did not except this final rule from section 553 of the APA, the NEA has good cause to dispense with notice and comment. Section 553(b)(B), authorizes agencies to dispense with notice and comment procedures for rulemaking if the agency finds good cause that notice and comment are impracticable, unnecessary, or contrary to public interest. The annual adjustments to civil penalties for inflation and the method of calculating those adjustments are established by section 5 of the 2015 Act, as amended, leaving no discretion for the NEA. Accordingly, public comment would be impracticable because the NEA would be unable to consider such comments in the rulemaking process.

Regulatory Planning and Review (Executive Order 12866)

Executive Order 12866 (E.O. 12866) established a process for review of rules by the Office of Information and Regulatory Affairs, which is within the Office of Management and Budget (OMB). Only ''significant'' proposed and final rules are subject to review under this Executive Order. ''Significant,'' as used in E.O. 12866, means ''economically significant.'' It refers to rules with (1) an impact on the economy of $100 million; or that (2) were inconsistent or interfered with an action taken or planned by another agency; (3) materially altered the budgetary impact of entitlements, grants, user fees, or loan programs; or (4) raised novel legal or policy issues.

This final rule would not be a significant policy change and OMB has not reviewed this final rule under E.O. 12866. The NEA has made the

[1] OMB Memorandum M–20–05 (December 16, 2019).

assessments required by E.O. 12866 and determined that this final rule: (1) Will not have an effect of $100 million or more on the economy; (2) will not adversely affect in a material way the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or Tribal governments or communities; (3) will not create a serious inconsistency or otherwise interfere with an action taken or planned by another agency; (4) does not alter the budgetary effects of entitlements, grants, user fees, or loan programs or the rights or obligations of their recipients; and (5) does not raise novel legal or policy issues.

Reducing Regulation and Controlling Regulatory Costs (Executive Order 13771)

Executive Order 13771 (E.O. 13771) section 5 requires that agencies, in most circumstances, remove or rescind two regulations for every regulatory action (such as the promulgation of regulations) unless they request and are specifically exempted from that order's requirements by the Director of the Office of Management and Budget (the Director).

This final rule is not subject to the requirements of E.O. 13771 because this final rule is not significant under E.O. 12866. Per OMB guidance, annual inflation adjustments ''are not significant regulatory actions under E.O. 12866, they are not considered E.O. 13771 regulatory actions.'' [2] Furthermore, the NEA has requested and has received an exemption from the requirement that the agency rescind two regulations for every regulation it promulgates from the Director.

Federalism (Executive Order 13132)

This final rule does not have Federalism implications, as set forth in E.O. 13132. As used in this order, federalism implications mean ''substantial direct effects 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.'' The NEA has determined that this final rule will not have federalism implications within the meaning of E.O. 13132.

Civil Justice Reform (Executive Order 12988)

This final rule meets the applicable standards set forth in section 3(a) and 3(b)(2) of E.O. 12988. Specifically, this final rule is written in clear language designed to help reduce litigation.

[2] *Id.*

Indian Tribal Governments (Executive Order 13175)

Under the criteria in E.O. 13175, the NEA has evaluated this final rule and determined that it would have no potential effects on federally recognized Indian Tribes.

Takings (Executive Order 12630)

Under the criteria in E.O. 12630, this final rule does not have significant takings implications. Therefore, a takings implication assessment is not required.

Regulatory Flexibility Act of 1980 (5 U.S.C. 605(b))

This final rule will not have a significant adverse impact on a substantial number of small entities, including small businesses, small governmental jurisdictions, or certain small not-for-profit organizations.

Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35)

This final rule will not impose any ''information collection'' requirements under the Paperwork Reduction Act. Under the act, information collection means the obtaining or disclosure of facts or opinions by or for an agency by 10 or more nonfederal persons.

Unfunded Mandates Act of 1995 (Section 202, Pub. L. 104–4)

This final rule does not contain a Federal mandate that will result in the expenditure by State, local, and Tribal governments, in the aggregate, or by the private sector of $100 million or more in any one year.

National Environmental Policy Act of 1969 (5 U.S.C. 804)

The final rule will not have a significant effect on the human environment.

Small Business Regulatory Enforcement Fairness Act of 1996 (Sec. 804, Pub. L. 104–121)

This final rule would not be a major rule as defined in section 804 of the Small Business Regulatory Enforcement Fairness Act of 1996. This final rule will not result in an annual effect on the economy of $100 million or more, a major increase in costs or prices, significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based companies to compete with foreign based companies in domestic and export markets.

E-Government Act of 2002 (44 U.S.C. 3504)

Section 206 of the E-Government Act requires agencies, to the extent practicable, to ensure that all information about that agency required to be published in the **Federal Register** is also published on a publicly accessible website. All information about the NEA required to be published in the **Federal Register** may be accessed at *www.arts.gov.* This Act also requires agencies to accept public comments on their rules ''by electronic means.''

Finally, the E-Government Act requires, to the extent practicable, that agencies ensure that a publicly accessible Federal Government website contains electronic dockets for rulemakings under the Administrative Procedure Act of 1946 (5 U.S.C. 551 *et seq.*). Under this Act, an electronic docket consists of all submissions under section 553(c) of title 5, United States Code; and all other materials that by agency rule or practice are included in the rulemaking docket under section 553(c) of title 5, United States Code, whether or not submitted electronically. The website *https://www.regulations.gov* contains electronic dockets for the NEA's rulemakings under the Administrative Procedure Act of 1946.

Plain Writing Act of 2010 (5 U.S.C. 301)

Under this Act, the term ''plain writing'' means writing that is clear, concise, well-organized, and follows other best practices appropriate to the subject or field and intended audience. To ensure that this final rule has been written in plain and clear language so that it can be used and understood by the public, the NEA has modeled the language of this final rule on the Federal Plain Language Guidelines.

Public Participation (Executive Order 13563)

The NEA encourages public participation by ensuring its documentation is understandable by the general public, and has written this final rule in compliance with Executive Order 13563 by ensuring its accessibility, consistency, simplicity of language, and overall comprehensibility.

List of Subjects in 45 CFR Parts 1149 and 1158

Administrative practice and procedure, Government contracts, Grant programs, Loan programs, Lobbying, Penalties.

For the reasons stated in the preamble, the NEA amends 45 CFR chapter XI, subchapter B, as follows:

PART 1149—PROGRAM FRAUD CIVIL REMEDIES ACT REGULATIONS

■ 1. The authority citation for part 1149 continues to read as follows:

Authority: 5 U.S.C. App. 8G(a)(2); 20 U.S.C. 959; 28 U.S.C. 2461 note; 31 U.S.C. 3801–3812.

■ 2. Revise § 1149.9(a)(1) to read as follows:

§ 1149.9 What civil penalties and assessments may I be subjected to?

(a) * * *

(1) A civil penalty of not more than $11,664 for each false, fictitious or fraudulent statement or claim; and

* * * * *

PART 1158—NEW RESTRICTIONS ON LOBBYING

■ 3. The authority citation for part 1158 continues to read as follows:

Authority: 20 U.S.C. 959; 28 U.S.C. 2461; 31 U.S.C. 1352.

§ 1158.400 [Amended]

■ 4. Amend § 1158.400(a), (b), and (e) by:

■ a. Removing ''$20,134'' and adding in its place ''$20,478'' each place it appears.

■ b. Removing ''$201,340'' and adding in its place ''$204,891.64'' each place it appears.

Appendix A to Part 1158 [Amended]

■ 5. Amend appendix A to part 1158 by:

■ a. Removing ''$20,134'' and adding in its place ''$20,478'' each place it appears.

■ b. Removing ''$201,340'' and adding in its place ''$204,891.64'' each place it appears.

Dated: January 3, 2020.

Gregory Gendron,

Director of Administrative Services.

[FR Doc. 2020–00121 Filed 1–10–20; 8:45 am]

BILLING CODE P

FEDERAL MARITIME COMMISSION

46 CFR Part 506

[Docket No. 20–01]

RIN 3072–AC79

Inflation Adjustment of Civil Monetary Penalties

AGENCY: Federal Maritime Commission.

ACTION: Final rule.

SUMMARY: The Federal Maritime Commission (Commission) is publishing this final rule to adjust for inflation the civil monetary penalties assessed or enforced by the Commission, pursuant to the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (2015 Act). The 2015 Act requires that agencies adjust and publish their civil penalties by January 15 each year.

DATES: This rule is effective January 15, 2020.

FOR FURTHER INFORMATION CONTACT: William H. Shakely, Acting General Counsel, Federal Maritime Commission, 800 North Capitol Street NW, Room 1018, Washington, DC 20573; (202) 523–5740.

SUPPLEMENTARY INFORMATION: This rule adjusts the civil monetary penalties assessable by the Commission in accordance with the 2015 Act, which became effective on November 2, 2015, section 701 of Public Law 114–74. The 2015 Act further amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (FCPIAA), Public Law 101–410, 104 Stat. 890 (codified as amended at 28 U.S.C. 2461 note), in order to improve the effectiveness of civil monetary penalties and to maintain their deterrent effect.

The 2015 Act requires agencies to adjust civil monetary penalties under their jurisdiction by January 15 each year, based on changes in the consumer price index (CPI–U) for the month of October in the previous calendar year. On December 16, 2019, the Office of Management and Budget published guidance stating that the CPI–U multiplier for October 2019 is 1.01764.[1] In order to complete the adjustment for January 2020, the Commission must multiply the most recent civil penalty amounts in 46 CFR part 506 by the multiplier, 1.01764.

Rulemaking Analyses and Notices

Notice and Effective Date

Adjustments under the FCPIAA, as amended by the 2015 Act, are not subject to the procedural rulemaking requirements of the Administrative Procedure Act (APA) (5 U.S.C. 553), including the requirements for prior notice, an opportunity for comment, and a delay between the issuance of a final rule and its effective date.[2] As noted above, the 2015 Act requires that the Commission adjust its civil monetary penalties no later than January 15 of each year.

[1] Office of Management and Budget, M–20–05, Implementation of Penalty Inflation Adjustments for 2020, Pursuant to the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015, at 1 (Dec. 16, 2019) (M–20–05).

[2] FCPIAA section 4(b)(2); M–20–05 at 4.

Congressional Review Act

The rule is not a ''major rule'' as defined by the Congressional Review Act, codified at 5 U.S.C. 801 *et seq.* The rule will not result in: (1) An annual effect on the economy of $100,000,000 or more; (2) a major increase in costs or prices; or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or the ability of United States-based companies to compete with foreign-based companies. 5 U.S.C. 804(2).

Regulatory Flexibility Act

The Regulatory Flexibility Act (codified as amended at 5 U.S.C. 601–612) provides that whenever an agency promulgates a final rule after being required to publish a notice of proposed rulemaking under the APA (5 U.S.C. 553), the agency must prepare and make available a final regulatory flexibility analysis describing the impact of the rule on small entities or the head of the agency must certify that the rule will not have a significant economic impact on a substantial number of small entities. 5 U.S.C. 604–605. As indicated above, this final rule is not subject to the APA's notice and comment requirements, and the Commission is not required to either conduct a regulatory flexibility analysis or certify that the final rule would not have a significant economic impact on a substantial number of small entities.

Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3521) requires an agency to seek and receive approval from the Office of Management and Budget (OMB) before collecting information from the public. 44 U.S.C. 3507. The agency must submit collections of information in rules to OMB in conjunction with the publication of the notice of proposed rulemaking. 5 CFR 1320.11. This final rule does not contain any collection of information, as defined by 44 U.S.C. 3502(3) and 5 CFR 1320.3(c).

Regulation Identifier Number

The Commission assigns a regulation identifier number (RIN) to each regulatory action listed in the Unified Agenda of Federal Regulatory and Deregulatory Actions (Unified Agenda). The Regulatory Information Service Center publishes the Unified Agenda in April and October of each year. The public may use the RIN contained in the heading at the beginning of this document to find this action in the Unified Agenda, available at *http://www.reginfo.gov/public/do/eAgendaMain.*

List of Subjects in 46 CFR Part 506

Administrative practice and procedure, Claims, Penalties.

For the reasons stated in the preamble, 46 CFR part 506 is amended as follows:

PART 506—CIVIL MONETARY PENALTY INFLATION ADJUSTMENT

■ 1. The authority citation for part 506 continues to read as follows:

Authority: 28 U.S.C. 2461.

■ 2. Amend § 506.4 by revising paragraph (d) to read as follows:

§ 506.4 Cost of living adjustments of civil monetary penalties.

* * * * *

(d) *Inflation adjustment.* Maximum civil monetary penalties within the jurisdiction of the Federal Maritime Commission are adjusted for inflation as follows:

TABLE 1 TO PARAGRAPH (d)

United States Code citation	Civil monetary penalty description	Maximum penalty as of January 15, 2019	Maximum penalty as of January 15, 2020
46 U.S.C. 42304	Adverse impact on U.S. carriers by foreign shipping practices	$2,103,861	$2,140,973
46 U.S.C. 41107(a)	Knowing and Willful violation/Shipping Act of 1984, or Commission regulation or order.	60,039	61,098
46 U.S.C. 41107(a)	Violation of Shipping Act of 1984, Commission regulation or order, not knowing and willful.	12,007	12,219
46 U.S.C. 41108(b)	Operating in foreign commerce after tariff suspension	120,079	122,197
46 U.S.C. 42104	Failure to provide required reports, etc./Merchant Marine Act of 1920	9,472	9,639
46 U.S.C. 42106	Adverse shipping conditions/Merchant Marine Act of 1920	1,894,261	1,927,676
46 U.S.C. 42108	Operating after tariff or service contract suspension/Merchant Marine Act of 1920.	94,713	96,384
46 U.S.C. 44102, 44104	Failure to establish financial responsibility for non-performance of transportation.	23,924 798	24,346 812
46 U.S.C. 44103, 44104	Failure to establish financial responsibility for death or injury	23,924 798	24,346 812
31 U.S.C. 3802(a)(1)	Program Fraud Civil Remedies Act/making false claim	11,463	11,665
31 U.S.C. 3802(a)(2)	Program Fraud Civil Remedies Act/giving false statement	11,463	11,665

By the Commission.

Rachel Dickon,

Secretary.

[FR Doc. 2020–00294 Filed 1–10–20; 8:45 am]

BILLING CODE 6731–AA–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 54

[WC Docket No. 10–90; DA 19–1165; FRS 16332]

Connect America Fund

AGENCY: Federal Communications Commission.

ACTION: Final action.

SUMMARY: In this document, the Wireline Competition Bureau (the Bureau) establishes procedures to ensure swift and efficient administration of the voluntary process for the long-form applicants in the Connect America Phase II Auction (Phase II Auction) to facilitate post-auction review of the defined deployment obligations (and associated support) on a state-by-state basis when the total number of actual locations in eligible areas is less than the number of funded locations.

DATES: Effective February 12, 2020.

FOR FURTHER INFORMATION CONTACT: Alexander Minard, Wireline Competition Bureau, (202) 418–7400 or TTY: (202) 418–0484.

SUPPLEMENTARY INFORMATION: This is a summary of the Commission's Order in WC Docket No. 10–90; DA 19–1165, adopted and released on November 12, 2019. The full text of the document is available for public inspection during regular business hours in the FCC Reference Center, Room CY–A257, 445 12th Street SW, Washington, DC 20554 or at the following internet address: *https://docs.fcc.gov/public/attachments/DA-19-1165A1.pdf.*

I. Introduction

1. The Phase II Auction is one part of a multi-step process comprehensively reforming and modernizing the high-cost component of the Universal Service Fund. At the conclusion of this auction, 103 bidders won $1.49 billion in support over 10 years to provide fixed broadband and voice services to over 700,000 locations in high-cost areas in 45 states. Then, 134 applicants submitted the long-form application portion of the FCC Form 683 by the October 15, 2018 deadline. For these long-form applicants, the Commission created a voluntary process to facilitate post-auction review of the defined deployment obligations (and associated support) on a state-by-state basis when the total number of actual locations in eligible areas is less than the number of funded locations. The Bureau in the Order establishes procedures to ensure swift and efficient administration of this process.

II. Discussion

2. In the Order, the Bureau establishes an Eligible Locations Adjustment Process (ELAP) consistent with the parameters set forth in the *Phase II Auction Reconsideration Order,* 83 FR 15982, April 13, 2018, and prior Commission guidance for making adjustments to defined deployment obligations. The Bureau adopts a challenge framework, generally as proposed in the *Locations Adjustment Public Notice,* 83 FR 49040, September 28, 2018. After setting forth this framework, the Bureau follows with more detailed information regarding evidentiary standards, location data formatting, confidentiality of information, and future post-adjudication verification. The Bureau conforms this process, where necessary, to the requirements of the Privacy Act of 1974, as amended, and related federal rules.

3. *Participant Submission.* This process begins with a new, one-time collection of information from support recipients that seek to participate in ELAP (participants) that includes

information about all eligible locations within the state as well as evidence substantiating the completeness and accuracy of such information. Participants must certify the accuracy of their submissions as of the date of submission under penalty of perjury in accordance with the proposal in the *Locations Adjustment Public Notice.* As specified in the Bureau's proposal, this certification must be signed by an individual with relevant knowledge (such as an officer of the company), certifying under penalty of perjury that the participant has engaged in due diligence to verify statements and evidence presented in this challenge process and that such information is accurate to the best of the certifying party's knowledge and belief.

4. Participants may certify their submissions at any time and amend and recertify their submissions until the filing deadline. In permitting this flexibility, the Bureau concurs with Verizon's comment that the Bureau's original proposal—requiring certification of submissions at or near the deadline for submitting information—is too onerous because it requires participants to continuously monitor and update their data and submissions as updates are made to a data source/sources; instead, participants will be able to rely on any reasonably current data source, *i.e.,* a source containing data that describes conditions as they exist within the year preceding the submission deadline.

5. In the *Phase II Auction Reconsideration Order,* the Commission required participants to file actual location data ''within a year'' of the publication of the Phase II auction closing public notice which occurred on August 28, 2018. Pursuant to the delegated authority entrusted to us in the *Phase II Auction Reconsideration Order* to adopt ''necessary implementation details,'' and to issue an order ''detailing instructions, deadlines and requirements for filing valid geolocation data and evidence for both support recipients and commenters,'' the Bureau waives and extends this deadline consistent with the timing of the Bureau's implementation. The Bureau's implementation of ELAP has and will continue to involve significant coordination of resources, including the creation of a specific module in the High Cost Universal Broadband (HUBB) portal to accept ELAP-related filings and to facilitate access to such information; the module, in turn, will help facilitate swift implementation of similar processes in other high-cost programs. The Bureau will announce by public notice when the module is ready to accept the required information from participants as well as the deadline for submitting and certifying such information. The Bureau will set a deadline that provides participants with at least a three-month timeframe to upload information into the module, correct any errors identified through the module's validation processes, and certify such information. The submission deadline cannot occur before the Commission receives OMB approval of the collection pursuant to the Paperwork Reduction Act of 1995 (PRA), Public Law 104–13.

6. *Protective Order.* Before the participant's filing deadline, the Bureau will adopt a protective order consistent with the requirements specified herein to protect against disclosure or misuse of information submitted by parties pursuant to ELAP.

7. *Prima Facie Determination.* Within 60 days following the participant submission deadline, the Bureau will release a list of participants that have met the prima facie evidentiary standards for location modification, along with the certain location information for qualifying locations and prospective locations, *i.e.,* state, study area code (SAC), addresses, geocoordinates, and number of units. The Bureau directs the Universal Service Administrative Company (USAC) to use the reported geocoordinates of these locations to populate a publicly available map (ELAP Map) of presumptively eligible locations so that outside parties that qualify as a relevant stakeholder may decide whether to file challenges. The Bureau will dismiss any participant submission that is not certified, that includes incomplete or improperly formatted location data, that fails to include a description of methodology for identifying all eligible locations, or that fails to provide at least some supporting evidence (or show cause why supporting evidence is not needed or unavailable).

8. *Stakeholder Challenge.* Eligible stakeholders will then have 90 days from the public release of the participants' location information to establish their eligibility, sign the protective order, and review and challenge the participants' evidence (challenge window). WISPA recommends that the Bureau limits the challenge window to 60 days, stressing that stakeholders will prepare their challenge information concurrent with the preparation and submission of information by participants. While stakeholders may do some preparation at the same time as participants, stakeholders will submit challenges that are responsive to the participants' location information by identifying locations, or multiple units, that were not reported or misreported by the participant. For this reason, stakeholders will need time to access and review participants' location information and to compare such information against their own. A 60-day time frame does not afford stakeholders adequate time to complete these steps prior to submitting their challenges, particularly as some stakeholders may be state regulatory or public interest entities that will be responding to participant information for large or widespread geographic areas.

9. The stakeholder location information will be used to further populate and revise the ELAP Map to inform and supplement the work of other stakeholders filing challenges against the same participant in the same state prior to the close of the challenge window. Participants will have access to this information as it is processed but will not be able to file replies until after the close of the challenge window. Unlike participant location information, stakeholder location information will not be publicly available.

10. *Participant Reply.* Challenged participants will have 30 days from the stakeholder submission deadline (response window) to: (1) Access and review certified data submitted by the stakeholder with respect to the challenged area; and (2) submit additional data/information to oppose the challenge (response window). If a challenged participant does not oppose the challenge, the participant need not submit any additional information. A challenged participant, however, will not have a further opportunity to submit any additional information or data for the Bureau's consideration after the response window closes.

11. The response window is for a longer time frame than the Bureau originally proposed, as most commenters stress the need for at least 30 days to review stakeholder filings and prepare a response. Participants must certify, under penalty of perjury, the truth and accuracy of information submitted in the reply. Verizon requests a 45-day window for preparing and filing a reply to ''give support recipients enough time to review the diverse forms of evidence and, if necessary, conduct field research to determine whether the additional addresses submitted by commenters meet the Commission's definition of a 'location.' '' Participants, however, should be well familiar with supporting evidence, will have a targeted number of locations to research, and are likely to already have (or should

have) some information about those locations because of their initial submissions. For this reason, the Bureau determines that a 30-day response window strikes the appropriate balance between the interests of the participant and the public interest in swift resolution of these claims.

12. *Location Adjudication.* In the *Phase II Auction Reconsideration Order,* the Commission directed the Bureau to adjudicate participants' requests for adjustment of defined deployment obligations based on the preponderance of the evidence standard. In the *Locations Adjustment Public Notice,* the Bureau proposed that participants would also bear the burden of persuasion. The Bureau received no comments on such proposal. Accordingly, the Bureau will only modify a participant's defined deployment obligation to the extent that the participant produces adequate evidence demonstrating that it is more likely than not that the defined deployment obligation is greater than the number of actual locations within the state. In adjudicating these claims, the Bureau will consider stakeholder challenges and participant replies to determine not only the overall credibility of participants' information but also to adjust the participants' qualifying location count.

13. The Bureau declines WISPA's suggestion that it resolves these cases within 90 days of the reply deadline. While the Bureau acknowledges that expeditious resolution is critical to participants' financial and deployment plans (including adjustments to the letter of credit), it is difficult to predict the number of participants and stakeholders, and the associated amount of information that may be submitted; moreover, the Bureau expects that information is likely to be highly variable. During ELAP, participants may deploy service to, and report as served, any known actual location and must report such locations in their initial ELAP submission. The Bureau expects to resolve all ELAP disputes well in advance of the participants' first deployment milestone. The Bureau also declines to adopt WISPA's suggestion that the Bureau allow participants and stakeholders to bypass the ELAP adjudication process by entering into negotiated settlements, subject to review and adjustment by the Bureau. Allowing for a negotiated settlement process would introduce additional administrative burdens without corresponding efficiencies, as both processes should produce the same result, *i.e.,* a complete and accurate accounting of all qualifying locations. Without careful Bureau oversight, a settlement process between outside parties is less optimal and could introduce into ELAP additional considerations contrary to USF-related goals as well as disparities in bargaining power and expertise that ELAP protects against.

14. *Support Adjustment.* The Commission has directed that, in circumstances where the Bureau determines that modification of the participant's number of funded locations is warranted, it must reduce the authorized support on a pro rata basis. Consistent with the Bureau's proposal, it will order a pro-rata reduction in future payments for the remainder of the support term proportionally to reflect the total amount of reduction. Participants will be permitted to adjust their letters of credit to reflect the new authorized funding amount once the Bureau's order modifying the authorized support is issued.

15. As an initial step, the Commission requires participants to submit a list of qualifying locations within the state. Qualifying locations include every location eligible for high-cost support, *i.e.,* residential housing unit or small business served with mass market services. In the Bureau's *HUBB Reporting Public Notice,* the Bureau clarified that qualifying locations cannot be abandoned, derelict, condemned, or otherwise uninhabitable. The Bureau and USAC have provided further guidance and clarification on the meaning of a qualifying location for carriers reporting location data into the HUBB to demonstrate compliance with defined deployment obligations, which the Bureau now incorporates here as generally applicable to ELAP. *HUBB Public Notice,* 31 FCC Rcd 12900; HUBB Frequently Asked Questions, *https://www.usac.org/_res/documents/hc/pdf/tools/HC-HUBB-FAQ.pdf.* Participants should follow this guidance unless and until the Bureau or the Commission issues different guidance.

16. As the Bureau noted in the *Locations Adjustment Public Notice,* however, there are important distinctions in reporting served locations in the HUBB for the purpose of demonstrating compliance with a defined deployment obligation and reporting qualifying locations for the purpose of seeking adjustment to a defined deployment obligation. Carriers reporting information in the HUBB must report information about served locations, *i.e.,* qualifying locations to which the reporting carrier can provide the requisite level of service within ten business days of a customer request. Such locations need not be occupied but cannot be unfinished or an ongoing or future real estate development. In ELAP, however, participants seeking to reduce their defined deployment obligation are to report all locations that they will be capable of serving within the six-year build out period. Accordingly, the Bureau sought comment on whether participants should be required or permitted to include in their location information, information about unfinished properties or prospective developments that have a reasonable certainty of coming into existence within the six-year build-out period (prospective locations).

17. ITTA argues that participants must report prospective locations to avoid a ''perverse'' effect on universal service goals where the ''net diminution in unserved locations would be undermined by the addition of new unserved locations that would have been served'' had the participants' defined deployment obligation not been adjusted. ITTA stresses that this is particularly true when ''unfinished residential or business locations are at the edge of participants' service areas and the business case does not exist to extend service to these locations absent universal service support.'' Most commenters, however, argue against such a requirement, stressing that there are too many variables in determining the probability of whether and, if so, when, an unfinished or planned development or construction project will be completed. These commenters stress that the research and documentation requirements necessary to identify all prospective locations is too burdensome. Further, USTelecom asserts, requiring participants to serve a revised location count that includes prospective locations would be an ''unfair burden completely outside of the provider's control.''

18. The Bureau agrees with the majority of commenters. Accordingly, the Bureau will not require, but will permit, participants to report prospective locations as part of their initial submission. The Bureau finds that this approach is consistent with the purpose and scope of ELAP, a process designed to address the inherent limitations in the model's underlying data inputs by reducing funded location estimates. This process refines the defined deployment obligation but does not alter the nature of the obligation; participants, like all other funding recipients in the same programs, must serve a specific number of locations with the requisite level of service by certain deadlines. The number of locations that they must serve is based

on data estimates describing conditions at a point in time. Participants may report toward satisfaction of their build-out requirements, any qualifying location within eligible areas, regardless of whether such location preexists the estimates or is newly built. They are also expected to adopt flexible network plans that permit reallocation of resources, as necessary, to deal with inevitable changes in consumer demand, network capacity, as well as location eligibility.

19. The Bureau does not expect significant changes in the net number of actual locations in these high-cost areas within the time-limited build-out period, although it recognizes that there is likely to be some fluctuation in where locations are situated as certain locations become unserviceable and new locations are built. If the Bureau were to require participants to count *all* prospective locations toward their overall qualifying location count, participants would have less overall flexibility in responding to such fluctuations in comparison to a Phase II auction support recipient that did not participate in ELAP and therefore, has a defined deployment obligation that does not include prospective locations. The Bureau agrees with the views of several commenters that mandatory reporting of all prospective locations introduces uncertainty into an otherwise clear evidentiary burden. The Bureau further recognizes, however, consistent with ITTA comments, that there may be circumstances where a participant intentionally excludes from its location counts almost completed developments at the edge of denser communities, where service costs may exceed that of the average qualifying location due to the necessity of extending network facilities. For this reason, the Bureau will permit relevant stakeholders to argue for inclusion of these kinds of locations in actual locations counts.

20. Some participants may want to commit to serving some number of locations greater than the number of qualifying actual locations that it has been able to find, but less than the CAM-estimated number of locations. Accordingly, and consistent with some commenters' suggestion, the Bureau will permit participants to report location data for prospective locations. These prospective locations may include plots, parcels, or partially completed structures in planned unit developments or structures currently undergoing renovation. Participants should exercise due diligence when assessing the likelihood that these reported prospective locations will become qualifying locations and in assessing the overall probability of fluctuations in the net number of qualifying locations within the six-year buildout time frame to ensure future compliance with adjusted defined deployment obligations.

21. Together, qualifying locations and voluntarily-reported prospective location data form the actual location count that provides the evidentiary basis for adjusting participants' defined deployment obligation. As recognized by the Commission in the *Phase II Auction Reconsideration Order,* however, participants have the incentive to maximize their average ratio of support and build-out costs, even when such maximization means leaving actual locations unserved and support unclaimed. For this reason, the Commission directed the Bureau to adopt requirements that would help ensure that the actual location counts submitted by participants are complete and demonstrate that ''no additional locations could be found.'' As explained more fully in the following, these requirements include the submission of a methods description and some supporting evidence that those methods were applied systematically in the relevant areas.

22. *Methods Description.* In the *Locations Adjustment Public Notice,* the Bureau proposed that participants submit, in addition to location information, information regarding the participants' methodology for identifying all such locations within eligible areas within the state. The Bureau sought comment on whether it should require participants to use specific Global Positioning System (GPS) methods or if they should be permitted to rely on any of the three generally accepted GPS methods outlined by USAC in its HUBB guidance, *i.e.,* field research, computer-based geolocation, or automated address geolocation (databases). All commenters commenting on this issue supported flexibility of method, stating that the best choice of method may be determined by variable geographic features, availability of resources, and the technology used to provide service. The Bureau agrees with commenters' suggestions. Accordingly, participants will be able to use any of the three generally accepted GPS methods to compile location information.

23. In the *Locations Adjustment Public Notice,* the Bureau also sought comment on whether participants should be required to justify their methodological choices and make clear that they systematically and reasonably gathered location data for all eligible areas. Such information is essential to the Bureau's ability to evaluate whether the participants' location information is accurate and complete. Consistent with this proposal, several commenters acknowledge that a description of method is necessary for the evaluation of location information.

24. The Bureau acknowledges Hughes' concern that many commercial vendors treat their methods for identifying locations as proprietary content and prevent disclosure. The Bureau declines to follow Hughes' suggestion, however, to require all potential commercial vendors or the actual vendors upon which participants rely to establish that their databases meet Commission standards. Commission collection and comparison of such data methods and information from such vendors (which could be numerous), as well as the management of such information, is prohibitively burdensome, particularly given the limited purpose and time constraints of this process. Further, the Bureau lacks delegated authority to impose such obligations.

25. The Bureau also disagrees with Hughes contention that absent such a process, requiring participants to establish that their location data is accurate, reliable and complete excludes reliance on most commercial databases. Participants need not disclose the specific proprietary methods used by vendors to compile location data so long as they demonstrate that the database or geolocation software has an evidentiary basis, such as customer records. Participants must also establish the source's accuracy and reliability in the relevant geographic areas, which may be accomplished through, for example, statistical sampling and verification of sampled locations in eligible areas. While the Bureau encourages participants to use publicly available databases/information, including E911, tax records, real estate records, and other publicly available resources, participants must account for differences between such databases/information and the Commission's requirements (such as in how buildings and other structures are defined as locations).

26. The Bureau also declines to adopt USTelecom's suggestion that the Commission make available to participants all CAM data relevant to CAM funded location estimates so that participants can demonstrate that their information is more accurate than CAM estimates. USTelecom stresses, in particular, the need to access information about the ''surrogate'' locations that the model randomly placed along roadways when precise

geocoordinates could not be identified. The Connect America Cost Model (CAM), however, is used to provide an estimate of the overall number of locations in eligible areas and, as explained in the *CAM Inputs Order,* 79 FR 29111, May 21, 2014, whether a location is identified by geocoordinates or randomly placed is irrelevant to whether the location is reasonably determined to be a high-cost location in the relevant census block. The Bureau also explained that providing geographic coordinates of locations would require the Bureau to publicly release proprietary commercial data—the geographic coordinates of those locations that came from a commercial data source, and ''[a]s a practical matter, after the location demand data are generated, information about whether any individual location was based on a geocoded address or randomly assigned is not retained.'' Accordingly, the Bureau cannot release information that no longer exists and it would decline to release it if it did. To meet their evidentiary burdens, participants are not measuring their location information against CAM estimates but providing detailed information about individual actual locations in eligible areas subject to challenge.

27. *Supporting Evidence.* In the *Locations Adjustment Public Notice,* the Bureau also proposed that participants submit evidence supporting their descriptions of methods and location information. Several commenters express concern that this requirement is ''excessive'' or ''overly prescriptive.'' The Bureau disagrees. Absent supporting evidence, the Bureau's evaluation of the *completeness* of the location list would largely be based on the truth and candor of the participant and where applicable, stakeholder challenges. Moreover, requiring the submission of supporting evidence does not impose significantly greater evidentiary burdens since it is the by-product of participants' research methods and should be kept by participants for future auditing purposes.

28. The Bureau will, however, allow participants flexibility in determining what and how much evidence to submit. Participants may, for example, submit print-outs (or links to) web-based photography, database pages, and/or public records information for a sample of randomly selected land units (*i.e.,* parcels, plots) within the relevant eligible areas cross-referenced against reported locations. Participants may also choose to submit location information for any location that it has affirmatively determined to be a non-qualifying location together with a description of the reason why such structure should not be counted, *e.g.,* derelict, industrial facility, temporary or mobile unit, or incomplete build. To support such a conclusion, participants may submit, as requested by WISPA in its comment, ''qualitative evidence,'' such as roof size or other visual evidence.

29. In making these decisions, the Bureau has carefully weighed the burdens on participants (and stakeholders) against the need to have sufficient data and evidence to ensure that the adjusted defined deployment obligations will not undercut service to locations that are the most expensive to serve. As with any process, these benefits and burdens may not fall equally on every participant. WISPA, for example, states that small providers may find participation cost-prohibitive, time-consuming, and generally not worth the benefits, particularly if the participant must purchase expensive software and/or conduct ground studies. To limit potential burdens on small providers, the Bureau has provided participants with considerable discretion in adopting processes to identify locations in eligible areas. The Bureau has only required participants describe the steps that they have taken to ensure that their eligible location lists are complete and accurate and submit a limited amount of readily-available supporting evidence. If such requirements are too expensive or burdensome for successful Phase II Auction applicants, then they may choose not to participate in this process and thereby assume the associated risk of noncompliance if they are unable to meet their defined deployment obligation.

30. *Stakeholder Eligibility.* The Bureau adopts its proposal to define relevant stakeholders eligible to participate as challengers in this process as government entities (state, local, and Tribal) as well as individuals or non-governmental entities with a legitimate and verifiable interest in ensuring service in the relevant areas. In this regard, ELAP is distinguishable from other similar processes designed to test service in eligible areas because, unlike in those processes, entities or individuals are likely to have specific knowledge required to support a challenge: Information about omitted or incorrectly reported locations. Moreover, individuals or entities might have more specific and up-to-date information than possessed by governing authorities and accordingly they may be able to represent their interest in service to eligible areas. Finally, the Bureau is motivated to conduct an adjustment process that is as open and transparent as possible to ensure the most complete, accurate, and reliable outcomes. Accordingly, the Bureau's definition includes individuals or entities residing or doing business in the relevant areas as well as those entities with a legitimate and verifiable interest, such as landlords or property developers. Commenters generally supported the Bureau's proposal.

31. Several commenters also support excluding individuals or entities otherwise meeting the definition of a relevant stakeholder if such individual or entity has a controlling interest in a competitive provider in the same area and market. The Bureau finds that such a restriction is necessary. Competitors have unique incentives that work at cross purposes with this process, including an interest in facilitating future default of participants by obstructing this process. In other challenge processes designed to distinguish between unserved and served areas, competitors were uniquely situated in terms of access to the relevant information, *i.e.,* they have records demonstrating service at a particular location. Here, while competitive providers may have some location information, such information is likely to be more readily available to individuals and other entities in the communities in question. While any individual or entity otherwise eligible to participate as a stakeholder may request waiver of this restriction, the Bureau generally finds that the public interest in protecting the integrity of this process against potential anticompetitive behaviors outweighs the benefits of permitting a limited number of competitive entities to challenge participant location information.

32. To determine the eligibility of non-government entities or individuals to participate as a stakeholder, the Bureau will use one more ore automated data source that compile public records information, such as LexisNexis Public Records, to verify identity and eligibility. The Bureau will collect from all prospective stakeholders through the HUBB module basic identifying and contact information, *e.g.,* name, residential or business address, phone number, and email addresses. The Bureau may also collect other kinds of information as required by the automated data source to verify identity. To demonstrate eligibility, the prospective stakeholder must also provide the address of the relevant locations in the eligible areas and information regarding the nature of the interest in that location, *e.g.,* residency,

ownership, lease management. To the extent that such information is available in public records, the commercial data source may verify that the interest is held by the individual/entity. If the Bureau cannot verify the identity of the stakeholder and his/her/its interest in ensuring service in eligible areas using automated data sources, the Bureau will not permit the stakeholder to access participant information.

33. As a condition of participating in this process, the stakeholder must acknowledge and consent to the disclosure of its contact information to the relevant participant and the linking of such information to the challenge evidence submitted. The stakeholder must also certify that it satisfies the Bureau's definition of relevant stakeholder. The Bureau will review such information and make an affirmative determination whether to allow further access and participation by the stakeholder.

34. *Stakeholder Location Evidence.* Once a stakeholder demonstrates that it meets the definition of a relevant stakeholder, makes the requisite certifications, and enters into a protective order, as appropriate, a stakeholder may (1) access confidential participant information for areas it wishes to challenge; (2) identify the area(s) it wants to challenge; (3) submit evidence supporting the challenge; and (4) certify its challenge for the specified area(s). Based on the Bureau's consideration of the record and given the policy objectives of this process, it finds that to certify a challenge, a stakeholder must submit location information for omitted or inaccurately reported locations generally in the same format as required of participants, *e.g.,* geocodes, addresses, number of units. Such information may include omitted prospective locations, but such locations must be separately identified as existing and prospective locations.

35. GeoLinks and WISPA assert that, in addition to location information, the Commission should require stakeholders to provide a short description of their methods, including an explanation as to why their methods produce a more accurate data set than that of the participant. These commenters assert that the Commission should reject any challenge that merely alleges deficiencies in participants' methods or evidence without presenting any additional location information since such a challenge would be too onerous to verify or refute when applied to the particular facts relevant to the eligible areas. These commenters also would require stakeholders to submit supporting evidence to the same extent that the Bureau requires participants to submit this information. WISPA adds to such assertions that any stakeholder relying on publicly-available data must submit such data as part of its challenge.

36. Despite what commenters argue, the Commission decided that participants carry the burden of proof and, therefore, heavier evidentiary burdens. In the Order, the Bureau has determined that participants will also carry the burden of persuasion. The Bureau also notes that the imposing certain evidentiary requirements might dissuade stakeholders with limited experience and expertise from participating. Accordingly, the Bureau is not convinced by the assertions of some commenters that it should impose the same evidentiary requirements on stakeholders that the Bureau imposes on participants. Instead, the Bureau requires stakeholders to submit some but not all the information required of participants.

37. Stakeholders must describe their methods for identifying locations, including any limitations thereof, and must submit proof that the location data describes a qualifying residential or small business location. We expect that there will be a variety of stakeholders responding to participants' submissions. Accordingly, the description of methodology may range from a simple explanation, such as might occur if a homeowner reports that his/her home has been omitted from the participant's list of qualifying locations, or a more in-depth explanation, such as might occur if a local government entity claims that several locations have been omitted from the participant's list. Generally, the Bureau has determined that sets of geocoordinates a distance of 36 feet or more from another will describe separate structures. Accordingly, when a stakeholder's location data falls within 36 feet of the geocoordinates reported by the participant (generally, an overlap in the first three decimal places of geocoordinates), the stakeholder must also explain why the location should be considered a separate and unique location from the location reported (*e.g.,* the location data describes a separate business or residential location or unit within the same property/parcel). These locations will be identified by USAC through its automated validation process. If a stakeholder reports prospective locations as omitted locations, it must explain why such location should be considered when determining participants' defined deployment obligations and submit some supporting evidence that the location will become a qualifying location within the six-year build-out period. Stakeholders may include factual arguments demonstrating why their methodology produces location information more complete or accurate than that of the participant but are not required to do so. A stakeholder must certify that its submission is true and accurate and may revise and recertify its filing until the filing deadline.

38. Once a stakeholder submits its evidence in the HUBB, the system will conduct an automatic validation process to determine whether the stakeholder provided enough evidence to justify proceeding with each submitted challenge. The system will inform the stakeholder of any problems associated with the prior submission in due course. The stakeholder may submit additional or modified data, as required, to resolve the problem if it can do so before the deadline. Once the challenge window closes, however, the stakeholder will have no further opportunity to correct existing, or provide additional, information in support of its challenge. Only those challenges to areas that are certified by a stakeholder at the close of the window and validated by the HUBB will be considered.

39. The Bureau finds that providing challenged participants with a limited 30-day opportunity to submit additional data in response to a challenge promotes its goals of a fair and balanced process. It will also help ensure that the adjusted defined deployment obligations accurately reflect the actual number of locations (plus any prospective locations that the participant chooses to include). However, the Bureau expects stakeholders to provide irrefutable evidence of any omitted qualified locations overlooked by the participant, making responses largely unnecessary. The Bureau does not adopt specific evidentiary requirements for this reply process, preferring instead to defer to participants' judgment regarding the most probative evidence to rebut the stakeholders' information. The reply should not be used to introduce new evidence not responsive to the challenge or update preexisting evidence that is non-responsive to one or more stakeholder challenges. The information must be submitted in the same format as specified for participants' and stakeholders' data and information. Any information submitted must be certified as true and accurate by an officer of the participant under penalty of perjury.

40. In the *Phase II Auction Reconsideration Order,* the Commission determined that participants should be required to submit addresses and geocoordinates for eligible locations but otherwise requested that the Bureau develop formatting and evidentiary

requirements for location data after seeking notice and comment. In the *Locations Adjustment Public Notice,* the Bureau proposed adopting data format requirements for this process similar to those used for the HUBB, stressing several advantages to such an approach, including streamlined validations and future auditing of data, potential transferability of data to the HUBB, and preexisting and refined guidance for carriers reporting in the HUBB that can be adapted to the locations adjustment process. The Bureau and USAC developed these HUBB formatting standards to help ensure that a location may be easily distinguished from nearby properties and readily determined to be located within eligible areas. By adopting these standards, the Bureau gives both participants and stakeholders a meaningful opportunity to review location data. Commenters generally express support for the adoption of such standards.

41. Participants and stakeholders must submit location information in a tabular format (*e.g.,* a .csv file) into a module within the HUBB. Such information will include (1) basic information, *e.g.,* participant/stakeholder name and contact information; (2) information regarding the relevant geographic area, *e.g.,* the relevant state and SAC; (3) location specific information, *e.g.,* addresses, geocoordinates, and number of units; (4) method information, *e.g.,* GPS methods and/or source used and the ''as-of'' date of such method or source; and (5) certification information, including the name of the officer certifying that the information is true and correct and his or her contact information. The module will also accept the participants' methods description (*e.g.,* as a .pdf file) and the supporting evidence (*e.g.,* .pdf, jpeg).

42. In its comment (and in ex parte filings with the Bureau relating to HUBB functionality), USTelecom requests that geocoordinate reporting requirements be limited to the five decimal places rather than the currently required six places. USTelecom asserts that in the predominately rural areas served by participants, reporting at the fifth decimal place adequately ensures that the location will be readily identifiable by stakeholders and for future auditing purposes. USTelecom stresses that, in comparison, requiring a higher degree of accuracy places a significant burden on participants, noting that in CAF areas, the ''rooftop level geocoding accuracy'' is only approximately 55%. The Bureau generally agrees. Reporting accuracy at the fifth decimal place generally will enable stakeholders (and any future auditor) to identify attached properties and to distinguish such properties from apartments and other multiple dwelling units. The Bureau does not, however, wish to foreclose a participant or stakeholder from entering more precise coordinates. Accordingly, the Bureau will configure the HUBB to allow participants to enter a trailing ''0'' in lieu of a sixth decimal place. Such entry will not be interpreted to suggest that the participant is certifying the accuracy of its information to the sixth decimal place.

43. In the *Phase II Auction Reconsideration Order,* the Commission provided that all evidence submitted by participants pursuant to this process would be subject to future audit and directed the Bureau to adopt parameters for such audits. These verifications will mirror HUBB verification processes. Because, however, participants' submissions produce a ''snapshot'' of conditions as they exist at a specific point in time, verifying the accuracy, reliability, and completeness of participants' location information may be increasingly difficult as time passes. For this reason, WISPA suggests that the Bureau limit verification to CAF Phase II support recipients' six-year deployment period, while USTelecom proposes a more abbreviated time frame, *i.e.,* 18-months after the participants' certification.

44. The Bureau concludes that these verifications should be limited to the support term (plus any time reserved by USAC for final verification of HUBB deployment information). Such a time frame provides USAC and the participants with a realistic time frame to sample and test location information. The Bureau reminds participants that under section 54.320(b) of the Commission's rules, all recipients of high-cost support must maintain all records required to demonstrate to auditors that the support received was consistent with the universal service high-cost program rules and must maintain such records for a minimum of 10 years from the receipt of funding, and the Bureau interprets such requirement as applicable to this process. Participants may need to produce supporting evidence or documentation that is not already in the record in this proceeding and thus should retain all evidence and documentation gathered to identify all locations, as well as any documentation supporting its methodology.

45. In response to the Bureau's request for comments, several commenters suggested specific circumstances when verification would be appropriate. For example, Hughes proposes that verifications should be triggered when a participant frequently misreports location evidence toward its defined deployment obligation or when there are significant differences between the participant's served location information and its ELAP location information. WISPA suggests that verifications are appropriate when the participant defaults or misreports served locations over 30% in any year or 15% in two years. The Bureau finds such suggestions compelling and will consider them in its verification decisions. The Bureau declines, however, to adopt any limiting criteria that would trigger verification and that might encourage participants to engage in strategic HUBB reporting or that would impliedly limit its discretion to conduct random audits.

46. If the Bureau discovers that actual locations were not reported by the participant, the Bureau will add the locations to the participant's defined deployment obligation. If the participant cannot demonstrate compliance with the readjusted defined deployment obligation, the Bureau will find the participant in performance default and subject to the Commission's default measures. In situations where it appears that the participant may have intentionally or negligently misrepresented the number of actual locations in ELAP, the Bureau may refer the case to the FCC's Enforcement Bureau for further investigation and possible forfeiture penalty. The Bureau stresses that it is not limiting these actions to the deployment or support term and reserves the right, coterminous with Commission authority to recover improperly disbursed support, to act on information about inaccurate participant filings at any future point.

47. *Participant's Information.* In the *Locations Adjustment Public Notice,* the Bureau noted similarities between served location data, which the Commission treats as non-confidential and makes publicly available, and ELAP location information. The Bureau also noted, however, important differences, namely, that unverified lists of actual locations, particularly when coupled with related evidence, could reveal competitively sensitive information regarding participants' future deployment plans or link addresses and other information to specific individuals. For this reason, the Bureau will publicly disclose only certain ELAP location information, *i.e.,* information that is generally publicly available from multiple data sources. All other information will be treated as presumptively confidential.

48. Competitors could use the confidential information filed by participants to the competitive disadvantage of the participant. Therefore, as some commenters suggest, the Bureau will permit participants to file such information pursuant to a Protective Order. In particular, as specified in more detail in the Protective Order, the Bureau restricts availability of this information as follows: (1) In the case of commercial entities having a competitive or business relationship with the participant whose confidential information it seeks and which have obtained a waiver of the definition of stakeholder, to In-House Counsel not involved in competitive decision-making, and to their Outside Counsel of Record, their Outside Consultants and experts whom they retain to assist them in this and related proceedings, and employees of such Outside Counsel and Outside Consultants; (2) to employees and representatives of commercial entities having no competitive or business relationship with the participant whose confidential information it seeks; and (3) to individuals with no competitive or business relationship with the company. The Bureau concludes that adopting such procedures in a Protective Order will give stakeholders appropriate access to participant information while protecting competitively sensitive information from improper disclosure, and that disclosure pursuant to the Protective Order thereby serves the public interest.

49. The Bureau will also restrict access to this information. Stakeholders will only be permitted to access confidential participant location data for the census blocks in which the stakeholder has demonstrated a verifiable interest in ensuring service and the bordering census blocks. Stakeholders may access information about the methods used to gather location data for all locations identified in these census blocks by participants, the entire description of the methodology provided by the participant, and the supporting evidence associated with such methodology unless such evidence clearly and exclusively relates to locations and areas outside of the relevant census blocks, *e.g.,* photographic evidence of derelict structures in a different area of the state or in a different state.

50. *Stakeholder Information.* Information submitted by the stakeholder to establish eligibility and to challenge participants' information may also be abused by participants and outside parties and raises significant privacy concerns. The Bureau sought comment on these concerns as well as the appropriate methods for addressing such concerns but received no comments on these issues. The Bureau determines that it is necessary treat all stakeholder information as presumptively confidential. All information gathered to determine the stakeholder's eligibility to participate will not be disclosed publicly or to any other participant in this process. Stakeholder contact information and challenge information will be made available to the relevant participant and other stakeholders filing challenges based in the same census block areas but stakeholders may file such information pursuant to a Protective Order that limits the use of such information.

51. Specifically, as a condition of obtaining access to stakeholder information, the participant or stakeholder agrees to use the information solely for the preparation and conduct of this proceeding before the Commission and any subsequent judicial proceeding arising directly from this proceeding and, except as provided herein, shall not use such documents or information for any other purpose, including without limitation business, governmental, or commercial purposes, or in other administrative, regulatory or judicial proceedings. The information may only be accessed by employees and representatives of the participant/stakeholder that have no competitive, business, or legal relationship with the stakeholder.

52. Participants/other stakeholders may discuss stakeholder information with the Commission and its staff and with the stakeholder's employees, representatives, and counsel, including paralegals assisting in this proceeding. Participants/other stakeholders may also discuss location data with third-party contractors involved solely in one or more aspects of organizing, filing, coding, converting, storing, or retrieving documents or data or designing programs for handling data connected with this proceeding, or performing other clerical or ministerial functions with regard to documents connected with this proceeding. This location data must not be linked in any manner to the contact information of the stakeholder.

53. The Bureau will work with USAC to create a module in the HUBB to accept and retain ELAP submissions and to control access to such information. The Bureau will also coordinate with USAC in the development of the ELAP Map. To the extent any information submitted to the module by or about individuals is a ''record,'' and to the extent that the module may function as a ''system of records,'' as those terms are defined in the Privacy Act of 1974, USAC will collect, maintain, and use the information in accordance with that law. In addition, the Bureau directs USAC to ensure that the ELAP module and map complies with all other applicable laws and Federal government guidance on privacy and security and other applicable technology requirements such as those enacted by the Federal Information Security Modernization Act (FISMA). In connection with the creation of these online record systems, the Bureau will coordinate with the Office of Management and Budget (OMB) to ensure compliance with all relevant federal rules and requirements, including the Paperwork Reduction Act of 1995.

III. Procedural Matters

A. Paperwork Reduction Act Analysis

54. This document contains new information collection requirements subject to the Paperwork Reduction Act of 1995 (PRA), Public Law 104–13. It will be submitted to the Office of Management and Budget (OMB) for review under section 3507(d) of the PRA. OMB, the general public, and other Federal agencies will be invited to comment on the new information collection requirements contained in this proceeding. In addition, the Bureau notes that pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107–198, *see* 44 U.S.C. 3506(c)(4), it previously sought specific comment on how the Commission might further reduce the information collection burden for small business concerns with fewer than 25 employees.

B. Congressional Review Act

55. The Bureau has determined, and the Administrator of the Office of Information and Regulatory Affairs, Office of Management and Budget, concurs that this rule is ''non-major'' under the Congressional Review Act. The Bureau will send a copy of this Order to Congress and the Government Accountability Office pursuant to 5 U.S.C. 801(a)(1)(A).

56. As required by the Regulatory Flexibility Act of 1980, as amended (RFA), an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the *Locations Adjustment Public Notice.* The Bureau sought written public comment on the proposals, including comment on the IRFA. The Commission

received no comments in response to the IRFA.

57. In the Order, the Bureau is implementing a process, established by the Commission in its *Phase II Auction Reconsideration Order* for successful applicants for Phase II auction support, to modify defined deployment obligations where the number of locations within the applicant's relevant bid areas within the state falls short of the number of locations that the applicant must serve within eligible areas in the state. Interested parties received notice and opportunity to comment on the Bureau's proposals for this process.

58. Pursuant to this process, a participant must submit into a module in the HUBB, location information describing the number of actual qualifying locations (and any additional prospective locations), a description of the methods it employed to identify all actual locations, and some additional supporting evidence to demonstrate that all actual locations were identified and reported. The Bureau will identify those participants that have met the prima facie standard for submitting a claim and will order the release of a limited amount of location information in a publicly available map. Outside parties will then use such information to determine whether they can and should submit challenges to specific claims for specific areas. As a condition of accessing relevant participant information and submitting a challenge, parties must demonstrate that they meet certain criteria and must sign a protective order. To make a successful challenge, challengers must submit information similar to the information submitted by participants, including location information, a method description, and some supporting evidence, although the requirements are less rigorous. Participants must also sign a protective order to access stakeholder information. They may then respond to the stakeholder's challenge. Based on the record, the Bureau will adjudicate participants' claims for relief based on a preponderance of the evidence standard, and where such standard has been met, reduce participants' obligations and support on a pro rata basis. Participants' information is subject to future verification.

59. The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the rules adopted herein. The RFA generally defines the term ''small entity'' as having the same meaning as the terms ''small business,'' ''small organization,'' and ''small governmental jurisdiction.'' In addition, the term ''small business'' has the same meaning as the term ''small business concern'' under the Small Business Act.'' A ''small business concern'' is one which: (1) Is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the SBA.

60. The Bureaus actions, over time, may affect small entities that are not easily categorized at present. The Bureau therefore describes in this document, at the outset, three comprehensive small entity size standards that could be directly affected herein. First, while there are industry specific size standards for small businesses that are used in the regulatory flexibility analysis, according to data from the SBA's Office of Advocacy, in general a small business is an independent business having fewer than 500 employees. These types of small businesses represent 99.9% of all businesses in the United States which translates to 28.8 million businesses.

61. Next, the type of small entity described as a ''small organization'' is generally ''any not-for-profit enterprise which is independently owned and operated and is not dominant in its field.'' Nationwide, as of August 2016, there were approximately 356,494 small organizations based on registration and tax data filed by nonprofits with the Internal Revenue Service (IRS).

62. Finally, the small entity described as a ''small governmental jurisdiction'' is defined generally as ''governments of cities, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand.'' U.S. Census Bureau data from the 2012 Census of Governments indicate that there were 90,056 local governmental jurisdictions consisting of general purpose governments and special purpose governments in the United States. Of this number there were 37, 132 General purpose governments (county, municipal and town or township) with populations of less than 50,000 and 12,184 Special purpose governments (independent school districts and special districts) with populations of less than 50,000. The 2012 U.S. Census Bureau data for most types of governments in the local government category show that the majority of these governments have populations of less than 50,000. Based on this data the Bureau estimates that at least 49,316 local government jurisdictions fall in the category of ''small governmental jurisdictions.''

63. Commenters, including small entities, wishing to participate in this process would be required to comply with the listed reporting and evidentiary standards. Such standards include location information, methodology descriptions, and supporting evidence in specific formats. Such information must be submitted by specific deadlines. In addition, parties may file challenges if they submit information demonstrating that they qualify as a relevant stakeholder. Relevant stakeholder's challenges must include information like that submitted by the participant. Participants may reply to stakeholder challenges.

64. The small entities that may be affected are Wireline and Wireless Providers, Broadband internet Access Service Providers, Satellite Telecommunications, Electric Power Generators, Transmitters, and Distributors, and All Other Telecommunications.

65. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): ''(1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) and exemption from coverage of the rule, or any part thereof, for small entities.''

66. This process considers the resources available to small entities by permitting participants flexibility in choosing how to identify locations within eligible areas as well as discretionary control over the amount and nature of the supporting evidence that they will submit. Small entities may also present evidence regarding the available geocoding and other resources necessary to meet the Commission's prima facie evidentiary standards. Further, by participating in this process at the beginning of the term, small entities will be able to more effectively plan their network deployments.

IV. Ordering Clauses

67. Accordingly, *it is ordered,* pursuant to the authority contained in sections 254 of the Communications Act of 1934, as amended, 47 U.S.C. 254, and the authority delegated in §§ 0.91 and 0.291 of the Commission's rules, 47 CFR 0.91, 0.291, and §§ 1.1 and 1.427 of the Commission's rules, 47 CFR 1.1, 1.427, that the Order *is adopted.*

68. *It is further ordered* that, pursuant to § 1.103 of the Commission's rules, 47

CFR 1.103, the Order *shall become effective* thirty (30) days after publication of the text or summary thereof in the **Federal Register**, except for those rules and requirements involving Paperwork Reduction Act burdens, which shall become effective immediately upon announcement in the **Federal Register** of OMB approval.

Federal Communications Commission.

Kirk Burgee,

Chief of Staff, Wireline Competition Bureau.

[FR Doc. 2019–28501 Filed 1–10–20; 8:45 am]

BILLING CODE 6712–01–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 218

[Docket No. 191211–0106]

RIN 0648–BI85

Taking and Importing Marine Mammals; Taking Marine Mammals Incidental to the U.S. Navy Training and Testing Activities in the Atlantic Fleet Training and Testing Study Area

Correction

In rule document 2019–27098, appearing on pages 70712 through 70794, in the issue of Monday, December 23, 2019, make the following correction:

On page 70719, in Table 2—Naval Air Systems Command Testing Activities Analyzed For Seven-Year Period in The AFTT Study Area, in the 5th column, in the sixth line down, ''234'' should read ''928''.

[FR Doc. C1–2019–27098 Filed 1–10–20; 8:45 am]

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Proposed Rules

Federal Register
Vol. 85, No. 8
Monday, January 13, 2020

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.

DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

9 CFR Part 201

[Document Number AMS–FTTP–18–0101]

RIN 0581–AD81

Undue and Unreasonable Preferences and Advantages Under the Packers and Stockyards Act

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Proposed rule.

SUMMARY: Comments are invited on the proposed establishment of a new regulation under the Packers and Stockyards Act, which protects fair trade, financial integrity, and competitive marketing for livestock, meat, and poultry. The proposed regulation would specify criteria the Secretary of Agriculture would consider when determining whether an undue or unreasonable preference or advantage has occurred in violation of that Act. Establishment of these criteria is required by a provision of the Food, Conservation, and Energy Act of 2008 (2008 Farm Bill).

DATES: Comments on the proposed rule must be received by March 13, 2020.

ADDRESSES: Interested persons are invited to submit written comments concerning this proposed rule. All comments must be submitted through the Federal e-rulemaking portal at *http://www.regulations.gov* and should reference the document number and the date and page number of this issue of the **Federal Register**. All comments submitted in response to this proposed rule will be included in the record and will be made available to the public. Please be advised that the identity of the individuals or entities submitting comments will be made public on the internet at the address provided above.

FOR FURTHER INFORMATION CONTACT: S. Brett Offutt, Chief Legal Officer/Policy Advisor; Packers and Stockyards Division, USDA AMS Fair Trade Practices Program; phone: 202–690–4355; or email: *S.Brett.Offutt@ams.usda.gov.*

SUPPLEMENTARY INFORMATION: Section 202(b) of the Packers and Stockyards Act, 1921 (the Act), as amended (7 U.S.C. 181 *et seq.*), specifies that it is unlawful for any packer, swine contractor, or live poultry dealer to either make or give any undue or unreasonable preference or advantage to any particular person or locality in any respect. In administering this provision of the Act, the United States Secretary of Agriculture (Secretary) determines whether the conduct of regulated entities is considered a violation of the Act.

In the past, each determination has been analyzed using general principles in a case-by-case basis, exercising the regulatory flexibility Congress provided when it passed the Act. Provisions of the 2008 Farm Bill (Public Law 110–234) require the Secretary to promulgate regulations establishing criteria the Secretary would consider in determining whether an undue or unreasonable preference or advantage has occurred in violation of the Act. *See* Sec. 11006(1). The Secretary originally delegated responsibility for establishing the required criteria to the Grain Inspection, Packers and Stockyards Administration (GIPSA), which subsequently merged with the Agricultural Marketing Service (AMS). AMS now administers the regulations under the Act and has undertaken this rulemaking. To meet the statutory requirement, AMS proposes adding a new § 201.211 to 9 CFR part 201—Regulations Under the Packers and Stockyards Act (P&S regulations), retaining the necessarily flexible framework for the Secretary's determinations, while providing criteria that supports the transparency of the Secretary's determinations. Accordingly, the regulated industry and the public will have a reference to the general framework that AMS will use to determine whether there is an unlawful preference or advantage under section 202(b) of the Act.

Proposed § 201.211 would require the Secretary to consider one or more of four specified criteria when determining whether any undue or unreasonable preference or advantage has been given or made to any particular person or locality in any respect in violation of section 202(b) of the Act. The Secretary would not be limited to considering only the four proposed criteria, but could also take other factors into consideration as appropriate on a case-by-case basis. We discuss each of the four proposed criteria later in this document.

A 60-day comment period is provided to allow interested persons to respond to this proposed rule. All written comments received in response to this proposed rule by the date specified will be considered.

Background

The Packers and Stockyards Division (PSD) of AMS's Fair Trade Practices Program oversees day-to-day administration of the P&S regulations and is called upon to investigate alleged violations of section 202(b) of the Act, many related to contractual dealings with livestock producers, swine production contract growers, and poultry growers. Other entities, including retailers and the public, can also be harmed by violations of section 202(b). Difficulty lies in determining whether particular instances of preferences or advantages made or given to one or more persons or localities would be undue or unreasonable and violations of the Act.

As mentioned above, the 2008 Farm Bill directs the Secretary to establish criteria the Secretary will consider in determining whether an undue or unreasonable preference or advantage has occurred in violation of the Act. At the time the 2008 Farm Bill was enacted, what is now PSD operated within GIPSA. GIPSA undertook the responsibility for developing criteria for consideration. In June 2010, GIPSA published a proposed rule (75 FR 35338; June 22, 2010) that was never finalized, due to Congressional prohibitions included in the Consolidated Appropriations Acts for fiscal years 2012 through 2015, which disallowed any further work on the new criteria rulemaking. *See* Sec. 721, Public Law 112–55, November 18, 2011; Sec. 742, Public Law 113–6, March 26, 2013; Sec. 744, Public Law 113–76, January 17, 2014; and Sec. 731, Public Law 113–235, December 16, 2014. GIPSA resumed its efforts to promulgate the required criteria in December 2016 with publication of a second proposed rule

(81 FR 92703; December 20, 2016), but decided to take no further action on that proposal (82 FR 48603; October 18, 2017).

The Secretary is issuing this NPRM to establish criteria to consider when determining whether a violation of section 202(b) of the Act has occurred as required by the 2008 Farm Bill. The proposed criteria would provide an analytical framework to evaluate whether a violation may have occurred. This proposed rule addresses a situation occasionally encountered in the industry, namely the need to determine whether a preference or advantage in a specific instance is undue or unreasonable. AMS intends the proposed new regulation to establish a framework for consideration of potential violations of section 202(b) of the Act, to bring transparency to the Secretary's determination process for the industry.

Proposed Provisions

This proposed rule would establish criteria the Secretary would consider in determining whether an undue or unreasonable preference or advantage has been made or given in violation of the Act, and therefore establish an appropriate framework for analysis. It is not unusual for buyers or sellers of livestock or poultry to receive advantages. For example, as between two competing sellers, one may receive a better price from a buyer. The Act only prohibits those preferences or advantages that are undue or unreasonable. It follows that there are legitimate reasons for the existence of preferences or advantages that are not undue or unreasonable. Reasonable differences in contract terms may result from negotiations over particular interests between the parties. It is not the purpose of the Act to interfere with contract negotiations or to upset the traditional principles of freedom of contract. Nor does the Act statutorily create an entitlement to obtain the same type of contract offered to other producers or growers. However, greater clarity on the terms associated with grower contracts could increase transparency in the marketplace and reduce the claims of undue or unreasonable preference.

Under proposed § 201.211, the Secretary would consider one or more specific criteria when determining whether a packer, swine contractor, or live poultry producer has made or given any undue or unreasonable preference or advantage to any particular person or locality in any respect. Proposed § 201.211 lists four criteria for consideration and would provide that the Secretary not be limited to consideration of those four criteria.

Under proposed § 201.211(a), the Secretary would consider whether the preference or advantage under consideration cannot be justified on the basis of a cost savings related to dealing with different producers, sellers, or growers. Under proposed § 201.211(b), the Secretary would consider whether the preference or advantage in question cannot be justified on the basis of meeting a competitor's prices. Under proposed § 201.211(c), the Secretary would consider whether the preference or advantage in question cannot be justified on the basis of meeting other terms offered by a competitor. Under proposed § 201.211(d), the Secretary would consider whether the preference or advantage in question cannot be justified as a reasonable business decision that would be customary in the industry.

Historically, the Secretary has considered some of these criteria and other factors similar to these in determining whether or not to bring an enforcement action regarding an alleged violation of the Act. AMS has based its proposal on the experience of PSD, which has administered the Packers and Stockyards Act and regulations and understands what complaints are commonly made regarding compliance. AMS is proposing this list of criteria that the Secretary would consider, but it is also proposing that the Secretary have the flexibility to consider other criteria that may be relevant on a case-by-case basis. In doing so, AMS is attempting to strike a balance between the interests of all segments of the industry. On the one hand, AMS is charged with protecting producers, growers, retailers, and others, including the public, from potential harm resulting from undue or unreasonable preferences or advantages. On the other hand, AMS recognizes that among the numerous complaints examined in the past, many preferences and advantages made or given to individuals or groups in the industry have been determined to be lawful, and relatively few have been determined to be undue or unreasonable.

Legitimate disparities in contract terms could be attributed to reasonable business negotiations between contracting parties. For example, price differences offered to different sellers could reflect differences in transportation costs to a slaughter facility or could reflect one producer's ability and willingness to supply livestock in the early morning hours to start the day's processing while others cannot. Disparate contract terms are not considered undue or unreasonable just because they are not identical.

For example, a live poultry dealer pays a premium to one poultry grower who agrees to use experimental vaccines, thus putting the grower at increased risk of financial loss if the vaccine proves to be unsuccessful and the birds die or do not grow well. Based on the criteria in proposed § 201.211, the apparent preference or advantage might be justified on the basis of the company saving the expense of testing the vaccines though other means, and the premium paid to the grower for providing the extra service of testing vaccines and for accepting greater financial risk might not be considered undue or unreasonable. In another example, a livestock packer pays higher prices later in the day or week after competitors have raised the market price. Based on the criteria in proposed § 201.211, the apparent preference or advantage might be justified as necessary to meet competitors' prices, and the higher price might not be considered undue or unreasonable. Finally, where a live poultry dealer's competitors have offered long term contracts to their growers, the poultry dealer finds that he must offer comparable terms to his growers in the same locality. Based on the criteria in proposed § 201.211, the apparent preference given to growers in that locality is unlikely to be considered undue or unreasonable because the difference in contract terms might be justified by the need to meet a competitor's other contract terms in that locality.

On the other hand, some preferences or advantages might be considered undue or unreasonable if they are so unfair that they would tend to restrain trade, creating such excessively favorable conditions for one or more persons that their competitors would have reduced chances of business success. For instance, premiums offered to one person or locality but not offered to other persons or localities similarly situated could constitute a violation of the Act. A livestock packer negotiating preferential live basis prices with only one favored livestock supplier and not with similarly situated suppliers, may be in violation of the Act. PSD would examine the proposed criteria and likely conclude that the packer cannot justify its actions on the basis of cost savings, meeting a competitor's prices, meeting other terms offered by a competitor, or as a reasonable business decision.

Under proposed § 201.211(a) through (c), the Secretary would consider whether preferences or advantages made or given to one or more persons are

based on cost savings related to dealing with different producers, sellers, or growers, or the need to meet a competitor's prices or other contract terms. For example, a live poultry dealer offering a higher base price to a favored grower, but not to other growers in the same complex with the same housing types, may be in violation of the Act. The Secretary would consider the proposed criteria. Under criterion (a), there would be no cost savings in a higher base price. But under criteria (b) and (c), the Secretary would consider whether the higher base price meets a competitor's price or other terms. If the reason for giving the favored grower the higher price cannot be justified by meeting a competitor's price or other terms, then the higher base price may be an undue or unreasonable preference or advantage.

Under proposed 201.211(d), the Secretary would consider whether the preference or advantage cannot be justified as a reasonable business decision that is customary in the industry. A packer, swine contractor, or live poultry dealer may have a legitimate business reason for treating some persons or groups more favorably than others. For example, it is customary in the cattle industry for the packer to pay freight expenses on live weight purchases, but not on carcass weight purchases. Based on the criteria in proposed § 201.211, it is unlikely that the apparent preference or advantage to live weight cattle sellers in that situation would be considered undue or unreasonable because it could be justified as a reasonable business decision that is customary in the industry. In another example, a live poultry dealer may pay a premium to growers who construct new poultry houses or update their houses with the latest technology. Based on the criteria in proposed § 201.211, such a premium might be justified as a reasonable business decision that would be customary in the industry, so it is unlikely that the Secretary would determine the preference or advantage to be undue or unreasonable.

Live poultry dealers, packers, and swine contractors should enter into contracts that do not discriminate, unless the differences are due to cost, meeting competitors prices, or normal industry standards. Preferences that are not grounded in ordinary business considerations may be based upon reasons of unjust advantage. AMS believes these criteria promote honest competition in the supply chain, instead of advantages that could result from bribery or other influences. Therefore, AMS focused on four criteria that promote honest competition: Cost savings, meeting a competitor's prices, meeting other terms offered by a competitor, and other reasonable business reasons for preference and advantages.

While the agency expects a short-term increase in the cost of review for livestock producers, poultry growers, and regulated entities in existing contracts, in the long-term, innovative contracts should be less costly to negotiate even when those contracts provide for preferences and advantages. Because this framework of criteria could be understood in the context of ordinary and customary business decisions, regulated entities may more easily review contracts for compliance with the Act.

By following a framework of criteria that promote fair dealing based in rational decision-making, AMS promotes protection for producers and localities that might be otherwise have been unable to obtain preferential contract terms or price advantages. This, therefore, should also improve the negotiating position of growers and producers.

AMS expects that adding the proposed criteria described above to the P&S regulations would provide a framework in which the Secretary can consider potential violations of the Act, help the industry understand what the Secretary would consider when evaluating violation claims, and fulfill the Congressional mandate to establish criteria for making determinations regarding potentially unacceptable conduct under the Act.

Required Impact Analyses

Executive Orders 12866, 13563, and 13771 and the Regulatory Impact Analysis

AMS is issuing this rule in conformance with Executive Orders 12866 and 13563, which direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits, including potential economic, environmental, public health and safety effects, distributive impacts, and equity. Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility.

In the development of this proposed rule, AMS determined to take a different approach to developing the necessary criteria than previous rulemaking efforts. AMS determined that including the proposed criteria as part of the framework for consideration of preferences and advantages in buyer-seller contracts would best serve the needs of the industry and fulfill the 2008 Farm Bill mandate. AMS expects the proposed new regulation would bring transparency to considerations of potential violations of section 202(b) of the Act and certainty to industry members forging contracts related to the buying and selling of poultry and livestock. The proposed rule is not expected to provide any environmental, public health, or safety benefits.

This proposed rule has been determined to be significant for the purposes of Executive Order 12866 and therefore has been reviewed by OMB. This proposed rule is expected to be an Executive Order 13771 regulatory action. Details on the estimated costs of this proposed rule can be found in the rule's economic analysis.

AMS is proposing a new § 201.211, which would provide four criteria in response to requirements of the 2008 Farm Bill for the Secretary of Agriculture to consider in determining whether a packer, swine contractor, or live poultry dealer has engaged in conduct resulting in an undue preference or advantage to any particular person or locality in any respect in violation of section 202(b) of the Act. Based on its familiarity with the industry, PSD prepared an economic analysis of proposed § 201.211 as part of the regulatory process. The economic analysis presents the cost-benefit analysis of proposed § 201.211. PSD then discusses the impact on small businesses.

This proposed rule is independent of previous rulemaking. PSD reviewed certain cost projections developed in conjunction with previous rulemaking in analyzing the regulatory impact of this proposed rule. All costs and benefits described in this economic analysis pertain to the language in this proposed rule.

Regulatory Impact Analysis

The 2008 Farm Bill requires the Secretary of Agriculture to promulgate a regulation establishing criteria that the Secretary will consider in determining whether an undue or unreasonable preference or advantage has occurred in violation of section 202(b) of the Act. This rulemaking is to fulfill that requirement.

Responsibility for establishing the required criteria was originally delegated to the Grain Inspection, Packers and Stockyards Administration (GIPSA), which subsequently merged with AMS. AMS now administers the

regulations under the Act and has undertaken this rulemaking.

For this economic analysis, PSD considered the impact of three alternatives for this proposed rule. PSD considered the impact of maintaining the status quo, the impact of adopting regulatory language that had been proposed in 2016, and the impact of adopting the current proposed language.

PSD considered the impact of taking no further action on a previous version of § 201.211 GIPSA [1] had proposed on December 20, 2016.[2] GIPSA subsequently provided notice in the **Federal Register** on October 18, 2017,[3] that it would take no further action on the 2016 proposed rule. Taking no action would result in no additional out-of-pocket costs to businesses in the livestock and poultry industries but would not fulfill the requirements of the 2008 Farm Bill.

AMS could have proposed the same regulatory language proposed as in the 2016 proposed rule. The 2016 proposed rule contained six criteria the Secretary would consider in determining whether conduct or action constitutes an undue or unreasonable preference or advantage and a violation of section 202(b) of the Act. To determine the impact of adopting the 2016 proposed rule, PSD looked to the estimated costs of the rule contained in the economic analysis discussed in detail in the notice of proposed rulemaking. The total first year costs of the proposed rule in 2016 were $15.37 million.

This current rulemaking represents a different approach than previous rulemakings that would establish an analytical framework for considering whether a violation of section 202(b) of the Act has occurred. The proposed rule includes new criteria to bring transparency to the determination process for the industry. PSD estimates that the total first year costs of this proposed rule are $9.67 million.

Introduction

As required by the 2008 Farm Bill, proposed § 201.211 specifies criteria the Secretary would consider when determining whether an undue or unreasonable preference or advantage has occurred in violation of section 202(b) of the Act. The proposed criteria provide a framework to analyze whether a particular person or locality receives an undue or unreasonable preference or advantage as compared to other similarly situated persons or localities. AMS expects the proposed four criteria would clarify the legal standard for the public and promote honest competition, fair dealing, and improve the negotiating position of growers and producers.

Cost-Benefit Analysis

PSD has estimated the costs and benefits of the proposed rule assuming the final rule is published and effective in May 2020. The costs and benefits of the proposed rule are discussed in order below.

A. Cost Estimation

PSD believes that the costs of proposed § 201.211 would mostly consist of the direct costs of reviewing and, if necessary, re-writing marketing and production contracts to ensure that packers, swine contractors, and live poultry dealers are not providing an undue or unreasonable preference or advantage to any livestock producer, swine production contract grower, or poultry grower compared to other similarly situated person or localities. PSD also believes that proposed § 201.211 may lead to additional litigation costs to test court precedents relating to section 202(b) violations. In past cases, courts have considered whether a specific preference or advantage would be a violation of the Act if the preference or advantage did not harm competition. However, AMS does not intend to create criteria that conflict with case precedent, so PSD expects that court precedents relating to competitive harm are likely to remain unchanged.

Proposed § 201.211 does not impose any new requirements on regulated entities, but would serve as guidance for their compliance with section 202(b) of the Act. Since the proposed rule would clarify the Secretary's consideration of unlawful undue or unreasonable preferences or advantages, regulated entities should face less risk of violating the Act. Because of this reduced risk, and the fact that PSD does not expect court precedents requiring the demonstration of harm or potential harm to competition to change, PSD does not expect the proposed rule to result in a decrease in the use of alternative marketing agreements [4] (AMAs), poultry tournament systems, or other incentive payment systems, or decreased economic efficiencies in the cattle, hog, and poultry industries. Additionally, PSD does not expect the proposed rule to inhibit the ability of regulated entities and producers and growers to develop and enter into mutually advantageous contracts.

To estimate costs, PSD divided costs into two major categories, direct and indirect costs. In addition, PSD expects there are two direct costs: Administrative costs and litigation costs.

With respect to direct costs, administrative costs for regulated entities would include items such as review of marketing and production contracts, additional record keeping,[5] and all other associated administrative office work to demonstrate that they do not provide an undue or unreasonable preference or advantage to any livestock producer, swine production contract grower, or poultry grower compared to other similarly situated person or localities.

Litigation costs for the livestock and poultry industries would initially increase while precedent confirming decisions are established. However, since court precedents have generally required the demonstration of harm to competition, PSD expects the increased litigation costs would decline after initial court decisions. Once precedents are confirmed, PSD expects additional litigation to decline.

With respect to indirect costs, those costs include costs caused by changes in supply and/or demand and any resulting efficiency losses in the national markets for beef, pork, and chicken and the related input markets for cattle, hogs, and poultry resulting from the direct costs of the proposed rule.

1. Direct Costs—Administrative Costs

To estimate administrative costs of the proposed rule, PSD relied on its experience reviewing contracts and other business records commonly maintained in the livestock and poultry industries for compliance with the Act and regulations. PSD has data on the number of production contracts between swine production contract growers and

[1] On November 14, 2017, Secretary of Agriculture, Sonny Perdue, issued a memorandum eliminating GIPSA as a standalone agency and transferred the regulatory authority for the Act to AMS. PSD has day-to-day oversight of the Packers and Stockyards activities in AMS.

[2] **Federal Register**, Volume 81, No. 244, pages 92703–92723.

[3] **Federal Register**, Volume 82, No. 200, pages 48603–48604.

[4] AMAs are marketing contracts, where producers market their livestock to a packer under a verbal or written agreement. Pricing mechanisms vary across AMAs. Some rely on a spot market for at least one aspect of their prices, while others involve complicated pricing formulas with premiums and discounts based on carcass merits. The livestock seller and packer agree on a pricing mechanism under AMAs, but usually not on a specific price.

[5] There are no additional mandatory record keeping requirements in the proposed rule. PSD expects that regulated entities may opt to keep additional records to justify advantages or preferences to demonstrate compliance with the proposed rule in case of a PSD investigation or private litigation action.

swine contractors and poultry growers and live poultry dealers. PSD estimated the number of cattle marketing contracts between producers and packers based on the number of feedlots and the percentage of livestock procured under AMAs. PSD then multiplied hourly estimates of the administrative functions of reviewing and revising contracts by average hourly labor costs for administrative, management, and legal personnel to arrive at the total estimated administrative costs. PSD measured all costs in constant 2016 dollars in accordance with guidance on complying with E.O. 13771.[6]

Since packers, swine contractors, and live poultry dealers would likely choose to review their contracts as a precautionary measure to ensure that they are not engaging in conduct or action that in any way gives an undue or unreasonable preference or advantage to any livestock producer, swine production contract grower, or poultry grower, PSD estimates that the regulated entities would review each contract or each contract type once and would renegotiate any contracts that contain language that could be considered a violation of section 202(b) of the Act.

One may view this estimate as an upper bound to the direct cost of the proposed rule, as not every packer, swine contractor, or live poultry dealer would choose to conduct such a review. Some may choose to ''wait and see'' what effect, if any, the rule had on the industry, and if courts ruled on it in any way that would warrant such a review of their contracts.

Based on PSD's experience, it developed estimates for regulated entities of the number of hours for attorneys and company managers to review and revise marketing and production contracts and for administrative staff to make changes, copy, and obtain signed copies of the contracts. For poultry contracts, PSD estimates that each unique contract type would require one hour of attorney time to review and rewrite a contract, two hours of company management time, and for each individual contract, one hour of administrative time, and one hour of additional record keeping time.[7] PSD estimates that each of the 93 live poultry dealers who report to PSD rely on 10 unique contract types on average. PSD data indicates that there are 24,101 individual poultry growing contracts. PSD estimates that each of the 237 hog packers has 10 marketing agreements. The 2017 Census of Agriculture (Ag. Census)[8] indicates that the universe of swine production contracts in the U.S. is 8,557. For hog production and marketing contracts, PSD estimates that each production contract and marketing agreement would require one-half hour of attorney time to review and rewrite a contract, one hour of company management time, one hour of administrative time, and one hour of additional record keeping time. For cattle processors, PSD estimates that each of the estimated 1,099 marketing agreements would require one hour of attorney time to review and rewrite a contract, two hours of company management time, one hour of administrative time, and one hour of additional record keeping time.[9]

PSD multiplied estimated hours to conduct these administrative tasks by the average hourly wages for managers at $62/hour, attorneys at $84/hour, and administrative assistants at $36/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics to arrive at its estimate of contract review costs for regulated entities.[10]

PSD recognizes that contract review costs would also be borne by livestock producers, swine production contract growers, and poultry growers. PSD estimates that each livestock producer, swine production contract grower, and poultry grower would, in its due course of business, spend one hour of time reviewing a contract or marketing agreement and would spend one-half hour of its attorney's time to review the contract. As with the regulated entities, one may view this estimate as an upper bound to the direct cost of the proposed rule, as not every producer or grower would choose to conduct such a review. Some may choose to ''wait and see'' what effect, if any, the rule had on the industry, and if courts ruled on it in any way that would warrant such a review of their contracts.

PSD multiplied one hour of livestock producer, swine production contract grower, and poultry grower management time and one-half hour of attorney time to conduct the marketing and production contract review by the average hourly wages for attorneys at $84/hour and managers at $62/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics to arrive at its estimate of contract review costs for livestock producers, swine contract growers, and poultry growers. PSD then applied this cost to the estimated 1,099 cattle marketing contracts, 2,370 hog marketing contracts, 8,557 hog production contracts, and 24,101 poultry growing contracts that have been reported to PSD.

After determining the administrative costs to both the regulated entities and those they contract with, PSD added the administrative costs of the regulated entities and the livestock producers, swine production contract growers, and poultry growers together to arrive at the first-year total estimated administrative costs attributable to the regulation. A summary of the first-year total estimated administrative costs for proposed § 201.211 appear in the following table:

TABLE 1—FIRST-YEAR ADMINISTRATIVE COSTS

Regulation	Cattle ($ millions)	Hogs ($ millions)	Poultry ($ millions)	Total ($ millions)
201.211	$0.42	$3.05	$4.42	$7.89

The first-year total administrative costs are $7.89 million for proposed § 201.211, and include costs for cattle, hogs, and poultry because packers, swine contractors, live poultry dealers, livestock producers, swine production contract growers, and poultry growers would conduct administrative functions of contract review and record keeping in response to the regulation. The administrative costs are the highest for poultry, followed by hogs and cattle. This is due to the greater prevalence of contract growing arrangements in the poultry industry.

[6] *https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/memoranda/2017/M-17-21-OMB.pdf*

[7] Again, there are no additional mandatory record keeping requirements in the proposed rule.

[8] *https://www.nass.usda.gov/Publications/AgCensus/2017/Full_Report/Volume_1,_Chapter_1_US/usv1.pdf*

[9] Ibid.

[10] All salary costs are based on mean annual salaries for May 2018, adjusted for benefit costs, set to an hourly basis, and converted in to constant 2016 dollars. *http://www.bls.gov/oes/*. Accessed on April 9, 2019.

2. Direct Costs—Litigation Costs

In considering the costs of the rules it proposed in 2016, GIPSA performed an in-depth analysis of litigation costs expected as a result of the package of four proposed new regulations.[11] GIPSA estimated the total costs of litigating a case alleging violations of the P&S Act. The main costs are attorney fees to litigate a case in a court of law. The cost of litigating a case includes the costs to all parties including the respondent and the USDA in a case brought by the USDA and the costs of the plaintiff and the defendant in the case of private litigation.

To estimate litigation costs for the 2016 proposed rules, GIPSA examined the actual cases decided under the P&S Act from 1926 to 2014 as reported by the National Agricultural Law Center at the University of Arkansas.[12] The litigation costs estimated in the 2016 proposed rules are measured in constant 2016 dollars and are for regulated entities, producers, and growers. The 2016 analysis of litigation costs estimated that the interim final rule at § 201.3(a) was the primary source of litigation costs and that the litigation costs for all four proposed rules were counted under § 201.3(a).[13] The 2016 analysis split out the estimated litigation costs between sections 202(a) and 202(b).

The National Agricultural Law Center at the University of Arkansas has not reported any additional cases decided under the P&S Act since 2015. Since proposed § 201.211 would establish criteria for violations of section 202(b) and there has not been any new recent litigation reported by the National Agricultural Law Center at the University of Arkansas, PSD used the estimated litigation costs associated with section 202(b) from the 2016 proposed rules as the starting point for this proposed rule.

The 202(b) estimated litigation costs serve as an upper boundary of estimated costs since the estimates assumed that § 201.3(a) and § 201.211 would both be promulgated. PSD estimates that there would be additional litigation when § 201.211 becomes effective, even in the absence of § 201.3(a). Therefore, PSD uses the following 202(b) litigation costs estimates in Table 14 from the 2016 proposed rule as the estimated first-year litigation costs assuming the rule becomes effective in May 2020.[14]

TABLE 2—PROJECTED FIRST-YEAR LITIGATION COSTS

Section 202(b) of the Act	Cattle ($ millions)	Hog ($ millions)	Poultry ($ millions)	Total ($ millions)
Total	$0.24	$0.04	$1.49	$1.77

PSD expects proposed § 201.211 would result in an additional $1.77 million in litigation costs in the first full year after the rule becomes effective. Using the number of complaints PSD has received from industry participants as an indicator, PSD estimates that the majority of the litigation will be in the poultry industry. Most of the complaints concerning undue or unreasonable preferences that PSD has received since 2009 have come from the poultry industry.

3. Total Direct Costs

The total first-year direct costs of proposed § 201.211 are the sum of administrative and litigation costs from above and are summarized in the following table.

TABLE 3—FIRST YEAR DIRECT COSTS [15]

Cost type	Cattle ($ millions)	Hogs ($ millions)	Poultry ($ millions)	Total ($ millions)
Admin Costs	$0.42	$3.05	$4.42	$7.89
Litigation Costs	0.24	0.04	1.49	1.77
Total Direct Costs	0.66	3.09	5.91	9.67

PSD estimates that the total direct costs of proposed § 201.211 to be $9.67 million. As the above table shows, the costs are highest for the poultry industry, followed by hogs and cattle. The primary reason is the high utilization of growing contracts and the corresponding higher estimated administrative costs in the poultry industry. To put this direct cost in perspective, the actual impact on retail prices from these direct costs would be less than one one-hundredth of a cent.

4. Indirect Costs

PSD estimates that the indirect costs of proposed § 201.211 on the cattle, hog, and poultry industries are zero. For the purposes of this analysis, indirect costs are social welfare losses due to any potential price and output changes from the direct costs of proposed rule and in are addition to the direct costs (administrative and litigation costs) on regulated entities, producers, and growers who are directly impacted by the proposed rule. The economy will experience indirect costs, for example, if the proposed rule causes packers and live poultry dealers to reduce production, increasing the price of meat products and reducing the amount of meat consumed by consumers.

As previously discussed, the regulation clarifies the Secretary's consideration of whether a conduct or action constitutes an undue or unreasonable preference or advantage. PSD does not expect, therefore, that proposed § 201.211 would result in a decreased use of AMAs, use of poultry grower ranking systems or other incentive pay, reduced capital formation, inhibit development of new

[11] The four proposed rules were published on December 20, 2016, in Volume 81, No. 244 of the **Federal Register**.

[12] http://nationalaglawcenter.org/aglaw-reporter/case-law-index/packers-and-stockyards.

[13] The USDA withdrew § 201.3(a) on October 18, 2017, in Volume 82, No. 200 of the **Federal Register**.

[14] **Federal Register**, Volume 81, No. 244, page 92580.

[15] The detail in this table and other tables in this analysis may not add to the totals due to rounding.

contracts, or decreased economic efficiencies in the livestock, meat and poultry industries. Accordingly, PSD does not project indirect costs resulting from decreases in AMAs, reduced capital, efficiency losses, or lost consumer and producer surplus. Indirect costs that could theoretically be anticipated are due to shifts in industry demand and supply curves resulting from the increases in industry direct costs attributable to the proposed rule. These shifts may result in quantity and price changes in the retail markets for beef, pork, and poultry, and the related input markets for cattle, hogs, and poultry. However, litigation costs are unrelated to the quantity of production—in other words, they are not marginal costs—so it is not appropriate to include them in the amount of a supply curve shift. Contract reviews and revisions are somewhat related to production quantity, but even they are less than fully compelling as a component of marginal cost. These nuances are not reflected in the assessment that follows, and thus it should be interpreted as a bounding exercise.

To calculate an upper bound on this type of indirect costs based on supply curves shifting, PSD modeled the impact of the increase in direct costs of implementing proposed § 201.211 in a Marketing Margins Model (MMM) framework.[16] The MMM allows for the estimation of changes in consumer and producer prices and quantities produced caused by changes in supply and demand in the retail markets for beef, pork, and poultry and the input markets for cattle, hogs, and poultry.

PSD modeled—again, as a bounding exercise—the indirect costs as an inward (or upward) shift in the supply curves for beef, pork, and poultry. This has the effect of increasing the equilibrium prices and reducing the equilibrium quantity produced. This also has the effect of reducing the derived demand for cattle, hogs, and poultry, which causes a reduction in the equilibrium prices and quantity produced. Economic theory suggests that these shifts in the supply curves and derived demand curves will result in price and quantity impacts and potential dead weight losses to society.[17]

To estimate the output and input supply and demand curves for the MMM, PSD constructed linear supply and demand curves around equilibrium price and quantity points using price elasticities of supply and demand from the GIPSA Livestock Meat and Marketing Study and from USDA's Economic Research Service.[18] With the supply curves established from this data, PSD then shifted the supply curves for beef, pork, and chicken up by the amount of the increase in direct costs for each industry. PSD calculated the new equilibrium prices and quantities in the input markets resulting from the decreases in derived demand that result from higher direct costs. This allows for the calculation of the indirect cost from the lower relative quantity produced at the relatively higher price when the industry's direct costs increase.

The calculation of an upper bound on the price impacts from the increases in direct costs from proposed § 201.211 resulted in price increases of less than one one-hundredth of a cent in retail prices for beef, pork, and poultry. This is because the increase in direct costs is very small in relation to total industry costs.[19] The result is that the price and quantity effects from the increases in direct costs are indistinguishable from zero and, therefore, PSD concludes that the indirect costs of proposed § 201.211 for each industry are also zero.

5. Total Costs

PSD added all direct costs to the indirect costs (equal to zero), to arrive at the estimated total first-year costs of proposed § 201.211. The total first-year costs are summarized in Table 4.

TABLE 4—TOTAL FIRST YEAR COSTS

Cost type	Cattle ($ millions)	Hogs ($ millions)	Poultry ($ millions)	Total ($ millions)
Admin Costs	$0.42	$3.05	$4.42	$7.89
Litigation Costs	0.24	0.04	1.49	1.77
Total Direct Costs	0.66	3.09	5.91	9.67
Total Indirect Costs	0.00	0.00	0.00	0.00
Total Costs	0.66	3.09	5.91	9.67

PSD estimates that the total costs would be $9.67 million in the first year of implementation.

6. Ten-Year Total Costs

To arrive at the estimated ten-year administrative costs of proposed § 201.211, PSD estimates that in each of the first five years, 20 percent of all contracts will either expire and need to be renewed each year or new marketing and production contracts will be put in place each year. While PSD expects the costs of reviewing and revising, if necessary, each contract would remain constant in the first five years, it expects the administrative costs would be lower after the first year because the direct administrative costs of reviewing and revising contracts would only apply to the 20 percent of expiring contracts or new contracts. PSD estimates that in the second five years, the direct administrative costs of reviewing and revising contracts would decrease by 50 percent per year as the contracts would already reflect language modifications, if any, necessitated by implementation of the regulation. PSD estimates that after ten years, the direct administrative costs would return to where they would have been absent the rule, and the additional administrative costs associated with the rule would remain at $0 after ten years.

In estimating the estimated ten-year litigation costs of proposed § 201.211, PSD expects the litigation costs to be constant for the first five years while courts are setting precedents for the interpretation of § 201.211. PSD expects that case law with respect to the

[16] The framework is explained in detail in Tomek, W.G. and K.L. Robinson ''Agricultural Product Prices,'' third edition, 1990, Cornell University Press.

[17] A dead weight loss is the cost to society of an inefficient allocation of resources in a market. Causes of deadweight losses can include market failures, such as market power or externalities, or an intervention by a non-market force, such as government regulation or taxation.

[18] RTI International ''GIPSA Livestock Meat and Marketing Study'' prepared for Grain Inspection, Packers and Stockyards Administration, 2007. ERS Price Elasticities: *http://www.ers.usda.gov/data-products/commodity-and-food-elasticities/demand-elasticities-from-literature.aspx.*

[19] The $9.67 million increase in total industry costs from proposed § 201.211 is only 0.0043 percent of direct industry costs of approximately $223 billion for the beef, pork, and poultry industries.

regulation would be settled after five years and by then, industry participants would know how PSD would enforce the regulation and how courts would interpret the regulation. The effect of courts establishing precedents is that litigation costs would decline after five years as the livestock and poultry industries understand how the courts interpret the regulation.

To arrive at the estimated ten-year litigation costs of proposed § 201.211, PSD estimates that litigation costs for the first five years would occur at the same rate and at the same cost as in the first full year of the rule ending in May 2021. In the sixth through tenth years, PSD estimates that additional litigation costs would decrease each year and return to where they would have been absent the rule in the tenth year after the rule is effective and remain at $0 after 10 years. PSD estimates this decrease in litigation costs to be linear with the same decrease in costs each year.

The ten-year total costs of proposed § 201.211 appear in the table below.[20]

TABLE 5—TEN-YEAR TOTAL COSTS—YEARS ENDED MAY[21]

Year	Administrative ($ millions)	Litigation ($ millions)	Total direct ($ millions)
2021	$7.89	$1.77	$9.67
2022	1.58	1.77	3.35
2023	1.58	1.77	3.35
2024	1.58	1.77	3.35
2025	1.58	1.77	3.35
2026	0.79	1.48	2.27
2027	0.39	1.18	1.58
2028	0.20	0.89	1.08
2029	0.10	0.59	0.69
2030	0.05	0.30	0.35
Totals	15.74	13.31	29.05

Based on the analysis, PSD expects the ten-year total costs would be $29.05 million.

7. Present Value of Ten-Year Total Costs

The total costs of proposed § 201.211 in the table above show that the costs are highest in the first year, decline to a constant and significantly lower level over the next four years, and then gradually decrease again over the subsequent five years. Costs to be incurred in the future are less expensive than the same costs to be incurred today. This is because the money that would be used to pay the costs in the future could be invested today and earn interest until the time period in which the costs are incurred.

To account for the time value of money, the costs of the regulation to be incurred in the future are discounted back to today's dollars using a discount rate. The sum of all costs discounted back to the present is called the present value (PV) of total costs. PSD relied on both a three percent and seven percent discount rate as discussed in Circular A–4.[22] PSD measured all costs using constant 2016 dollars.

PSD calculated the PV of the ten-year total costs of the regulation using both a three percent and seven percent discount rate and the PVs appear in the following table.

TABLE 6—PV OF TEN-YEAR TOTAL COSTS

Discount rate	($ millions)
3 Percent	$26.31
7 Percent	23.33

PSD expects the PV of the ten-year total costs would be $26.31 million at a three percent discount rate and $23.33 million at a seven percent discount rate.

8. Annualized Costs

PSD annualized the PV of the ten-year total costs (referred to as annualized costs) of proposed § 201.211 using both a three percent and seven percent discount rate as required by Circular A–4 and the results appear in the following table.[23]

TABLE 7—TEN-YEAR ANNUALIZED COSTS

Discount rate	($ millions)
3 Percent	$3.08
7 Percent	3.32

PSD expects the annualized costs of § 201.211 would be $3.08 million at a three percent discount rate and $3.32 million at a seven percent discount rate.

PSD also annualized the PV of the ten-year total costs into perpetuity of proposed § 201.211 using both a three percent and seven percent discount rate following the guidance on complying with E.O. 13771 and the results appear in the following table.[24]

TABLE 8—ANNUALIZED COSTS INTO PERPETUITY

Discount rate	($ millions)
3 Percent	$0.69
7 Percent	1.21

PSD expects the costs of § 201.211 annualized into perpetuity would be $0.69 million at a three percent discount rate and $1.21 million at a seven percent discount rate. Based on the costs in Table 8 and in accordance with guidance on complying with E.O. 13771, the single primary estimate of the costs of this proposed rule is $1.21 million, the total costs annualized in perpetuity using a 7 percent discount rate.

B. Benefits

PSD was unable to quantify the benefits of § 201.211. However, proposed § 201.211 contains several

[20] As discussed above, PSD expects total administrative and litigation costs to return to where they would have been absent the rule and the additional costs associated with the rule would remain at $0 after ten years.

[21] PSD uses May 2021 as the end of the first year after the proposed rule would be in effect for analytical purposes only. The date the proposed rule becomes final is not known.

[22] *https://www.whitehouse.gov/sites/default/files/omb/assets/regulatory_matters_pdf/a-4.pdf*

[23] Ibid.

[24] *https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/memoranda/2017/M-17-21-OMB.pdf.*

provisions that PSD expects would improve economic efficiencies in the regulated markets for cattle, hogs, and poultry and reduce market failures. Regulations that increase the amount of relevant information available to market participants, protect private property rights, and foster competition improve economic efficiencies and generate benefits for consumers and producers.

Proposed § 201.211 would increase the amount of relevant information available to market participants and offset any potential abuse of buyer-side market power by clearly stating to all contracting parties the criteria that the Secretary will consider in determining whether conduct or action constitutes an undue or unreasonable preference or advantage in violation of 202(b) of the Act.

The regulation would also reduce the risk of violating section 202(b) because it would clarify the criteria that the Secretary will consider in determining whether the conduct or action in the livestock and poultry industries constitutes an undue or unreasonable preference or advantage and a violation of section 202(b) of the Act. Other benefits of clarifying the criteria may include: Reducing litigation risk; decreasing contracting costs; promoting competitiveness and fairness in contracting; and providing protections for livestock producers, swine production contract growers, and poultry growers.

Benefits to the livestock and poultry industries and the cattle, hog, and poultry markets would also arise from improving parity of negotiating power between packers, swine contractors, and live poultry dealers and livestock producers, swine production contract growers, and poultry growers. The improvement in parity would come when contracting parties negotiate new contracts and when they review and renegotiate any existing contract terms that contain language that could be considered a violation of section 202(b) of the Act.

Since the regulation would increase the amount of relevant information by clarifying what might be considered an undue or unreasonable preference, it would increase parity in negotiating contracts, and thereby reduce the ability to abuse buyer-side market power with the resulting welfare losses.[25] Establishing parity of negotiating power in contracts promotes fairness and equity and is consistent with PSD's mission to protect fair trade practices, financial integrity, and competitive markets for livestock, meats, and poultry.[26]

C. Cost-Benefit Summary

PSD expects the ten-year annualized costs of § 201.211 would be $3.08 million at a three percent discount rate and $3.32 million at a seven percent discount rate and the costs annualized into perpetuity to be $0.69 million at a three percent discount rate and $1.21 million at a seven percent discount rate. PSD expects the costs would be highest for the poultry industry due to its extensive use of poultry growing contracts, followed by the hog industry and the cattle industry, respectively.

PSD was unable to quantify the benefits of the proposed regulation, but they explained numerous qualitative benefits that would protect livestock producers, swine production contract growers, and poultry growers, promote fairness and equity in contracting, increase economic efficiencies, and reduce the negative effects of market failures throughout the entire livestock and poultry value chain. The primary benefit of proposed § 201.211 would be reduced occurrences of undue or unreasonable preferences or advantages and increased economic efficiencies in the marketplace. This benefit of additional enforcement of the Act would accrue to all segments of the value chain in the production of livestock and poultry, and ultimately to consumers.

Regulatory Flexibility Analysis

The Small Business Administration (SBA) defines small businesses by their North American Industry Classification System Codes (NAICS).[27] SBA considers broiler and turkey producers/growers and swine contractors, NAICS codes 112320, 112330, and 112210 respectively, to be small businesses if sales are less than $1,000,000 per year. Cattle feeders are considered small if they have less than $8 million in sales per year. Beef and pork packers, NAICS 311611, are small businesses if they have fewer than 1,000 employees.

The Packers and Stockyards Act regulates live poultry dealers, which is a group similar but not identical to the NAICS category for poultry processors. Poultry processors, NAICS 311611, are considered small business if they have fewer than 1,250 employees. PSD applied SBA's definition for small poultry processors to live poultry dealers as the best standard available, and considers live poultry dealers with fewer than 1,250 employees to be small businesses.

PSD maintains data on live poultry dealers from the annual reports these firms file with PSD. Currently, 93 live poultry dealers would be subject to the proposed regulation. Seventy-Four of the live poultry dealers would be small businesses according to the SBA standard. Although there were many more small businesses than large, small business produced only about 6.5 percent of the poultry in the United States in 2017.

Live poultry dealers classified as large businesses are responsible for about 93.5 percent of the poultry contracts. Assuming that small businesses would bear 6.5 percent of the costs, in the first year the regulation is effective, $222,687[28] would fall on live poultry dealers classified as small businesses. This amounts to average estimated costs for each small live poultry dealer of $3,009.

As of February 2019, PSD records identified 381 beef and pork packers actively purchasing cattle or hogs for slaughter. Many firms slaughtered more than one species of livestock. Of the 381 beef and pork packers, 172 processed both cattle and hogs, 144 processed cattle but not hogs, and 65 processed hogs but not cattle.

PSD estimates that small businesses accounted for 23.1 percent of the cattle and 19.2 percent of the hogs slaughtered in 2017. If the costs of implementing proposed § 201.211 are proportional to the number of head processed, then in first full year the regulation would be effective, PSD estimates that $126,501[29] in additional costs would fall on beef packers classified as small businesses. This amounts to estimated costs of $407 for each small beef packer.

In total, $81,603[30] in additional first-year costs would be expected to fall on pork packers classified as small

[25] Nigel Key and Jim M. MacDonald discuss evidence for the effect of concentration on grower compensation in ''Local Monopsony Power in the Market for Broilers? Evidence from a Farm Survey'' selected paper American Agri. Economics Assn. meeting Orlando, Florida, July 27–29, 2008.

[26] See additional discussion in Steven Y. Wu and James MacDonald (2015) ''Economics of Agricultural Contract Grower Protection Legislation,'' *Choices* 30(3): 1 -6.

[27] U.S. Small Business Administration. *Table of Small Business Size Standards Matched to North American Industry Classification System Codes. effective August 19, 2019. https://www.sba.gov/sites/default/files/2019-08/SBA%20Table%20of%20Size%20Standards_Effective%20Aug%2019%2C%202019.pdf*

[28] Estimated cost to live poultry dealers of $3,412,301 × 6.52 percent of firms that are small businesses = $222,687.

[29] Estimated cost to beef packers of $547,643 × 23.1 percent of firms that are small businesses = $126,501.

[30] Estimated cost to hogs and pork of $1,959,550 × 19.2 percent of slaughter in small businesses × 21.7 percent of costs attributed to packers = $81,603.

businesses, and $30,863 [31] would fall on swine contractors classified as small businesses. This amounts to average estimated costs for each small pork packer of $356, and average estimated costs for each small swine contractor of $286 in the first year the regulation would be effective. To the extent that smaller beef and pork packers rely on AMA purchases less than large packers, the estimates might tend to overstate costs.

Ten-year annualized costs discounted at a three percent rate would be $61,097 for the cattle and beef industry, $32,463 for the hog and pork industry, and $119,271 for the poultry industry. This amounts to annualized costs of $196 for each beef packer, $103 for each pork packer, $82 for each swine contractor, and $1,612 for each live poultry dealer that is a small business. The total annualized costs for regulated small businesses would be $212,830.

Ten-year annualized costs at a seven percent discount rate would be $64,458 for the regulated cattle and beef industry, $35,416 for the regulated hog and pork industry, and $125,696 for the poultry industry. This amounts to ten-year annualized costs of $207 for each beef packer, $112 for each pork packer, $90 for each swine contractor, and $1,699 for each live poultry dealer that is a small business. The total ten-year annualized costs at 7 percent for regulated small businesses would be $225,570.

The table below lists the estimated additional costs associated with the proposed regulation in the first year. It also lists annualized costs discounted at three percent and seven percent discount rates, and annualized PV of costs extended into perpetuity discounted at three and seven percent.

TABLE 9—ESTIMATED INDUSTRY TOTAL COSTS TO REGULATED SMALL BUSINESSES

Estimate type	Beef packers ($)	Pork packers and swine contractors ($)	Poultry processors ($)	Total ($)
First-Year Costs	126,501	112,466	222,687	461,653
10 years Annualized at 3 Percent	61,097	32,463	119,271	212,830
10 years Annualized at 7 Percent	64,458	35,416	125,696	225,570
Annualized Total Cost into Perpetuity Discounted at 3 Percent	13,720	7,290	26,784	47,794
Annualized Total Cost into Perpetuity Discounted at 7 Percent	23,492	12,907	45,810	82,209

In considering the impact on small businesses, PSD considered the average costs and revenues of each regulated small business impacted by proposed § 201.211. The number of small businesses impacted, by NAICS code, as well as the costs per entity in the first-year, ten-year annualized costs per entity at both the three percent and seven percent discount rates, and annualized PV of the total costs extended into perpetuity discounted at three and seven percent appear in the following table.

TABLE 10—PER ENTITY COSTS TO REGULATED SMALL BUSINESSES

NAICS	Number of small businesses	First year ($)	Ten-year annualized costs—3% ($)	Ten-year annualized costs—7% ($)	Perpetuity 3% ($)	Perpetuity 7% ($)
112210—Swine Contractor	108	286	82	90	19	33
311615—Poultry Processor	74	3,009	1,612	1,699	362	619
311611—Beef Packer	311	407	196	207	44	76
311611—Pork Packer	229	356	103	112	23	41

The following table compares the average per entity first-year and annualized costs of proposed § 201.211 to the average revenue per establishment for all regulated small businesses in the same NAICS code. The annualized costs are slightly higher at the seven percent rate than at the three percent rate, so only the seven percent rate is included in the table as the more conservative estimate.

TABLE 11—COMPARISON OF PER ENTITY COST TO REVENUES FOR REGULATED SMALL BUSINESSES

NAICS	Average revenue per establishment ($)	First-year cost as percent of revenue (%)	Ten-year annualized cost as percent of revenue (%)	Annualized cost to perpetuity as percent of revenue (%)
112210—Swine Contractor	485,860	0.06	0.02	0.007
311615—Poultry Processor	13,842,548	0.02	0.01	0.004
311611—Beef Packer	6,882,205	0.01	0.00	0.001
311611—Pork Packer	6,882,205	0.01	0.00	0.001

[31] Estimated cost to hogs and pork of $1,959,550 × 2.01 percent of contracted hogs produced by swine contractors that are small businesses × 78.3 percent of costs attributed to contractors = $30,863.

The revenue figures in the above table come from U.S. Census data for live poultry dealers and cattle and hog slaughterers, NAICS codes 311615 and 311611, respectively.[32] Ag. Census data have the number of head sold by size classes for farms that sold their own hogs and pigs in 2017 and that identified themselves as contractors or integrators, but not the value of sales nor the number of head sold from the farms of the contracted production. To estimate average revenue per establishment, PSD used the estimated average value per head for sales of all swine operations and the production values for firms in the Ag. Census size classes for swine contractors. The results in Table 11 demonstrate, the costs of proposed § 201.211 as a percent of revenue are less than one percent.[33]

Although the Packers and Stockyards Act does not regulate livestock producers or poultry growers, PSD recognizes that they will also incur contract review costs. PSD estimates that each livestock producer and poultry grower would, in its due course of business, spend one hour of time reviewing a contract or marketing agreement and would spend one-half hour of its attorney's time to review the contract. As with the regulated entities, one may view this estimate as an upper bound to the direct cost of the proposed rule, as not every producer or grower would choose to conduct such a review. Some may choose to ''wait and see'' what effect, if any, the rule had on the industry, and if courts ruled on it in any way that would warrant such a review of their contracts.

PSD multiplied one hour of livestock producer, swine production contract grower, and poultry grower management time and one-half hour of attorney time to conduct the marketing and production contract review by the average hourly wages for attorneys at $84/hour and managers at $62/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics to arrive at its estimate of contract review costs for livestock producers, swine contract growers, and poultry growers. The result is that each small livestock producer and each small poultry that sells livestock or raises poultry on a contract is expected to bear $104 in first year costs, $23 in ten year annualized costs discounted at 3 percent, $25 in ten year annualized costs discounted at 7 percent, and $9 discounted into perpetuity at 7 percent. Table 12 lists expected costs to livestock producers and poultry growers that are small businesses.

TABLE 12—TOTAL COSTS TO UNREGULATED SMALL BUSINESSES

Estimate type	Cattle feeders ($)	Hog producers ($)	Poultry growers ($)	Total ($)
First-Year Costs	111,866	459,707	2,501,106	3,072,679
10 years Annualized at 3 Percent	24,274	99,754	542,727	666,755
10 years Annualized at 7 Percent	26,917	110,614	601,812	739,342
Annualized Total Cost into Perpetuity Discounted at 3 Percent	5,451	22,401	121,876	149,728
Annualized Total Cost into Perpetuity Discounted at 7 Percent	9,810	40,313	219,329	269,452

The Ag. Census indicates there were 575 farms that sold hogs or pigs in 2017 and identified themselves as contractors or integrators. About 19 percent of swine contractors had sales of less than $1,000,000 in 2017 and would have been classified as small businesses. These small businesses accounted for only 2 percent of the hogs produced under production contracts.

Additionally, there were 8,557 swine producers in 2017 with swine contracts, and about 41 percent of these producers would have been classified as small businesses. PSD estimated an additional 2,370 pork producers had marketing agreements with pork packers. If 41 percent are small businesses, then 4,480 hog producers could incur contract review costs. PSD estimated as many as 1,099 cattle feeders had marketing agreements or contracts that could need adjustment due to the proposed rule. If 98 percent are small businesses, 1,078 could bear costs of reviewing contracts. Table 13 compares cost to revenues for producer unregulated producers that are small businesses.

PSD records indicated poultry processors had 24,101 poultry production contracts in effect in 2017. The 24,101 poultry growers holding the other end of the contracts are almost all small businesses by SBA's definitions.

TABLE 13—COMPARISON OF TOTAL COST TO REVENUES FOR UNREGULATED SMALL BUSINESSES

NAICS	Number of small businesses	Average revenue ($)	First-year cost as percent of revenue (%)	Ten-year annualized cost as percent of revenue (%)	Annualized cost to perpetuity as percent of revenue (%)
112212—Cattle Feeders	1,078	305,229	0.03	0.01	0.003
112210—Hog Producers	4,480	333,607	0.03	0.01	0.003
112320—Poultry Growers	24,101	181,545	0.06	0.01	0.005

Ten-year annualized cost savings of exempting small businesses would be $212,830 using a three percent discount rate and $225,570 using a seven percent discount rate. The cost savings annualized into perpetuity of exempting small businesses would be $47,794 using a three percent discount rate and $82,209 using a seven percent discount

[32] *https://www.nass.usda.gov/Publications/AgCensus/2017/Full_Report/Volume_1,_Chapter_1_US/*

[33] There are significant differences in average revenues between swine contractors and cattle, hog, and poultry processors, resulting from the difference in SBA thresholds.

rate. However, one purpose of proposed § 201.211 is to protect all livestock producers, swine production contract growers, and poultry growers from unfair and unreasonable preferences or advantages, regardless of whether the producer or grower and the packer, swine contractor, or live poultry dealer to which they sell or contract is a large or small business. PSD believes that the benefits of proposed § 201.211 would be captured by all livestock producers, swine production contract growers, and poultry growers. For this reason, AMS did not consider exempting small business from the proposed rule.

The number of regulated entities that could experience a cost increase is substantial. Most regulated packers and live poultry dealers are small businesses. However, the expected costs are not significant. For all four groups of regulated entities: Beef packers, pork packers, live poultry dealers, and swine contractors, average first year costs are expected to amount to less than one tenth of one percent of annual revenue. Ten-year annualized costs discounted at 7 percent are highest for swine contractors at two one hundredths of a percent of revenue. Annualized expected costs of $90 and $112 for swine contractors, and pork packers, respectively are near the cost of one hog. An annualized expected cost of $207 for beef packers is much less than the cost of one fed steer. Expected costs for live poultry dealers are higher, but as percent of revenue, expected costs to live poultry dealers are very low. AMS expects that the additional costs to small packers, live poultry dealers, and swine contractors will not change their ability to continue operations or place any of them at a competitive disadvantage.

The number of unregulated entities that could experience a cost increase is also substantial. Most effected livestock producers and poultry growers are small businesses. Expected costs are not significant. The expected first year cost for each unregulated livestock producer or poultry grower is $104. Annualized expected 10-year costs discounted at 3 percent are $23. Costs as percent of revenue are expected to be well below 1 percent. AMS expects that $23 per year will not change any producers' or poultry grower's ability to continue operations or place any livestock producer or poultry grower at a competitive disadvantage.

As discussed in the Regulatory Impact Analysis, AMS does not expect welfare transfers among market segments or within segments. Estimated changes in prices and quantities are indistinguishable from zero. AMS does not expect proposed § 201.211 to cause changes in production or marketing for small businesses, and the increase in direct costs is very small in relation to total costs.

Based on the above analyses, AMS does not expect that proposed § 201.211 would have a significant economic impact on a substantial number of small business entities as defined in the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). However, AMS seeks public comment on whether proposed § 201.211 will have a significant economic impact on a substantial number of small business entities before making a determination.

Civil Rights Review

AMS has considered the potential civil rights implications of this rule on members of protected groups to ensure that no person or group would be adversely or disproportionately at risk or discriminated against on the basis of race, color, national origin, gender, religion, age, disability, sexual orientation, marital or family status, political beliefs, parental status, or protected genetic information. This proposed rule does not contain any requirements related to eligibility, benefits, or services that would have the purpose or effect of excluding, limiting, or otherwise disadvantaging any individual, group, or class of persons on one or more prohibited bases. AMS has developed an outreach program to ensure information about the proposed regulation and the opportunity to comment on it is made available to socially and economically disadvantaged or limited resource farmers, producers, growers, and members of racial and ethnic minority groups.

Paperwork Reduction Act

This proposed rule does not contain new or amended information collection requirements subject to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). It does not involve collection of new or additional information by the Federal Government. According to PSD records, there were approximately 312 bonded packers; 1,326 market agencies selling on commission; 4,582 livestock dealers and commission buyers; and 95 live poultry dealers regulated under the Act in 2018. The 2017 Census of Agriculture indicated that there were 575 swine contractors in 2017. The 2017 Census of Agriculture also indicated that there were 826,733 livestock producers and poultry growers. None of these entities would be required to submit forms or other information to AMS or to keep additional records in consequence of this proposed rule.

E-Government Act

USDA is committed to complying with the E-Government Act by promoting the use of the internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

Executive Order 13175

This rule has been reviewed in accordance with the requirements of Executive Order 13175—Consultation and Coordination with Indian Tribal Governments. Executive Order 13175 requires Federal agencies to consult with tribes on a government-to-government basis on policies that have tribal implications, including regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes or the distribution of power and responsibilities between the Federal Government and Indian tribes.

The USDA's Office of Tribal Relations (OTR) has assessed the impact of this rule on Indian tribes and determined that this rule may have tribal implications that require continued outreach efforts to determine if tribal consultation under Executive Order 13175 is required.

If a tribe requests consultation, AMS will work with the OTR to ensure meaningful consultation is provided where changes, additions, and modifications identified herein are not expressly mandated by Congress.

Congressional Review Act

Pursuant to the Congressional Review Act (5 U.S.C. 801 *et seq.*), the Office of Information and Regulatory Affairs designated this rule as not a major rule as defined by 5 U.S.C. 804(2).

Executive Order 12988

This proposed rule has been reviewed under Executive Order 12988—Civil Justice Reform. This proposed rule is not intended to have retroactive effect. This proposed rule would not preempt state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule. There are no administrative procedures that must be exhausted prior to any judicial challenge to the provisions of this rule. Nothing in this proposed rule is intended to interfere with a person's right to enforce liability against any

person subject to the Act under authority granted in section 308 of the Act.

List of Subjects in 9 CFR Part 201

Confidential business information, Reporting and recordkeeping requirements, Stockyards, Surety bonds, Trade practices.

For the reasons set forth in the preamble, USDA proposes to amend 9 CFR part 201 as follows:

PART 201—REGULATIONS UNDER THE PACKERS AND STOCKYARDS ACT

■ 1. The authority citation for part 201 continues to read as follows:

Authority: 7 U.S.C. 181–229c.

■ 2. Section 201.211 is added to read as follows:

§ 201.211 Undue or unreasonable preferences or advantages.

The Secretary will consider one or more criteria when determining whether a packer, swine contractor, or live poultry dealer has made or given any undue or unreasonable preference or advantage to any particular person or locality in any respect in violation of section 202(b) of the Act. These criteria include, but are not limited to, whether the preference or advantage under consideration:

(a) Cannot be justified on the basis of a cost savings related to dealing with different producers, sellers, or growers;

(b) Cannot be justified on the basis of meeting a competitor's prices;

(c) Cannot be justified on the basis of meeting other terms offered by a competitor; and

(d) Cannot be justified as a reasonable business decision that would be customary in the industry.

Dated: January 6, 2020.

Bruce Summers,

Administrator, Agricultural Marketing Service.

[FR Doc. 2020–00152 Filed 1–10–20; 8:45 am]

BILLING CODE 3410–02–P

SMALL BUSINESS ADMINISTRATION

13 CFR Part 120

RIN 3245–AH04

SBA Supervised Lenders Application Process

AGENCY: U.S. Small Business Administration.

ACTION: Proposed rule.

SUMMARY: The U.S. Small Business Administration (SBA) is proposing to update the regulations applicable to Small Business Lending Companies (SBLCs) and state-regulated lenders (Non-Federally Regulated Lenders (NFRLs)) in order to improve efficiencies and potentially reduce costs related to the application and review process. The rule proposes to establish a comprehensive application and review process for SBLC and NFRL applicants (collectively referred to as SBA Supervised Lenders), including for transactions involving a change of ownership or control, and to clarify and incorporate into the regulations the factors SBA considers in its evaluation of an application. The rule also proposes to address SBA's requirements for the minimum amount of capital needed to be maintained by SBA Supervised Lenders, some of which have not been updated since 1996.

DATES: SBA must receive comments on this proposed rule on or before March 13, 2020.

ADDRESSES: You may submit comments, identified by RIN 3245–AH04, by any of the following methods:

- *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *Mail:* Bethany J. Shana, Office of Credit Risk Management, Office of Capital Access, Small Business Administration, 409 Third Street SW, Washington, DC 20416.
- *Hand Delivery/Courier:* Bethany J. Shana, Office of Credit Risk Management, Office of Capital Access, Small Business Administration, 409 Third Street SW, Washington, DC 20416.

SBA will post all comments on *http://www.regulations.gov.* If you wish to submit confidential business information (CBI) as defined in the User Notice at *http://www.regulations.gov,* please submit the information to Bethany J. Shana, Office of Credit Risk Management, Office of Capital Access, 409 Third Street SW, Washington, DC 20416. Highlight the information that you consider to be CBI and explain why you believe SBA should hold this information as confidential. SBA will review the information and make the final determination whether it will publish the information.

FOR FURTHER INFORMATION CONTACT: Susan E. Streich, Director, Office of Credit Risk Management, Office of Capital Access, Small Business Administration, 409 3rd Street SW, Washington, DC 20416; email address: *susan.streich@sba.gov.*

SUPPLEMENTARY INFORMATION:

I. Background Information

The 7(a) Loan Program is a business loan program authorized by section 7(a) of the Small Business Act (15 U.S.C. 636(a)) and is governed primarily by the regulations in part 120 of Title 13 of the Code of Federal Regulations (CFR). The core mission of the 7(a) Loan Program is to provide SBA-guaranteed financial assistance to small businesses that lack access to capital on reasonable terms and conditions in order to support our nation's economy.

Under the 7(a) Loan Program, a lender (Lender) participates with SBA by making loans directly to eligible small businesses and SBA guarantees a portion of each loan made by Lenders in the program. The Lender is responsible for funding and servicing the loan and must comply with SBA's Loan Program Requirements (as defined in 13 CFR 120.10) throughout the life of the loan. SBA may delegate to a Lender the authority to approve small business loans made under the 7(a) Loan Program. The Lender may also sell the guaranteed portion of a 7(a) loan in SBA's secondary market and, in certain circumstances, may securitize or sell a participating interest in the unguaranteed portion of a 7(a) loan. In the event that a borrower defaults on a 7(a) loan, the Lender must conduct the liquidation efforts and, if applicable, litigation efforts in accordance with SBA Loan Program Requirements. The Lender and SBA share in the loss, if any, in accordance with their respective interests in the loan.

Most Lenders participating in the 7(a) Loan Program are depository institutions that have a primary Federal regulator (*e.g.,* the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the National Credit Union Administration (NCUA)) that oversees the Lender's lending activities. SBA also has the statutory authority under section 7(a)(17) of the Small Business Act to authorize non-federally regulated entities to make 7(a) loans, including entities that have state-regulators. Under this authority, SBA has authorized SBA Supervised Lenders to make loans in the 7(a) Loan Program. SBA Supervised Lenders are defined in 13 CFR 120.10 to include SBLCs and NFRLs, and are subject to SBA regulation, oversight and enforcement, including the imposition of civil monetary penalties.

SBLCs, as defined in 13 CFR 120.10, are non-depository lending institutions that are authorized only to make loans pursuant to section 7(a) of the Small Business Act and loans to Intermediaries in SBA's Microloan

program. SBLCs are regulated, supervised and examined solely by SBA, except for the subset of SBLCs defined as Other Regulated SBLCs in 13 CFR 120.10. In January of 1982, SBA imposed a moratorium on issuing additional SBA lending authorities (referred to as SBLC Licenses) to SBLCs. Today, there are fourteen (14) SBLCs with full authority to make 7(a) loans up to the maximum loan amount (currently $5 million).[1] An entity may purchase one of the fourteen SBLC Licenses from an existing SBLC with SBA's prior written approval.

NFRLs, as defined in 13 CFR 120.10, are business concerns that are subject to regulation, supervision and oversight by a state regulator that must be satisfactory to SBA. By definition, an NFRL's lending activities are not regulated by a Federal Financial Institution Regulator (as defined in 13 CFR 120.10). Typically, NFRLs are organized as state licensed Business and Industrial Development Companies (BIDCOs), but may also include other types of state-regulated lending institutions, such as non-profit corporations or financial institutions without Federal deposit insurance or share insurance protection.

To become an SBA Supervised Lender, a prospective applicant must be qualified as determined by SBA in its sole discretion. Applicants must meet, inter alia, the participation criteria and ethical requirements for all Lenders set forth in the regulations at 13 CFR 120.140 and 120.410, the regulations specific to SBA Supervised Lenders (13 CFR 120.460 through 120.465) and, if applicable, the regulations specific to SBLCs (13 CFR 120.470 through 120.490). An entity interested in becoming an SBA Supervised Lender must submit an application to SBA containing the information specified in SBA's Standard Operating Procedures 50 10, Lender and Development Company Loan Programs, as amended from time to time (SOP 50 10).[2]

II. Summary of Proposed Changes

In this proposed rule, SBA aims to enhance the application and review process for organizations seeking to participate as an SBA Supervised Lender in the 7(a) Loan Program and to mitigate the risk inherent in their participation in the program. The proposed changes would improve efficiencies associated with applications submitted to SBA by prospective SBLCs and NFRLs, including transactions involving a change of ownership or control, without compromising performance or increasing risk to the 7(a) Loan Program.

This rule also proposes to incorporate into the regulations the factors SBA considers in its evaluation of an SBA Supervised Lender application, including an assessment of the applicant's capitalization, organizational structure, the risk associated with its business plan, the professional qualifications and the historical loan performance record of the applicant and its management team (including key employees), the prior history or involvement of the Applicant or its management team (including key employees) with any SBA program, and other relevant information obtained by SBA through due diligence.

Typically, SBA Supervised Lenders are non-depository institutions, and, as such, rely on secondary market loan sales, warehouse lines of credit, participations or securitizations to support their lending operations. These activities, by their nature, create additional risk to SBA. Many of the changes in this proposed rule, including changes related to the safety and soundness and the lending activities of SBA Supervised Lenders (*e.g.,* capital maintenance requirements), seek to mitigate the increased risk associated with the operations of SBA Supervised Lenders.

III. Section-by-Section Analysis of Proposed Changes

SBA proposes to amend the following sections in 13 CFR part 120:

A. Substantive Changes

1. *Section 120.460 What are SBA's additional requirements for SBA Supervised Lenders*?

SBA proposes to add new paragraphs (c) and (d) to § 120.460. Paragraph (c) would incorporate into the regulations a requirement that NFRLs must employ qualified full-time professional management, as is currently required of SBLCs. This new paragraph would clarify the meaning of qualified full-time professional management for SBA Supervised Lenders to include, at a minimum, the employment of a chief executive officer or equivalent to manage daily operations, a chief credit/risk officer, and at least one other full-time employee qualified by training and experience to carry out the SBA Supervised Lender's business plan. Existing SBA Supervised Lenders would not be required to comply with the new regulatory definition of qualified full-time professional management unless, after the effective date of a final rulemaking, they make or acquire any 7(a) loans or engage in a transaction that constitutes a change of ownership or control of the SBA Supervised Lender. Based on the quarterly condition reports and the annual reports that are required to be submitted to the Agency by SBA Supervised Lenders (including audited financial statements), most SBA Supervised Lenders already comply with the proposed new definition of qualified full-time professional management. SBA believes this proposed rule represents the minimum level of oversight and responsibility necessary for a lender receiving the benefit of SBA loan guarantees.

SBA is proposing to add a new paragraph (d) to limit an NFRL's lending area for 7(a) loan originations to the state in which the NFRL's primary state regulator is located. A number of NFRLs participating in the 7(a) Loan Program currently have limitations imposed by state law or by their state regulator that restrict their lending activities to the state in which their primary state regulator is located. In recent years, however, certain state regulators have permitted NFRLs to expand their business plan and lending area to make loans outside of the state or even nationwide. SBA is concerned that state regulators may not have sufficient resources or capacity to adequately supervise, regulate and examine NFRLs with a business plan to make or acquire 7(a) loans outside of their state, and SBA does not have the resources necessary to fill in the gaps in oversight and enforcement.

[1] SBA waived certain regulations for the purpose of permitting mission-oriented lenders to participate in SBA's Community Advantage Pilot Program (referred to as CA Lenders), a pilot program within the 7(a) Loan Program. Each CA Lender is identified as either an SBLC or NFRL, depending on whether the lender is subject to regulation by a state. CA Lenders are limited to making loans in the CA Pilot Program, which generally requires a CA Lender to make loans to underserved markets (*e.g.,* low-to-moderate income communities, rural areas, opportunity zones, veteran-owned businesses) and in an amount not to exceed $250,000. The CA Pilot Program is governed by all regulations applicable to the 7(a) Loan Program generally and to SBA Supervised Lenders specifically unless waived or modified in the **Federal Register** Notices published in connection with the CA Pilot Program. SBA is not proposing to apply the changes in this proposed rule to the CA Pilot Program. For more information about the CA Pilot Program please refer to the CA Participant Guide, Version 5.0 (October 1, 2018), available at *https://www.sba.gov/document/support-community-advantage-participant-guide.*

[2] The current version of the SOP is the 50 10 5(K), effective April 1, 2019. The application requirements can be found in this SOP in Subpart A, Chapter 1, Paragraph II.C.2 with respect to NFRLs and Subpart A, Chapter 2, Paragraph II with respect to SBLCs. The SOP is available at *https://www.sba.gov/document/sop-50-10-5-lender-development-company-loan-programs.*

SBA has also found that many NFRLs lack the experience and expertise necessary to manage the risks associated with multistate lending, such as the financial risks inherent in the servicing and liquidation of 7(a) loans in other state jurisdictions. With the exception of two NFRLs, approximately 90% of the lending by NFRLs within the 7(a) Loan Program is done within the state where the NFRL's primary state regulator is located. In an effort to manage the risks associated with NFRLs participating in the 7(a) Loan Program, SBA proposes to incorporate a new paragraph (d) to limit the lending area of NFRLs (with respect to 7(a) loans only) to the state in which their primary state regulator is located, except that an NFRL's lending area may include a local trade area that is contiguous to such state (*e.g.,* a city or metropolitan statistical area that is bisected by a state line) if the NFRL receives SBA's prior written approval. This is consistent with the general understanding that state-regulated lenders focus on economic development in their state and local communities. Existing NFRLs would not be subject to this requirement unless, after the effective date of a final rulemaking, they make or acquire any 7(a) loans or engage in a transaction that constitutes a change of ownership or control of the NFRL. For further discussion on the impact of this proposed rule see the initial regulatory flexibility analysis (IRFA) below.

2. *Section 120.462 What are SBA's additional requirements on capital maintenance for SBA Supervised Lenders*?

SBA is authorized to supervise the safety and soundness of NFRLs and regulate their lending activities pursuant to section 23(a) of the Small Business Act. *See* 15 U.S.C. 650(a). Currently, NFRLs must maintain the minimum amount of capital established by their state regulator to meet SBA's regulatory requirements for capital maintenance. *See* 13 CFR 120.462(d). SBA has determined, however, that the minimum level of capital established by an NFRL's state regulator may not be sufficient to manage the credit risk associated with an NFRL's lending operation or the potential loss to SBA due to an NFRL's financial failure.[3] This rule proposes to amend the regulations to require NFRLs to maintain a baseline minimum amount of capital necessary for participation in the 7(a) Loan Program. The proposed minimum amount of capital that an NFRL would need to maintain would be equal to the higher of (1) the minimum amount of capital required by the NFRL's state regulator, or (2) $2,500,000. Existing NFRLs that have capital amounts less than the proposed minimum would have three years after the effective date of a final rulemaking to reach the new minimum capital amount. An NFRL that does not meet the new minimum capital requirement by the end of the three-year period could remain in the program but would not be permitted to make or acquire 7(a) loans after such date, until it satisfies the requirement. In addition, the new minimum capital requirement would apply immediately in the event of a change of ownership or control of an NFRL during the three-year time frame.

SBA believes that most NFRLs already comply with this requirement[4] and that it represents the baseline minimum level of capital necessary for an NFRL to maintain while making loans with the benefit of SBA loan guarantees. The proposed new minimum level of capital is equal to one-half the amount of minimum capital proposed for SBLCs in this rulemaking (see Section III.A.6 below), consistent with SBA's intent in this proposed rule to limit 7(a) loan making by NFRLs to the state in which their primary state regulator is located (as opposed to nationwide for SBLCs).

3. *Section 120.466 SBA Supervised Lender application.*

SBA proposes to add a new § 120.466 to incorporate into the regulations a new application and review process for prospective SBA Supervised Lenders. SBA proposes to evaluate applications through an initial review and, if warranted, a final review.

The initial review, as proposed under § 120.466(a), would require an SBA Supervised Lender applicant to submit a written plan (known as a Lender Assessment Plan (LAP)). The LAP would allow SBA to more effectively review key elements of an application and reach a preliminary assessment about the qualifications of an applicant more quickly and efficiently. SBA recognizes that the current SBA Supervised Lender application process can be costly for the applicant and represents an inefficient use of SBA's time and limited resources.

An initial review phase would assist SBA in identifying incomplete applications and unqualified applicants much earlier in the review process. The initial review will include an initial assessment of the applicant's business plan, capitalization and professional management team (including key employees). As part of this initial review, SBA may also require an in-person interview between the applicant and appropriate employees of the Office of Capital Access. The interview will serve as an opportunity for the applicant to explain the information provided in its LAP and answer any preliminary questions posed by SBA. During the initial review phase, SBA may also contact listed and unlisted references and verify the accuracy of the information provided in the LAP.

If SBA determines, based on the information provided in the LAP and in the in-person interview (if required), that the applicant may proceed to the final review phase, it will notify the applicant in writing. Notification by SBA that the applicant may proceed to final review does not mean that the applicant will be favorably assessed or approved by SBA to participate as an SBA Supervised Lender in the 7(a) Loan Program. If SBA notifies an applicant in writing that it may not proceed to the final review, the applicant may not submit a new LAP until nine months from the date of such notification. This nine month time period should allow sufficient time for the applicant to address any issues identified by SBA during the initial review phase without overburdening SBA with premature resubmissions. SBA will determine whether a LAP submitted during this nine month time period is being submitted by the same applicant.

The final review, as proposed under § 120.466(b), would require each SBA Supervised Lender applicant to submit a complete application as further described in official SBA policies and procedures.[5] A complete application would update the information disclosed in the LAP and would provide additional information for SBA's review, such as the applicant's organizational documents, operational plan, credit policies, internal control

[3] In 2017, a state licensed lender participating as an NFRL in the 7(a) Loan Program was put into liquidation by order of its state regulator and under the supervision of a state court. After approximately two years, the appointed liquidator sold the lender's assets. The events leading up to the lender's liquidation indicate that although the lender was in compliance with the minimum capital required by its state regulator, the NFRL did not have a sufficient amount of capital to manage the credit risk associated with its 7(a) lending activities. Because the NFRL did not maintain a sufficient amount of capital SBA was put in a position to sustain a loss at the time of the lender's financial failure.

[4] Of the twenty-one NFRLs that are participating in the 7(a) Loan Program, three do not currently meet the proposed new minimum capital requirement of $2.5 million based on information submitted to SBA periodically in quarterly condition reports or annual reports. See 13 CFR 120.464.

[5] The information required to be submitted in a complete application would not be set forth in SBA's regulation but would continue to be in SBA's official policies and procedures. See SOP 50 10.

policies, loan risk rating system, capital adequacy plan, proposed credit facilities, organizational chart, audited financial statements, bank statements, legal opinions and other necessary documentation. After completion of the final review, SBA (the Director, Office of Financial Assistance, in consultation with the Director, Office of Credit Risk Management) will issue a final decision to approve or deny the application. SBA believes the proposed new application and review process will provide greater clarity and transparency, will expedite SBA's review of applications, and may be less burdensome for applicants and on SBA's limited administrative resources.

SBA recognizes that in some instances an SBA Supervised Lender applicant may be able to cure certain deficiencies in its application over a period of time, such as raising additional capital to support its business plan, adding more experienced members to its management team, or demonstrating to SBA a longer track record of successful loan making performance. This proposed rule provides that if an SBA Supervised Lender's application is denied, the applicant may submit a new LAP and restart the application process anytime after 18 months from the date of denial. SBA believes this 18 month time period is necessary to avoid resubmissions from declined applicants before sufficient time has elapsed for meaningful changes to occur and to be reflected in an SBA Supervised Lender application.

Lastly, under § 120.466(c), SBA is proposing to require an entity seeking to become an NFRL to have at least one year of current operating and relevant commercial lending experience before the entity may submit an application to become an SBA Supervised Lender. The requirement of having at least one year of experience is consistent with the standards that have been established for other SBA business loan programs, such as the Microloan Program, where entities are required to have at least one year of prior experience in order to be eligible to participate in the program as an Intermediary.

4. *Section 120.467 Evaluation of SBA Supervised Lender applicants.*

SBA proposes to add a new § 120.467 to incorporate into the regulations the factors that SBA currently considers in evaluating an SBA Supervised Lender applicant. SBA's evaluation includes a review of, among other things, the applicant's business plan, organizational structure, operational plan, management qualifications, the historical performance of the loans originated by the applicant or attributable to its management team, the applicant's capitalization, financial projections and liquidity, and prior history or involvement of the applicant or its management team (including key employees) with any SBA guaranteed lending program or any other Federal or state lending program. In addition, SBA reviews the results of background investigations (*e.g.,* through SBA Form 1081) and other information obtained through due diligence, such as reference checks.

In addition, this proposed rule makes it clear that SBA may prohibit individuals or entities from participating as an officer, director, manager, owner or key employee of an applicant if such individual or entity: (1) Has a previous record of failing to comply with SBA Loan Program Requirements; (2) previously participated in a material way with any past or present SBA Lender or Intermediary that failed to maintain satisfactory SBA performance; (3) previously defaulted on any Federal loan or Federally assisted financing that resulted in the Federal Government or any of its agencies or departments sustaining a loss in any of its programs; or (4) ever failed to pay when due any debt or obligation, including any amounts in dispute, to the Federal Government or guaranteed by the Federal Government (including but not limited to taxes or business or student loans). These provisions are consistent with SBA's current policies in evaluating an SBA Supervised Lender applicant.

5. *Section 120.468 Change of ownership or control requirements for SBA Supervised Lenders.*

SBA proposes to move the regulation applicable to a change of ownership or control of an SBLC (§ 120.475) to a new § 120.468 with certain modifications. The purpose of this change is to incorporate into the regulations the current policy requirement that all SBA Supervised Lenders, including NFRLs, must obtain SBA approval prior to any change of ownership or control. This proposed rule provides clarification as to what would be considered a change of ownership or control, including any series of transfers that, in the aggregate over an 18 month period, transfers 10 percent or more of an SBA Supervised Lender's stock or ownership interests. This rule also seeks to add a new paragraph (a)(5) to clarify that the definition of a change of ownership or control includes any transaction or event that results in any change in the possession (direct or indirect) of the right to control, or the power to direct or cause the direction of, the management or policies of an SBA Supervised Lender. The rule also clarifies that SBA Supervised Lenders must receive SBA prior written approval before entering into any definitive agreement regarding a change of ownership or control.

This rule also proposes to incorporate into the regulations as § 120.468(c) the current policy that a new application (as described above in new § 120.466) must be submitted to SBA in connection with a change of ownership or control of an SBA Supervised Lender.

In addition, this proposed rule would add a new paragraph (d) to provide an SBA Supervised Lender with the opportunity to voluntarily surrender its SBA lending authority (*i.e.,* its SBLC License or its NFRL lending authority) and withdraw from the 7(a) Loan Program with SBA's prior written approval. This would provide SBA Supervised Lenders with a path to exit the 7(a) Loan Program in an efficient and organized manner. As proposed, a voluntary surrender would require an SBA Supervised Lender to (i) transfer its entire loan portfolio to one or more Lenders acceptable to SBA, and (ii) enter into a withdrawal agreement. The purpose of the withdrawal agreement is to resolve any outstanding issues between the SBA Supervised Lender and SBA, including any outstanding monetary liabilities.

6. *Section 120.471 What are the minimum capital requirements for SBLCs*?

SBA proposes to amend § 120.471(a) to increase the minimum capital requirement for SBLCs, which has not been updated since 1996. SBA has determined that the current minimum capital requirement that an SBLC must maintain (*i.e.,* the greater of $1 million or 10 percent of the aggregate of its share of all outstanding loans) is insufficient to assure an SBLC's continued financial viability or provide for any necessary growth. In 1996, the maximum 7(a) loan amount was $1,000,000. The maximum 7(a) loan amount has increased several times since then, the last time occurring in September of 2010. Section 1111 of the Small Business Jobs Act of 2010 (SBJA), Pub. L. 111–240, 124 Stat. 2504, which was enacted on September 27, 2010, permanently increased the maximum guaranteed portion and the maximum loan amount for 7(a) loans. Under the SBJA, the maximum 7(a) loan amount was increased from $2 million to $5 million and the maximum 7(a) loan guaranteed portion was increased to the

current amount of $3,750,000.[6] No corresponding changes were made by SBA to increase the minimum capital requirements for SBA Supervised Lenders either at that time or in connection with any of the prior increases in the maximum 7(a) loan amount that have occurred since 1996.

This proposed rule would adopt a new minimum capital requirement for SBLCs equal to unencumbered paid-in capital and paid-in surplus of at least $5 million, or ten percent of the aggregate of its share of all outstanding loans, whichever is greater. Most of the existing SBLCs have capital in amounts well in excess of the minimum amount required by current § 120.471(a). The proposed change would again ensure that no SBLC has minimum capital in an amount less than the size of a single 7(a) loan permitted in the program. *See* 15 U.S.C. 636(a)(3)(A). An existing SBLC that has capital in an amount less than the proposed minimum would have three years after the effective date of a final rulemaking to reach the new minimum capital amount, after which it would be permitted to remain in the program but would not be permitted to make or acquire 7(a) loans until such time as the minimum capital requirement was satisfied. The new minimum capital requirement would apply immediately, however, in the event of a change of ownership or control of an SBLC.

SBA is proposing to amend § 120.471(b) to expand the definition of capital to include ''unrestricted net assets'' for non-profit corporations. In recent years, SBA has seen an increase in the interest of non-profit corporations seeking to become an SBLC; however, the definition of capital has not been updated to reflect that an SBLC may be organized as either a for-profit or non-profit corporation. This proposed change would address that issue.

Finally, SBA is considering whether it should make any additional changes to the definition of capital under § 120.471(b). Capital currently consists only of the following: Common stock, preferred stock (non-cumulative and with no maturity date), additional paid-in capital (representing amounts paid for stock in excess of par value), retained earnings, and capital contributions to limited liability companies and limited partnerships that are not subject to repayment or withdrawal and have no cumulative priority return. In recent years, SBA has become concerned that retained earnings can include amounts, such as the estimated value of loan servicing rights, that may not be as reliable as paid-in capital. Specifically, SBA is concerned that the valuation of servicing rights assets is based on assumptions such as prepayment speeds and loan default rates that are subject to change. SBA is seeking to determine whether, and in what amount, servicing rights should contribute to an SBA Supervised Lender's required minimum capital, and to ensure that there is a consistent understanding of the appropriate treatment of servicing rights by SBA Supervised Lenders. SBA is soliciting comments from the public on the current definition of capital (as defined in § 120.471(b)) and whether it should be modified to limit any contribution that servicing rights may have towards an SBA Supervised Lender's minimum capital requirement. Alternative options could include, for purposes of the minimum capital calculation: (1) Limiting the percentage of retained earnings that are permitted to be comprised of the value of servicing rights, or (2) limiting the percentage of servicing rights that are permitted to be included in retained earnings.

B. Technical Changes

1. *Section 120.410 Requirements for all participating Lenders.*

SBA proposes a conforming technical change to § 120.410(a)(1) to reflect the new minimum capital requirements for SBA Supervised Lenders.

2. *Section 120.470 What are SBA's additional requirements for SBLCs*?

SBA proposes a conforming technical change to remove § 120.470(g) ''Management'' and redesignate paragraph (h) as paragraph (g). A new regulatory definition of qualified full-time professional management for SBA Supervised Lenders will be incorporated into proposed new § 120.460(c) as described above in Section III.A.1.

3. *Section 120.475 Change of ownership or control.*

SBA proposes a conforming technical change to remove and reserve § 120.475. The current text of § 120.475 will be incorporated with modifications into proposed new § 120.468 as described above in Section III.A.5.

Compliance With Executive Orders 12866, 13563, 13771, 12988, and 13132, the Paperwork Reduction Act (44 U.S.C., Ch. 35), and the Regulatory Flexibility Act (5 U.S.C. 601–612).

Executive Order 12866

The Office of Management and Budget (OMB) has determined that this proposed rule is not a ''significant'' regulatory action for the purposes of Executive Order 12866, and therefore, SBA has not prepared a Regulatory Impact Analysis. This is not a major rule under the Congressional Review Act, 5 U.S.C. 801 *et seq.*

Executive Order 13563

This executive order supplements and reaffirms the principles and requirements in Executive Order 12866, including the requirement to provide the public with an opportunity to participate in the regulatory process. SBA Supervised Lenders have been involved in the 7(a) Loan Program for over 35 years. Over the years, the Agency has received feedback from many SBA Supervised Lender applicants and program participants including valuable insight and suggestions for improvements to the application and review process.

Executive Order 13771

This proposed rule is not expected to be an Executive Order 13771 regulatory action because this proposed rule is not significant under Executive Order 12866.

Executive Order 12988

This action meets applicable standards set forth in Sections 3(a) and 3(b)(2) of Executive Order 12988, Civil Justice Reform, to minimize litigation, eliminate ambiguity, and reduce burden. The action does not have retroactive or preemptive effect.

Executive Order 13132

SBA has determined that this proposed rule would not have substantial, direct effects 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, for the purposes of Executive Order 13132, SBA has determined that this proposed rule has no federalism implications warranting preparation of a federalism assessment.

Paperwork Reduction Act, 44 U.S.C., Ch. 35

SBA has determined that this proposed rule would impose a new

[6] For International Trade and Export Working Capital loans the maximum 7(a) loan amount is $5 million, and the maximum 7(a) loan guaranteed portion is $4.5 million. *See* 15 U.S.C. 636(a)(2)(D) and (E); 15 U.S.C. 636(a)(3)(B); and 15 U.S.C. 636(a)(14)(B)(i).

reporting and/or recordkeeping requirement under the Paperwork Reduction Act (PRA). Specifically, the proposed rule would require SBA Supervised Lenders to submit a written Lender Assessment Plan (LAP) in order for SBA to conduct an initial review of the applicant. In addition, this rule also proposes to codify a requirement for applicants to submit a complete application in order for SBA to determine whether the applicant has the qualifications necessary to participate in the 7(a) Loan Program as an SBA Supervised Lender. As discussed above, this requirement is currently described in SBA's official policies and procedures.

The applicant will also use some of the same forms as other Lenders that apply to participate in the 7(a) Loan Program, including the SBA Form 1081, Statement of Personal History. SBA Form 1081 is an OMB-approved form under OMB Control number 3245–0080.

The title, summary of the new information collection, description of respondents, and an estimate of the reporting burden related to this collection are discussed below.

Title of Collection: SBA Supervised Lender Application and Review.

OMB Control Number: New Collection.

(a) Description: Lender Assessment Plan.

The proposed rule would require organizations seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control) to submit a LAP to SBA. The LAP includes the legal name and contact information of the applicant, a written business plan, current and projected financial statements and other important information about the applicant and its management team (including key employees).

Need and Purpose: A LAP is necessary for SBA to conduct an initial review of an applicant seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control). The LAP provides SBA with key elements of an application so that SBA can reach a preliminary assessment about the qualifications of an applicant more efficiently. This initial review phase will assist SBA in identifying incomplete applications and unqualified applicants much earlier in the application review process.

Description and Estimated Number of Respondents: Pursuant to proposed § 120.466(a), the information in the LAP will be collected from each organization seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control). SBA estimates that it will likely receive no more than four LAPs each year.

Total Estimated Response Time: It is estimated that each applicant would need approximately 35 hours to prepare and submit the proposed LAP for an estimated total of 140 hours annually.

(b) Description: SBA Supervised Lender Application.

If an applicant seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control) is authorized by SBA to proceed to the final review phase, the applicant will be required to submit a complete application in order for SBA to determine whether the applicant has the qualifications necessary to participate in the 7(a) Loan Program.

Need and Purpose: The information submitted with the collection is necessary for SBA to reach a final decision regarding an applicant seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control). The complete application requires an SBA Supervised Lender applicant to provide more detail about the information previously disclosed to SBA in the LAP and will include additional information about the applicant's proposed operation and lending activities as a participant in the 7(a) Loan Program. As stated above, the application requirements are not new since they are currently set out in SBA's official policies and procedures. Under those policies and procedures, an organization applying to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control) is required to, among other things, submit documentation in support of its organizational structure, internal control policies, operational plan, proposed credit policies, loan risk rating system, proposed secondary market activities, capital adequacy plan, audited financial statements and other information (*e.g.,* certifications and legal opinions) necessary for SBA to evaluate the qualifications of the applicant. See SOP 50 10. Although the requirements currently apply to about four organizations each year, now that SBA is proposing to codify the application requirements in its regulations, under the PRA it is deemed to impact ten or more respondents; therefore, SBA must now obtain OMB approval in compliance with the PRA procedures.

Description and Estimated Number of Respondents: The information in the complete application will be collected from organizations that are seeking to become an SBA Supervised Lender and have successfully reached the final review phase. Based on current experience, SBA estimates that it will likely receive no more than four complete applications each year.

Total Estimated Response Time: It is estimated that each applicant would need approximately 50 hours to prepare and submit a complete application, for an estimated total of 200 hours annually.

SBA invites comments on: (1) Whether this collection of information is necessary for the proper performance of SBA's functions, including whether the information will have a practical utility; (2) the accuracy of SBA's estimate of the time for preparing and completing the collection of information, including the validity of the methodology and assumptions used; (3) ways to enhance the quality, utility, and clarity of the information to be collected; and (4) ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques, when appropriate, and other forms of information technology.

Regulatory Flexibility Act, 5 U.S.C. 601–612

Under the Regulatory Flexibility Act (RFA), this proposed rule, if adopted, may have an impact on a substantial number of small entities that participate as SBA Supervised Lenders in the 7(a) Loan Program. Immediately below, SBA sets forth an initial regulatory flexibility analysis (IRFA) examining the impact of the proposed rule in accordance with section 603, Title 5, of the United States Code. The IRFA addresses (1) the reasons, objectives and legal basis for this proposed rule; (2) a description of the kind and number of small entities that may be affected; (3) the projected reporting, recordkeeping and other compliance requirements; (4) whether there are any Federal rules that may duplicate, overlap, or conflict with this proposed rule; and (5) whether there are any significant alternatives to this proposed rule.

1. What are the reasons, objectives and legal basis for the rule?

The proposed rule is designed to improve efficiencies and enhance the application and review process for organizations seeking to participate in the 7(a) Loan Program as SBA Supervised Lenders by conducting an initial review (LAP) and, if warranted, a final review (complete application). The objective is to provide a process for a more efficient and effective evaluation of the qualifications of applicants seeking to become SBA Supervised Lenders. The new application and review process would provide greater clarity and transparency to applicants

and would expedite SBA's review, which will potentially reduce costs on applicants and on SBA's limited administrative resources.

The proposed rule also seeks to raise the minimum capital requirement that SBA Supervised Lenders must maintain in order to assure their continued financial viability and to provide for any necessary growth. The minimum capital requirement for SBA Supervised Lenders has not been updated by SBA for more than twenty-three years. The Agency has determined that the regulations addressing minimum capital must be amended to correspond with the 500% increase in the maximum 7(a) loan amount ($1 million to $5 million) that Congress has authorized by statute over the last twenty-three years.

The proposed rule also limits the 7(a) lending area for NFRLs to the state in which their primary regulator is located, except that an NFRL may request SBA's prior written approval to make 7(a) loans in a local trade area that is contiguous to such state (*e.g.,* a city or metropolitan statistical area that is bisected by a state line). Most NFRLs participating in the 7(a) Loan Program already limit their lending activities to the state in which their primary state regulator is located. In recent years, some state regulators have permitted NFRLs to make loans outside of their state or even nationwide. The expansion of an NFRL's 7(a) lending area increases risk to SBA and the Agency is concerned that some state regulators do not have the resources and the capacity to adequately supervise, regulate and examine non-depository lenders that operate outside of their state. In addition, state laws that apply to state-regulated lenders do not address the different conditions associated with lending in other states or nationwide. This part of the proposed rule is also consistent with the general understanding that state-regulated lenders (such as BIDCOs) are licensed under specific state laws to focus primarily on economic development in their respective state and local communities.

SBA is authorized to supervise the safety and soundness of SBA Supervised Lenders and may regulate their 7(a) lending activities pursuant to section 23(a) of the Small Business Act. 15 U.S.C. 650(a), see also 15 U.S.C. 634(b)(7). SBA has the authority to promulgate rules, regulations and requirements for the 7(a) Loan Program. 15 U.S.C. 634(b)(6).

2. What are SBA's description and estimate of the number of small entities to which the rule will apply?

SBA Supervised Lenders comprise a unique class of 35 non-depository lenders that may only participate in the 7(a) Loan Program and make 7(a) loans if authorized by SBA. If the proposed rule is adopted in its current form, the rule would be applicable to all SBA Supervised Lenders (other than lenders participating as CA Lenders in the CA Pilot Program). SBA estimates that approximately 88 percent of SBA Supervised Lenders are considered small entities based on NAICS sector code 52 (finance and insurance) and industry code 52298 (All Other Non-depository Credit Intermediation) and have annual receipts of less than $38.5 million. This estimate of 31 small SBA Supervised Lenders is based on information contained in the quarterly condition reports and the annual reports that are required to be submitted to SBA by such lenders.

3. What are the projected reporting, recordkeeping, and other compliance requirements of the rule and an estimate of the classes of small entities which will be subject to the requirements?

The proposed rule would impose a new reporting and/or recordkeeping requirement for organizations seeking to become an SBA Supervised Lender (or seeking SBA approval of a change of ownership or control). The proposed rule seeks to codify an existing requirement that applicants submit a complete application in order for SBA to determine whether an organization has the qualifications necessary to participate in the 7(a) Loan Program as an SBA Supervised Lender.

The LAP includes key information about an organization that would allow SBA to reach a preliminary assessment about the qualifications of an applicant more efficiently. SBA estimates it would receive approximately four LAPs each year. SBA estimates that it would take approximately 35 hours for an organization to prepare a LAP at a cost of $2,870 per LAP. Based on SBA's experience with similar data collections, we expect an organization that submits a LAP would need to employ the services of a financial manager and an administrative assistant when preparing a LAP for submission to SBA.[7] SBA specifically requests comments on whether the number of hours estimated to prepare a LAP is appropriate.

If an organization is authorized by SBA to proceed to the final review phase, a complete application must be submitted to SBA. As mentioned above, the application requirements for SBA Supervised Lenders are not new and are currently set forth in SBA's official policies and procedures. See SOP 50 10 5(K), Subpart A, Chapter 1, Paragraph II.C.2 for NFRLs and Subpart A, Chapter 2, Paragraph II for SBLCs. SBA estimates that it will receive approximately four complete applications each year. SBA estimates that it would take approximately 50 hours for an organization to prepare a complete application at a cost of $3,813 per application. Based on SBA's experience with similar data collections, an organization applying to become an SBA Supervised Lender would typically employ the services of a financial manager, an accountant, an attorney and an administrative assistant when preparing a complete application for submission to SBA.[8] SBA specifically requests comments on whether the number of hours estimated to prepare a complete application is appropriate.

SBA anticipates that there would be some costs related to the new minimum capital requirement under the proposed rule for SBA Supervised Lenders. This proposed rule establishes a new minimum capital requirement for SBLCs and NFRLs of at least $5 million and $2.5 million, respectively. Based on information provided to SBA by SBA Supervised Lenders in quarterly condition reports, 11 of the 14 SBLCs (*i.e.,* 79%) have at least $4.75 million in capital (and of those 11 SBLCs, nine have more than $5 million in capital). In addition, 18 of the 21 NFRLs (*i.e.,* 86%) have more than $2.5 million in capital.

SBA has determined that there are eight small entities that would be impacted by the new capital requirements in the proposed rule. In other words, eight of the 35 SBA Supervised Lenders that are considered small entities would need to increase their capital to reach the new minimum capital requirement of either $2.5 million or $5 million (as applicable). The estimated amount of capital that would need to be raised by these small entities ranges between $240,000 and

[7] The cost estimate for the LAP is based on hourly job position wages published by the U.S. Department of Labor's Bureau of Labor Statistics for 2018 and increased by 30% to account for benefits. The cost breakdown is as follows: Financial Manager (30 hours times an hourly rate of $91.77) plus Administrative Assistant (5 hours times an hourly rate of $23.43) equals $2,870.

[8] The cost estimate for a complete application is based on hourly job position wages published by the U.S. Department of Labor's Bureau of Labor Statistics for 2018 and increased by 30% to account for benefits. The cost breakdown is as follows: Financial Manager (30 hours times an hourly rate of $91.77) plus Accountant (10 hours times an hourly rate of $49.26) plus Attorney (5 hours times an hourly rate of $90.14) plus Administrative Assistant (5 hours times an hourly rate of $23.43) equals $3,813.

$3,580,000. SBA estimates that this proposed rule may have a significant economic impact on six of the 35 SBA Supervised Lenders (*i.e.,* 17%), each of which is considered a small entity. As noted above, all existing SBA Supervised Lenders would have three years from the effective date of a final rulemaking to comply with this part of the proposed rule (other than for transactions involving a change of ownership or control of an SBA Supervised Lender).

SBA estimates that the cost of raising capital for SBA Supervised Lenders is approximately 9.8% of the amount of equity capital raised based on the Capital Asset Pricing Model (CAPM). The CAPM is one of the most widely used pricing models by financial professionals and considered the preferred method to estimate the cost of equity capital. See Duff & Phelps 2019 Valuation Handbook—U.S. Industry Cost of Capital (data through June 30, 2019).[9] SBA estimates that the total cost of raising new equity capital for the eight SBA Supervised Lenders based on the requirements of the proposed rule would range in amount from approximately $23,000 to $350,000.[10] However, the cost is mitigated by the fact that under the proposed rule SBA Supervised Lenders would have three years to increase their capital. Thus, the maximum amount that it would cost an existing SBA Supervised Lender to reach the new minimum capital requirement would be approximately $117,000 per year for three consecutive years.[11]

SBA determined that a three year time frame was a sufficient amount of time for SBA Supervised Lenders to increase their capital. The three year time period is also consistent with SBA's existing requirements that SBA Supervised Lender applicants must have a detailed business and operations plan that includes three years of projected loan activity, secondary market activity and financial statements. See SOP 50 10. SBA specifically requests comments on whether SBA Supervised Lenders should have three years to comply with the new minimum capital requirements under this proposed rule or should be required to comply sooner.

The proposed rule also seeks to limit the 7(a) lending area for NFRLs to the state in which their primary state regulator is located, except that it may include a local trade area that is contiguous to such state (such as a city or metropolitan statistical area bisected by a state line). There are currently 21 NFRLs participating in the 7(a) Loan Program. During the last three fiscal years, two NFRLs (each of which is considered a small entity) requested loan authorizations to make the majority of their 7(a) loans outside of the state in which their primary state regulator is located. With the exception of these two NFRLs, approximately 90% of the lending within the 7(a) Loan Program during the last three fiscal years was done in the state where the NFRL's primary state regulator is located. Approximately 79% of all 7(a) loan approvals obtained by NFRLs during the last three fiscal years were for loans to be made to small businesses located within their own state. This part of the proposed rule would not impact a substantial number of small entities. It is important to note that this proposed rule will not impose any restrictions regarding an NFRL's non-7(a) lending activities. Therefore, the proposed rule would not have any impact on an NFRL's ability to generate business by making other types of loans (*e.g.,* conventional loans) outside of their own state.

In summary, SBA estimates that the total cost to a particular SBA Supervised Lender associated with this proposed rule (including the costs related to data collection) will range from zero to $356,683, substantially all of which relates to the cost of raising capital and may be spread over a three year time period.

4. What are the relevant Federal rules which may duplicate, overlap or conflict with the rule?

We are not aware of any Federal rules that duplicate, overlap or conflict with this rule. SBA's SOP 50 10 will have to be amended to conform to portions of this rule, which will be done separately.

5. *What alternatives will allow the Agency to accomplish its regulatory objectives while minimizing the impact on small entities?*

The Agency originally considered imposing the new minimum capital requirements for SBA Supervised Lenders immediately due to the risk associated with their lending operations. SBA recognized, however, that providing a three year period of time for SBA Supervised Lenders to increase their capital would be less burdensome on lenders and their operational plans. SBA took into consideration that some lenders may need time to plan their capital raising efforts and negotiate favorable terms and conditions for increasing their capital. The proposed three year time period will provide SBA Supervised Lenders with a sufficient amount of time to raise new equity capital and an opportunity to increase capital by retaining earnings (which will reduce the estimated overall cost of raising such capital).

SBA believes many of the proposed changes in this rule would benefit small entities interested in becoming an SBA Supervised Lender by clarifying areas in the application process where there was confusion and to make the process more transparent. This rule would also allow SBA to evaluate the qualifications of new applicants more efficiently and make well-informed decisions on SBA Supervised Lender applications. SBA believes this proposed rule encompasses best practice guidance that aligns with the Agency's mission to increase access to capital for small businesses and facilitate American job preservation and creation.

List of Subjects in 13 CFR Part 120

Community development, Equal employment opportunity, Loan programs—business, Reporting and recordkeeping requirements, Small businesses.

For the reasons stated in the preamble, SBA proposes to amend 13 CFR part 120 as follows:

PART 120—BUSINESS LOANS

■ 1. The authority for 13 CFR part 120 continues to read as follows:

Authority: 15 U.S.C. 634(b)(6), (b)(7), (b)(14), (h), and note, 636(a), (h) and (m), 650, 687(f), 696(3) and (7), and 697(a) and (e); Pub. L. 111–5, 123 Stat. 115, Pub. L. 111–240, 124 Stat. 2504.

§ 120.410 [Amended]

■ 2. Amend § 120.410(a)(1) by removing the phrase ''for SBLCs, meeting its SBA minimum capital requirement; and for NFRLs, meeting its state minimum capital requirement); and'' and adding in its place the phrase ''and for SBLCs and NFRLs, meeting their respective minimum capital requirement); and''.

■ 3. Amend § 120.460 by adding paragraphs (c) and (d) to read as follows:

[9] The 2019 Valuation Handbook—U.S. Industry Cost of Capital published by Duff & Phelps provides cost of capital estimates for approximately 170 industries identified by Standard Industrial Classification codes (SIC). For purposes of estimating the cost of raising equity capital for SBA Supervised Lenders, SBA used SIC code 61—non-depository credit institutions, which includes 21 companies that are engaged primarily in extending credit in the form of loans (but are not engaged in deposit banking). SBA compared the estimated cost of raising capital cited above with other sources and found the data to be similar.

[10] The estimated cost to raise $240,000 or $3.58 million in equity capital would be as follows: $240,000 times 9.8% equals $23,000; $3.58 million times 9.8% equals $350,000.

[11] It should be noted that some existing SBA Supervised Lenders may decide to increase their capital by retaining earnings instead of raising new equity capital, which would reduce the cost of this proposed rule.

§ 120.460 What are SBA's additional requirements for SBA Supervised Lenders?

* * * * *

(c) An SBA Supervised Lender must have qualified full-time professional management including, but not limited to, a chief executive officer or the equivalent to manage daily operations, and a chief credit/risk officer. An SBA Supervised Lender must also have at least one other full-time professional employee qualified by training and experience to carry out its business plan. An SBA Supervised Lender is expected to sustain a sufficient level of lending activity in its lending area. This paragraph only applies to SBA Supervised Lenders that make or acquire a 7(a) loan after [EFFECTIVE DATE OF THE FINAL RULE], or to any SBA Supervised Lender approved after such date, including in the event of a change of ownership or control.

(d) An NFRL may only make or acquire 7(a) loans in the state in which its primary state regulator is located, except that an NFRL's lending area may include a local trade area that is contiguous to such state (*e.g.,* a city or metropolitan statistical area that is bisected by a state line) if the NFRL receives SBA's prior written approval. This paragraph (d) only applies to NFRLs that make or acquire a 7(a) loan after [EFFECTIVE DATE OF THE FINAL RULE], or to any NFRL approved after such date, including in the event of a change of ownership or control.

■ 4. Amend § 120.462 by:

■ a. Removing the phrase ''by state regulators'' wherever it appears and adding in its place the phrase ''in § 120.462(a)(1)'';

■ b. Redesignating paragraphs (a) through (e) as paragraphs (b) through (f); and

■ c. Adding a new paragraph (a).

The addition to read as follows:

§ 120.462 What are SBA's additional requirements on capital maintenance for SBA Supervised Lenders?

(a) *Minimum capital requirements*—(1) *For NFRLs.* (i) Beginning on or after [DATE THREE YEARS FROM THE EFFECTIVE DATE OF THE FINAL RULE], each NFRL that makes or acquires a 7(a) loan must maintain the minimum capital required by its state regulator, or $2,500,000, whichever is greater.

(ii) Any NFRL approved on or after [EFFECTIVE DATE OF THE FINAL RULE], including in the event of a change of ownership or control, must maintain the minimum capital requirement set forth in paragraph (a)(1)(i) of this section.

(iii) Unless subject to paragraph (a)(1)(i) or (ii) of this section, an NFRL must comply with the minimum capital requirements for NFRLs that were in effect on [DATE ONE DAY PRIOR TO THE EFFECTIVE DATE OF THE FINAL RULE].

(2) *For SBLCs.* For information on minimum capital requirements for SBLCs, see § 120.471.

* * * * *

■ 5. Add § 120.466 to read as follows:

§ 120.466 SBA Supervised Lender application.

An entity seeking to participate as an SBA Supervised Lender must apply to SBA. SBA evaluates SBA Supervised Lender applicants through an initial review and final review, as follows:

(a) *Initial review.* SBA Supervised Lender applicants must submit a written plan containing information about the organization and its current and proposed lending activities (''Lender Assessment Plan''). After SBA's review of the Lender Assessment Plan, the Office of Capital Access may require an interview with the applicant and its management team. SBA will determine, in its sole discretion, whether an applicant may proceed to the final review. If SBA determines that an applicant may not proceed to the final review, the applicant must wait at least nine months before it may submit a new Lender Assessment Plan. Each applicant must demonstrate to SBA's satisfaction that it meets the ethical requirements and the participation criteria set forth in 13 CFR 120.140 and 120.410. The Lender Assessment Plan must include the following items:

(1) The legal name, address, telephone number and email address of the applicant;

(2) Business plan, detailing the applicant's proposed lending area and the volume of loan activity projected over the next three years (supported by current and projected balance sheets, income statements and statements of cash flows);

(3) Capitalization (current and proposed), including the form of organization and the identification of all debt and classes of equity capital and proposed funding amounts, including any rights or preferences accorded to such interests (*e.g.,* voting rights, redemption rights and rights of convertibility) and any conditions for the transfer, sale or assignment of such interests;

(4) A list of all members of the applicant's management team, including the applicant's officers, directors, managers and key employees, as well as the applicant's owners, Associates (as defined in § 120.10) and Affiliates (as defined in § 121.103 of this chapter);

(5) A written summary of the professional experience (including any prior experience with any SBA program) of the applicant's management team (including key employees);

(6) In connection with any application to become an SBLC, the applicant must include a letter agreement signed by an authorized official of an existing SBLC certifying that the SBLC is seeking to transfer its SBA lending authority to the applicant; and

(7) If approval of any state or Federal chartering, licensing or other regulatory authority is required, copies of any licenses issued by or documents filed with such authority.

(b) *Final review.* Each applicant that receives notice from SBA in writing that it may proceed to the final review must submit a complete application to SBA within 90 calendar days. The application requirements for SBA Supervised Lenders are set forth in official SBA policy and procedures. An incomplete application submitted to SBA will not be processed and will be returned to the applicant. SBA may, in its sole discretion, approve or deny any SBA Supervised Lender application. The decision to approve or deny an SBA Supervised Lender application is a final agency decision. If an SBA Supervised Lender application is denied by SBA or if a complete application is not timely submitted, the applicant may not submit a new Lender Assessment Plan and restart the application process until 18 months from the date of denial or the date a complete application was due to SBA, as applicable.

(c) *NFRL operating and lending experience requirement.* For an entity seeking to become an NFRL, evidence of at least one year of current operating and relevant commercial lending experience must be provided.

■ 6. Add § 120.467 to read as follows:

§ 120.467 Evaluation of SBA Supervised Lender applicants.

(a) SBA will evaluate an SBA Supervised Lender applicant based on information from, among other sources, the Lender Assessment Plan, an interview with the applicant's management team (if required), the application and any other documentation submitted by the applicant, the results of background investigations, public record searches and due diligence conducted by SBA or other Federal or state agencies. SBA's evaluation will consider factors such as the following:

(1) Professional qualifications of its management team (including key employees), including demonstrated commercial lending experience,

business reputation, adherence to legal and ethical standards, track record in making and monitoring business loans, and prior history, if any, working as an officer, manager, director or key employee of a lender involved in any SBA program or any other Federal or state lending program.

(2) Historical performance measures of loans originated by the applicant or attributable to its management team (including key employees), including loan default rates, purchase rates and loss rates, measured in both percentage terms and in comparison to appropriate industry benchmarks, review/examination assessments and other performance measures.

(3) The applicant's capitalization, organizational structure, business plan (including any risk factors), projected financial performance, financial strength, liquidity, the soundness of its financial projections and underlying assumptions, loan underwriting process, operations plan and the history of compliance of the applicant and its management team (including key employees) with SBA Loan Program Requirements.

(4) Whether the NFRL's state regulator and the state statute or regulations governing the NFRL's operations, including but not limited to those pertaining to audit, examination, supervision, enforcement and information sharing, are satisfactory to SBA in its sole discretion.

(5) For changes of ownership or control, in addition to the factors listed in paragraphs (a)(1) through (4) of this section, SBA will consider whether the applicant's plan for the resolution of any outstanding monetary liabilities to SBA, including repairs and denials and civil monetary penalties, is acceptable to SBA in its sole discretion.

(b) SBA may prohibit any individual or entity from participating as an officer, director, manager, owner or key employee of the applicant if such individual or entity:

(1) Has a previous record of failing to comply with SBA Loan Program Requirements;

(2) Previously participated in a material way with any past or present SBA Lender or Intermediary that failed to maintain satisfactory SBA performance;

(3) Previously defaulted on any Federal loan or Federally assisted financing that resulted in the Federal Government or any of its agencies or departments sustaining a loss in any of its programs; or

(4) Ever failed to pay when due any debt or obligation, including any amounts in dispute, to the Federal Government or guaranteed by the Federal Government (including but not limited to taxes or business or student loans).

■ 7. Add § 120.468 to read as follows:

§ 120.468 Change of ownership or control requirements for SBA Supervised Lenders.

(a) *SBA prior approval required.* Any change of ownership or control of an SBA Supervised Lender without SBA's prior written approval is prohibited. Prior to entering into any definitive agreement for a change of ownership or control, SBA Supervised Lenders must receive SBA's prior written approval from the appropriate SBA official in accordance with Delegations of Authority. An SBA Supervised Lender may not register proposed new owners on its books and records or permit them to participate in any manner in the conduct of the SBA Supervised Lender's affairs unless approved in writing by SBA. Any type of agreement or letter of intent regarding a prospective change of ownership or control must be reported to SBA within 30 calendar days as required by § 120.464(a)(5). A change of ownership or control includes the following:

(1) Any transfer(s) (direct or indirect) of 10 percent or more of any class of the SBA Supervised Lender's stock or ownership interests (or series of transfers which, in the aggregate over an 18 month period, equals 10 percent or more), or any agreement providing for such transfer;

(2) Any transfer(s) (direct or indirect) that could result in the beneficial ownership by any person or group of persons acting in concert of 10 percent or more of any class of the SBA Supervised Lender's stock or ownership interests, or any agreement providing for such transfer(s);

(3) Any merger, consolidation, or reorganization;

(4) Any other transaction or agreement that transfers control of an SBA Supervised Lender; or

(5) Any other transaction or event that results in any change in the possession (direct or indirect) of the right to control, or the power to direct or cause the direction of, the management or policies of an SBA Supervised Lender, whether through the ownership of voting securities, by contract or otherwise.

(b) *Approval required by other regulatory authorities.* If a change of ownership or control of an SBA Supervised Lender is subject to the approval of any state or Federal chartering, licensing or other regulatory authority, copies of any documents filed with such authority must, at the same time, be transmitted to the appropriate SBA official in accordance with Delegations of Authority. The approval of any state or Federal authority will be required in addition to SBA's prior written approval.

(c) *Application requirements for changes of ownership or control.* An applicant must submit a Lender Assessment Plan and a new application in accordance with § 120.466 for any change of ownership or control. If a proposed change of ownership is for less than 50% of the ownership interests in an SBA Supervised Lender, SBA may, in its sole discretion, limit the requirements of the Lender Assessment Plan or the complete application as set forth in official SBA policy and procedures.

(d) *Voluntary surrender of SBA lending authority.* An SBA Supervised Lender may voluntarily surrender its SBA lending authority (including its SBLC license, as applicable) and withdraw as a participating Lender with SBA's prior written approval. The SBA Supervised Lender must agree to transfer its entire 7(a) loan portfolio to one or more Lenders acceptable to SBA in accordance with § 120.432(a), and enter into a withdrawal agreement to resolve any outstanding issues, including any outstanding monetary liabilities, to SBA's satisfaction.

§ 120.470 [Amended]

■ 8. Amend § 120.470 by removing paragraph (g) and redesignating paragraph (h) as paragraph (g).

■ 9. Amend § 120.471 by:

■ a. Revising paragraph (a);

■ b. Redesignating paragraphs (b)(3) through (5) as paragraphs (b)(4) through (6) respectively; and

■ c. Adding new paragraph (b)(3).

The revision and addition to read as follows:

§ 120.471 What are the minimum capital requirements for SBLCs?

(a) *Minimum capital requirements.* (1) Beginning on or after [DATE THREE YEARS FROM THE EFFECTIVE DATE OF THE FINAL RULE], each SBLC that makes or acquires a 7(a) loan must maintain, at a minimum, unencumbered paid-in capital and paid-in surplus of at least $5,000,000, or ten percent of the aggregate of its share of all outstanding loans, whichever is greater.

(2) Any SBLC approved on or after [EFFECTIVE DATE OF THE FINAL RULE], including in the event of a change of ownership or control, must maintain the minimum capital requirement set forth in paragraph (a)(1) of this section.

(3) Unless subject to paragraph (a)(1) or (2) of this section, an SBLC must

comply with the minimum capital requirements that were in effect on [DATE ONE DAY PRIOR TO THE EFFECTIVE DATE OF THE FINAL RULE].

(b) * * *

(3) Unrestricted net assets (for non-profit corporations);

* * * * *

§ 120.475 [Removed and Reserved]

■ 10. Remove and reserve § 120.475.

Dated: December 31, 2019.

Christopher Pilkerton,

Acting Administrator.

[FR Doc. 2019–28500 Filed 1–10–20; 8:45 am]

BILLING CODE 8025–01–P

DEPARTMENT OF TRANSPORTATION

Federal Highway Administration

23 CFR Part 650

[FHWA Docket No. FHWA–2017–0047]

RIN 2125–AF55

National Bridge Inspection Standards

AGENCY: Federal Highway Administration (FHWA), U.S. Department of Transportation (DOT).

ACTION: Notice of proposed rulemaking; extension of comment period.

SUMMARY: The FHWA is extending the comment period for a notice of proposed rulemaking (NPRM) and request for comments, which was published on November 12, 2019. The original comment period is set to close on January 13, 2020. The extension is based on FHWA's desire to allow interested parties sufficient time to review and provide comprehensive comments on this NPRM. Therefore, the closing date for comments is changed to March 13, 2020, which will provide those interested in commenting additional time to discuss, evaluate, and submit responses to the docket.

DATES: The comment period for the proposed rule published November 12, 2019, at 84 FR 61494, is extended. Comments must be received on or before March 13, 2020.

ADDRESSES: Mail or hand deliver comments to the U.S. Department of Transportation, Dockets Management Facility, 1200 New Jersey Avenue SE, Washington, DC 20590, or submit electronically at *http://www.regulations.gov.* All comments should include the docket number that appears in the heading of this document. All comments received will be available for examination and copying at the above address from 9 a.m. to 5 p.m., e.t., Monday through Friday, except Federal holidays. Those desiring notification of receipt of comments must include a self-addressed, stamped postcard or may print the acknowledgment page that appears after submitting comments electronically. Anyone is able to search the electronic form of all comments received into any of our dockets by the name of the individual submitting the comment (or signing the comment, if submitted on behalf of an association, business, labor union, etc.). You may review DOT's complete Privacy Act Statement in the **Federal Register** published on April 11, 2000 (Volume 65, Number 70, Pages 19477–78) or you may visit *http://www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: Mr. John Thiel, P.E., Office of Bridges and Structures, HIBS–30, (202) 366–8795, or Mr. William Winne, Office of the Chief Counsel, HCC–30, (202) 366–1397, Federal Highway Administration, 1200 New Jersey Avenue SE, Washington, DC 20590.

SUPPLEMENTARY INFORMATION:

Electronic Access and Filing

You may submit or access all comments received by DOT online through: *http://www.regulations.gov.* Electronic submission and retrieval help and guidelines are available on the website. It is available 24 hours each day, 365 days each year. Please follow the instructions. An electronic copy of this document may also be downloaded from the **Federal Register**'s home page at: *http://www.federalregister.gov.*

Background

On November 12, 2019, at 84 FR 61494, FHWA published in the **Federal Register** an NPRM proposing to update the National Bridge Inspection Standards (NBIS). Through this NPRM, FHWA proposes to update the NBIS to address the Moving Ahead for Progress in the 21st Century Act requirements, incorporate technological advancements including the use of unmanned aerial systems, and address ambiguities identified since the last update to the regulation in 2009. The FHWA also proposes to repeal two outdated regulations: The Highway Bridge Replacement and Rehabilitation Program and the Discretionary Bridge Candidate Rating Factor.

The original comment period for the NPRM closes on January 13, 2020. The FHWA believes that this closing date may not provide sufficient time to review and provide comprehensive comments. The extension is in the public interest based on FHWA's desire to allow interested parties sufficient time to review and provide comprehensive comments on this NPRM. To allow the public to submit comprehensive comments, the closing date is changed from January 13, 2020, to March 13, 2020.

Authority: 23 U.S.C. 119, 144, and 315.

Issued on: January 7, 2020.

Nicole R. Nason,

Administrator, Federal Highway Administration.

[FR Doc. 2020–00315 Filed 1–10–20; 8:45 am]

BILLING CODE 4910–22–P

DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 167

[USCG–2018–1058]

Extension of Comment Period for the Port Access Route Study: Alaskan Arctic Coast

AGENCY: Coast Guard, DHS.

ACTION: Notice of extension of comment period.

SUMMARY: The United States Coast Guard is extending the comment period for the notice of study and request for comments for the Port Access Route Study: Alaskan Arctic Coast that we published on December 21, 2018. This action will provide the public with additional time and opportunity to provide the Coast Guard with information regarding the Port Access Route Study: Alaskan Arctic Coast. The comment period is extended until June 30, 2020.

DATES: Comments and related material must be received by the Coast Guard on or before June 30, 2020.

ADDRESSES: You may submit comments identified by docket number USCG–2018–1058 using the Federal eRulemaking Portal at *https://www.regulations.gov.* If your material cannot be submitted using *https://www.regulations.gov,* contact the person in the **FOR FURTHER INFORMATION CONTACT** section of this document for alternate instructions.

FOR FURTHER INFORMATION CONTACT: If you have questions about this notice, please contact LCDR Michael Newell, Seventeenth Coast Guard District (dpw), at telephone number (907) 463–2263 or email *Michael.D.Newell@uscg.mil,* or Mr. David Seris, Seventeenth Coast Guard District (dpw), at telephone

number (907) 463–2267 or email to *David.M.Seris@uscg.mil,* or LT Stephanie Bugyis, Seventeenth Coast Guard District (dpw), at telephone number (907) 463–2265 or email to *Stephanie.M.Bugyis@uscg.mil.*

SUPPLEMENTARY INFORMATION: On December 21, 2018, the Coast Guard published a notice of study and request for comments for the Port Access Route Study: Alaskan Artic Coast (83 FR 65701). The comment period in that document closed September 1, 2019. On September 4, 2019, the Coast Guard published a notice to extend the public comment period until January 30, 2020. In this action, the Coast Guard is providing notice that the public comment period is extended until June 30, 2020. Documents mentioned in this notice, and all public comments, are in our online docket at *https://www.regulations.gov* and can be viewed by searching the docket number ''USCG–2018–1058''.

This notice is issued under authority of 33 U.S.C. 1223(c) and 5 U.S.C. 552.

Dated: January 6, 2020.

Matthew T. Bell, Jr.,

Rear Admiral, U.S. Coast Guard, Commander, Seventeenth Coast Guard District.

[FR Doc. 2020–00279 Filed 1–10–20; 8:45 am]

BILLING CODE 4910–15–P

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[EPA–R07–OAR–2019–0707; FRL–10004–00–Region 7]

Air Plan Approval; Missouri; Open Burning

AGENCY: Environmental Protection Agency (EPA).

ACTION: Proposed rule.

SUMMARY: The Environmental Protection Agency (EPA) is proposing approval of a State Implementation Plan (SIP) revision submitted by Missouri on March 7, 2019. Missouri requests that EPA revise its open burning rule. These revisions include adding definitions to the rule, removing certain provisions from the rule, consolidating requirements, and removing incorporations by reference. The EPA's proposed approval of this rule revision is being done in accordance with the requirements of the Clean Air Act (CAA).

DATES: Comments must be received on or before February 12, 2020.

ADDRESSES: You may send comments, identified by Docket ID No. EPA–R07–OAR–2019–0707 to *https://www.regulations.gov.* Follow the online instructions for submitting comments.

Instructions: All submissions received must include the Docket ID No. for this rulemaking. Comments received will be posted without change to *https://www.regulations.gov/,* including any personal information provided. For detailed instructions on sending comments and additional information on the rulemaking process, see the ''Written Comments'' heading of the **SUPPLEMENTARY INFORMATION** section of this document.

FOR FURTHER INFORMATION CONTACT: Tracey Casburn, Environmental Protection Agency, Region 7 Office, Air Quality Planning Branch, 11201 Renner Boulevard, Lenexa, Kansas 66219; telephone number (913) 551–7016; email address *casburn.tracey@epa.gov.*

SUPPLEMENTARY INFORMATION: Throughout this document ''we,'' ''us,'' and ''our'' refer to the EPA.

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I. Written Comments

Submit your comments, identified by Docket ID No. EPA–R07–OAR–2019–0707, at *https://www.regulations.gov.* Once submitted, comments cannot be edited or removed from *Regulations.gov.* The EPA may publish any comment received to its public docket. Do not submit electronically any information you consider to be Confidential Business Information (CBI) or other information whose disclosure is restricted by statute. Multimedia submissions (audio, video, etc.) must be accompanied by a written comment. The written comment is considered the official comment and should include discussion of all points you wish to make. The EPA will generally not consider comments or comment contents located outside of the primary submission (*i.e.,* on the web, cloud, or other file sharing system). For additional submission methods, the full EPA public comment policy, information about CBI or multimedia submissions, and general guidance on making effective comments, please visit *https://www.epa.gov/dockets/commenting-epa-dockets.*

II. What is being addressed in this document?

The EPA is proposing to approve revisions to 10 Code of State Regulation (CSR) 10–6.045, *Open Burning,* in the Missouri SIP. Missouri made several revisions to the rule. These revisions are described in detail in the technical support document (TSD) included in the docket for this action.

Missouri received seventeen comments from five sources during the comment period. EPA provided five comments on the rule. Missouri responded to all seventeen comments, as noted in the state submission included in the docket for this action. Missouri responded to EPA's comments and, as described in the TSD for this action, amended the rule, in response to some of EPA's comments.

Therefore, EPA is proposing to approve the revisions to this rule because it will not have a negative impact on air quality.

III. Have the requirements for approval of a SIP revision been met?

The State submission has met the public notice requirements for SIP submissions in accordance with 40 CFR 51.102. The submission also satisfied the completeness criteria of 40 CFR part 51, appendix V. The State provided public notice on this SIP revision from August 1, 2018 to September 30, 2018 and received seventeen comments. As stated above, MDNR responded to all comments. In addition, as explained above, the revision meets the substantive SIP requirements of the CAA, including section 110 and implementing regulations.

IV. What action is the EPA taking?

The EPA is proposing to approve Missouri's request to revise 10 CSR 10–6.045. We are processing this as a proposed action because we are soliciting comments on this proposed action. Final rulemaking will occur after consideration of any comments.

V. Incorporation by Reference

In this document, the EPA is proposing to include regulatory text in an EPA final rule that includes incorporation by reference. In accordance with requirements of 1 CFR 51.5, the EPA is proposing to incorporate by reference the Missouri Regulations described in the proposed amendments to 40 CFR part 52 set forth below. The EPA has made, and will continue to make, these materials generally available through www.regulations.gov and at the EPA Region 7 Office (please contact the person identified in the **FOR FURTHER**

INFORMATION CONTACT section of this preamble for more information).

VI. Statutory and Executive Order Reviews

Under the CAA, the Administrator is required to approve a SIP submission that complies with the provisions of the Act and applicable Federal regulations. 42 U.S.C. 7410(k); 40 CFR 52.02(a). Thus, in reviewing SIP submissions, the EPA's role is to approve state choices, provided that they meet the criteria of the CAA. Accordingly, this action merely approves state law as meeting Federal requirements and does not impose additional requirements beyond those imposed by state law. For that reason, this action:

- Is not a significant regulatory action subject to review by the Office of Management and Budget under Executive Orders 12866 (58 FR 51735, October 4, 1993) and 13563 (76 FR 3821, January 21, 2011);
- Is not an Executive Order 13771 (82 FR 9339, February 2, 2017) regulatory action because SIP approvals are exempted under Executive Order 12866.
- Does not impose an information collection burden under the provisions of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*);
- Is certified as not having a significant economic impact on a substantial number of small entities under the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*);
- Does not contain any unfunded mandate or significantly or uniquely affect small governments, as described in the Unfunded Mandates Reform Act of 1995 (Pub. L. 104–4);
- Does not have Federalism implications as specified in Executive Order 13132 (64 FR 43255, August 10, 1999);
- Is not an economically significant regulatory action based on health or safety risks subject to Executive Order 13045 (62 FR 19885, April 23, 1997);
- Is not a significant regulatory action subject to Executive Order 13211 (66 FR 28355, May 22, 2001);
- Is not subject to requirements of the National Technology Transfer and Advancement Act (NTTA) because this rulemaking does not involve technical standards; and
- Does not provide EPA with the discretionary authority to address, as appropriate, disproportionate human health or environmental effects, using practicable and legally permissible methods, under Executive Order 12898 (59 FR 7629, February 16, 1994).

The SIP is not approved to apply on any Indian reservation land or in any other area where EPA or an Indian tribe has demonstrated that a tribe has jurisdiction. In those areas of Indian country, the rule does not have tribal implications and will not impose substantial direct costs on tribal governments or preempt tribal law as specified by Executive Order 13175 (65 FR 67249, November 9, 2000).

List of Subjects in 40 CFR Part 52

Environmental protection, Air pollution control, Incorporation by reference, Reporting and recordkeeping requirements, Volatile organic compounds, Particulate matter, Sulfur dioxide, Nitrogen oxide.

Dated: January 7, 2020.

Edward Chu,

Acting Regional Administrator, Region 7.

For the reasons stated in the preamble, the EPA proposes to amend 40 CFR part 52 as set forth below:

PART 52—APPROVAL AND PROMULGATION OF IMPLEMENTATION PLANS

■ 1. The authority citation for part 52 continues to read as follows:

Authority: 42 U.S.C. 7401 *et seq.*

Subpart–AA Missouri

■ 2. In § 52.1320, the table in paragraph (c) is amended by revising the entry ''10–6.045'' to read as follows:

§ 52.1320 Identification of plan.

* * * * *

(c) * * *

EPA-APPROVED MISSOURI REGULATIONS

Missouri citation	Title	State effective date	EPA approval date	Explanation
Missouri Department of Natural Resources				
*	*	*	*	*
Chapter 6—Air Quality Standards, Definitions, Sampling and Reference Methods, and Air Pollution Control Regulations for the State of Missouri				
*	*	*	*	*
10–6.045	Open Burning	2/28/2019	[Date of publication of the final rule in the **Federal Register**], [**Federal Register** citation of the final rule].	
*	*	*	*	*

* * * * *

[FR Doc. 2020–00266 Filed 1–10–20; 8:45 am]

BILLING CODE 6560–50–P

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[EPA–R04–OAR–2019–0457; FRL–10004–06–Region 4]

Air Plan Approval; Georgia; Revisions to Aerospace VOC Rule

AGENCY: Environmental Protection Agency (EPA).

ACTION: Proposed rule.

SUMMARY: The Environmental Protection Agency (EPA) is proposing to approve a State Implementation Plan (SIP) revision submitted by the State of Georgia, through the Georgia Environmental Protection Division (GA EPD), on June 6, 2019, for the purpose of updating Georgia's rule titled *Volatile Organic Compound (VOC) Emissions from Aerospace Manufacturing and Rework Facilities.* EPA is proposing action on this Georgia SIP revision under the Clean Air Act (CAA or Act).

DATES: Comments must be received on or before February 12, 2020.

ADDRESSES: Submit your comments, identified by Docket ID No. EPA–R04–OAR–2019–0457 at *www.regulations.gov.* Follow the online instructions for submitting comments. Once submitted, comments cannot be edited or removed from *Regulations.gov*. EPA may publish any comment received to its public docket. Do not submit electronically any information you consider to be Confidential Business Information (CBI) or other information whose disclosure is restricted by statute. Multimedia submissions (audio, video, etc.) must be accompanied by a written comment. The written comment is considered the official comment and should include discussion of all points you wish to make. EPA will generally not consider comments or comment contents located outside of the primary submission (*i.e.,* on the web, cloud, or other file sharing system). For additional submission methods, the full EPA public comment policy, information about CBI or multimedia submissions, and general guidance on making effective comments, please visit *www2.epa.gov/dockets/commenting-epa-dockets.*

FOR FURTHER INFORMATION CONTACT: Evan Adams, Air Regulatory Management Section, Air Planning and Implementation Branch, Air and Radiation Division, U.S. Environmental Protection Agency, Region 4, 61 Forsyth Street SW, Atlanta, Georgia 30303–8960. The telephone number is (404) 562–9009. Mr. Adams can also be reached via electronic mail at *adams.evan@epa.gov.*

SUPPLEMENTARY INFORMATION:

I. EPA's Action

A. Background

The action being proposed revises the reasonably available control technology (RACT) standard for VOC emissions at aerospace manufacturing and rework facilities in the State of Georgia. Additionally, other administrative changes are being proposed in this action.

Section 182(b)(2) of the CAA requires states to adopt RACT rules for all areas designated nonattainment for ozone and classified as moderate or above. Under Section 182(b)(2), these RACT requirements apply to: (1) Sources covered by an existing Control Technique Guideline (CTG) (*i.e.,* a CTG issued prior to enactment of the 1990 amendments to the CAA); (2) sources covered by a post-enactment CTG; and (3) all major sources not covered by a CTG (*i.e.,* non-CTG sources). Pursuant to 40 CFR 51.165, a major source for a moderate ozone area is a source that emits 100 tons per year (tpy) or more of VOC or nitrogen oxides (NO_X).

EPA defines RACT as ''the lowest emission limit that a particular source is capable of meeting by the application of control technology that is reasonably available considering technological and economic feasibility.'' *See* 44 FR 53761, 53762 (September 17, 1979). EPA has issued CTGs that present feasible RACT control measures for VOC source categories. The CTGs recommend a ''presumptive norm'' or ''presumptive RACT'' that EPA believes satisfies the definition of RACT.

The CTGs established by EPA are guidance to the states and only provide recommendations. A state can develop its own strategy for what constitutes RACT for the various CTG categories. EPA will review that strategy in the context of the SIP process and determine whether it meets the RACT requirements of the CAA and its implementing regulations.

EPA promulgated a National Emission Standard for Hazardous Air Pollutants (NESHAP) applicable to aerospace manufacturing and rework facilities on September 1, 1995. *See* 60 FR 45948. The NESHAP is codified at 40 CFR part 63, subpart GG. Subsequently, in December 1997, EPA published a CTG titled ''Control of Volatile Organic Compound Emissions from Coating Operations at Aerospace Manufacturing and Rework Operations.'' [1] EPA subsequently amended the NESHAP on December 7, 2015 (80 FR 76152) to incorporate revisions to the emission standards for specialty coatings, allow for annual purchase records of certain coatings, exempt two additional application methods, and update definitions.

EPA initially approved GA EPD's RACT for aerospace manufacturing and rework facilities—codified at Rule 391–3–1–.02(2)(kkk)—on July 10, 2001 (66 FR 35906). EPA approved subsequent amendments to that rule on September 28, 2012 (77 FR 55994) and March 19, 2013 (78 FR 16783) (correcting amendments), including Georgia's expansion of the rule's applicability to include all the counties in the Atlanta nonattainment area. The purpose of this rule is to limit VOC emissions from aerospace manufacturing and rework facilities that are located within or contribute to ozone levels in ozone nonattainment areas. The rules also limit VOC emissions from major sources (emitting greater than 100 tpy of VOC emissions) located outside the ozone nonattainment area.

B. Why is EPA proposing this action?

Georgia's June 6, 2019, submission amends RACT requirements applicable to VOC emissions from aerospace manufacturing and rework facilities at Georgia Rule 391–3–1–.02(2)(kkk). The rule changes incorporate EPA's December 7, 2015 (80 FR 76152) revisions to the NESHAP. As discussed below, EPA is proposing to conclude that the revisions are consistent with the CAA and the CTG.

The changes in the June 6, 2019, submittal replicate updates made to 40 CFR part 63, subpart GG, and are compliant with the State's RACT requirements. The amendments begin at Table (kkk)–1 *Specialty Coating VOC Limitations* and make changes to include the metric equivalent of the VOC Content Limit. The addition of the VOC Content Limit (g/L) column replicates Table 4–1. *Specialty Coatings VOC Content Limit* (g/L) in the CTG guidance document. This specific revision provides no substantive change and better serves the regulated community.

Georgia also revises the allowable application techniques for primers, topcoats, and specialty coatings under subparagraph 3 of the Rule. First, GA EPD adds language clarifying that the

[1] *Available at https://www3.epa.gov/airquality/ctg_act/199712_voc_epa453_r-97-004_aerospace_rework.pdf.*

limits on application techniques apply only to ''spray applied'' methods. GA EPD also removes from the list all non-spray application methods, such as brush, roll, and dip coating. As EPA explained in its final rule amending the NESHAP applicable to aerospace facilities, non-spray application techniques are properly exempted from the scope of the rule because they do not cause VOC emissions. *See* 80 FR at 76155.

GA EPD also adds to subparagraph 9 several activities that would be exempted from Rule 391–3–1–.02(2)(kkk). First, GA EPD exempts chemical milling, as well as specific primers, topcoats, specialty coatings, chemical milling maskants, strippers, and cleaning solvents that meet the definition of non-VOC materials. EPA notes that these types of coatings are not regulated by the CTG or the NESHAP.[2] Moreover, GA EPD retains requirements applicable to chemical milling maskants (defined as coatings that are applied directly to aluminum components to protect surface areas when chemical milling the component with a Type I or Type II etchant), as well as maskants that must be used with a combination of Type I or II etchants and any of the above types of maskants (*i.e.,* bonding, critical use and line sealer, and seal coat).[3] EPA has preliminarily concluded that these changes are consistent with the CTG.

In Subparagraph 9(xiv), parts and assemblies not critical to the structural integrity of the vehicle or flight performance would be exempted from Rule 391–3–1–.02(2)(kkk). This provision would exempt from the RACT requirements the manufacture or rework of certain non-critical airplane components, such as tray tables and seat panels. EPA notes that the manufacture or rework of these non-critical components are already subject to separate RACT requirements under Georgia's SIP-approved Rule 391–3–1–.02(2)(vvv)—VOC Emissions from Surface Coating of Miscellaneous Plastic Parts and Products.[4] Thus, EPA believes that the exemption of these activities from Georgia's aerospace RACT rule will not negatively impact VOC emissions. Accordingly, EPA is preliminarily concluding that the exemption of these activities from the aerospace-specific Rule 391–3–1–.02(2)(kkk) is consistent with the CTG and with RACT.

Additionally, the revised Rule 391–3–1–.02(2)(kkk) would provide an exemption for primers, topcoats, and specialty coatings that meet the definition of ''classified national security information'' in Subparagraph 17(xvii). This exemption is consistent with RACT, as well as Executive Order 13526, ''Classified National Security Information,'' December 29, 2009, which outlines the different components and restrictions applicable to certain classified materials.

Finally, GA EPD adds an exemption for the rework of aircraft or aircraft components if the holder of the Federal Aviation Administration design approval, or the holder's licensee, is not actively manufacturing the aircraft or aircraft components. As EPA noted in its September 1, 1998 rulemaking amending 40 CFR part 63, subpart GG, this exemption would apply to facilities that rework aircraft or aircraft components whose original manufacturer has gone out of business. *See* 63 FR 46526, 46528 (Sept. 1, 1998). EPA also noted that this exemption only affects small numbers of aircraft, and that compliance with VOC limits in these circumstances would involve considerable expense. *Id.* For these reasons, EPA is preliminarily concluding that this exemption is consistent with RACT.

At subparagraph 10, GA EPD removes an exemption from specialty coating requirements for low volume specialty coatings used under a specified twelve-month average quantity. EPA believes the removal of this exemption will be SIP strengthening and is, thus, proposing to approve it.

At Subparagraph 11, GA EPD removes the exemption for specialty coatings and exempts spray applications of no more than 3.0 fluid ounces of coating in a single application from a hand-held device with a paint cup capacity that is equal to or less than 3.0 fluid ounces. EPA believes that application of this quantity of coating will cause minimal, if any, emissions.

The revision would also exempt adhesives, sealants, maskants, caulking materials, and inks under Subparagraph 11, as well as the application of coatings that contain less than 0.17 pounds of VOC per gallon of coating. EPA notes that adhesives, sealants, maskants, caulking materials, and inks are not atomized in the same way as other coatings during application and, therefore, are not high emitters of VOCs during the application process. In addition, coatings that contain less than 0.17 pounds of VOC per gallon (20 grams/liter) are low category emitters.[5] EPA also notes that activities qualifying for the exemption must comply with the emission limits at subparagraphs 1 and 2—and are only exempted from certain operational limits in Subparagraphs 3 and 4 (*i.e.,* limits on application techniques, requirement to comply with applicable operational procedures). In these circumstances, EPA has preliminarily concluded that GA EPD's revisions to the exemption at Subparagraph 11 are consistent with RACT.

In subparagraph 15, GA EPD adds additional recordkeeping requirements, as determined by the specific compliance option chosen at Subparagraph 2. EPA believes the addition of these recordkeeping requirements will be SIP strengthening it requires affected facilities to retain certain records that are directly related to their chosen method of compliance. Thus, EPA has preliminarily concluded that these requirements are consistent with the CTG's monitoring, recordkeeping, and reporting requirements.

GA EPD also makes minor administrative changes throughout the rule, such as revising definitions at Subparagraph 17 and renumbering certain sections and subparagraphs. In conclusion, EPA has preliminarily determined the standard in the Georgia SIP that regulates aerospace and rework facilities aligns with the applicable CTG and meets the RACT requirements. Furthermore, EPA does not foresee any emissions increase from this SIP revision. EPA is thus proposing to approve changes to Rule 391–3–1–.02(2)(kkk), as included in Georgia's June 6, 2019 submittal.

II. Incorporation by Reference

In this document, EPA is proposing to include in a proposed EPA rule regulatory text that includes incorporation by reference. In accordance with requirements of 1 CFR 51.5, EPA is proposing to incorporate by reference the Georgia Regulation subparagraph 391–3–1–.02(2)(kkk) entitled ''VOC Emissions from Aerospace Manufacturing and Rework Facilities,'' effective February 17, 2019, which incorporates revisions to the emission standards for specialty coatings, allows for annual purchase records of certain coatings, exempts two

[2] Non-VOC materials are defined as a primer, topcoat, specialty coating, chemical milling maskant, cleaning solvent or stripper that contains no more than 1.0 percent by mass VOC in Subparagraph 17 of this Rule.

[3] *See* EPA's action on December 7, 2015 (80 FR 76152), ''National Emissions Standard for Aerospace Manufacturing and Rework Facilities Risk and Technology Review''; *see also* Type I and Type II etchant definitions in this rulemaking.

[4] *See* 67 FR 72276, 72280 (Dec. 4, 2002).

[5] EPA notes that the CTG and GA's RACT rule regulate coatings with significantly higher VOC concentrations at Table 4–1 of the CTG and Table (kkk)–1 of Georgia Rule 391–3–1–.02(2)(kkk), respectively.

additional application methods, and updates definitions.

EPA has made, and will continue to make, these materials generally available through *www.regulations.gov* and at the EPA Region 4 office (please contact the person identified in the ''For Further Information Contact'' section of this preamble for more information).

III. Proposed Action

EPA is proposing to approve the Georgia SIP revision to Rule 391–3–1–.02(2)(kkk), ''VOC Emissions from Aerospace Manufacturing and Rework Facilities,'' submitted on June 6, 2019. EPA has evaluated Georgia's submittal and preliminarily determined that they meet the applicable requirements of the CAA and EPA regulations.

IV. Statutory and Executive Order Reviews

Under the CAA, the Administrator is required to approve a SIP submission that complies with the provisions of the Act and applicable Federal regulations. *See* 42 U.S.C. 7410(k); 40 CFR 52.02(a). Thus, in reviewing SIP submissions, EPA's role is to approve state choices, provided that they meet the criteria of the CAA. This action merely proposes to approve state law as meeting Federal requirements and does not impose additional requirements beyond those imposed by state law. For that reason, this proposed action:

- Is not a significant regulatory action subject to review by the Office of Management and Budget under Executive Orders 12866 (58 FR 51735, October 4, 1993) and 13563 (76 FR 3821, January 21, 2011);
- Is not an Executive Order 13771 (82 FR 9339, February 2, 2017) regulatory action because SIP approvals are exempted under Executive Order 12866;
- Does not impose an information collection burden under the provisions of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*);
- Is certified as not having a significant economic impact on a substantial number of small entities under the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*);
- Does not contain any unfunded mandate or significantly or uniquely affect small governments, as described in the Unfunded Mandates Reform Act of 1995 (Pub. L. 104–4);
- Does not have Federalism implications as specified in Executive Order 13132 (64 FR 43255, August 10, 1999);
- Is not an economically significant regulatory action based on health or safety risks subject to Executive Order 13045 (62 FR 19885, April 23, 1997);
- Is not a significant regulatory action subject to Executive Order 13211 (66 FR 28355, May 22, 2001);
- Is not subject to requirements of Section 12(d) of the National Technology Transfer and Advancement Act of 1995 (15 U.S.C. 272 note) because application of those requirements would be inconsistent with the CAA; and
- Does not provide EPA with the discretionary authority to address, as appropriate, disproportionate human health or environmental effects, using practicable and legally permissible methods, under Executive Order 12898 (59 FR 7629, February 16, 1994).

The SIP is not approved to apply on any Indian reservation land or in any other area where EPA or an Indian tribe has demonstrated that a tribe has jurisdiction. In those areas of Indian country, the rule does not have tribal implications as specified by Executive Order 13175 (65 FR 67249, November 9, 2000), nor will it impose substantial direct costs on tribal governments or preempt tribal law.

List of Subjects in 40 CFR Part 52

Environmental protection, Incorporation by reference, Ozone, Reporting and recordkeeping requirements, Volatile organic compounds.

Authority: 42 U.S.C. 7401 *et seq.*

Dated: December 26, 2019.

Blake M. Ashbee,

Acting Regional Administrator, Region 4.

[FR Doc. 2020–00327 Filed 1–10–20; 8:45 am]

BILLING CODE 6560–50–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Chapter I

[CC Docket No. 98–170, WC Docket No. 04–36; DA 19–1271; FRS 16334]

Consumer and Governmental Affairs Bureau Seeks Comment To Refresh the Record on Truth-in-Billing Rules To Ensure Protections for All Consumers of Voice Services

AGENCY: Federal Communications Commission.

ACTION: Proposed rule.

SUMMARY: In this document, the Commission, via the Consumer and Governmental Affairs Bureau (Bureau), seeks to refresh the record on two issues related to the Commission's truth-in-billing rules. Specifically, the Bureau seeks additional comment on proposals to extend the truth-in-billing rules to providers of interconnected Voice over internet Protocol (VoIP) services and to require carriers to separate government-mandated charges from other charges on consumers' telephone bills. The Bureau also seeks additional comment on how to define ''government-mandated charge'' for these purposes.

DATES: Comments are due February 12, 2020, and reply comments are due March 13, 2020.

ADDRESSES: You may submit comments, identified by CC Docket No. 98–170 and WC Docket No. 04–36, by any of the following methods:

- *Federal Communications Commission's Website: http://apps.fcc.gov/ecfs/.* Follow the instructions for submitting comments.
- *Paper Mail:* Parties who choose to file by paper must file an original and one copy of each filing. Filers must submit two additional copies for each additional docket or rulemaking number. Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail. All filings must be addressed to the Commission's Secretary, Office of the Secretary, Federal Communications Commission.
- *People with Disabilities:* Contact the FCC to request reasonable accommodations (accessible format documents, sign language interpreters, CART, etc.) by email: *FCC504@fcc.gov* or phone: 202–418–0530 or TTY: 202–418–0432.

For detailed instructions for submitting comments and additional information on the rulemaking process, *see* the **SUPPLEMENTARY INFORMATION** section of this document.

FOR FURTHER INFORMATION CONTACT: For further information, contact Erica McMahon of the Consumer and Governmental Affairs Bureau at (202) 418–0346 or *Erica.McMahon@fcc.gov.*

SUPPLEMENTARY INFORMATION: This is a summary of the Commission's *Public Notice,* in CC Docket No. 98–170, WC Docket No. 04–36; DA 19–1271, released on December 13, 2019. The full text of document DA 19–1271 will be available for public inspection and copying via the Electronic Comment Filing System (ECFS), and during regular business hours at the FCC Reference Information Center, Portals II, 445 12th Street SW, Room CY–A257, Washington, DC 20554. To request materials in accessible formats for people with disabilities (Braille, large print, electronic files, audio format), send an email to *fcc504@fcc.gov* or call the Consumer and Governmental Affairs Bureau at (202) 418–0530 (voice), or (202) 418–0432 (TTY).

This matter shall be treated as a ''permit-but-disclose'' proceeding in accordance with the Commission's *ex parte* rules. 47 CFR 1.1200 *et seq.* Persons making oral *ex parte* presentations are reminded that memorandum summarizing the presentations must contain summaries of the substance of the presentations and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required. *See* 47 CFR 1.1206(b). Other rules pertaining to oral and written *ex parte* presentations in permit-but-disclose proceedings are set forth in § 1.1206(b) of the Commission's rules, 47 CFR 1.1206(b).

Synopsis

1. In the *Public Notice,* the Bureau seeks comment on several issues related to the Commission's truth-in-billing rules. Specifically, the Bureau seeks additional comment on proposals to extend the truth-in-billing rules to providers of interconnected VoIP services and to require carriers to separate government-mandated charges from other charges on consumers' telephone bills.

2. *First,* the Bureau seeks comment on extending the Commission's existing truth-in-billing rules, which currently apply only to wireline and wireless common carriers, to interconnected VoIP service providers. The Commission previously sought comment on this issue. *See IP-Enabled Services,* WC Docket No. 04–36, Notice of Proposed Rulemaking, published at 69 FR 16193, March 29, 2004. The Bureau seeks to refresh the record in light of the increasing numbers of consumers who have replaced their traditional circuit-switched phone service with interconnected VoIP service. Would consumers of interconnected VoIP service benefit from the truth-in-billing rules? Would such rules aid consumers both in determining whether to subscribe to an interconnected VoIP service in the first place and, thereafter, in assessing a provider's ongoing fees and conditions vis-à-vis those of other providers? Would rules requiring that charges be clear and conspicuous enhance interconnected VoIP consumers' ability to detect erroneous charges and unauthorized changes in their service arrangements?

3. If the Commission were to extend the truth-in-billing rules to interconnected VoIP services, what rules should it extend, *i.e.,* those that currently are designed to apply to legacy wireline carriers or the more recent rules that apply to wireless carriers? In other words, what rules are appropriate for interconnected VoIP and how should they apply? And should the Commission take the opportunity to revisit the need for any possibly outdated rules? If so, the Bureau seeks comment on why any such rules no longer benefit consumers.

4. *Second,* the Bureau seeks to refresh the record on whether the Commission should require all voice service providers to separate on consumer bills those line-item fees that are government-mandated from those that are not to the extent they include separate line items on a consumer's bill. *See Truth-in-Billing and Billing Format,* CC Docket No. 98–170, CG Docket No. 04–208, Second Report and Order, Declaratory Ruling, and Second Further Notice of Proposed Rulemaking, published at 70 FR 30044, May 25, 2005. Would such an approach serve the Commission's historical truth-in-billing goal ''to aid customers in understanding their telecommunications bills, and to provide them with the tools they need to make informed choices in the market for telecommunications services''? If the Commission were to require such separation, what would be the most consumer-beneficial way to do so while minimizing regulatory burdens on voice service providers? Should the Commission consider steps beyond simple separation and require that different charges appear in a distinct section of the consumer's bill, one clearly labeled to show that it contains government-mandated charges? Some service providers promote all-inclusive prices, with no added line-item charges, for certain offerings. How should the Commission address government-mandated charges in this context?

5. The Bureau seeks additional comment on how to define ''government-mandated charge'' for these purposes. In the *Truth-in-Billing FNPRM,* the Commission noted that mandated charges could be defined as those that providers are required by law to collect from consumers and remit directly to federal, state, or local governments, or could also include charges that providers are not required to collect from consumers but choose to do so through separate line items, to reimburse themselves for their own payments toward government programs. Under this definition, charges for universal service, state and local taxes, 911/E911, and other line-item fees should be considered government-mandated. The Bureau seeks further comment on how to define government-mandated charges.

6. In contrast, most other line-item charges would not be considered government-mandated. For example, charges historically associated with network access, such as the Subscriber Line Charge and Access Recovery Charge; charges designed to recover the administrative or other costs for complying with federal and state law, such as a ''Regulatory Fee'' or ''Regulatory Cost Recovery Charge;'' and charges to reimburse providers for more general operating costs, such as permit fees, application fees, or licensing fees, are not charges remitted to the government but are line items collected by carriers of their own volition. The Bureau seeks comment on whether such fees should be separated from government-mandated charges.

7. The Commission's authority to adopt truth-in-billing rules for common carriers derives in large part from section 201(b) of the Communications Act to deter carriers from engaging in unjust and unreasonable practices.

The Bureau seeks to refresh the record on the Commission's authority to extend the truth-in-billing rules to interconnected VoIP service providers, including both two-way and one-way interconnected VoIP services.

Federal Communications Commission.

Gregory Haledjian,

Legal Advisor, Consumer and Governmental Affairs Bureau.

[FR Doc. 2020–00260 Filed 1–10–20; 8:45 am]

BILLING CODE 6712–01–P

Notices

Federal Register

Vol. 85, No. 8

Monday, January 13, 2020

This section of the FEDERAL REGISTER contains documents other than rules or proposed rules that are applicable to the public. Notices of hearings and investigations, committee meetings, agency decisions and rulings, delegations of authority, filing of petitions and applications and agency statements of organization and functions are examples of documents appearing in this section.

DEPARTMENT OF AGRICULTURE

Submission for OMB Review; Comment Request

January 8, 2020.

The Department of Agriculture has submitted the following information collection requirement(s) to OMB for review and clearance under the Paperwork Reduction Act of 1995, Public Law 104–13. Comments are requested regarding whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; the accuracy of the agency's estimate of burden including the validity of the methodology and assumptions used; ways to enhance the quality, utility and clarity of the information to be collected; and ways to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

Comments regarding this information collection received by February 12, 2020 will be considered. Written comments should be addressed to: Desk Officer for Agriculture, Office of Information and Regulatory Affairs, Office of Management and Budget (OMB), New Executive Office Building, 725 17th Street NW, Washington, DC 20502. Commenters are encouraged to submit their comments to OMB via email to: *OIRA_Submission@OMB.EOP.GOV* or fax (202) 395–5806 and to Departmental Clearance Office, USDA, OCIO, Mail Stop 7602, Washington, DC 20250–7602. Copies of the submission(s) may be obtained by calling (202) 720–8958.

An agency may not conduct or sponsor a collection of information unless the collection of information displays a currently valid OMB control number and the agency informs potential persons who are to respond to the collection of information that such persons are not required to respond to the collection of information unless it displays a currently valid OMB control number.

Food Safety and Inspection Service

Title: Interstate Shipment of Meat and Poultry Products.

OMB Control Number: 0583–0143.

Summary of Collection: The Food Safety and Inspection Service (FSIS) has been delegated the authority to exercise the functions of the Secretary (7 CFR 2.18, 2.53), as specified in the Federal Meat Inspection Act (FMIA) (21 U.S.C. 601, *et seq.*) and the Poultry Products Inspection Act (PPIA) (21 U.S.C. 451 *et seq.*). These statutes mandate that FSIS protect the public by ensuring that meat and poultry products are safe, wholesome, not adulterated, and properly labeled and packaged.

Need and Use of the Information: FSIS will collect information to ensure that all establishments operating under the voluntary cooperative inspection program under which State-inspected establishments in participating states with 25 or fewer employees are eligible to ship meat and poultry products in interstate commerce (21 U.S.C. 683 and U.S.C. 472) (9 CFR 321.3, Part 332, 381.187, and Part 381 Subpart Z) comply with all Federal standards under the FMIA and the PPIA, as well as with all State standards. Establishments under the voluntary cooperative inspection program receive inspection services from State inspection personnel that have been trained in the enforcement of the FMIA and PPIA.

Description of Respondents: State, local or tribal government.

Number of Respondents: 67.

Frequency of Responses: Recordkeeping; Reporting: On occasion.

Total Burden Hours: 733.

Ruth Brown,

Departmental Information Collection Clearance Officer.

[FR Doc. 2020–00282 Filed 1–10–20; 8:45 am]

BILLING CODE 3410– DM–P

DEPARTMENT OF AGRICULTURE

Forest Service

Hood-Willamette Resource Advisory Committee

AGENCY: Forest Service, USDA.

ACTION: Notice of meeting.

SUMMARY: The Hood-Willamette Resource Advisory Committee (RAC) will meet in Keizer Oregon. The committee is authorized under the Secure Rural Schools and Community Self-Determination Act (the Act) and operates in compliance with the Federal Advisory Committee Act. The purpose of the committee is to improve collaborative relationships and to provide advice and recommendations to the Forest Service concerning projects and funding consistent with Title II of the Act. The meeting is open to the public. The purpose of the meeting is to review and make recommendations on Title II project proposals and on proposals for new recreation fees. Additional RAC information, including the meeting agenda and the meeting summary/minutes will be available at the following website: *https://www.fs.usda.gov/main/willamette/workingtogether/advisorycommittees.*

DATES: The meeting will be held on February 11, 2020 beginning at 9:00 a.m. All RAC meetings are subject to cancellation. For status of meeting prior to attendance, please contact the person listed under **FOR FURTHER INFORMATION CONTACT.**

ADDRESSES: The meeting will be held at Keizer Community Center, Claggett Room, 930 Chemawa Road NE, Keizer, Oregon 97303.

Written comments may be submitted as described under **SUPPLEMENTARY INFORMATION**. All comments, including names and addresses when provided, are placed in the record and are available for public inspection and copying. The public may inspect comments received at the Willamette Supervisor's Interagency Office in Springfield, OR. Please call ahead to facilitate entry into the building.

FOR FURTHER INFORMATION CONTACT: Jennifer Sorensen, RAC Coordinator, by phone at 541–510–1102 or via email at *Jennifer.Sorensen@usda.gov.*

Individuals who use telecommunication devices for the deaf

(TDD) may call the Federal Information Relay Service (FIRS) at 1–800–877–8339 between 8:00 a.m. and 8:00 p.m., Eastern Standard Time, Monday through Friday.

SUPPLEMENTARY INFORMATION: The purpose of the meeting is to:

1. Update all RAC members on the status of the SRS program, and the pending nomination package for new RAC memebers;

2. Review, discuss and make funding reccomendations on Title II project proposals submited during the 2019 solicitation window;

3. Hear a summary of public comments received regarding a new recreation permit fees being proposed in conjunction with the Central Cascades Wilderness Permit system;

4. Review, discuss and make reccomendations on the special recreation permit fee being proposed in conjunction with the Central Cascades Wilderness Permit System.

The meeting is open to the public. The agenda will include time for people to make oral statements of three minutes or less. Individuals wishing to make an oral statement should request in writing by February 7, 2020 to be scheduled on the agenda. Anyone who would like to bring related matters to the attention of the committee may file written statements with the committee staff before or after the meeting. Written comments and requests for time for oral comments must be sent to Jennifer Sorensen, RAC Coordinator, 3106 Pierce Parkway, Suite D, Springfield, Oregon 97477; by email to *Jennifer.Sorensen@usda.gov.*

Meeting Accommodations: If you are a person requiring reasonable accommodation, please make requests in advance for sign language interpreting, assistive listening devices or other reasonable accommodation for access to the facility or proceedings by contacting the person listed in the section titled **FOR FURTHER INFORMATION CONTACT**. All reasonable accommodation requests are managed on a case by case basis.

Dated: December 12, 2019.

Cikena Reid,

USDA Committee Management Officer.

[FR Doc. 2020–00302 Filed 1–10–20; 8:45 am]

BILLING CODE 3411–15–P

DEPARTMENT OF COMMERCE

Census Bureau

Submission for OMB Review; Comment Request

The Department of Commerce will submit to the Office of Management and Budget (OMB) for clearance the following proposal for collection of information under the provisions of the Paperwork Reduction Act: The Fertility Supplement to the Current Population Survey. This survey, conducted every two years in June, is a supplemental survey asked of female household members ages 15 to 50. It will be collected in June 2020, to obtain the number of children ever given birth to (if any), the year the first child was born, and the marital or cohabitation status at the time the first child was born.

Agency: U.S. Census Bureau.

Title: Current Population Survey, Fertility Supplement.

OMB Control Number: 0607–0610.

Form Number(s): There are no forms. We conduct all interviews on computers.

Type of Request: Reinstatement, without change, of a previously approved collection for which approval has expired.

Number of Respondents: 30,000.

Average Hours per Response: Approximately 1 minute per response.

Burden Hours: 500.

Needs and Uses: This survey provides information used mainly by government and private analysts to project future population growth, to analyze child spacing, and to aid policymakers and private analysts in their decisions affected by changes in family size and composition. Past studies have discovered noticeable changes in the patterns of fertility rates and the timing of the first birth. Potential needs for government assistance, such as aid to families with dependent children, child care, and maternal health care for single parent households, can be estimated using CPS characteristics matched with fertility data.

Affected Public: Individuals or Households.

Frequency: Biennially.

Respondent's Obligation: Voluntary.

Legal Authority: Title 13, United States Code, Sections 8(b), 141, and 182; and Title 29, United States Code, Sections 1–9 authorize the Census Bureau to collect this information.

This information collection request may be viewed at www.reginfo.gov. Follow the instructions to view Department of Commerce collections currently under review by OMB.

Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *OIRA_Submission@omb.eop.gov* or fax to (202)395–5806.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–00310 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–07–P

DEPARTMENT OF COMMERCE

International Trade Administration

[C–570–913]

Certain New Pneumatic Off-the-Road Tires From the People's Republic of China: Notice of Court Decision Not in Harmony With Final Results of Administrative Review and Notice of Amended Final Results

AGENCY: Enforcement and Compliance, International Trade Administration, Department of Commerce.

SUMMARY: On December 26, 2019, the United States Court of International Trade (the Court) issued final judgment in *Guizhou Tyre Co. Ltd.; Guizhou Tyre Import & Export Co., Ltd; & Xuzhou Xugong Tyres Co., Ltd.* v. *United States,* Consol. Court No. 17–00101, Slip Op. 19–171, sustaining the Department of Commerce's (Commerce) remand results pertaining to the 2014 administrative review of the countervailing duty (CVD) order on certain pneumatic off-the-road tires (OTR Tires) from the People's Republic of China (China). Commerce is notifying the public that the Court has made a final judgment that is not in harmony with the final results of the 2014 administrative review, and that Commerce is amending the final results of the 2014 administrative review with respect to mandatory respondents and non-selected companies.

DATES: Applicable January 6, 2020.

FOR FURTHER INFORMATION CONTACT: Chien-Min Yang, AD/CVD Operations, Office VII, Enforcement and Compliance, International Trade Administration, U.S. Department of Commerce, 1401 Constitution Avenue NW, Washington, DC 20230; telephone: (202) 482–5484.

SUPPLEMENTARY INFORMATION:

Background

On April 18, 2017, Commerce published the *Final Results* pertaining to mandatory respondents Guizhou Tyre Co., Ltd. (Guizhou Tyre) and Xuzhou Xugong Tyres Co. Ltd. (Xuzhou Xugong)

in the 2014 administrative review of the CVD order on OTR Tires from China.[1] The period of review is January 1, 2014 through December 31, 2014. In the *Final Results,* Commerce found, based on adverse facts available (AFA), that the mandatory respondents had used the Export Buyer's Credit Program (EBCP).[2]

On October 25, 2018, the Court remanded the *Final Results* to Commerce to reconsider its decision to apply AFA to the EBCP program.[3] Specifically, the Court held that ''Commerce had a clear path to find non-use by either accepting the declarations submitted by {p}laintiffs and their U.S. Customers or by verifying these declarations,'' and ordered Commerce to reconsider the evidence of non-use by Government of China (GOC).[4]

On March 5, 2019, Commerce submitted its remand redetermination, in which it reconsidered its decision to apply AFA to the EBCP and provided extensive additional explanation in support of its treatment of the program.[5] Guizhou Tyre and Xuzhou Xugong continued to challenge Commerce's determination regarding the use of EBCP. Pursuant to the Court's remand order, Commerce had explained how the GOC's refusal to provide certain information concerning the operation of the program prevented a meaningful and accurate verification of the non-use claims of the respondents and their U.S. customers.[6]

On August 21, 2019, the Court again remanded the determination to Commerce, ordering Commerce to reconsider its application of AFA in light of the record evidence of non-use. The Court held that Commerce did not establish that there was a gap in the record that warranted the application of AFA with respect to the EBCP program.[7]

On November 19, 2019, Commerce filed its second remand redetermination with the Court reconsidering its decision to apply AFA in evaluating use of the EBCP, in which it determined, under respectful protest, that the EBCP program was not used by the respondents based on the certifications submitted by Guizhou Tyre from its customers stating that they did not use program and the record statements by Xuzhou Xugong that none of its customers used the program.[8] Accordingly, Commerce assigned Guizhou Tyre, Xuzhou Xugong and other non-selected companies net subsidy rates of 19.78 percent, 46.31 percent, and 33.05 percent, respectively.[9]

On December 26, 2019, the Court sustained Commerce's *Second Remand Results* and entered final judgment.[10]

Timken Notice

In its decision in *Timken,*[11] as clarified by *Diamond Sawblades,*[12] the U.S. Court of Appeals for the Federal Circuit (CAFC) held that, pursuant to section 516A(e) of the Tariff Act of 1930, as amended (the Act), Commerce must publish a notice of a court decision that is not ''in harmony'' with a Commerce determination and must suspend liquidation of entries pending a ''conclusive'' court decision. The Court's December 26, 2019 final judgment sustaining Commerce's *Second Remand Results* constitutes a final decision of the Court that is not in harmony with Commerce's *Final Results.*[13] This notice is published in fulfillment of the *Timken* publication requirements.

Amended Final Results

Because there is now a final court decision, we are amending the *Final Results* with respect to the CVD rates calculated for Guizhou Tyre and Xuzhou Xugong. Based on the *Second Remand Results,* as sustained by the Court, the revised CVD rates for Guizhou Tyre, Xuzhou Xugong, and non-selected companies, from January 1, 2014 through December 31, 2014, are 19.78 percent, 46.31 percent, and 33.05 percent, respectively.

In the event that the Court's ruling is not appealed, or, if appealed, is upheld by a final and conclusive court decision, Commerce will instruct Customs and Border Protection to assess countervailing duties on unliquidated entries of subject merchandise based on the revised subsidy rates summarized above.

Notification to Interested Parties

This notice is issued and published in accordance with section 516A(e)(1), 781(d), and 777(i)(1) of the Act.

Dated: January 7, 2020.

Jeffrey I. Kessler,

Assistant Secretary for Enforcement and Compliance.

[FR Doc. 2020–00300 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–DS–P

[1] *See Certain New Pneumatic Off-the-Road Tires from the People's Republic of China: Final Results of Countervailing Duty Administrative Review; 2014,* 82 FR 18285 (April 18, 2017) (*Final Results*), and the accompanying Issues and Decision Memorandum (IDM).

[2] *See Final Results* IDM.

[3] *See Guizhou Tyre Co., Ltd., et al.* v. *United States,* CIT Slip Op. 18–140, Consol. Ct. No. 17–00101 (October 17, 2018) (*First Remand Order*) at 25–26.

[4] *See First Remand Order* at 9 and 25.

[5] *See* Results of Redetermination Pursuant to Court Remand (March 5, 2018) (*First Remand Results*) at 5–17 and 24–33.

[6] *See First Remand Results* at 5–17.

[7] *See Guizhou Tyre Co., Ltd., et al.* v. *United States,* CIT Slip Op. 19–114, Consol. Ct. No. 17–00101 (August 21, 2019) (*Second Remand Order*) at 3–5 and 11.

[8] *See* Results of Redetermination Pursuant to Court Remand (November 19, 2019) (*Second Remand Results*) at 8–10.

[9] *Id.* at 9.

[10] *See Guizhou Tyre Co., Ltd.; Guizhou Tyre Import & Export Co., Ltd; & Xuzhou Xugong Tyres Co. Ltd.* v. *United States,* CIT Slip Op. 19–171, Consol. Ct. No. 17–00101 (December 26, 2019).

[11] *See Timken Co.* v. *United States,* 893 F. 2d 337, 341 (Fed. Cir. 1990) (*Timken*).

[12] *See Diamond Sawblades Mfrs. Coalition* v. *United States,* 626 F. 3d 1374 (Fed. Cir. 2010) (*Diamond Sawblades*).

[13] *See Final Results.*

DEPARTMENT OF COMMERCE

International Trade Administration

[A–570–040]

Truck and Bus Tires From the People's Republic of China: Final Results of Antidumping Duty Changed Circumstances Review

AGENCY: Enforcement and Compliance, International Trade Administration, Department of Commerce.

SUMMARY: On December 13, 2019, the Department of Commerce (Commerce) published a notice of initiation and preliminary results of a changed circumstances review (CCR) of the antidumping duty order on truck and bus tires from the People's Republic of China (China). For these final results, Commerce continues to find that Sailun Group Co., Ltd. (Sailun Group) is the successor-in-interest to Sailun Jinyu Group Co., Ltd. (Sailun Jinyu), and that Sailun (Shenyang) Tire Co., Ltd. (Sailun Shenyang) is the successor-in-interest to Shenyang Peace Radial Tyre Manufacturing Co., Ltd. (Shenyang Peace).

DATES: Applicable January 13, 2020.

FOR FURTHER INFORMATION CONTACT: Lochard Philozin, AD/CVD Operations, Office I, Enforcement and Compliance, International Trade Administration, U.S. Department of Commerce, 1401 Constitution Avenue NW, Washington, DC 20230; telephone: (202) 482–4260.

SUPPLEMENTARY INFORMATION:

Background

On December 13, 2019, Commerce published a notice of initiation and preliminary results of a CCR of the antidumping duty order on truck and bus tires from China, in which we found that Sailun Jinyu changed its name to Sailun Group, effective October 22, 2018, and Shenyang Peace changed its

name to Sailun Shenyang, effective December 3, 2018.[1] On October 25, 2019, Sailun Group requested that Commerce initiate an expedited CCR and determine Sailun Group is the successor-in-interest to Sailun Jinyu, and that Sailun Shenyang is the successor-in-interest to Shenyang Peace.[2]

Commerce preliminarily determined that Sailun Group is the successor-in-interest to Sailun Jinyu, and that Sailun Shenyang is the successor-in-interest to Shenyang Peace for purposes of determining antidumping duty liability.[3] In the *Initiation and Preliminary Results,* Commerce provided all interested parties with an opportunity to comment and request a public hearing regarding our preliminary results. On December 27, 2019, Sailun Group informed Commerce that it agrees with the preliminary results.[4] Commerce received no additional comments or requests for a public hearing.

Scope of the Order

The scope of the order covers truck and bus tires. Truck and bus tires are new pneumatic tires, of rubber, with a truck or bus size designation. Truck and bus tires covered by this order may be tube-type, tubeless, radial, or non-radial.

Subject tires have, at the time of importation, the symbol ''DOT'' on the sidewall, certifying that the tire conforms to applicable motor vehicle safety standards. Subject tires may also have one of the following suffixes in their tire size designation, which also appear on the sidewall of the tire:

TR—Identifies tires for service on trucks or buses to differentiate them from similarly sized passenger car and light truck tires; and

HC—Identifies a 17.5 inch rim diameter code for use on low platform trailers.

All tires with a ''TR'' or ''HC'' suffix in their size designations are covered by this order regardless of their intended use.

In addition, all tires that lack one of the above suffix markings are included in the scope, regardless of their intended use, as long as the tire is of a size that is among the numerical size designations listed in the ''Truck-Bus'' section of the *Tire and Rim Association Year Book,* as updated annually, unless the tire falls within one of the specific exclusions set out below.

Truck and bus tires, whether or not mounted on wheels or rims, are included in the scope. However, if a subject tire is imported mounted on a wheel or rim, only the tire is covered by the scope. Subject merchandise includes truck and bus tires produced in the subject country whether mounted on wheels or rims in the subject country or in a third country. Truck and bus tires are covered whether or not they are accompanied by other parts, *e.g.,* a wheel, rim, axle parts, bolts, nuts, etc. Truck and bus tires that enter attached to a vehicle are not covered by the scope.

Specifically excluded from the scope of this order are the following types of tires: (1) Pneumatic tires, of rubber, that are not new, including recycled and retreaded tires; (2) non-pneumatic tires, such as solid rubber tires; and (3) tires that exhibit each of the following physical characteristics: (a) The designation ''MH'' is molded into the tire's sidewall as part of the size designation; (b) the tire incorporates a warning, prominently molded on the sidewall, that the tire is for ''Mobile Home Use Only;'' and (c) the tire is of bias construction as evidenced by the fact that the construction code included in the size designation molded into the tire's sidewall is not the letter ''R.''

The subject merchandise is currently classifiable under Harmonized Tariff Schedule of the United States (HTSUS) subheadings: 4011.20.1015 and 4011.20.5020. Tires meeting the scope description may also enter under the following HTSUS subheadings: 4011.69.0020, 4011.69.0090, 4011.70.00, 4011.90.80, 4011.99.4520, 4011.99.4590, 4011.99.8520, 4011.99.8590, 8708.70.4530, 8708.70.6030, 8708.70.6060, and 8716.90.5059.

While HTSUS subheadings are provided for convenience and for customs purposes, the written description of the subject merchandise is dispositive.

Final Results of Changed Circumstances Review

For the reasons stated in the *Initiation and Preliminary Results,* and because we received no comments from interested parties to the contrary, Commerce continues to find that Sailun Group is the successor-in-interest to Sailun Jinyu, and that Sailun Shenyang is the successor-in-interest to Shenyang Peace.[5] As a result of this determination, Commerce finds that subject merchandise produced and exported by Sailun Group to the United States should receive the same cash deposit rate as subject merchandise produced and exported by Sailun Jinyu to the United States; and subject merchandise produced by Sailun Shenyang and exported by Sailun Group to the United States should receive the same cash deposit rate as subject merchandise produced by Shenyang Peace and exported by Sailun Jinyu to the United States. Accordingly, Commerce will instruct U.S. Customs and Border Protection to suspend liquidation of all shipments of subject merchandise for these two successor-in-interest producer/exporter combinations at their predecessor-in-interest producer/exporter combinations' cash deposit rate of 9.00 percent.[6] This cash deposit requirement will be effective upon the publication date of our final results for this CCR and shall remain in effect until further notice.

Notification to Interested Parties

This notice serves as a final reminder to parties subject to administrative protective order (APO) of their responsibility concerning the disposition of proprietary information disclosed under APO in accordance with 19 CFR 351.305(a)(3). Timely written notification of the return/destruction of APO materials or conversion to judicial protective order is hereby requested. Failure to comply with the regulations and terms of an APO is a sanctionable violation.

This notice of final results is in accordance with sections 751(b)(1) and 777(i) of the Tariff Act of 1930, as amended, and 19 CFR 351.216, 19 CFR 351.221(b)(5), and 19 CFR 351.221(c)(3).

Dated: January 7, 2020.

Jeffrey I. Kessler,

Assistant Secretary for Enforcement and Compliance.

[FR Doc. 2020–00301 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–DS–P

[1] *See Truck and Bus Tires from the People's Republic of China: Initiation and Preliminary Results of Antidumping Duty Changed Circumstances Review,* 84 FR 68118 (December 13, 2019) (*Initiation and Preliminary Results*).

[2] *See* Sailun Group's Letter, ''*Sailun Request for a Changed Circumstances Review in Truck and Bus Tires From the People's Republic of China, Case No. A–570–040,*'' dated October 25, 2019.

[3] *See Initiation and Preliminary Results.*

[4] *See* Sailun Group's Letter, ''*Sailun Letter in Lieu of Brief: Changed Circumstances Review in Truck and Bus Tires From the People's Republic of China, Case No. A–570–040,*'' dated December 27, 2019.

[5] *Initiation and Preliminary Results,* 84 FR 68118.

[6] *See Truck and Bus Tires from the People's Republic of China: Antidumping Duty Order,* 84 FR 4436 (February 15, 2019).

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

Submission for OMB Review; Comment Request

The Department of Commerce will submit to the Office of Management and

Budget (OMB) for clearance the following proposal for collection of information under the provisions of the Paperwork Reduction Act (44 U.S.C. chapter 35).

Agency: National Oceanic and Atmospheric Administration (NOAA).

Title: Western Alaska Community Development Quota (CDQ) Program.

OMB Control Number: 0648–0269.

Form Number(s): None.

Type of Request: Regular (extension of an approved collection).

Number of Respondents: 6.

Average Hours per Response: CDQ Vessel Registration System, 10 minutes; Groundfish/Halibut CDQ and PSQ Transfer Request, 30 minutes; Application for Approval of Use of Non-CDQ Harvest Regulations, 5 hours; Appeals, 4 hours.

Burden Hours: 46.

Needs and Uses: The Western Alaska Community Development Quota (CDQ) Program is an economic development program associated with federally managed fisheries in the Bering Sea and Aleutian Islands (BSAI). The purpose of the program is to provide eligible western Alaska communities with the opportunity to participate and invest in fisheries in the BSAI, to support economic development in western Alaska, to alleviate poverty and provide economic and social benefits to residents of western Alaska, and to achieve sustainable local economies in western Alaska. The Magnuson-Stevens Fishery Conservation and Management Act allocates a portion of the annual catch limit for each directed fishery of the BSAI management area among six non-profit entities (CDQ groups) that represent 65 western Alaska communities. The CDQ groups administer the CDQ allocations, investments, and economic development projects. The CDQ groups use the revenue derived from the harvest of their fisheries allocations to fund economic development activities and provide employment opportunities.

This information collection is comprised of four components.

- The CDQ Vessel Registration System is an online system used by the CDQ groups to add small hook-and-line catcher vessels to the CDQ vessel registration list. Registered vessels are exempt from the requirements to obtain and carry a License Limitation Program license under regulations at 50 part 679. This system is also used to remove vessels from the CDQ vessel registration list.
- The Groundfish/Halibut CDQ and Prohibited Species Quota (PSQ) Transfer Request form is used to transfer annual amounts of groundfish and halibut CDQ and halibut PSQ between two CDQ groups. This form is completed by the transferring and receiving CDQ groups.
- The Application for Approval of Use of Non-CDQ Harvest Regulations is used by a CDQ group, an association representing CDQ groups, or a voluntary fishing cooperative to request approval to use non CDQ harvest regulations when the CDQ regulations are more restrictive than the regulations otherwise required for participants in non-CDQ groundfish fisheries.
- An appeals process is provided for an applicant who receives an adverse initial administrative determination (IAD) related to its Application for Approval of Use of Non-CDQ Harvest Regulations. No such adverse IADs have been issued to date. In general, the cooperative managers present the cooperative reports during the April.

Affected Public: Businesses or other for-profit organizations.

Frequency: Periodically.

Respondent's Obligation: Mandatory; Voluntary.

This information collection request may be viewed at *reginfo.gov.* Follow the instructions to view Department of Commerce collections currently under review by OMB.

Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *OIRA_Submission@omb.eop.gov* or fax to (202) 395–5806.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–00275 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

Submission for OMB Review; Comment Request

The Department of Commerce will submit to the Office of Management and Budget (OMB) for clearance the following proposal for collection of information under the provisions of the Paperwork Reduction Act (44 U.S.C. chapter 35).

Agency: National Oceanic and Atmospheric Administration (NOAA).

Title: Alaska American Fisheries Act (AFA) Permits.

OMB Control Number: 0648–0393.

Form Number(s): None.

Type of Request: Regular (extension of a currently approved information collection).

Number of Respondents: 27.

Average Hours per Response: 1 hour each for AFA Permit: Rebuilt, Replacement, or Removed Vessel Application and Application for Transfer of Bering Sea Chinook Salmon PSC Allocations; 2 hours for Application for AFA Inshore Catcher Vessel Cooperative Permit; 4 hours for AFA Inshore Vessel Contract Fishing Notification; 8 hours for Application for Approval as an Entity to Receive Transferable Chinook Salmon PSC Allocation.

Burden Hours: 251 hours.

Needs and Uses: The American Fisheries Act (AFA) was signed into law in October 1998. The purpose of the AFA was to tighten U.S. ownership standards that had been exploited under the Anti-reflagging Act, and to provide the Bering Sea and Aleutian Islands (BSAI) pollock fleet the opportunity to conduct their fishery in a more rational manner while protecting non-AFA participants in the other fisheries. The AFA established sector allocations in the BSAI pollock fishery, determined eligible vessels and processors, allowed the formation of cooperatives, set limits on the participation of AFA vessels in other fisheries, and imposed special catch weighing and monitoring requirements on AFA vessels.

This information collection contains five AFA permitting and reporting requirements.

- The AFA Permit: Rebuilt, Replacement, or Removed Vessel Application is submitted by an owner of an AFA vessel to notify NMFS the vessel has been rebuilt; to request an AFA permit for a replacement catcher vessel, catcher/processor, or mothership; or to request removal of an AFA catcher vessel that is a member of an inshore cooperative and assign its catch history to another vessel or vessels in the same cooperative.
- The Application for AFA Inshore Catcher Vessel Cooperative Permit is submitted annually by each AFA inshore catcher vessel cooperative to obtain an AFA Inshore Catcher Vessel Cooperative Permit and identify the vessels and processors that will be participating in the BSAI pollock fishery prior to the start of each fishing year.
- The AFA Inshore Vessel Contract Fishing Notification is submitted by an AFA inshore cooperative that intends to contract with a non-member vessel to harvest a portion of the cooperative's annual pollock allocation to notify NMFS of vessels that might be reporting with an alternative cooperative ID.

• The Application for Approval as an Entity to Receive Transferable Chinook Salmon PSC Allocation is submitted by an entity representing the catcher/processor sector or the mothership sector to request approval to receive transferable Chinook salmon PSC allocations on behalf of members of the sector. This application is also used to update contact and other information related to the entity and its members.

• The Application for Transfer of Bering Sea Chinook Salmon PSC Allocations is submitted by an authorized representative of the catcher/processor sector, the mothership sector, an inshore cooperative, or a CDQ group to transfer Chinook salmon PSC allocations to another entity's account.

Affected Public: Businesses or other for-profit organizations; Individuals or households, Not-for-profit institutions.

Frequency: On occasion, Annually.

Respondent's Obligation: Required to obtain or retain benefits.

This information collection request may be viewed at *reginfo.gov.* Follow the instructions to view Department of Commerce collections currently under review by OMB.

Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *OIRA_Submission@omb.eop.gov* or fax to (202) 395–5806.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–00297 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[0648–XA008]

Mid-Atlantic Fishery Management Council (MAFMC); Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice; public meeting.

SUMMARY: The Mid-Atlantic Fishery Management Council's (Council) Northeast Trawl Advisory Panel (NTAP) will hold a meeting.

DATES: The meeting will be held on January 31, 2020, beginning at 9 a.m. and conclude by 1 p.m. For agenda details, see **SUPPLEMENTARY INFORMATION.**

ADDRESSES: This will be a webinar meeting. Details for the webinar will be posted on MAFMC NTAP web page *http://www.mafmc.org/ntap.*

Council address: Mid-Atlantic Fishery Management Council, 800 N State Street, Suite 201, Dover, DE 19901; telephone: (302) 674–2331 or on their website at *www.mafmc.org.*

Council address: Mid-Atlantic Fishery Management Council, 800 N State Street, Suite 201, Dover, DE 19901; telephone: (302) 674–2331; website: *www.mafmc.org.*

FOR FURTHER INFORMATION CONTACT: Christopher M. Moore, Ph.D., Executive Director, Mid-Atlantic Fishery Management Council, telephone: (302) 526–5255.

SUPPLEMENTARY INFORMATION: The purpose of the meeting is for the NTAP to (1) Review remaining analyses of data from 2019 Karen Elizabeth wingspread experiment, (2) Evaluate/review implications of analytic results of wingspread experiment for 2020 field experiment plans. (3) Discuss other relevant business.

Special Accommodations

The meeting is physically accessible to people with disabilities. Requests for sign language interpretation or other auxiliary aid should be directed to M. Jan Saunders, (302) 526–5251, at least 5 days prior to the meeting date.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: January 7, 2020.

Karyl K. Brewster-Geisz,

Acting Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–00276 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

Marine Mammals and Endangered Species

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice; issuance of permits.

SUMMARY: Notice is hereby given that permits or permit amendments have been issued to the following entities under the Marine Mammal Protection Act (MMPA) and the Endangered Species Act (ESA), as applicable.

ADDRESSES: The permits and related documents are available for review upon written request or by appointment in the Permits and Conservation Division, Office of Protected Resources, NMFS, 1315 East-West Highway, Room 13705, Silver Spring, MD 20910; phone: (301) 427–8401; fax: (301) 713–0376.

FOR FURTHER INFORMATION CONTACT: Shasta McClenahan (Permit Nos. 23023, 23169, and 23467) and Sara Young (Permit No. 22677); at (301) 427–8401.

SUPPLEMENTARY INFORMATION: Notices were published in the **Federal Register** on the dates listed below that requests for a permit or permit amendment had been submitted by the below-named applicants. To locate the **Federal Register** notice that announced our receipt of the application and a complete description of the research, go to *www.federalregister.gov* and search on the permit number provided in the table below.

Permit No.	RIN	Applicant	Previous **Federal Register** notice	Permit or amendment issuance date
22677	0648–XR039	NMFS Pacific Islands Fisheries Science Center, 1845 WASP Blvd., Building 176, Honolulu, HI 96818 (Responsible Party: Charles Littnan).	84 FR 57016; October 24, 2019.	December 18, 2019.
23023	0648–XR046	Robert Wayne, University of California, Los Angeles, 610 Charles E. Young Drive East, Los Angeles, CA 90095.	84 FR 61025; November 12, 2019.	December 13, 2019.
23169	0648–XR047	Red Rock Films, 625 Sligo Avenue, Silver Spring, MD 20910 (Responsible Party: Brian Armstrong).	84 FR 57403; October 25, 2019.	December 9, 2019.
23467	0648–XR064	Sarah Conner, Wild Space Productions, St. Stephens House, Colston Avenue, Bristol, BS1 4ST, United Kingdom.	84 FR 61025; November 12, 2019.	December 19, 2019.

In compliance with the National Environmental Policy Act of 1969 (42 U.S.C. 4321 *et seq.*), a final determination has been made that the activities proposed for Permit Nos. 23023, 23169, and 23467 are categorically excluded from the requirement to prepare an environmental assessment or environmental impact statement. For Permit No. 22677, NMFS has determined that the activities proposed are consistent with the Preferred Alternative in the Final Hawaiian Monk Seal Recovery Actions Programmatic Environmental Impact Statement (NMFS 2014), and that issuance of the permit would not have a significant adverse impact on the human environment.

As required by the ESA, as applicable, issuance of these permit was based on a finding that such permits: (1) Were applied for in good faith; (2) will not operate to the disadvantage of such endangered species; and (3) are consistent with the purposes and policies set forth in Section 2 of the ESA.

Authority: The requested permits have been issued under the Marine Mammal Protection Act of 1972, as amended (16 U.S.C. 1361 *et seq.*), the regulations governing the taking and importing of marine mammals (50 CFR part 216), the Endangered Species Act of 1973, as amended (ESA; 16 U.S.C. 1531 *et seq.*), and the regulations governing the taking, importing, and exporting of endangered and threatened species (50 CFR parts 222–226), as applicable.

Dated: January 8, 2020.

Julia Marie Harrison,

Chief, Permits and Conservation Division, Office of Protected Resources, National Marine Fisheries Service.

[FR Doc. 2020–00316 Filed 1–10–20; 8:45 am]

BILLING CODE 3510–22–P

BUREAU OF CONSUMER FINANCIAL PROTECTION

Advisory Committees Solicitation of Applications for Membership

AGENCY: Consumer Financial Protection Bureau.

ACTION: Notice.

SUMMARY: Pursuant to the authorities given to the Director of the Bureau of Consumer Financial Protection (Bureau) under the Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Director Kraninger invites the public to apply for membership for appointment to its Consumer Advisory Board (CAB), Community Bank Advisory Council (CBAC), Credit Union Advisory Council (CUAC), and Academic Research Council (ARC) (collectively, advisory committees). Membership of the advisory committees includes representatives of consumers, diverse communities, the financial services industry, academics, and economists. Appointments to the committees are generally for two years. However, the Director may amend the respective committee charters from time to time during the charter terms, as the Director deems necessary to accomplish the purpose of the committees. The Bureau expects to announce the selection of new members in late-summer 2020.

DATES: The application will be available on January 13, 2020 here: *https://consumer-financial-protection-bureau.forms.fm/2020-application-to-serve-on-the-cfpb-s-advisory-committees.* Complete application packets received on or before 11:59 p.m. EST on February 27, 2020, will be given consideration for membership on the committees.

ADDRESSES: If an applicant requires a reasonable accommodation to complete the application, please contact Kimberley Medrano, Operations and PM Analyst, *CFPB_BoardandCouncilApps@cfpb.gov.*

All applications for membership on the advisory committees should be sent:

- *Electronically: https://consumer-financial-protection-bureau.forms.fm/2020-application-to-serve-on-the-cfpb-s-advisory-committees[.*
- *Mail:* Kimberley Medrano, Operations and PM Analyst, Bureau of Consumer Financial Protection, 1700 G Street NW, Washington, DC 20552. Submissions must be postmarked on or before February 27, 2020.
- *Hand Delivery/Courier:* Kimberley Medrano, Operations and PM Analyst, Bureau of Consumer Financial Protection, 1700 G Street NW, Washington, DC 20552. Submissions must be received on or before 11:59 p.m. EST on February 27, 2020.

FOR FURTHER INFORMATION CONTACT: Kimberley Medrano, Operations and PM Analyst, 202–435–9623, *CFPB_BoardandCouncilApps@cfpb.gov.*

SUPPLEMENTARY INFORMATION:

I. Background

The Bureau is charged with regulating ''the offering and provision of consumer financial products or services under the Federal consumer financial laws,'' so as to ensure that ''all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive.'' Pursuant to section 1021(c) of the Wall Street Reform and Consumer Protection Act, Public Law 111–203, Dodd-Frank Act, the Bureau's primary functions are:

1. Conducting financial education programs;
2. Collecting, investigating, and responding to consumer complaints;
3. Collecting, researching, monitoring, and publishing information relevant to the function of markets for consumer financial products and services to identify risks to consumers and the proper functioning of such markets;
4. Supervising persons covered under the Dodd-Frank Act for compliance with Federal consumer financial law, and taking appropriate enforcement action to address violations of Federal consumer financial law;
5. Issuing rules, orders, and guidance implementing Federal consumer financial law; and
6. Performing such support activities as may be needed or useful to facilitate the other functions of the Bureau.

As described in more detail below, section 1014 of the Dodd-Frank Act calls for the Director of the Bureau to establish a Consumer Advisory Board to advise and consult with the Bureau regarding its functions, and to provide information on emerging trends and practices in the consumer financial markets.

Pursuant to the executive and administrative powers conferred on the Bureau by section 1012 of the Dodd-Frank Act, the Director of the Bureau established the discretionary committees, CBAC, CUAC, and ARC, under agency authority in accordance with the provisions of the Federal Advisory Committee Act, as amended, 5 U.S.C., App. 2.

III. Qualifications

Pursuant to section 1014(b) of the Dodd-Frank Act, in appointing members to the Consumer Advisory Board, ''the Director shall seek to assemble experts in consumer protection, financial services, community development, fair lending and civil rights, and consumer financial products or services and representatives of depository institutions that primarily serve underserved communities, and representatives of communities that have been significantly impacted by higher-priced mortgage loans, and seek representation of the interests of covered persons and consumers, without regard to party affiliation.'' The determinants of ''expertise'' shall depend, in part, on the constituency, interests, or industry sector the nominee

seeks to represent, and where appropriate, shall include significant experience as a direct service provider to consumers.

Pursuant to section 12 of the Community Bank Advisory Council Charter, in appointing members to the committee the Director shall seek to assemble members with diverse points of view, institution asset sizes, and geographical backgrounds. Only bank or thrift employees (CEOs, compliance officers, government relations officials, etc.) will be considered for membership. Membership is limited to employees of banks and thrifts with total assets of $10 billion or less that are not affiliates of depository institutions or community banks with total assets of more than $10 billion.

Pursuant to section 12 of the Credit Union Advisory Council Charter, in appointing members to the committee the Director shall seek to assemble members with diverse points of view, institution asset sizes, and geographical backgrounds. Only credit union employees (CEOs, compliance officers, government relations officials, etc.) will be considered for membership. Membership is limited to employees of credit unions with total assets of $10 billion or less that are not affiliates of depository institutions or credit unions with total assets of more than $10 billion.

Pursuant to section 12 of the Academic Research Council Charter, in appointing members to the committee the Director shall seek to assemble members who are economic experts and academics with diverse points of view; such as experienced economists with a strong research and publishing background, and a record of involvement in research and public policy, including public or academic service. Additionally, members should be prominent experts who are recognized for their professional achievements and rigorous economic analysis including those specializing in household finance, finance, financial education, labor economics, industrial organization, public economics, and law and economics; and experts from related social sciences related to the Bureau's mission. In particular, the Director will seek to identify academics with strong methodological and technical expertise in structural or reduced form econometrics; modeling of consumer decision-making; survey and random controlled trial methods; benefit cost analysis, welfare economics and program evaluation; or marketing.

The Bureau has a special interest in ensuring that the perspectives of women and men, all racial and ethnic groups, and individuals with disabilities are adequately represented on the advisory committees, and therefore, encourages applications from qualified candidates from these groups. The Bureau also has a special interest in establishing advisory committees that are represented by a diversity of viewpoints and constituencies, and therefore encourages applications from qualified candidates who:

1. Represent the United States' geographic diversity; and

2. Represent the interests of special populations identified in the Dodd-Frank Act, including service members, older Americans, students, and traditionally underserved consumers and communities.

IV. Application Procedures

Any interested person may apply for membership on the committees.

A complete application packet must include:

1. A recommendation letter from a third party describing the applicant's interests and qualifications to serve on the committee;

2. A complete résumé or curriculum vitae for the applicant; and

3. A one-page cover letter, which summarizes the applicant's expertise and provides reason(s) why he or she would like to join the committee.

4. A complete questionnaire. *https://consumer-financial-protection-bureau.forms.fm/2020-application-to-serve-on-the-cfpb-s-advisory-committees[.*

To evaluate potential sources of conflicts of interest, the Bureau will ask potential candidates to provide information related to financial holdings and/or professional affiliations, and to allow the Bureau to perform a background check. The Bureau will not review applications and will not answer questions from internal or external parties regarding applications until the application period has closed.

The Bureau does not accept applications from federally registered lobbyists or current elected officials for a position on the advisory committees.

Only complete applications will be given consideration for membership on the advisory committees.

Dated: January 8, 2020.

Kirsten Sutton,

Chief of Staff, Bureau of Consumer Financial Protection.

[FR Doc. 2020–00308 Filed 1–10–20; 8:45 am]

BILLING CODE 4810–AM–P

DEPARTMENT OF DEFENSE

Department of the Army, Corps of Engineers

Notice of Intent To Prepare a Tiered Environmental Impact Statement for the New York New Jersey Harbor and Tributaries Coastal Storm Risk Management Feasibility Study

AGENCY: U.S. Army Corps of Engineers, DoD.

ACTION: Notice of intent.

SUMMARY: Pursuant to the requirements of the National Environmental Policy Act (NEPA), the U.S. Army Corps of Engineers, New York District (Corps) is preparing an integrated Feasibility Report/Tiered Environmental Impact Statement (EIS) for the proposed New York and New Jersey Harbor and Tributaries Coastal Storm Risk Management Feasibility Study (NYNJHAT). The study is assessing the feasibility of coastal storm risk management alternatives to be implemented within the authorized study area with a specific emphasis on the New York and New Jersey Harbor, including Raritan Bay, the tidally affected stretches of the Passaic and Hackensack Rivers, and the Hudson River to Troy, New York.

DATES: Comments and suggestions must be submitted by February 12, 2020.

ADDRESSES: Pertinent information about the study can be found at: *http://www.nan.usace.army.mil/Missions/Civil-Works/Projects-in-New-York/New-York-New-Jersey-Harbor-Tributaries-Focus-Area-Feasibility-Study/.* Interested parties are welcome to send written comments and suggestions concerning the scope of issues to be evaluated within the Tiered EIS to Cheryl R. Alkemeyer, NEPA Lead, Environmental Analysis Branch, Watershed Section, Planning Division, U.S. Army Corps of Engineers, New York District. Mail: Cheryl R. Alkemeyer, USACE Planning Environmental 17–421 c/o PSC Mail Center, 26 Federal Plaza, New York, NY 10278; phone: (917) 790– 8723; email: *Cheryl.R.Alkemeyer@usace.army.mil.*

FOR FURTHER INFORMATION CONTACT: Questions about the overall NYNJHAT study should be directed to Bryce Wisemiller, Project Manager, U.S. Army Corps of Engineers, New York District, Programs and Project Management Division, Civil Works Programs Branch. Mail: Bryce W. Wisemiller, USACE Programs and Project Management 17–401, c/o PSC Mail Center, 26 Federal Plaza, New York, NY 10278; Phone:

(917) 790–8307; email: *Bryce.W.Wisemiller@usace.army.mil.*

SUPPLEMENTARY INFORMATION:

1. Background

The U.S. Army Corps of Engineers (Corps), in partnership with the New York State Department of Environmental Conservation (NYSDEC) and the New Jersey Department of Environmental Protection (NJDEP) as the non-federal sponsors, are undertaking this study. In addition, the City of New York is a non-federal partner. The NYNJHAT study area, which encompasses the New York metropolitan area, is highly vulnerable to damage from coastal storm surge, wave attack, erosion, and intense rainfall-storm water runoff events that cause riverine or inland flooding, which can exacerbate coastal flooding. The Corps is authorized under Public Law 84–71, June 15, 1955 (69 Stat. 132) to conduct an investigation into potential coastal storm risk management solutions within the NYNJHAT study area. A Feasibility Cost Sharing Agreement (FCSA) was executed in 2016 with the NYSDEC and NJDEP.

2. Study Area

The study area encompasses approximately 2,150 square miles and includes parts of Bergen, Passaic, Morris, Essex, Hudson, Union, Somerset, Middlesex, and Monmouth Counties in New Jersey and Rensselaer, Albany, Columbia, Greene, Duchess, Ulster, Putnam, Orange, Westchester, Rockland, Bronx, New York, Queens, Kings, Richmond, and Nassau Counties in New York. The study area extends upstream of the Hudson River to the federal lock and dam at Troy, New York, the Passaic River to the Dundee Dam, and the Hackensack River to the Oradell Reservoir.

3. Corps Decision Making

As required by Council on Environmental Quality's Principles, Requirements and Guidelines for Water and Land Related Resources Implementation Studies all reasonable alternatives to the proposed Federal action that meet the purpose and need will be considered in the Tiered EIS. The initial focused array of alternatives being formulated are ranging from harbor-wide coastal storm risk management (CSRM) methods to land-based, perimeter CSRM methods, with three alternatives between. All alternatives are anticipated to also include complementary non-structural measures and natural and nature based features as appropriate. To be conservative, all other ongoing studies and projects by USACE and other agencies that can reasonably be expected to be implemented by 2020 are assumed to be in place as part of this study's assumed future ''without project'' condition.

4. Public Participation

The Corps, the NYSDEC and the NJDEP hosted three agency workshop meetings in January and February 2017, with representatives from federal and state agencies, as well as representatives from local agencies and towns. The Corps initially announced the preparation of an integrated Feasibility Report/Tiered EIS for study in the February 13, 2018 **Federal Register**. The 45-day NEPA scoping period (July 6–August 20, 2018) was extended to November 5, 2018 based on requested from the public. Nine public NEPA scoping meetings were held throughout the study area. Subsequent to the publication of the February 13, 2018 NOI, the Study was granted an exemption from the requirement to complete the feasibility study within 3 years, as required in Section 1001(a) of the Water Resources Reform and Development Act of 2014. This exemption was granted on October 31, 2018 on an interim basis, and allowed for an additional 15 months to complete the Draft Integrated Feasibility Report and Tier 1 EIS. Therefore, in order to align the revised study schedule with Executive Order 13807, Notice to Withdraw the original NOI was published in the February 13, 2019 **Federal Register**. To further provide the public with study information, an Interim Report was released on February 19, 2019 that identified the preliminary economic, environmental, engineering and other studies performed to date of the above referenced alternatives. Eight public meetings related to the Interim Report were also held. Comments, concerns and information submitted to the Corps are being evaluated and considered during the development of the Draft EIS. Comments received are continuing to aid the study progress and included in the draft report and will be part of the administrative record

5. Lead and Cooperating Agencies

The U.S. Army Corps of Engineers is the lead federal agency for the preparation of a Tiered EIS in order to meet the requirements of the NEPA and the NEPA Implementing Regulations of the President's Council on Environmental Quality (40 CFR 1500–1508). The following agencies have accepted the invitation to be Cooperating Agencies: U.S. Coast Guard, the U.S. Environmental Protection Agency, the U.S. Fish and Wildlife Service, the National Marine Fisheries Service, the National Park Service, and the Federal Emergency Management Agency agreed to be a Participating Agency. The preparation of a Tiered EIS will be coordinated with New York State, New Jersey State and local municipalities with discretionary authority relative to the proposed actions. The Draft Integrated Feasibility Report/Tiered EIS is currently scheduled for distribution to the public in the summer of 2020.

Jeffrey L. Milhorn,

Major General, USA, Commanding.

[FR Doc. 2020–00289 Filed 1–10–20; 8:45 am]

BILLING CODE 3720–58–P

DEPARTMENT OF EDUCATION

[Docket No. ED–2019–ICCD–0131]

Agency Information Collection Activities; Submission to the Office of Management and Budget for Review and Approval; Comment Request; Targeted Teacher Shortage Areas Data Collection

AGENCY: Office of Postsecondary Education (OPE), Department of Education (ED) .

ACTION: Notice.

SUMMARY: In accordance with the Paperwork Reduction Act of 1995, ED is proposing a revision of an existing information collection.

DATES: Interested persons are invited to submit comments on or before February 12, 2020.

ADDRESSES: To access and review all the documents related to the information collection listed in this notice, please use *http://www.regulations.gov* by searching the Docket ID number ED–2019–ICCD–0131. Comments submitted in response to this notice should be submitted electronically through the Federal eRulemaking Portal at *http://www.regulations.gov* by selecting the Docket ID number or via postal mail, commercial delivery, or hand delivery. If the regulations.gov site is not available to the public for any reason, ED will temporarily accept comments at *ICDocketMgr@ed.gov.* Please include the docket ID number and the title of the information collection request when requesting documents or submitting comments. *Please note that comments submitted by fax or email and those submitted after the comment period will not be accepted.* Written requests for information or comments submitted by postal mail or delivery should be

addressed to the Director of the Strategic Collections and Clearance Governance and Strategy Division, U.S. Department of Education, 400 Maryland Ave. SW, LBJ, Room 6W–208D, Washington, DC 20202–4537.

FOR FURTHER INFORMATION CONTACT: For specific questions related to collection activities, please contact Freddie Cross, 202–453–7224.

SUPPLEMENTARY INFORMATION: The Department of Education (ED), in accordance with the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3506(c)(2)(A)), provides the general public and Federal agencies with an opportunity to comment on proposed, revised, and continuing collections of information. This helps the Department assess the impact of its information collection requirements and minimize the public's reporting burden. It also helps the public understand the Department's information collection requirements and provide the requested data in the desired format. ED is soliciting comments on the proposed information collection request (ICR) that is described below. The Department of Education is especially interested in public comment addressing the following issues: (1) Is this collection necessary to the proper functions of the Department; (2) will this information be processed and used in a timely manner; (3) is the estimate of burden accurate; (4) how might the Department enhance the quality, utility, and clarity of the information to be collected; and (5) how might the Department minimize the burden of this collection on the respondents, including through the use of information technology. Please note that written comments received in response to this notice will be considered public records.

Title of Collection: Targeted Teacher Shortage Areas Data Collection.

OMB Control Number: 1840–0595.

Type of Review: A revision of an existing information collection.

Respondents/Affected Public: State, Local, and Tribal Governments.

Total Estimated Number of Annual Responses: 57.

Total Estimated Number of Annual Burden Hours: 2,793.

Abstract: This request is for approval of reporting requirements that are contained in the Federal Family Education Loan Program (FFELP) regulations (34 CFR 682.210) which address the targeted teacher deferment provision of the Higher Education Act of 1965 as amended by the Higher Education Amendment of 1986, sections 427(a)(2)(C)(vi), 428 (b)(1)(M)(vi), and 428 (b)(4)(A), which provide for the targeted teacher deferment.

The FFELP (34 CFR 682.210(q)), Paul Douglas Teacher Scholarship Program (34 CFR 653.50(a)), TEACH Grant Program, and Federal Perkins Loan Program (34 CFR 674.53(c)) regulations contain information collection requirements. The Chief State School Officers of each state provide the Secretary annually with a list of proposed teacher shortage areas for that state.

Dated: January 8, 2020.

Kate Mullan,

PRA Coordinator, Strategic Collections and Clearance, Governance and Strategy Division, Office of Chief Data Officer.

[FR Doc. 2020–00281 Filed 1–10–20; 8:45 am]

BILLING CODE 4000–01–P

DEPARTMENT OF EDUCATION

Eligibility Designations and Applications for Waiving Eligibility Requirements; Programs Under Parts A and F of Title III and Programs Under Title V of the Higher Education Act of 1965, as Amended (HEA)

AGENCY: Office of Postsecondary Education, Department of Education.

ACTION: Notice; correction.

SUMMARY: On December 16, 2019, we published in the **Federal Register** a notice inviting applications for the waiver of eligibility requirements for fiscal year (FY) 2020 (Eligibility NIA) for programs authorized by Parts A and F of Title III and by Title V of the HEA. This notice revises (a) the Deadline for Transmittal of Applications and (b) information provided in Section I of the notice. All other requirements and conditions in the notice remain the same.

DATES: The correction is applicable January 13, 2020.

FOR FURTHER INFORMATION CONTACT: Dr. Jason Cottrell, U.S. Department of Education, 400 Maryland Avenue SW, Room 250–50, Washington, DC 20202. Telephone: (202) 453–7530. Email: *Jason.cottrell@ed.gov.*

If you use a telecommunications device for the deaf (TDD) or a text telephone (TTY), call the Federal Relay Service (FRS), toll free, at 1–800–877–8339.

SUPPLEMENTARY INFORMATION: On December 16, 2019, we published in the **Federal Register** a notice inviting applications for designation as an eligible institution for programs under Parts A and F of Title III and under Title V of the HEA (84 FR 68434). This notice revises: (a) The deadline for transmittal of applications; and (b) the base year 2017–2018 average Pell Grant Percentage for two-year public institutions. All other requirements and conditions in the notice remain the same.

Correction

In FR Doc. 2019–27048, in the **Federal Register** of December 16, 2019, we make the following revisions:

(a) On page 68434, in the third column, under **DATES** and after ''Deadline for Transmittal of Applications'', we remove the date ''January 15, 2020'' and replace it with the date ''January 31, 2020''.

(b) On page 68436, in the table, under ''Base year 2017–2018 average Pell Grant percentage'' in the first row, we remove the number ''26'' and replace it with the number ''36''. The corrected table is as follows:

Type of institution	Base year 2017–2018 average Pell Grant percentage	Base year 2017–2018 average core expenses per FTE student
Two-year Public Institutions	36	$14,194
Two-year Non-profit Private Institutions	55	15,960
Four-year Public Institutions	37	31,578
Four-year Non-profit Private Institutions	39	40,752

Accessible Format: Individuals with disabilities can obtain this notice and a copy of the application in an accessible format (*e.g.,* braille, large print, audio tape, or compact disc) on request to the contact person listed under **FOR FURTHER INFORMATION CONTACT**.

Electronic Access to This Document: The official version of this document is the document published in the **Federal Register**. You may access the official edition of the **Federal Register** and the Code of Federal Regulations at *www.govinfo.gov.* At this site you can view this document, as well as all other documents of this Department published in the **Federal Register**, in text or Portable Document Format (PDF). To use PDF you must have Adobe Acrobat Reader, which is available free at the site.

You may also access documents of the Department published in the **Federal Register** by using the article search feature at: *www.federalregister.gov.* Specifically, through the advanced search feature at this site, you can limit your search to documents published by the Department.

Dated:

Robert L. King,

Assistant Secretary for the Office of Postsecondary Education.

[FR Doc. 2020–00290 Filed 1–10–20; 8:45 am]

BILLING CODE 4000–01–P

ENVIRONMENTAL PROTECTION AGENCY

[EPA–HQ–OW–2004–0015; FRL–10003–62–OW]

Proposed Information Collection Request; Comment Request; Clean Water Act State Revolving Fund Program

AGENCY: Environmental Protection Agency (EPA).

ACTION: Notice.

SUMMARY: The U.S. Environmental Protection Agency (EPA) is planning to submit a request to renew an existing information collection request (ICR), ''Clean Water State Revolving Fund Program'' (EPA ICR No. 1391.11, OMB Control No. 2040–0118) to the Office of Management and Budget (OMB) for review and approval in accordance with the Paperwork Reduction Act (PRA). Before doing so, the EPA is soliciting public comments on specific aspects of the proposed information collection as described below. This is a proposed extension of the ICR, which is currently approved through September 30, 2020. An Agency may not conduct or sponsor and a person is not required to respond to a collection of information unless it displays a currently valid OMB control number.

DATES: Comments must be submitted on or before March 13, 2020.

ADDRESSES: Submit your comments, referencing Docket ID No. EPA–HQ–OW–2004–0015, online using *www.regulations.gov* (our preferred method), by email to *ow-docket@epa.gov,* or by mail to: EPA Docket Center, Environmental Protection Agency, Mail Code 28221T, 1200 Pennsylvania Ave. NW, Washington, DC 20460.

The EPA's policy is that all comments received will be included in the public docket without change including any personal information provided, unless the comment includes profanity, threats, information claimed to be Confidential Business Information (CBI) or other information whose disclosure is restricted by statute.

FOR FURTHER INFORMATION CONTACT: Mark Mylin, Water Infrastructure Division, Office of Wastewater Management, 4204M, Environmental Protection Agency, 1200 Pennsylvania Ave. NW, Washington, DC 20460; telephone number: 202–564–0607; email address: *mylin.mark@epa.gov.*

SUPPLEMENTARY INFORMATION: Supporting documents which explain in detail the information that the EPA will be collecting are available in the public docket for this ICR. The docket can be viewed online at *www.regulations.gov* or in person at the EPA Docket Center, WJC West, Room 3334, 1301 Constitution Ave. NW, Washington, DC. The telephone number for the Docket Center is 202–566–1744. For additional information about EPA's public docket, visit *https://www.epa.gov/dockets.*

Pursuant to section 3506(c)(2)(A) of the PRA, the EPA is soliciting comments and information to enable it to: (1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Agency, including whether the information will have practical utility; (2) Evaluate the accuracy of the Agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) Enhance the quality, utility, and clarity of the information to be collected; and (4) Minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated electronic, mechanical, or other technological collection techniques or other forms of information technology, *e.g.,* permitting electronic submission of responses. The EPA will consider the comments received and amend the ICR as appropriate. The final ICR package will then be submitted to OMB for review and approval. At that time, the EPA will issue another **Federal Register** document to announce the submission of the ICR to OMB and the opportunity to submit additional comments to OMB.

Abstract: The Clean Water State Revolving Funds (CWSRF) were established by the 1987 amendments to the Clean Water Act (CWA) as a financial assistance program for a wide-range of wastewater infrastructure and other water quality projects. The 1987 amendments added Title VI to the CWA, enabling EPA to provide grants to all 50 states and Puerto Rico to capitalize CWSRFs. The CWSRFs can provide loans and other forms of assistance for a wide array of projects, including construction of wastewater treatments facilities, green infrastructure projects, agricultural best management practices, and water and energy efficiency improvements. Eligible borrowers of CWSRF funding range from municipalities to nonprofit organizations and other private entities. In 2014, Title VI of the CWA was amended by the Water Resources Reform and Development Act (WRRDA). Additional information about the CWSRFs is available at *https://www.epa.gov/cwsrf/learn-about-clean-water-state-revolving-fund-cwsrf.*

This ICR renews the Office of Management and Budget (OMB) Number 2040–0118 CWSRF ICR and provides updated estimates of the reporting burden associated with the information collection activities.

The individual information collections covered under this ICR are briefly described as follows:

Capitalization Grant Agreement/ Intended Use Plan

The Capitalization Grant Agreement is the principal instrument by which a CWSRF commits to manage its revolving fund program in conformity with the requirements of the CWA. The grant agreement contains or incorporates by reference the intended use plan, application materials, required certifications, and other documentation required by the EPA. The intended use plan describes how a CWSRF program intends to use its funds for the upcoming year to meet the objectives of the CWA.

Annual Report

The annual report indicates how the CWSRF has met its goals and objectives of the previous state fiscal year as stated in the grant agreement and, more specifically, in the intended use plan. The report provides information on loan recipients, loan amounts, loan terms, project categories of eligible costs, and

similar data on other forms of assistance.

Annual Audit

The CWA requires a CWSRF to undergo an annual audit. Though an audit conducted under the Single Audit Act meets this requirement, the EPA still recommends that a CWSRF also undergo a separate independent audit as a best management practice. The audit must contain an opinion on the financial condition of the CWSRF program, a report on its internal controls, and a report on compliance with applicable laws and the CWA.

Clean Water National Information Management System (CWNIMS) and CWSRF Benefits Reporting (CBR)

To meet the CWA objective of ''promoting the efficient use of fund resources,'' states must enter financial data, including project disbursements, into the CWNIMS database on an annual basis. This publicly available information is used by the EPA to assess compliance with the CWSRFs' mandate to use all funds in an ''expeditious and timely'' manner and achieve the objectives of the CWA. Project level data is collected on a quarterly basis using the CBR System to record projected environmental results from CWSRF projects.

CWSRF Applications

The application is developed and used by the CWSRFs to determine the project's eligibility, to evaluate the borrower's financial capability to repay the CWSRF, and to ensure that the borrower will comply with all applicable program requirements. The information collected by the CWSRF applications is consistent with requirements set forth by the CWA.

Public Awareness Policy

Per EPA Grants Policy Issuance (GPI) 14–02: Enhancing Public Awareness of EPA Assistance Agreements, CWSRF borrowers must publicize the EPA's involvement in project funding only up to the funding amount in each year's capitalization grant. The CWSRFs have various options to meet this requirement.

Except for the public awareness policy and CWSRF applications, the respondents for the information collection activities are the state environmental departments and/or finance agencies responsible for operating the CWSRFs. The CWSRFs have procedures in place to assist borrowers in completing the applications. The public awareness policy directly impacts CWSRF borrowers that are designated as recipients of federal funds. The burden associated with the public awareness policy should not have an impact on small entities since the CWSRFs have flexibility in determining which borrowers must comply with this requirement.

Form numbers: None.

Respondents/affected entities: Entities affected by this action are state environmental departments and/or finance agencies responsible for operating the CWSRFs and eligible CWSRF borrowers.

Respondent's obligation to respond: Required to obtain or retain a benefit per Title VI of CWA as amended by WRRDA.

Estimated number of respondents: 51 state environmental departments and/or finance agencies (per year); 1,544 eligible CWSRF borrowers (per year).

Frequency of response: Varies by requirement (*i.e.,* quarterly and annually).

Total estimated burden: 659,390 hours (per year). Burden is defined at 5 CFR 1320.03(b).

Total estimated cost: $33,199,314 (per year).

Changes in estimates: There is an increase of 72,004 hours (per year) in the total estimated reporting burden compared with the ICR currently approved by OMB. This increase is from an upward adjustment of the annual number of CWSRF applications expected to occur during this collection period. Specifically, the estimated annual number of CWSRF applications has been increased from 1,359 to 1,544 in response to recent activity.

Dated: December 20, 2019.

Andrew D. Sawyers,

Director, Office of Wastewater Management.

[FR Doc. 2020–00274 Filed 1–10–20; 8:45 am]

BILLING CODE 6560–50–P

FEDERAL RESERVE SYSTEM

Formations of, Acquisitions by, and Mergers of Bank Holding Companies

The companies listed in this notice have applied to the Board for approval, pursuant to the Bank Holding Company Act of 1956 (12 U.S.C. 1841 *et seq.*) (BHC Act), Regulation Y (12 CFR part 225), and all other applicable statutes and regulations to become a bank holding company and/or to acquire the assets or the ownership of, control of, or the power to vote shares of a bank or bank holding company and all of the banks and nonbanking companies owned by the bank holding company, including the companies listed below.

The applications listed below, as well as other related filings required by the Board, are available for immediate inspection at the Federal Reserve Bank indicated. The applications will also be available for inspection at the offices of the Board of Governors. Interested persons may express their views in writing on the standards enumerated in the BHC Act (12 U.S.C. 1842(c)). If the proposal also involves the acquisition of a nonbanking company, the review also includes whether the acquisition of the nonbanking company complies with the standards in section 4 of the BHC Act (12 U.S.C. 1843), and interested persons may express their views in writing on the standards enumerated in section 4. Unless otherwise noted, nonbanking activities will be conducted throughout the United States.

Comments regarding each of these applications must be received at the Reserve Bank indicated or the offices of the Board of Governors, Ann E. Misback, Secretary of the Board, 20th and Constitution Avenue NW, Washington, DC 20551–0001, not later than February 12, 2020.

A. Federal Reserve Bank of Minneapolis (Chris P. Wangen, Assistant Vice President), 90 Hennepin Avenue, Minneapolis, Minnesota 55480–0291:

1. *L1 Holding Corporation, Minneapolis, Minnesota;* to become a bank holding company by acquiring Eagle Community Bank, Maple Grove, Minnesota. In connection with this application, L1 Holding Corporation has applied to engage in mortgage lending activities by acquiring LeaderOne Financial Corporation, Overland Park, Kansas, pursuant to section 4 of the BHC Act.

Board of Governors of the Federal Reserve System, January 8, 2020.

Yao-Chin Chao,

Assistant Secretary of the Board.

[FR Doc. 2020–00278 Filed 1–10–20; 8:45 am]

BILLING CODE P

FEDERAL RESERVE SYSTEM

Change in Bank Control Notices; Acquisitions of Shares of a Bank or Bank Holding Company

The notificants listed below have applied under the Change in Bank Control Act (Act) (12 U.S.C. 1817(j)) and § 225.41 of the Board's Regulation Y (12 CFR 225.41) to acquire shares of a bank or bank holding company. The factors that are considered in acting on the notices are set forth in paragraph 7 of the Act (12 U.S.C. 1817(j)(7)).

The applications listed below, as well as other related filings required by the Board, if any, are available for immediate inspection at the Federal Reserve Bank indicated. The applications will also be available for inspection at the offices of the Board of Governors. Interested persons may express their views in writing on the standards enumerated in paragraph 7 of the Act.

Comments regarding each of these applications must be received at the Reserve Bank indicated or the offices of the Board of Governors, Ann E. Misback, Secretary of the Board, 20th and Constitution Avenue NW, Washington DC 20551–0001, not later than January 28, 2020.

A. Federal Reserve Bank of Atlanta (Kathryn Haney, Assistant Vice President) 1000 Peachtree Street NE, Atlanta, Georgia 30309. Comments can also be sent electronically to *Applications.Comments@atl.frb.org:*

1. *Kenneth Lee Barber, Villa Rica, Georgia; Greg Logan Lee, Birmingham, Alabama; Jeff Daniel Couey, Acworth, Georgia; Johnny Lee Blankenship, Douglasville, Georgia; Eric Leonard Johnson, Atlanta, Georgia; Paul David Orr, Fairburn, Georgia; and Douglas Craig Davidson, Johns Creek, Georgia;* to acquire voting shares of Peoples Bankshares, Inc., and thereby indirectly acquire voting shares of The Peoples Bank, both of Eatonton, Georgia.

Board of Governors of the Federal Reserve System, January 8, 2020.

Yao-Chin Chao,

Assistant Secretary of the Board.

[FR Doc. 2020–00277 Filed 1–10–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Food and Drug Administration

[Docket No. FDA–2019–D–5422]

Peripheral Percutaneous Transluminal Angioplasty and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff; Availability

AGENCY: Food and Drug Administration, HHS.

ACTION: Notice of availability.

SUMMARY: The Food and Drug Administration (FDA or Agency) is announcing the availability of the draft guidance entitled ''Peripheral Percutaneous Transluminal Angioplasty (PTA) and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff.'' The FDA is issuing this draft guidance document to provide recommendations for 510(k) submissions for peripheral percutaneous transluminal angioplasty (PTA) balloons and specialty catheters (*e.g.,* infusion catheters, PTA balloon catheters for in-stent restenosis (ISR), scoring/cutting balloons). This draft guidance is not final nor is it in effect at this time.

DATES: Submit either electronic or written comments on the draft guidance by March 13, 2020 to ensure that the Agency considers your comment on this draft guidance before it begins work on the final version of the guidance.

ADDRESSES: You may submit comments on any guidance at any time as follows:

Electronic Submissions

Submit electronic comments in the following way:

• *Federal eRulemaking Portal: https://www.regulations.gov.* Follow the instructions for submitting comments. Comments submitted electronically, including attachments, to *https://www.regulations.gov* will be posted to the docket unchanged. Because your comment will be made public, you are solely responsible for ensuring that your comment does not include any confidential information that you or a third party may not wish to be posted, such as medical information, your or anyone else's Social Security number, or confidential business information, such as a manufacturing process. Please note that if you include your name, contact information, or other information that identifies you in the body of your comments, that information will be posted on *https://www.regulations.gov.*

• If you want to submit a comment with confidential information that you do not wish to be made available to the public, submit the comment as a written/paper submission and in the manner detailed (see ''Written/Paper Submissions'' and ''Instructions'').

Written/Paper Submissions

Submit written/paper submissions as follows:

• *Mail/Hand Delivery/Courier (for written/paper submissions):* Dockets Management Staff (HFA–305), Food and Drug Administration, 5630 Fishers Lane, Rm. 1061, Rockville, MD 20852.

• For written/paper comments submitted to the Dockets Management Staff, FDA will post your comment, as well as any attachments, except for information submitted, marked and identified, as confidential, if submitted as detailed in ''Instructions.''

Instructions: All submissions received must include the Docket No. FDA–2019–D–5422 for ''Peripheral Percutaneous Transluminal Angioplasty (PTA) and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff.'' Received comments will be placed in the docket and, except for those submitted as ''Confidential Submissions,'' publicly viewable at *https://www.regulations.gov* or at the Dockets Management Staff between 9 a.m. and 4 p.m., Monday through Friday.

• Confidential Submissions—To submit a comment with confidential information that you do not wish to be made publicly available, submit your comments only as a written/paper submission. You should submit two copies total. One copy will include the information you claim to be confidential with a heading or cover note that states ''THIS DOCUMENT CONTAINS CONFIDENTIAL INFORMATION.'' The Agency will review this copy, including the claimed confidential information, in its consideration of comments. The second copy, which will have the claimed confidential information redacted/blacked out, will be available for public viewing and posted on *https://www.regulations.gov.* Submit both copies to the Dockets Management Staff. If you do not wish your name and contact information to be made publicly available, you can provide this information on the cover sheet and not in the body of your comments and you must identify this information as ''confidential.'' Any information marked as ''confidential'' will not be disclosed except in accordance with 21 CFR 10.20 and other applicable disclosure law. For more information about FDA's posting of comments to public dockets, see 80 FR 56469, September 18, 2015, or access the information at: *https://www.gpo.gov/fdsys/pkg/FR-2015-09-18/pdf/2015-23389.pdf.*

Docket: For access to the docket to read background documents or the electronic and written/paper comments received, go to *https://www.regulations.gov* and insert the docket number, found in brackets in the heading of this document, into the ''Search'' box and follow the prompts and/or go to the Dockets Management Staff, 5630 Fishers Lane, Rm. 1061, Rockville, MD 20852.

You may submit comments on any guidance at any time (see 21 CFR 10.115(g)(5)). An electronic copy of the guidance document is available for

download from the internet. See the **SUPPLEMENTARY INFORMATION** section for information on electronic access to the guidance. Submit written requests for a single hard copy of the draft guidance document entitled ''Peripheral Percutaneous Transluminal Angioplasty (PTA) and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff'' to the Office of Policy, Guidance and Policy Development, Center for Devices and Radiological Health, Food and Drug Administration, 10903 New Hampshire Ave., Bldg. 66, Rm. 5431, Silver Spring, MD 20993–0002. Send one self-addressed adhesive label to assist that office in processing your request.

FOR FURTHER INFORMATION CONTACT: Eleni Whatley, Center for Devices and Radiological Health, Food and Drug Administration, 10903 New Hampshire Ave., Bldg. 66, Rm. 2267, Silver Spring, MD 20993–0002, 301–796–6372.

SUPPLEMENTARY INFORMATION:

I. Background

The FDA is issuing this draft guidance to clarify the FDA's recommendations for testing and information to include in 510(k) submissions for PTA catheters and specialty catheters to promote consistency across submissions. These devices are catheter-based devices intended to treat lesions in the peripheral vasculature. This draft guidance expands on the FDA's current thinking for testing of PTA balloon catheters and specialty catheters (*e.g.,* infusion catheters, PTA balloon catheters for ISR, scoring/cutting balloons), and provides specific recommendations regarding performance testing and anatomy-specific assessments. This document supplements other FDA documents regarding the specific content requirements of premarket submissions.

II. Significance of Guidance

This draft guidance is being issued consistent with FDA's good guidance practices regulation (21 CFR 10.115). The draft guidance, when finalized, will represent the current thinking of FDA on ''Peripheral Percutaneous Transluminal Angioplasty (PTA) and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff.'' It does not establish any rights for any person and is not binding on FDA or the public. You can use an alternative approach if it satisfies the requirements of the applicable statutes and regulations.

III. Electronic Access

Persons interested in obtaining a copy of the draft guidance may do so by downloading an electronic copy from the internet. A search capability for all Center for Devices and Radiological Health guidance documents is available at *https://www.fda.gov/MedicalDevices/DeviceRegulationandGuidance/GuidanceDocuments/default.htm.* This guidance document is also available at *https://www.regulations.gov.* Persons unable to download an electronic copy of ''Peripheral Percutaneous Transluminal Angioplasty (PTA) and Specialty Catheters—Premarket Notification (510(k)) Submissions; Draft Guidance for Industry and Food and Drug Administration Staff'' may send an email request to *CDRH-Guidance@fda.hhs.gov* to receive an electronic copy of the document. Please use the document number 16018 and complete title to identify the guidance you are requesting.

IV. Paperwork Reduction Act of 1995

This draft guidance refers to previously approved collections of information. These collections of information are subject to review by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3521). The collections of information in the following FDA regulations and guidance have been approved by OMB as listed in the following table:

21 CFR part or guidance	Topic	OMB control No.
807, subpart E	Premarket Notification	0910–0120
812	Investigational Device Exemption	0910–0078
''Requests for Feedback on Medical Device Submissions: The Pre-Submission Program and Meetings with Food and Drug Administration Staff''.	Q-Submissions	0910–0756
801	Medical Device Labeling Regulations	0910–0485
820	Current Good Manufacturing Practice (CGMP); Quality System (QS) Regulation.	0910–0073
50, 56	Protection of Human Subjects: Informed Consent; Institutional Review Boards.	0910–0755
56	Institutional Review Boards	0910–0130
58	Good Laboratory Practice (GLP) Regulations for Nonclinical Laboratory Studies.	0910–0119

Dated: January 7, 2020.

Lowell J. Schiller,

Principal Associate Commissioner for Policy.

[FR Doc. 2020–00296 Filed 1–10–20; 8:45 am]

BILLING CODE 4164–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Meeting of the Advisory Committee on Minority Health

AGENCY: Office of Minority Health, Office of the Secretary, Department of Health and Human Services.

ACTION: Notice of meeting.

SUMMARY: As stipulated by the Federal Advisory Committee Act, the U.S. Department of Health and Human Services (HHS or Department) is hereby giving notice that the Advisory Committee on Minority Health (ACMH) will hold a meeting. This meeting will be open to the public. Preregistration by January 24, 2020, is required for the public to attend the meeting, provide comments, and/or distribute printed material(s) to ACMH members. Information about the meeting is available from the designated contact person and will be posted on the website for the Office of Minority Health (OMH), *www.minorityhealth.hhs.gov.* Information about ACMH activities can

be found on the OMH website under the heading *About OMH.*

DATES: The meeting will be held on Thursday, January 30, 2020, 9:00 a.m. to 5:00 p.m. ET, and Friday, January 31, 2020, 9:00 a.m. to 3:00 p.m. ET. Day 2 may end earlier than 3:00 p.m. ET if ACMH completes it work before 3:00 p.m. ET.

ADDRESSES: The meeting will be accessible by attendance in-person or by webcast on the internet. In-person and webcast participants must register prior to the meeting. The meeting will be held at the 5600 Fishers Lane Building, Room 05E49, 5600 Fishers Lane, Rockville, Maryland 20187. Registered webcast participants will receive the webcast information prior to the meeting.

FOR FURTHER INFORMATION CONTACT: Violet Woo, Designated Federal Officer, Advisory Committee on Minority Health, Office of Minority Health, Department of Health and Human Services, Tower Building, 1101 Wootton Parkway, Plaza Level, Rockville, Maryland 20852. Phone: 240–453–2882; fax: 240–453–2883; email *OMH–ACMH@hhs.gov.*

SUPPLEMENTARY INFORMATION: In accordance with Public Law 105–392, the ACMH was established to provide advice to the Deputy Assistant Secretary for Minority Health on improving the health of each racial and ethnic minority group and on the development of goals and specific program activities of the OMH.

The topics to be discussed during this meeting will include strategies to improve access to and success of clinical prevention services among racial and ethnic minority populations. The recommendations will be given to the Deputy Assistant Secretary for Minority Health to inform efforts related to the Department's community-wide, chronic disease prevention strategies.

The meeting is open to the public. Any individual who wishes to attend the meeting in person or by webcast must register by sending an email to *OMH–ACMH@hhs.gov* by January 24, 2020. Each registrant should provide their name, affiliation, phone number, email address, days attending, and if participation is in-person or via webcast. After registration, individuals participating by webcast will receive webcast access information via email. Individuals who plan to attend and need special assistance, such as sign language interpretation or other reasonable accommodations, should contact BLH Technologies, Inc. at (240) 399–8735 and reference this meeting. Requests for special accommodations should be made at least ten (10) business days prior to the meeting.

Members of the public will have an opportunity to provide comments at the meeting. Public comments will be limited to two minutes per speaker during the time allotted. Individuals who would like to submit written statements should email *OMH–ACMH@hhs.gov* or mail their comments to the Designated Federal Officer contact cited above so it is received by the Designated Federal Officer at least five (5) business days prior to the meeting.

Any members of the public who wish to distribute electronic or printed material(s) related to this meeting's topic to ACMH members should email *OMH–ACMH@hhs.gov* or mail their material to the Designated Federal Officer contact cited above. The material should be received by the Designated Federal Officer at least five (5) business days prior to the meeting.

Dated: December 30, 2019.

Violet Woo,

Designated Federal Officer, Advisory Committee on Minority Health.

[FR Doc. 2020–00307 Filed 1–10–20; 8:45 am]

BILLING CODE 4150–29–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Institute of Allergy and Infectious Diseases; Notice of Closed Meeting

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meeting.

The meeting will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: National Institute of Allergy and Infectious Diseases Special Emphasis Panel; PAR–16–412: NIAID Resource-Related Research Projects (R24).

Date: February 4, 2020.

Time: 11:00 a.m. to 12:30 p.m.

Agenda: To review and evaluate grant applications.

Place: National Institutes of Health, 5601 Fishers Lane, Room 3E71, Rockville, MD 20892 (Telephone Conference Call).

Contact Person: Ann Marie M. Brighenti, Ph.D., Scientific Review Officer, Program Management & Operations Branch, Division of Extramural Activities, Scientific Review Program, Room 3E71, National Institutes of Health, National Institute of Allergy and Infectious Diseases, 5601 Fishers Lane Rockville, MD 20852, 301–761–3100, *AnnMarie.Cruz@niaid.nih.gov.*

(Catalogue of Federal Domestic Assistance Program Nos. 93.855, Allergy, Immunology, and Transplantation Research; 93.856, Microbiology and Infectious Diseases Research, National Institutes of Health, HHS)

Dated: January 7, 2020.

Tyeshia M. Roberson,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00270 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Institute on Minority Health and Health Disparities; Notice of Closed Meetings

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meetings.

The meetings will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: National Institute on Minority Health and Health Disparities Special Emphasis Panel; ZMD1 DRI M1 Special Emphasis Panel for Review of Mentored Research Scientist Development Award (K01).

Date: February 12–13, 2020.

Time: 12:00 p.m. to 5:00 p.m.

Agenda: To review and evaluate grant applications.

Place: National Institutes of Health, Gateway Plaza, 7201 Wisconsin Ave., Bethesda, MD 20817 (Telephone Conference Call).

Contact Person: Deborah Ismond, Ph.D., Scientific Review Officer, Division of Scientific Programs, National Institutes of Health, NIMHD, Gateway Building, 7201 Wisconsin Avenue, Bethesda, MD 20892, (301) 402–1366, *ismonddr@mail.nih.gov.*

Name of Committee: National Institute on Minority Health and Health Disparities Special Emphasis Panel; NIMHD Research Career Development Awards (Ks).

Date: March 4, 2020.
Time: 1:00 p.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: National Institutes of Health, Gateway Building, 7201 Wisconsin Avenue, Bethesda, MD 20892 (Virtual Meeting).
Contact Person: Xinli Nan, M.D., Ph.D., Scientific Review Officer, Division of Scientific Programs, National Institutes of Health, NIMHD, Gateway Building, 7201 Wisconsin Avenue, Bethesda, MD 20892, (301) 594–7784, *Xinli.Nan@nih.gov*.

Name of Committee: National Institute on Minority Health and Health Disparities Special Emphasis Panel; Specialized Centers of Excellence on Environmental Health Disparities Research (P50 Clinical Trial Optional).
Date: March 10–12, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Holiday Inn Gaithersburg, Walker Conference Room and Whetstone Conference Room 2, Montgomery Village Avenue, Gaithersburg, MD 20879.
Contact Person: Maryline Laude-Sharp, Ph.D., Scientific Review Officer, Division of Scientific Programs, National Institutes of Health, NIMHD, Gateway Building, 7201 Wisconsin Avenue, Ste. 525, MSC. 9206, Bethesda, MD 20892, (301) 451–9536, *mlaudesharp@mail.nih.gov*.

Dated: January 7, 2020.

Miguelina Perez,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00273 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Center for Advancing Translational Sciences; Notice of Closed Meeting

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meeting.

The meeting will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: National Center for Advancing Translational Sciences Special Emphasis Panel; NTU.
Date: February 5, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: National Institutes of Health, DEM1, 6701 Democracy Blvd., Bethesda, MD 20892 (Virtual Meeting).
Contact Person: Barbara J. Nelson, Ph.D., Scientific Review Officer, Office of Scientific Review, National Center for Advancing Translational Sciences (NCATS), National Institutes of Health, 6701 Democracy Blvd., Democracy 1, Room 1080, Bethesda, MD 20892–4874, 301–435–0806, *nelsonbj@mail.nih.gov.*

(Catalogue of Federal Domestic Assistance Program Nos. 93.859, Pharmacology, Physiology, and Biological Chemistry Research; 93.350, B—Cooperative Agreements; 93.859, Biomedical Research and Research Training, National Institutes of Health, HHS)

Dated: January 7, 2020.

Ronald J. Livingston, Jr.,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00268 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Institute on Aging; Notice of Closed Meetings

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meetings.

The meetings will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: National Institute on Aging Special Emphasis Panel; Drug Repositioning and Combination Therapy for AD.
Date: February 11, 2020.
Time: 10:00 a.m. to 2:00 p.m.
Agenda: To review and evaluate grant applications.
Place: National Institute on Aging, Gateway Building, 7201 Wisconsin Avenue, Bethesda, MD 20892 (Telephone Conference Call).
Contact Person: Alexander Parsadanian, Ph.D., Scientific Review Officer, Scientific Review Branch, National Institute on Aging, National Institutes of Health, Gateway Building 2C/212, 7201 Wisconsin Avenue, Bethesda, MD 20892, (301) 496–9666, *parsadaniana@nia.nih.gov.*

Name of Committee: National Institute on Aging Special Emphasis Panel; Pepper Center Review.
Date: February 19–20, 2020.
Time: 3:00 p.m. to 3:30 p.m.
Agenda: To review and evaluate grant applications.
Place: Hilton Garden Inn Bethesda, Conference Room, Bethesda Chevy Chase, 7301 Waverly Street, Bethesda, MD 20814.
Contact Person: Anita H. Undale, MD, Ph.D., Scientific Review Officer, Scientific Review Branch, National Institute on Aging, National Institutes of Health, Gateway Building, Suite 2W200, 7201 Wisconsin Avenue, Bethesda, MD 20892, (301) 827–7428, *anita.undale@nih.gov.*

Name of Committee: National Institute on Aging Special Emphasis Panel; Alzheimer's Disease Drug Development.
Date: February 19, 2020.
Time: 12:30 p.m. to 4:00 p.m.
Agenda: To review and evaluate grant applications.
Place: National Institute on Aging, Gateway Building, 7201 Wisconsin Avenue, Bethesda, MD 20892 (Telephone Conference Call).
Contact Person: Alexander Parsadanian, Ph.D., Scientific Review Officer, Scientific Review Branch, National Institute on Aging, National Institutes of Health, Gateway Building 2C/212, 7201 Wisconsin Avenue, Bethesda, MD 20892, (301) 496–9666, *parsadaniana@nia.nih.gov.*

(Catalogue of Federal Domestic Assistance Program Nos. 93.866, Aging Research, National Institutes of Health, HHS)

Dated: January 7, 2020.

Miguelina Perez,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00269 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Institute on Deafness and Other Communication Disorders; Notice of Closed Meetings

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meetings.

The meetings will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: National Institute on Deafness and Other Communication Disorders Special Emphasis Panel; Translational Research Applications Review.

Date: January 21, 2020.

Time: 11:00 a.m. to 1:00 p.m.

Agenda: To review and evaluate grant applications.

Place: National Institutes of Health, Neuroscience Center, 6001 Executive Blvd., Ste 8300, Rockville, MD 20852 (Telephone Conference Call).

Contact Person: Shiguang Yang, DVM, Ph.D., Scientific Review Officer, Division of Extramural Activities, NIDCD, NIH, 6001 Executive Blvd., Room 8349, Bethesda, MD 20892, (301) 496–8683, *yangshi@nidcd.nih.gov*.

This notice is being published less than 15 days prior to the meeting due to the timing limitations imposed by the review and funding cycle.

Name of Committee: National Institute on Deafness and Other Communication Disorders Special Emphasis Panel; Voice, Speech, and Language Translational Review Meeting.

Date: January 23, 2020.

Time: 11:00 a.m. to 1:00 p.m.

Agenda: To review and evaluate grant applications.

Place: National Institutes of Health, Neuroscience Center, 6001 Executive Blvd., Ste, 8300, MSC 9670, Bethesda, MD 20892 (Telephone Conference Call).

Contact Person: Shiguang Yang, DVM, Ph.D., Scientific Review Officer, Division of Extramural Activities, NIDCD, NIH, 6001 Executive Blvd., Room 8349, Bethesda, MD 20892, (301) 496–8683, *yangshi@nidcd.nih.gov*.

This notice is being published less than 15 days prior to the meeting due to the timing limitations imposed by the review and funding cycle.

Any interested person may file written comments with the committee by forwarding the statement to the Contact Person listed on this notice. The statement should include the name, address, telephone number and when applicable, the business or professional affiliation of the interested person.

(Catalogue of Federal Domestic Assistance Program Nos. 93.173, Biological Research Related to Deafness and Communicative Disorders, National Institutes of Health, HHS)

Dated: January 7, 2020.

Miguelina Perez,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00272 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Institute on Deafness and Other Communication Disorders; Notice of Closed Meetings

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meetings.

The meetings will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: Communication Disorders Review Committee.

Date: February 20–21, 2020.

Time: 8:00 a.m. to 5:00 p.m.

Agenda: To review and evaluate grant applications.

Place: Embassy Suites—Chevy Chase Pavilion, 4300 Military Road NW, Washington, DC 20015.

Contact Person: Kausik Ray, Ph.D., Scientific Review Officer, National Institute on Deafness and Other Communication Disorders, National Institute of Health, 6001 Executive Blvd., Rockville, MD 20850, (301) 402–3587, *rayk@nidcd.nih.gov*.

Name of Committee: Communication Disorders Review Committee.

Date: June 11–12, 2020.

Time: 8:00 a.m. to 5:00 p.m.

Agenda: To review and evaluate grant applications.

Place: Embassy Suites—Chevy Chase Pavilion, 4300 Military Road NW, Washington, DC 20015.

Contact Person: Kausik Ray, Ph.D., Scientific Review Officer, National Institute on Deafness and Other Communication Disorders, National Institute of Health, 6001 Executive Blvd., Rockville, MD 20850, (301) 402–3587, *rayk@nidcd.nih.gov*.

Name of Committee: Communication Disorders Review Committee.

Date: October 15–16, 2020.

Time: 8:00 a.m. to 5:00 p.m.

Agenda: To review and evaluate grant applications.

Place: Embassy Suites—Chevy Chase Pavilion, 4300 Military Road NW, Washington, DC 20015.

Contact Person: Kausik Ray, Ph.D., Scientific Review Officer, National Institute on Deafness and Other Communication Disorders, National Institute of Health, 6001 Executive Blvd., Rockville, MD 20850, (301) 402–3587, *rayk@nidcd.nih.gov*

(Catalogue of Federal Domestic Assistance Program Nos. 93.173, Biological Research Related to Deafness and Communicative Disorders, National Institutes of Health, HHS)

Dated: January 7, 2020.

Miguelina Perez,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00271 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

Center for Scientific Review; Notice of Closed Meetings

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of the following meetings.

The meetings will be closed to the public in accordance with the provisions set forth in sections 552b(c)(4) and 552b(c)(6), Title 5 U.S.C., as amended. The grant applications and the discussions could disclose confidential trade secrets or commercial property such as patentable material, and personal information concerning individuals associated with the grant applications, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: Center for Scientific Review Special Emphasis Panel; Special Topics: Vision Imaging, Bioengineering and Low Vision Technology Development.

Date: February 3–4, 2020.

Time: 8:00 a.m. to 12:00 p.m.

Agenda: To review and evaluate grant applications.

Place: Residence Inn Washington, DC Downtown, 1199 Vermont Avenue NW, Washington, DC 20005.

Contact Person: Susan Gillmor, Ph.D., Scientific Review Officer, National Institutes of Health, Center for Scientific Review, 6701 Rockledge Drive, Bethesda, MD 20892, 240–762–3076, *susan.gillmor@nih.gov*.

Name of Committee: Center for Scientific Review Special Emphasis Panel; RFA–NS18–018 Brain Initiative: Biology and Biophysics of Neural Stimulation.

Date: February 4, 2020.

Time: 12:00 p.m. to 2:00 p.m.

Agenda: To review and evaluate grant applications.

Place: Residence Inn Washington, DC Downtown, 1199 Vermont Avenue NW, Washington, DC 20005.

Contact Person: Susan Gillmor, Ph.D., Scientific Review Officer, National Institutes of Health, Center for Scientific Review, 6701 Rockledge Drive, Bethesda, MD 20892, 240–762–3076, *susan.gillmor@nih.gov*.

Name of Committee: Biological Chemistry and Macromolecular Biophysics Integrated Review Group; Macromolecular Structure and Function D Study Section.

Date: February 5, 2020.

Time: 8:00 a.m. to 6:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Residence Inn Bethesda, 7335 Wisconsin Avenue, Bethesda, MD 20814.
Contact Person: James W. Mack, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 4154, MSC 7806, Bethesda, MD 20892, (301) 435–2037, *mackj2@csr.nih.gov*.

Name of Committee: Bioengineering Sciences & Technologies Integrated Review Group; Modeling and Analysis of Biological Systems Study Section.
Date: February 6–7, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Doubletree Hotel Bethesda (Formerly Holiday Inn Select), 8120 Wisconsin Avenue, Bethesda, MD 20814.
Contact Person: Craig Giroux, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 5150, Bethesda, MD 20892, 301–435–2204, *girouxcn@csr.nih.gov*.

Name of Committee: Surgical Sciences, Biomedical Imaging and Bioengineering Integrated Review Group; Clinical Translational Imaging Science Study Section.
Date: February 6–7, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Sir Francis Drake Hotel, 450 Powell Street at Sutter, San Francisco, CA 94102.
Contact Person: Xiang-Ning Li, MD, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 5112, MSC 7854, Bethesda, MD 20892, 301–435–1744, *lixiang@csr.nih.gov*.

Name of Committee: Surgical Sciences, Biomedical Imaging and Bioengineering Integrated Review Group; Imaging Probes and Contrast Agents Study Section.
Date: February 6–7, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Hilton Alexandria Mark Center, 5000 Seminary Road, Alexandria, VA 22311.
Contact Person: Donald Scott Wright, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 5108, MSC 7854, Bethesda, MD 20892, (301) 435–8363, *wrightds@csr.nih.gov*.

Name of Committee: Oncology 2—Translational Clinical Integrated Review Group; Mechanisms of Cancer Therapeutics—1 Study Section.
Date: February 6–7, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Ritz-Carlton Hotel, 1700 Tysons Boulevard, McLean, VA 22102.
Contact Person: Lambratu Rahman Sesay, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 6214, MSC 7804, Bethesda, MD 20892, 301–905–8294, *rahman-sesay@csr.nih.gov*.

Name of Committee: Brain Disorders and Clinical Neuroscience Integrated Review Group; Neural Basis of Psychopathology, Addictions and Sleep Disorders Study Section.
Date: February 6–7, 2020.
Time: 8:00 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Embassy Suites—Chevy Chase Pavilion, 4300 Military Road, NW, Washington, DC 20015.
Contact Person: Brian H Scott, Ph.D., Scientific Review Officer, National Institutes of Health, Center for Scientific Review, 6701 Rockledge Drive, Bethesda, MD 20892, 301–827–7490 *brianscott@mail.nih.gov*.

Name of Committee: Infectious Diseases and Microbiology Integrated Review Group; Pathogenic Eukaryotes Study Section.
Date: February 6–7, 2020.
Time: 8:30 a.m. to 5:00 p.m.
Agenda: To review and evaluate grant applications..
Place: Courtyard by Marriott Long Beach, 500 E 1st Street, Long Beach, CA 90802
Contact Person: Tera Bounds, DVM, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health 6701 Rockledge Drive, Room 3198, MSC 7808, Bethesda, MD 20892, 301–435–2306, *boundst@csr.nih.gov*.

Name of Committee: Population Sciences and Epidemiology Integrated Review Group; Social Sciences and Population Studies A Study Section.
Date: February 6–7, 2020.
Time: 8:30 a.m. to 12:00 p.m.
Agenda: To review and evaluate grant applications.
Place: Warwick Denver, 1776 Grant Street, Denver, CO 80203.
Contact Person: Suzanne Ryan, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 3139, MSC 7770, Bethesda, MD 20892, (301) 435–1712, *ryansj@csr.nih.gov*.

Name of Committee: Population Sciences and Epidemiology Integrated Review Group; Kidney, Nutrition, Obesity and Diabetes Study Section.
Date: February 6–7, 2020.
Time: 8:30 a.m. to 5:30 p.m.
Agenda: To review and evaluate grant applications.
Place: SpringHill Suites San Diego Downtown/Bayfront, 900 Bayfront Ct, San Diego, CA 92101.
Contact Person: Fungai Chanetsa, MPH, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 3135, MSC 7770, Bethesda, MD 20892, 301–408–9436, *fungai.chanetsa@nih.hhs.gov*.

Name of Committee: Digestive, Kidney and Urological Systems Integrated Review Group; Kidney Molecular Biology and Genitourinary Organ Development.
Date: February 6, 2020.
Time: 9:00 a.m. to 6:00 p.m.
Agenda: To review and evaluate grant applications.
Place: National Institutes of Health Rockledge II, 6701 Rockledge Drive, Bethesda, MD 20892 (Virtual Meeting).
Contact Person: Ganesan Ramesh, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 2182, MSC 7818, Bethesda, MD 20892, 301–827–5467, *ganesan.ramesh@nih.gov*.

Name of Committee: Center for Scientific Review Special Emphasis Panel; Molecular and Cellular Endocrinology.
Date: February 6, 2020.
Time: 11:30 a.m. to 12:30 p.m.
Agenda: To review and evaluate grant applications.
Place: Renaissance, Washington, DC Hotel, 999 Ninth Street NW, Washington, DC 20001–4427.
Contact Person: Elaine Sierra-Rivera, Ph.D., Scientific Review Officer, Center for Scientific Review, National Institutes of Health, 6701 Rockledge Drive, Room 6182, MSC 7892, Bethesda, MD 20892, 301–435–2514, *riverase@csr.nih.gov*.

(Catalogue of Federal Domestic Assistance Program Nos. 93.306, Comparative Medicine; 93.333, Clinical Research, 93.306, 93.333, 93.337, 93.393–93.396, 93.837–93.844, 93.846–93.878, 93.892, 93.893, National Institutes of Health, HHS)

Dated: January 7, 2020.

Tyeshia M. Roberson,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–00267 Filed 1–10–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HOMELAND SECURITY

U.S. Customs and Border Protection

[1651–0006]

Agency Information Collection Activities: Application and Approval To Manipulate, Examine, Sample or Transfer Goods

AGENCY: U.S. Customs and Border Protection (CBP), Department of Homeland Security.

ACTION: 60-Day notice and request for comments; extension of an existing collection of information.

SUMMARY: The Department of Homeland Security, U.S. Customs and Border Protection will be submitting the following information collection request to the Office of Management and Budget (OMB) for review and approval in accordance with the Paperwork Reduction Act of 1995 (PRA). The information collection is published in the **Federal Register** to obtain comments from the public and affected agencies. Comments are encouraged and must be submitted no later than March 13, 2020 to be assured of consideration.

ADDRESSES: Written comments and/or suggestions regarding the item(s)

contained in this notice must include the OMB Control Number 1651–0006 in the subject line and the agency name. To avoid duplicate submissions, please use only *one* of the following methods to submit comments:

(1) *Email.* Submit comments to: *CBP_PRA@cbp.dhs.gov.*

(2) *Mail.* Submit written comments to CBP Paperwork Reduction Act Officer, U.S. Customs and Border Protection, Office of Trade, Regulations and Rulings, Economic Impact Analysis Branch, 90 K Street NE, 10th Floor, Washington, DC 20229–1177.

FOR FURTHER INFORMATION CONTACT: Requests for additional PRA information should be directed to Seth Renkema, Chief, Economic Impact Analysis Branch, U.S. Customs and Border Protection, Office of Trade, Regulations and Rulings, 90 K Street NE, 10th Floor, Washington, DC 20229–1177, Telephone number 202–325–0056 or via email *CBP_PRA@cbp.dhs.gov.* Please note that the contact information provided here is solely for questions regarding this notice. Individuals seeking information about other CBP programs should contact the CBP National Customer Service Center at 877–227–5511, (TTY) 1–800–877–8339, or CBP website at *https://www.cbp.gov/.*

SUPPLEMENTARY INFORMATION: CBP invites the general public and other Federal agencies to comment on the proposed and/or continuing information collections pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). This process is conducted in accordance with 5 CFR 1320.8. Written comments and suggestions from the public and affected agencies should address one or more of the following four points: (1) Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (2) the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) suggestions to enhance the quality, utility, and clarity of the information to be collected; and (4) suggestions to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, *e.g.,* permitting electronic submission of responses. The comments that are submitted will be summarized and included in the request for approval. All comments will become a matter of public record.

Overview of This Information Collection

Title: Application and Approval to Manipulate, Examine, Sample or Transfer Goods

OMB Number: 1651–0006.

Form Number: Form 3499.

Abstract: CBP Form 3499, ''*Application and Approval to Manipulate, Examine, Sample or Transfer Goods,*'' is used as an application to perform various operations on merchandise located at a CBP approved bonded facility. This form is filed by importers, consignees, transferees, or owners of merchandise, and is subject to approval by the port director. The data requested on this form identifies the merchandise for which action is being sought and specifies what operation is to be performed. This form may also be approved as a blanket application to manipulate goods for a period of up to one year for a continuous or repetitive manipulation. CBP Form 3499 is provided for by 19 CFR 19.8, 19.11, and 158.43, and is accessible at: *https://www.cbp.gov/newsroom/publications/forms?title=3499&=Apply*

Current Actions: CBP proposes to extend the expiration date of this information collection with no change to the burden hours or to the information collected.

Type of Review: Extension (without change).

Affected Public: Businesses.

Estimated Number of Respondents: 2,519.

Estimated Number of Responses per Respondent: 60.

Estimated Number of Total Annual Responses: 151,140.

Estimated Time per Response: 6 minutes.

Estimated Total Annual Burden Hours: 15,114.

Dated: January 8, 2020.

Seth D. Renkema,

Branch Chief, Economic Impact Analysis Branch, U.S. Customs and Border Protection.

[FR Doc. 2020–00325 Filed 1–10–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF HOMELAND SECURITY

U.S. Customs and Border Protection

[1651–0019]

Agency Information Collection Activities: Vessel Entrance or Clearance Statement

AGENCY: U.S. Customs and Border Protection (CBP), Department of Homeland Security.

ACTION: 60-Day notice and request for comments; extension of an existing collection of information.

SUMMARY: The Department of Homeland Security, U.S. Customs and Border Protection will be submitting the following information collection request to the Office of Management and Budget (OMB) for review and approval in accordance with the Paperwork Reduction Act of 1995 (PRA). The information collection is published in the **Federal Register** to obtain comments from the public and affected agencies. Comments are encouraged and must be submitted (no later than March 13, 2020) to be assured of consideration.

ADDRESSES: Written comments and/or suggestions regarding the item(s) contained in this notice must include the OMB Control Number 1651–0019 in the subject line and the agency name. To avoid duplicate submissions, please use only *one* of the following methods to submit comments:

(1) Email. Submit comments to: *CBP_PRA@cbp.dhs.gov.*

(2) Mail. Submit written comments to CBP Paperwork Reduction Act Officer, U.S. Customs and Border Protection, Office of Trade, Regulations and Rulings, Economic Impact Analysis Branch, 90 K Street NE, 10th Floor, Washington, DC 20229–1177.

FOR FURTHER INFORMATION CONTACT: Requests for additional PRA information should be directed to Seth Renkema, Chief, Economic Impact Analysis Branch, U.S. Customs and Border Protection, Office of Trade, Regulations and Rulings, 90 K Street NE, 10th Floor, Washington, DC 20229–1177, Telephone number 202–325–0056 or via email *CBP_PRA@cbp.dhs.gov.* Please note that the contact information provided here is solely for questions regarding this notice. Individuals seeking information about other CBP programs should contact the CBP National Customer Service Center at 877–227–5511, (TTY) 1–800–877–8339, or CBP website at *https://www.cbp.gov/.*

SUPPLEMENTARY INFORMATION: CBP invites the general public and other

Federal agencies to comment on the proposed and/or continuing information collections pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). This process is conducted in accordance with 5 CFR 1320.8. Written comments and suggestions from the public and affected agencies should address one or more of the following four points: (1) Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (2) the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) suggestions to enhance the quality, utility, and clarity of the information to be collected; and (4) suggestions to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, *e.g.,* permitting electronic submission of responses. The comments that are submitted will be summarized and included in the request for approval. All comments will become a matter of public record.

Overview of This Information Collection

Title: Vessel Entrance or Clearance Statement.

OMB Number: 1651–0019.

Form Number: CBP Form 1300.

Current Actions: CBP proposes to extend the expiration date of this information collection with a decrease to the burden hours due to updated agency estimates. There is no change to the information being collected.

Type of Review: Extension (with change).

Abstract: CBP Form 1300, *Vessel Entrance or Clearance Statement,* is used to collect essential commercial vessel data at time of formal entrance and clearance in U.S. ports. The form allows the master to attest to the truthfulness of all CBP forms associated with the manifest package, and collects information about the vessel, cargo, purpose of entrance, certificate numbers, and expiration for various certificates. It also serves as a record of fees and tonnage tax payments in order to prevent overpayments. CBP Form 1300 was developed through agreement by the United Nations Intergovernmental Maritime Consultative Organization (IMCO) in conjunction with the United States and various other countries. This form is authorized by 19 U.S.C. 1431, 1433, and 1434, and provided for by 19 CFR part 4, and accessible at *http://www.cbp.gov/newsroom/publications/forms?title=1300.*

Affected Public: Businesses.

Estimated Number of Respondents: 2,624.

Estimated Number of Responses per Respondent: 72.

Estimated Total Annual Responses: 188,928.

Estimated Time per Response: 30 minutes.

Estimated Total Annual Burden Hours: 94,464.

Dated: January 8, 2020.

Seth D. Renkema,

Branch Chief, Economic Impact Analysis Branch, U.S. Customs and Border Protection.

[FR Doc. 2020–00323 Filed 1–10–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR–6194–N–01]

Manufactured Home Construction and Safety Standards; Request for Recommended Changes

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Notice.

SUMMARY: Consistent with the National Manufactured Housing Construction and Safety Standards Act of 1974, as amended, this notice invites interested persons to submit proposed changes to update and revise HUD's Manufactured Home Construction and Safety Standards. These proposed changes will be submitted to the Manufactured Housing Consensus Committee (MHCC) for review and consideration as part of its responsibility to provide periodic recommendations to HUD to adopt, revise, and interpret the HUD standards.

DATES: To ensure consideration, the deadline for submitting proposed changes from the public for the 2020–2021 review period is June 30, 2020. Any Proposals received after June 30, 2020will be held until the 2022–2023 review period.

ADDRESS: Proposed changes to the Manufactured Home Construction and Safety Standards are to be submitted using the following URL address: *www.mhcc.homeinnovation.com* or mailed to Home Innovation Research Labs, 400 Prince Georges Blvd., Upper Marlboro, MD 20774, Attention: Kevin Kauffman.

FOR FURTHER INFORMATION CONTACT: Teresa Payne, Administrator and Designated Federal Official (DFO), Office of Manufactured Housing Programs, Department of Housing and Urban Development, 451 7th Street SW, Room 9168, Washington, DC 20410, telephone number 202–708–6423 (this is not a toll-free number). Persons who have difficulty hearing or speaking may access this number via TTY by calling the Federal Relay Service at 800–877–8339 (this is a toll-free number).

SUPPLEMENTARY INFORMATION:

Section 604(a) of the National Manufactured Housing Construction and Safety Standards Act of 1974, as amended by the Manufactured Housing Improvement Act of 2000 (42 U.S.C. 5401 *et seq.*) (the Act) establishes the MHCC. Among other things, the MHCC is responsible for providing periodic recommendations to HUD to adopt, revise, and interpret the manufactured housing construction and safety standards. HUD's Manufactured Home Construction and Safety Standards are codified at 24 CFR part 3280. According to Section 604(a)(4) of the Act, the MHCC is required to consider revisions not less than once during each 2-year period.

Today's notice requests that interested persons provide proposed changes for revising or updating HUD's Manufactured Home Construction and Safety Standards. Consistent with the Act, recommendations are requested that further HUD's efforts to increase the quality, durability, safety and affordability of manufactured homes; facilitate the availability of affordable manufactured homes and increase homeownership for all Americans; and encourage cost-effective and innovative construction techniques for manufactured homes. To permit the MHCC to fully consider the proposed changes, commenters are encouraged to provide at least the following information:

- The specific section of the current Manufactured Home Construction and Safety Standards that require revision or update; or whether the recommendation would require a new standard;
- Specific detail regarding the recommendation including a statement of the problem intended to be corrected or addressed by the recommendation, how the recommendation would resolve or address the problem, and the basis of the recommendation; and
- Information regarding whether the recommendation would result in increased costs to manufacturers or consumers and the value of the benefits derived from HUD's implementation of

the recommendation, should be provided and discussed to the extent feasible.

The Act requires that an administering organization administer the process for the MHCC's development and interpretation of the Federal Standards and Procedural and Enforcement Regulations. The administering organization that has been selected by HUD to administer this process is Home Innovation Research Labs Inc. This Notice requests that proposed revisions to the Federal standards be submitted to the MHCC for consideration through the administering organization, Home Innovation Research Labs. This organization will be responsible for ensuring delivery of all appropriately prepared proposed changes to the MHCC for its review and consideration.

Dated: January 6, 2020.

John L. Garvin,

General Deputy Assistant Secretary of Housing.

[FR Doc. 2020–00320 Filed 1–10–20; 8:45 am]

BILLING CODE 4210–67–P

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[FR–6193–N–01]

Credit Watch Termination Initiative Termination of Direct Endorsement (DE) Approval

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, Department of Housing and Urban Development (HUD).

ACTION: Notice.

SUMMARY: This notice advises of the cause and effect of termination of Direct Endorsement (DE) approval taken by HUD's Federal Housing Administration (FHA) against HUD-approved mortgagees through the FHA Credit Watch Termination Initiative. This notice includes a list of mortgagees that have had their DE Approval terminated.

FOR FURTHER INFORMATION CONTACT: Quality Assurance Division, Office of Housing, Department of Housing and Urban Development, 451 Seventh Street SW, Room B133–P3214, Washington, DC 20410–8000; telephone (202) 708–5997 (this is not a toll-free number). Persons with hearing or speech impairments may access that number through TTY by calling the Federal Relay at (800) 877–8339 (this is a toll-free number).

SUPPLEMENTARY INFORMATION: HUD has the authority to address deficiencies in the performance of lenders' loans as provided in HUD's mortgagee approval regulations at 24 CFR 202.3. On May 17, 1999, HUD published a notice (64 FR 26769) on its procedures for terminating Origination Approval Agreements with FHA lenders and placement of FHA lenders on Credit Watch status (an evaluation period). In the notice, HUD advised that it would publish in the **Federal Register** a list of mortgagees that have had their Approval Agreements terminated. HUD Handbook 4000.1 section V.E.3.a.iii outlines current procedures for terminating Underwriting Authority of Direct Endorsement mortgagees.

Termination of Direct Endorsement Approval: HUD approval of a DE mortgagee authorizes the mortgagee to underwrite single family mortgage loans and submit them to FHA for insurance endorsement. The approval may be terminated on the basis of poor performance of FHA-insured mortgage loans underwritten by the mortgagee. The termination of a mortgagee's DE Approval is separate and apart from any action taken by HUD's Mortgagee Review Board under HUD regulations at 24 CFR part 25.

Cause: HUD regulations permit HUD to terminate the DE Approval of any mortgagee having a default and claim rate for loans endorsed within the preceding 24 months that exceeds 200 percent of the default and claim rate within the geographic area served by a HUD field office, and that exceeds the national default and claim rate.

Effect: Termination of DE Approval precludes the mortgagee from underwriting FHA-insured single-family mortgages within the HUD field office jurisdiction(s) listed in this notice. Mortgagees authorized to hold or service FHA-insured mortgages may continue to do so.

Loans that closed or were approved before the termination became effective may be submitted for insurance endorsement. Approved loans are those already underwritten and approved by a DE underwriter and cases covered by a firm commitment issued by HUD. Cases at earlier stages of processing cannot be submitted for insurance by the terminated mortgagee; however, the cases may be transferred for completion of processing and underwriting to another mortgagee with DE Approval in that geographic area. Mortgagees must continue to pay existing insurance premiums and meet all other obligations associated with insured mortgages.

A terminated mortgagee may apply for reinstatement if their DE Approval in the affected area or areas has been terminated for at least six months and the mortgagee continues to be an approved mortgagee meeting the requirements of 24 CFR 202.5, 202.6, 202.7, 202.10 and 202.12. The mortgagee's application for reinstatement must be in a format prescribed by the Secretary and signed by the mortgagee. In addition, the application must be accompanied by an independent analysis of the terminated office's operations as well as its mortgage production, specifically including the FHA-insured mortgages cited in its termination notice. This independent analysis shall identify the underlying cause for the mortgagee's high default and claim rate. The analysis must be prepared by an independent Certified Public Accountant (CPA) qualified to perform audits under Government Auditing Standards as provided by the Government Accountability Office. The mortgagee must also submit a written corrective action plan to address each of the issues identified in the CPA's report, along with evidence that the plan has been implemented. The application for reinstatement must be submitted through the Lender Electronic Assessment Portal (LEAP). The application must be accompanied by the CPA's report and the corrective action plan.

Action: The following mortgagees have had their DE Approval terminated by HUD:

Mortgagee name	Mortgagee home office address	HUD office jurisdiction	Termination effective date	Homeownership center
CityWorth Mortgage LLC	11781 Lee Jackson Memorial Highway, Fairfax, VA 22033.	Atlanta	12/5/19	Philadelphia.
CityWorth Mortgage LLC	11781 Lee Jackson Memorial Highway, Fairfax, VA 22033.	Greensboro	12/5/19	Philadelphia.
CityWorth Mortgage LLC	11781 Lee Jackson Memorial Highway, Fairfax, VA 22033.	Pittsburgh	12/5/19	Philadelphia.

Mortgagee name	Mortgagee home office address	HUD office jurisdiction	Termination effective date	Homeownership center
CityWorth Mortgage LLC	11781 Lee Jackson Memorial Highway, Fairfax, VA 22033.	Washington	12/5/19	Philadelphia.
The Home Lending Group LLC.	215 Katherine Drive Flowood, MS 39232	Jackson	12/5/19	Atlanta.

Dated: January 6, 2020.

John L. Garvin,

General Deputy Assistant Secretary for Housing.

[FR Doc. 2020–00321 Filed 1–10–20; 8:45 am]

BILLING CODE 4210–67–P

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR–7011–N–62]

30-Day Notice of Proposed Information Collection: Emergency Solutions Grant Data Collection; OMB #2506–0089

AGENCY: Office of the Chief Information Officer, HUD.

ACTION: Notice.

SUMMARY: HUD is seeking approval from the Office of Management and Budget (OMB) for the information collection described below. In accordance with the Paperwork Reduction Act, HUD is requesting comment from all interested parties on the proposed collection of information. The purpose of this notice is to allow for 30 days of public comment.

DATES: *Comments Due Date:* February 12, 2020.

ADDRESSES: Interested persons are invited to submit comments regarding this proposal. Comments should refer to the proposal by name and/or OMB Control Number and should be sent to: HUD Desk Officer, Office of Management and Budget, New Executive Office Building, Washington, DC 20503; fax:202–395–5806, Email: *OIRA Submission@omb.eop.gov*

FOR FURTHER INFORMATION CONTACT: Anna P.Guido, Reports Management Officer, QMAC, Department of Housing and Urban Development, 451 7th Street SW, Washington, DC 20410; email her at *Anna.P.Guido@hud.gov* or telephone 202–402–5535. This is not a toll-free number. Person with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Relay Service at (800) 877–8339. Copies of available documents submitted to OMB may be obtained from Ms. Guido.

SUPPLEMENTARY INFORMATION: This notice informs the public that HUD is seeking approval from OMB for the information collection described in Section A.

The **Federal Register** notice that solicited public comment on the information collection for a period of 60 days was published on October 11, 2019 at 84 FR 54917.

A. Overview of Information Collection

Title of Information Collection: Emergency Solutions Grant Data Collection.

OMB Approval Number: 2506–0089.

Type of Request: Reinstatement of currently approved collection.

Form Number: None.

Description of the need for the information and proposed use: This submission is to request an extension of a currently approved collection for the reporting burden associated with program and recordkeeping requirements that Emergency Solutions Grants (ESG) program recipients will be expected to implement and retain. This submission is limited to the recordkeeping burden under the ESG entitlement program. To see the regulations for the ESG program and applicable supplementary documents, visit the ESG page on the HUD Exchange at *https://www.hudexchange.info/programs/esg/.* The statutory provisions and the implementing interim regulations (also found at 24 CFR 576) that govern the program require these recordkeeping requirements.

Information collection	Number of respondents	Response frequency (average)	Total annual responses	Burden hours per response	Total annual hours	Hourly rate **	Burden cost per instrument
A	B	C	D	E	F		
576.100(b)(2) Emergency Shelter and Street Outreach Cap	360.00	1.00	360.00	1.00	360.00	39.96	14,385.60
576.400(a) Consultation with Continuums of Care	360.00	1.00	360.00	6.00	2,160.00	39.96	86,313.60
576.400(b) Coordination with other Targeted Homeless Services	2,360.00	1.00	2,360.00	8.00	18,880.00	39.96	754,444.80
576.400(c) System and Program Coordination with Mainstream Resources	2,360.00	1.00	2,360.00	16.00	37,760.00	39.96	1,508,889.60
576.400(d) Centralized or Coordinated Assessment	2,000.00	1.00	2,000.00	3.00	6,000.00	39.96	239,760.00
576.400(e) Written Standards for Determining the Amount of Assistance	808.00	1.00	808.00	5.00	4,040.00	39.96	161,438.40
576.400(f) Participation in HMIS	78,000.00	1.00	78,000.00	0.50	39,000.00	39.96	1,558,440.00
576.401(a) Initial Evaluation	50,000.00	1.00	50,000.00	1.00	50,000.00	39.96	1,998,000.00
576.401(b) Recertification	20,000.00	2.00	40,000.00	0.50	20,000.00	39.96	799,200.00
576.401(d) Connection to Mainstream Resources	78,000.00	3.00	234,000.00	0.25	58,500.00	39.96	2,337,660.00
576.401(e) Housing retention plan	50,000.00	1.00	50,000.00	.75	37,500.00	39.96	1,498,500.00
576.402 Terminating Assistance	808.00	1.00	808.00	4.00	3,232.00	39.96	129,150.72
576.403 Habitability review	52,000.00	1.00	52,000.00	0.60	31,200.00	39.96	1,246,752.00
576.405 Homeless Participation	2,360.00	12.00	28,320.00	1.00	28,320.00	39.96	1,131,667.20
576.500 Recordkeeping Requirements	2,360.00	1.00	2,360.00	12.75	30,090.00	39.96	1,202,396.40
576.501(b) Remedial Actions	20.00	1.00	20.00	8.00	160.00	39.96	6,393.60
576.501(c) Recipient Sanctions	360.00	1.00	360.00	12.00	4,320.00	39.96	172,627.20
576.501(c) Subrecipient Response	2,000.00	1.00	2,000.00	8.00	16,000.00	39.96	639,360.00

Information collection	Number of respondents	Response frequency (average)	Total annual responses	Burden hours per response	Total annual hours	Hourly rate **	Burden cost per instrument
A	B	C	D	E	F		
Total	78,000.00		546,116.00		387,522.00		15,485,379.12

B. Solicitation of Public Comment

This notice is soliciting comments from members of the public and affected parties concerning the collection of information described in Section A on the following:

(1) Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;

(2) The accuracy of the agency's estimate of the burden of the proposed collection of information;

(3) Ways to enhance the quality, utility, and clarity of the information to be collected; and

(4) Ways to minimize the burden of the collection of information on those who are to respond; including through the use of appropriate automated collection techniques or other forms of information technology, *e.g.,* permitting electronic submission of responses.

HUD encourages interested parties to submit comment in response to these questions.

C. Authority

Section 3507 of the Paperwork Reduction Act of 1995, 44 U.S.C. Chapter 35.

Dated: December 20, 2019.

Anna P. Guido,

Department Reports Management Officer, Office of the Chief Information Officer.

[FR Doc. 2020–00319 Filed 1–10–20; 8:45 am]

BILLING CODE 4210–67–P

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR–7016–N–05]

60-Day Notice of Proposed Information Collection: Family Unification Program/Family Self-Sufficiency Demonstration Evaluation

AGENCY: Office of the Assistant Secretary for Policy Development and Research, HUD.

ACTION: Notice.

SUMMARY: The U.S. Department of Housing and Urban Development (HUD) is seeking approval from the Office of Management and Budget (OMB) for the information collection described below. In accordance with the Paperwork Reduction Act, HUD is requesting comment from all interested parties on the proposed collection of information. The purpose of this notice is to allow for 60 days of public comment.

DATES: *Comments Due Date:* March 13, 2020.

ADDRESSES: Interested persons are invited to submit comments regarding this proposal. Comments should refer to the proposal by name and/or OMB Control Number and should be sent to: Anna P. Guido, Reports Management Officer, QDAM, Department of Housing and Urban Development, 451 7th Street SW, Room 4176, Washington, DC 20410–5000; telephone 202–402–5534 (this is not a toll-free number) or email at *Anna.P.Guido@hud.gov* for a copy of the proposed forms or other available information. Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Relay Service at (800) 877–8339.

FOR FURTHER INFORMATION CONTACT: Anna P. Guido, Reports Management Officer, QDAM, Department of Housing and Urban Development, 451 7th Street SW, Washington, DC 20410; email Anna P. Guido at *Anna.P.Guido@hud.gov* or telephone 202–402–5535. This is not a toll-free number. Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Relay Service at (800) 877–8339.

Copies of available documents submitted to OMB may be obtained from Ms. Guido.

SUPPLEMENTARY INFORMATION: This notice informs the public that HUD is seeking approval from OMB for the information collection described in Section A.

A. Overview of Information Collection

Title of Information Collection: Family Unification Program/Family Self Sufficiency Demonstration Evaluation.

OMB Approval Number: Pending.

Type of Request: New collection.

Form Number: N/A.

Description of the need for the information and proposed use: The Family Unification Program/Family Self-Sufficiency (FUP/FSS) Demonstration, authorized in HUD's FY 2015 appropriations, was designed to test whether combining FUP and FSS for eligible youth would result in beneficial outcomes. The demonstration program was first announced in January 2016, and a total of 51 PHAs are participating in the demonstration as of 2019. As a part of the demonstration, the time limit on rental assistance was extended to match the maximum allowable five-year FSS contract (at the start of the demonstration, this was an increase from 18 months, although FUP-Youth vouchers were extended to 36 months shortly after the time the demonstration was announced). No funds or additional FUP vouchers were allocated for the demonstration, although certain regulatory requirements were relaxed for participating Public Housing Agencies (PHAs), with the aim of better aligning the existing programs into the new approach. As a result, all participating PHAs already had FUP allocations. Participating PHAs can choose to modify their FSS programs to better meet the needs of youth participants. The most recent FUP awards (FY17 and FY18) require partnership with a local Continuum of Care (CoC), which can increase referrals of eligible youth through coordinated entry.

The main goal of the *FUP/FSS Demonstration Evaluation* is to assess whether the combination of FUP and FSS, along with the extension of time limits, has been an effective approach to improving housing stability and self-sufficiency outcomes for youth aging out of foster care. Related to this is whether participation in the demonstration has provided an avenue for closer and more productive partnerships between PHAs, Public Child Welfare Agencies (PCWAs), and other youth-focused organizations involved. This includes capturing information about how PHAs and their PCWA partners have worked together to implement the demonstration program and the challenges and lessons learned from their experience to date.

Initial take-up rates for the demonstration, as well as non-demonstration FUP-Youth voucher issuances, have both generally been low. Given these low take-up rates, an additional baseline goal will be to assess the extent to which the FUP/FSS Demonstration is being actively implemented across the 51 participating PHAs and why some sites that applied

to the demonstration do not appear to be implementing the program or issuing many FUP-Youth vouchers. To this end, while many of the core evaluation questions are focused on implementation questions and challenges, the study will also necessarily explore why some demonstration sites do not appear to be fully engaged with the program. Finally, a goal of the evaluation is to measure short-term outcomes for participating youth and determine any emerging common attributes among them.

This notice announces HUD's intent to collect information through the following methods: (1) Study investigators (from Urban Institute) will administer an agency-level web-based survey to all PHAs and PCWAs participating in the demonstration. (2) Investigators will conduct one-time telephone interviews with a sample of staff from 10 PHAs in the demonstration to gather more nuanced information than can be collected in the web-based surveys. (3) Investigators will also visit three FUP/FSS demonstration sites to conduct interviews with PHA and PCWA administrators, front-line workers, community service providers, as well as interviews with youth participants. (4) To describe the characteristics of the participating PHAs and FUP/FSS participants and measure short-term outcomes, the study investigators will analyze HUD Public and Indian Housing Information Center (PIC) and Voucher Management System (VMS) administrative data.

Respondents: Youth participants in the FUP/FSS demonstration and staff at the PHAs, PCWAs, CoCs, and other service providers.

Estimated Number of Respondents: Web-based agency survey (PHAs)—51; web-based agency survey (PCWAs)—51; PHA staff interviews—41; PCWA staff interviews—16; community service provider in-person interviews—6; youth participant in-person interviews—18.

Estimated Time per Response: Web-based agency survey (PHAs)—30 minutes; web-based agency survey (PCWAs)—30 minutes; PHA staff interviews—60 minutes; PCWA staff interviews—60 minutes; community service provider in-person interviews—60 minutes; youth participant interviews—60 minutes.

Frequency of Response: Web-based agency survey (PHA)—one time; web-based agency survey (PCWA)—one time; PHA staff interviews—one time; PCWA staff interview—one time; community service provider in-person interviews—one time; youth participant interviews—one time.

Estimated Total Annual Burden Hours: 132.

Estimated Total Annual Cost: $3,995.70.

Respondent's Obligation: Voluntary.

Legal Authority: The survey is conducted under Title 12, United States Code, Section 1701z and Section 3507 of the Paperwork Reduction Act of 1995, 44, U.S.C. 35, as amended.

Information collection	Number of respondents	Frequency of response	Responses per annum	Burden hour per response	Annual burden hours	Hourly cost per response	Cost
Web-based agency survey—PHA	51	1	51	0.5	25.5	[1] $34.46	$878.73
Web-based agency survey—PCWA	51	1	51	0.5	25.5	[1] 34.46	878.73
PHA staff interviews	41	1	41	1	41	[1] 34.46	1,412.86
PCWA staff interviews	16	1	16	1	16	[1] 34.46	551.36
Community service partner in-person interviews	6	1	6	1	6	[2] 23.92	143.52
Youth participant interviews	18	1	18	1	18	[3] 7.25	130.50
Total			183		132		3,995.70

B. Solicitation of Public Comment

This notice is soliciting comments from members of the public and affected parties concerning the collection of information described in Section A on the following:

(1) Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;

(2) The accuracy of the agency's estimate of the burden of the proposed collection of information;

(3) Ways to enhance the quality, utility, and clarity of the information to be collected; and

(4) Ways to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated collection techniques or other forms of information technology, *e.g.,* permitting electronic submission of responses.

HUD encourages interested parties to submit comment in response to these questions.

C. Authority

Section 3507 of the Paperwork Reduction Act of 1995, 44 U.S.C. Chapter 35.

Dated: December 23, 2019.

Seth D. Appleton,

Assistant Secretary for Policy Development and Research.

[FR Doc. 2020–00318 Filed 1–10–20; 8:45 am]

BILLING CODE 4210–67–P

[1] "Occupational Employment Statistics: Occupational Employment and Wages, May 2018—Social and Community Service Managers," Bureau of Labor Statistics, accessed December 6th, 2019, *https://www.bls.gov/oes/current/oes119151.htm.*

[2] "Occupational Employment Statistics: Occupational Employment and Wages, May 2018—Child, Family and Social Workers," Bureau of Labor Statistics, accessed December 6th, 2019, *https://www.bls.gov/oes/current/oes211021.htm.*

[3] For youth interviews, we assume an hourly wage of $7.25, the federal minimum wage.

INTERNATIONAL TRADE COMMISSION

[USITC SE–20–002]

Sunshine Act Meetings

Agency Holding the Meeting: United States International Trade Commission.

TIME AND DATE: January 31, 2020 at 11:00 a.m.

PLACE: Room 101, 500 E Street SW, Washington, DC 20436, Telephone: (202) 205–2000.

STATUS: Open to the public.

MATTERS TO BE CONSIDERED:

1. *Agendas for future meetings:* None.
2. Minutes.
3. Ratification List.
4. Vote on Inv. No. 731–TA–1465 (Final)(4th Tier Cigarettes from Korea). The Commission is currently scheduled to complete and file its determination on February 3, 2020; views of the Commission are currently scheduled to be completed and filed on February 10, 2020.
5. Vote on Inv. Nos. 701–TA–632–635 and 731–TA–1466–1468 (Preliminary) (Fluid End Blocks from China,

Germany, India, and Italy). The Commission is currently scheduled to complete and file its determinations on February 3, 2020; views of the Commission are currently scheduled to be completed and filed on February 10, 2020.

6. *Outstanding action jackets:* None.

CONTACT PERSON FOR MORE INFORMATION: William Bishop, Supervisory Hearings and Information Officer, 202–205–2595.

The Commission is holding the meeting under the Government in the Sunshine Act, 5 U.S.C. 552(b). In accordance with Commission policy, subject matter listed above, not disposed of at the scheduled meeting, may be carried over to the agenda of the following meeting.

By order of the Commission:

Issued: January 7, 2020.

William Bishop,

Supervisory Hearings and Information Officer.

[FR Doc. 2020–00391 Filed 1–9–20; 4:15 pm]

BILLING CODE 7020–02–P

DEPARTMENT OF JUSTICE

Notice of Lodging of Proposed Consent Decree Under The Clean Air Act

On December 3, 2019, the Department of Justice lodged a proposed Consent Decree with the United States District Court for the Eastern District of Pennsylvania in the lawsuit entitled *United States, et al.* v. *Lehigh Cement Company LLC and Lehigh White Cement Company, LLC,* Civil Action No. 5:19–cv–05688.

In a Complaint that was filed simultaneously with the Consent Decree, the United States and seven states and state or local agencies seek injunctive relief against Lehigh Cement Company LLC (''Lehigh'') and Lehigh White Cement Company, LLC (''Lehigh White'') and penalties against Lehigh, pursuant to Sections 113(b) and 167 of the Clean Air Act (''the Act''), 42 U.S.C. 7413(b) and 7477, for alleged violations of the Prevention of Significant Deterioration provisions of the Act, 42 U.S.C. 7470–7492; the nonattainment New Source Review provisions of the Act, 42 U.S.C. 7501–7515; the federally-approved and enforceable state implementation plans, which incorporate and/or implement the above listed requirements; and corresponding state laws. The Complaint alleges claims at one or more of eleven Portland cement facilities located in eight states owned or operated by Lehigh or Lehigh White. The states and state or local agencies that have joined the Complaint and are signatories to the Consent Decree consist of Indiana, Iowa, Maryland, New York, the Pennsylvania Department of Environmental Protection, the Jefferson County Board of Health (Alabama), and the Bay Area Air Quality Management District (California).

The Consent Decree would require installation of emissions control technology for nitrogen oxides (NO_X) and sulfur dioxide (SO_2), emissions monitoring systems, and specified NO_X and SO_2 emission limits (except that the emission limit for SO_2 at the Cupertino, CA facility would be established through a testing program). The Decree would also require Lehigh to pay a civil penalty of $1.3 million, and perform a mitigation project involving upgrading two off-road vehicle engines at an estimated cost of $650,000, which is expected to reduce smog-forming NO_X by approximately 25 tons per year.

Notice of the lodging of the proposed Consent Decree was originally published in the **Federal Register** on December 11, 2019. *See* 84 FR 67758 (Dec. 11, 2019). The publication of the original notice opened a 30-day period for public comment on the proposed Consent Decree that was scheduled to end on January 10, 2020. The publication of the current notice extends the period for public comment on the Consent Decree to February 10, 2020.

Comments should be addressed to the Assistant Attorney General, Environment and Natural Resources Division, and should refer to *United States, et al.* v. *Lehigh Cement Company LLC and Lehigh White Cement Company, LLC,* D.J. Ref. No. 90–5–2–1–08531/1. All comments must be submitted no later February 10, 2020. Comments may be submitted either by email or by mail:

To submit comments:	*Send them to:*
By e-mail	*pubcomment-ees.enrd@usdoj.gov.*
By mail	Assistant Attorney General, U.S. DOJ—ENRD, P.O. Box 7611, Washington, DC 20044–7611.

During the public comment period, the Consent Decree may be examined and downloaded at this Justice Department website: *http://www.justice.gov/enrd/consent-decrees.*

We will provide a paper copy of the Consent Decree upon written request and payment of reproduction costs. Please mail your request and payment to: Consent Decree Library, U.S. DOJ—ENRD, P.O. Box 7611, Washington, DC 20044–7611.

Please enclose a check or money order for $26.00 (25 cents per page reproduction cost) payable to the United States Treasury.

Randall M. Stone,

Acting Assistant Section Chief, Environmental Enforcement Section, Environment and Natural Resources Division.

[FR Doc. 2020–00293 Filed 1–10–20; 8:45 am]

BILLING CODE 4410–15–P

DEPARTMENT OF JUSTICE

Notice of Lodging of Proposed Consent Decree Under the Clean Air Act

On January 7, 2020, the Department of Justice lodged a proposed Consent Decree with the District Court of the Southern District of New York in a lawsuit entitled *United States* v. *Dover Greens, LLC,* Civil Action No. 20–124.

In this action the United States seeks, as provided under the Clean Air Act (''CAA'') and EPA's National Emissions Standards for Asbestos (''Asbestos NESHAP''), civil penalties and injunctive relief from Dover Greens in connection with its renovation of the former Harlem Valley Psychiatric Center in Wingdale, New York. The proposed Consent Decree resolves the United States' claims and requires Dover Greens to pay $575,000 and imposes injunctive relief.

The publication of this notice opens the public comment on the proposed Consent Decree. Comments should be addressed to the Assistant Attorney General, Environment and Natural Resources Division, and should refer to *United States* v. *Dover Greens, LLC,* Civil Action No. 20–124, D.J. Ref. 90–5–2–11427. All comments must be submitted no later than 30 days after the publication date of this notice. Comments may be submitted either by email or by mail:

To submit comments:	Send them to:
By email	*pubcomment-ees.enrd@usdoj.gov.*
By mail	Assistant Attorney General, U.S. DOJ—ENRD, P.O. Box 7611, Washington, DC 20044–7611.

During the public comment period, the Consent Decree may be examined and downloaded at this Justice Department website: *http://www.usdoj.gov/enrd/Consent_Decrees.html.* We will provide a paper copy of the Consent Decree upon

written request and payment of reproduction costs. Please email your request and payment to: Consent Decree Library, U.S. DOJ–ENRD, P.O. Box 7611, Washington, DC 20044–7611.

Please enclose a check or money order for $128.50 (25 cents per page reproduction cost) payable to the United States Treasury.

Henry Friedman,

Assistant Section Chief, Environmental Enforcement Section, Environment and Natural Resources Division.

[FR Doc. 2020–00265 Filed 1–10–20; 8:45 am]

BILLING CODE 4410–15–P

OFFICE OF MANAGEMENT AND BUDGET

Request for Comments on a Draft Memorandum to the Heads of Executive Departments and Agencies, "Guidance for Regulation of Artificial Intelligence Applications"

AGENCY: Executive Office of the President, Office of Management and Budget.

ACTION: Notice of availability and request for comments.

SUMMARY: The Office of Management and Budget (OMB) requests comments on a draft Memorandum that provides guidance to all Federal agencies to inform the development of regulatory and non-regulatory approaches regarding technologies and industrial sectors that are empowered or enabled by artificial intelligence (AI) and consider ways to reduce barriers to the development and adoption of AI technologies. OMB guidance on these matters seeks to support the U.S. approach to free-market capitalism, federalism, and good regulatory practices (GRPs). The draft Memorandum calls on agencies, when considering regulations or policies related to AI applications, to promote advancements in technology and innovation, while protecting American technology, economic and national security, privacy, civil liberties, and other American values, including the principles of freedom, human rights, the rule of law, and respect for intellectual property. The draft Memorandum is available at *https://www.whitehouse.gov/wp-content/uploads/2020/01/Draft-OMB-Memo-on-Regulation-of-AI-1-7-19.pdf.*

DATES: Comments are requested on the draft Memorandum no later than March 13, 2020.

ADDRESSES: All comments should be submitted via *http://www.regulations.gov.* Please submit comments only and include your name, company name (if any), and cite ''Guidance for Regulation of Artificial Intelligence Applications'' in all correspondence. All comments received will be posted, without change or redaction, to *www.regulations.gov,* so commenters should not include information they do not wish to be posted (*e.g.,* personal or confidential business information).

FOR FURTHER INFORMATION CONTACT: Alexander Hunt, Office of Management and Budget, Office of Information and Regulatory Affairs, at *ahunt@omb.eop.gov.*

SUPPLEMENTARY INFORMATION: Executive Order 13859, ''Maintaining American Leadership in Artificial Intelligence,'' which was issued on February 11, 2019, requires the Director of OMB, in coordination with the Director of the Office of Science and Technology Policy, the Director of the Domestic Policy Council, and the Director of the National Economic Council, to issue a memorandum that provides guidance to all Federal agencies to inform the development of regulatory and non-regulatory approaches regarding technologies and industrial sectors that are empowered or enabled by AI and consider ways to reduce barriers to the development and adoption of AI technologies.

Dominic J. Mancini,

Acting Administrator, Office of Information and Regulatory Affairs.

[FR Doc. 2020–00261 Filed 1–10–20; 8:45 am]

BILLING CODE 3110–01–P

NATIONAL SCIENCE FOUNDATION

RIN 3145–AA58

Notice on Penalty Inflation Adjustments for Civil Monetary Penalties

AGENCY: National Science Foundation.

ACTION: Notice announcing updated penalty inflation adjustments for civil monetary penalties for 2020.

SUMMARY: The National Science Foundation (NSF or Foundation) is providing notice of its adjusted maximum civil monetary penalties, effective January 15, 2020. These adjustments are required by the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (the 2015 Act).

FOR FURTHER INFORMATION CONTACT: Bijan Gilanshah, Assistant General Counsel, Office of the General Counsel, National Science Foundation, 2415 Eisenhower Avenue, Alexandria, VA 22314. Telephone: 703–292–5055.

SUPPLEMENTARY INFORMATION: On June 27, 2016 (81 FR 41451), NSF published an interim final rule amending its regulations to adjust, for inflation, the maximum civil monetary penalties that may be imposed for violations of the Antarctic Conservation Act of 1978 (ACA), as amended, 16 U.S.C. 2401 *et seq.,* and the Program Fraud Civil Remedies Act of 1986 (PFCRA), 31 U.S.C. 3801, *et seq.* These adjustments are required by the 2015 Act. The 2015 Act also requires agencies to make subsequent annual adjustments for inflation. Pursuant to OMB guidance dated December 16, 2019, the cost-of-living adjustment multiplier for 2020 is 1.01764. Accordingly, the 2020 annual inflation adjustments for the maximum penalties under the ACA are $17,583 ($17,278 × 1.01764) for violations and $29,755 ($29,239 × 1.01764) for knowing violations of the ACA. Finally, the 2020 annual inflation adjustment for the maximum penalty for violations under PFCRA is $11,665 ($11,463 × 1.01764).

Dated: January 6, 2020.

Suzanne Plimpton,

Reports Clearance Officer, National Science Foundation.

[FR Doc. 2020–00149 Filed 1–10–20; 8:45 am]

BILLING CODE 7555–01–P

NUCLEAR REGULATORY COMMISSION

[NRC–2017–0151]

Information Collection: Domestic Licensing of Production and Utilization Facilities

AGENCY: Nuclear Regulatory Commission.

ACTION: Revision of existing information collection; request for comment.

SUMMARY: The U.S. Nuclear Regulatory Commission (NRC) invites public comment on the revision of an existing collection of information. The information collection is entitled, Domestic Licensing of Production and Utilization Facilities

DATES: Submit comments by March 13, 2020. Comments received after this date will be considered if it is practical to do so, but the Commission is able to ensure consideration only for comments received on or before this date.

ADDRESSES: You may submit comments by any of the following methods:

- *Federal Rulemaking Website:* Go to *https://www.regulations.gov* and search

for Docket ID NRC–2018–0215. Address questions about NRC docket IDs in *Regulations.gov* to Jennifer Borges; telephone: 301–287–9127; email: *Jennifer.Borges@nrc.gov.* For technical questions, contact the individuals listed in the **FOR FURTHER INFORMATION CONTACT** section of this document.

• *Mail comments to:* David Cullison, Office of the Chief Information Officer, Mail Stop: T6–A10M, U.S. Nuclear Regulatory Commission, Washington, DC 20555–0001.

For additional direction on obtaining information and submitting comments, see ''Obtaining Information and Submitting Comments'' in the **SUPPLEMENTARY INFORMATION** section of this document.

FOR FURTHER INFORMATION CONTACT: David Cullison, Office of the Chief Information Officer, U.S. Nuclear Regulatory Commission, Washington, DC 20555–0001; telephone: 301–415–2084; email: *INFOCOLLECTS.Resource@NRC.GOV.*

SUPPLEMENTARY INFORMATION:

I. Obtaining Information and Submitting Comments

A. Obtaining Information

Please refer to Docket ID NRC–2017–0151 when contacting the NRC about the availability of information for this action. You may obtain publicly-available information related to this action by any of the following methods:

• *Federal Rulemaking Website:* Go to *https://www.regulations.gov* and search for Docket ID NRC–2018–0215.

• *NRC's Agencywide Documents Access and Management System (ADAMS):* You may obtain publicly available documents online in the ADAMS Public Document collection at *https://www.nrc.gov/reading-rm/adams.html.* To begin the search, select ''Begin Web-based ADAMS Search.'' For problems with ADAMS, contact the NRC's Public Document Room (PDR) reference staff at 1–800–397–4209, 301–415–4737, or by email to *pdr.resource@nrc.gov.* The supporting statement is available in ADAMS under Accession No. ML19184A634.

• *NRC's PDR:* You may examine and purchase copies of public documents at the NRC's PDR, Room O1–F21, One White Flint North, 11555 Rockville Pike, Rockville, Maryland 20852.

• *NRC's Clearance Officer:* A copy of the collection of information and related instructions may be obtained without charge by contacting NRC's Clearance Officer, David Cullison, Office of the Chief Information Officer, U.S. Nuclear Regulatory Commission, Washington, DC 20555–0001; telephone: 301–415–2084; email: *INFOCOLLECTS.Resource@NRC.GOV.*

B. Submitting Comments

Please include Docket ID NRC–2017–0151 in the subject line of your comment submission, in order to ensure that the NRC is able to make your comment submission available to the public in this docket.

The NRC cautions you not to include identifying or contact information in comment submissions that you do not want to be publicly disclosed in your comment submission. The NRC will post all comment submissions at *https://www.regulations.gov* as well as enter the comment submissions into ADAMS, and the NRC does not routinely edit comment submissions to remove identifying or contact information.

If you are requesting or aggregating comments from other persons for submission to the NRC, then you should inform those persons not to include identifying or contact information that they do not want to be publicly disclosed in their comment submission. Your request should state that the NRC does not routinely edit comment submissions to remove such information before making the comment submissions available to the public or entering the comment into ADAMS.

II. Background

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. chapter 35), the NRC is requesting public comment on its intention to request the OMB's approval for the information collection summarized below.

1. *The title of the information collection:* Appendix H to part 50 of title 10 of the *Code of Federal Regulations* (10 CFR), ''Domestic Licensing of Production And Utilization Facilities.''

2. *OMB approval number:* 3150–0011.

3. *Type of submission:* Revision.

4. *The form number, if applicable:* Not applicable.

5. *How often the collection is required or requested:* On occasion.

6. *Who will be required or asked to respond:* Holders of an operating license for commercial light-water power reactors.

7. *The estimated number of annual responses:* A reduction of 1 response. The total number of responses for the part 50 information collection will be reduced from 43,678 to 43,677.

8. *The estimated number of annual respondents:* There will be a reduction of 1 respondent submitting an extension request; however, the total number of respondents to the 10 CFR part 50 information collection remains unchanged.

9. *The estimated number of hours needed annually to comply with the information collection requirement or request:* A reduction of 78 hours of reporting burden. The total burden for the part 50 information collection will be reduced from 3,731,355 to 3,731,277 hours.

10. *Abstract:* The NRC intends to publish a Direct Final Rule amending the information collection requirements in appendix H to 10 CFR part 50 related to the reactor vessel material surveillance program reporting requirements. The requirements for a reactor vessel material surveillance program are specified in appendix H to 10 CFR part 50. Appendix H to 10 CFR part 50 requires light-water nuclear power reactor licensees to implement a reactor vessel material surveillance program when it cannot be shown that the end of design life neutron fluence for the reactor vessel is below certain criteria. This program monitors changes in the fracture toughness properties of the reactor vessel materials adjacent to the reactor core. This is done by testing of irradiated material specimens that are in surveillance capsules in the reactor vessel for changes in material fracture toughness. The test results are used to assesses the integrity of the reactor vessel.

Licensees are required to submit a summary technical report to the NRC within one year of the date of the surveillance capsule was withdrawn from the reactor vessel unless an extension is granted by the Director, Office of Nuclear Reactor Regulation. The report will contain the data required by ASTM E 185, and the results of all fracture toughness tests conducted on the beltline materials in the irradiated and unirradiated conditions. At that time this requirement was adopted (48 FR 24008; July 26, 1983), there was still a limited amount of data from irradiated materials from which to estimate embrittlement trends of reactor vessels at nuclear power plants; thus, making it crucial for timely reporting of test results.

Some licensees have found it challenging to meet this one-year requirement due to the time needed for coordination among the multiple licensees participating in the program. Because a significant number of test specimens have been analyzed since 1983, resulting in an extensive understanding of embrittlement mechanisms, there is no longer a need for submitting a report within one year. As a result, the NRC determined that the

reporting requirement in appendix H to 10 CFR part 50 could be revised.

This Direct Final Rule will extend the reporting period from 1 year to 18 months and reduce the need for licensees to prepare and submit extension requests and the NRC resources to review the requests.

III. Specific Requests for Comments

The NRC is seeking comments that address the following questions:

1. Is the proposed collection of information necessary for the NRC to properly perform its functions? Does the information have practical utility?
2. Is the estimate of the burden of the information collection accurate?
3. Is there a way to enhance the quality, utility, and clarity of the information to be collected?
4. How can the burden of the information collection on respondents be minimized, including the use of automated collection techniques or other forms of information technology?

Dated at Rockville, Maryland, this 8th day of January 2020.

For the Nuclear Regulatory Commission.

David C. Cullison,

NRC Clearance Officer, Office of the Chief Information Officer.

[FR Doc. 2020–00284 Filed 1–10–20; 8:45 am]

BILLING CODE 7590–01–P

NUCLEAR REGULATORY COMMISSION

[Docket No. 50–293; NRC–2019–0245]

Holtec Pilgrim, LLC; Holtec Decommissioning International, LLC; Pilgrim Nuclear Power Station

AGENCY: Nuclear Regulatory Commission.

ACTION: Exemption; issuance.

SUMMARY: The U.S. Nuclear Regulatory Commission (NRC) has issued an exemption in response to a request from the licensee that would permit Holtec Pilgrim, LLC and Holtec Decommissioning International, LLC to reduce the required level of primary offsite liability insurance from $450 million to $100 million and to eliminate the requirement to carry secondary financial protection for Pilgrim Nuclear Power Station.

DATES: The exemption was issued on January 6, 2020.

ADDRESSES: Please refer to Docket ID NRC–2019–0245 when contacting the NRC about the availability of information regarding this document. You may obtain publicly-available information related to this document using any of the following methods:

- *Federal Rulemaking Website:* Go to *https://www.regulations.gov* and search for Docket ID NRC–2019–0245. Address questions about NRC docket IDs in *Regulations.gov* to Jennifer Borges; telephone: 301–287–9127; email: *Jennifer.Borges@nrc.gov.* For technical questions, contact the individual listed in the **FOR FURTHER INFORMATION CONTACT** section of this document.
- *NRC's Agencywide Documents Access and Management System (ADAMS):* You may obtain publicly-available documents online in the ADAMS Public Documents collection at *https://www.nrc.gov/reading-rm/adams.html.* To begin the search, select ''Begin Web-based ADAMS Search.'' For problems with ADAMS, please contact the NRC's Public Document Room (PDR) reference staff at 1–800–397–4209, 301–415–4737, or by email to *pdr.resource@nrc.gov.* The ADAMS accession number for each document referenced (if it is available in ADAMS) is provided the first time that it is mentioned in this document.
- *NRC's PDR:* You may examine and purchase copies of public documents at the NRC's PDR, Room O1–F21, One White Flint North, 11555 Rockville Pike, Rockville, Maryland 20852.

FOR FURTHER INFORMATION CONTACT: Scott Wall, Office of Nuclear Reactor Regulation, U.S. Nuclear Regulatory Commission, Washington DC 20555–0001; telephone: 301–415–2855, email: *Scott.Wall@nrc.gov.*

SUPPLEMENTARY INFORMATION: The text of the exemption is attached.

Dated at Rockville, Maryland, this 7th day of January 2020.

For the Nuclear Regulatory Commission.

Scott P. Wall,

Senior Project Manager, Plant Licensing Branch III, Division of Operating Reactor Licensing, Office of Nuclear Reactor Regulation.

Attachment—Exemption

NUCLEAR REGULATORY COMMISSION

Docket No. 50–293

Holtec Pilgrim, LLC

Holtec Decommissioning International, LLC

Pilgrim Nuclear Power Station

Exemption

I. Background

By letter dated November 10, 2015 (Agencywide Documents Access and Management System (ADAMS) Accession No. ML15328A053), Entergy Nuclear Operations, Inc. (ENOI) certified to the U.S. Nuclear Regulatory Commission (NRC) that it planned to permanently cease power operations at Pilgrim Nuclear Power Station (Pilgrim) no later than June 1, 2019. On May 31, 2019, ENOI permanently ceased power operations at Pilgrim. By letter dated June 10, 2019 (ADAMS Accession No. ML19161A033), ENOI certified to the NRC that the fuel was permanently removed from the Pilgrim reactor vessel and placed in the spent fuel pool (SFP) on June 9, 2019. Accordingly, pursuant to Title 10 of the Code of Federal Regulations (10 CFR) Section 50.82(a)(2), the Pilgrim renewed facility operating license no longer authorizes operation of the reactor or emplacement or retention of fuel in the reactor vessel. The facility is still authorized to possess and store irradiated (*i.e.,* spent) nuclear fuel. Spent fuel is currently stored onsite at the Pilgrim facility in the SFP and in a dry cask independent spent fuel storage installation (ISFSI).

II. Request/Action

By letter dated March 25, 2019 (ADAMS Accession No. ML19088A127), as supplemented by letter dated July 30, 2019 (ADAMS Accession No. ML19211B509), ENOI requested an exemption from 10 CFR 140.11(a)(4) concerning offsite primary and secondary liability insurance. The exemption from 10 CFR 140.11(a)(4) would permit the licensee to reduce the required level of primary offsite liability insurance from $450 million to $100 million and to eliminate the requirement to carry secondary financial protection for Pilgrim.

By letter dated November 16, 2018 (ADAMS Accession No. ML18320A031), ENOI, on behalf of itself and Entergy Nuclear Generation Company (ENGC) (to be known as Holtec Pilgrim, LLC), Holtec International (Holtec), and Holtec Decommissioning International, LLC (HDI, the licensee) (together, Applicants), requested that the NRC consent to: (1) The indirect transfer of control of Renewed Facility Operating License No. DPR–35 for Pilgrim, as well as the general license for the Pilgrim ISFSI (together, the Licenses), to Holtec; and (2) the direct transfer of ENOI's operating authority (*i.e.,* its authority to conduct licensed activities at Pilgrim) to HDI. In addition, the Applicants requested that the NRC approve a conforming administrative amendment to the Licenses to reflect the proposed direct transfer of the Licenses from ENOI to HDI; a planned name change for ENGC from ENGC to Holtec Pilgrim, LLC; and deletion of certain license conditions to reflect satisfaction and termination of all ENGC obligations after the license transfer and equity sale.

By Order dated August 22, 2019 (ADAMS Accession No. ML19170A265), the NRC staff approved the direct and indirect transfers requested in the November 16, 2018 application. Additionally, on August 22, 2019, HDI informed the NRC (ADAMS Accession No. ML19234A357) that:

HDI will assume responsibility for all ongoing NRC regulatory actions and reviews currently underway for Pilgrim Nuclear Power Station. HDI respectfully requests NRC continuation of these regulatory actions and reviews.

On August 26, 2019, ENOI informed the NRC that the license transfer transaction closed on August 26, 2019 (ADAMS Accession No. ML19239A037). On August 27, 2019 (ADAMS Accession No. ML19235A050), the NRC staff issued Amendment No. 249 to reflect the license transfer. Accordingly, HDI is now the licensee for decommissioning operations at Pilgrim.

The regulation at 10 CFR 140.11(a)(4) requires each licensee to have and maintain primary financial protection in an amount of $450 million. In addition, the licensee is required to participate in an industry retrospective rating plan (secondary financial protection) that commits each licensee to pay into an insurance pool to be used for damages that may exceed primary insurance coverage. Participation in the industry retrospective rating plan will subject the licensee to deferred premium charges up to a maximum total deferred premium of $131,056,000 with respect to any nuclear incident at any operating nuclear power plant and up to a maximum annual deferred premium of $20,496,000 per incident.

Many of the accident scenarios postulated in the updated safety analysis reports for operating power reactors involve failures or malfunctions of systems, which could affect the fuel in the reactor core and, in the most severe postulated accidents, would involve the release of large quantities of fission products. With the permanent cessation of power operations at Pilgrim and the permanent removal of the fuel from the reactor vessel, many accidents are no longer possible. Similarly, the associated risk of offsite liability damages that would require insurance or indemnification is commensurately lower for permanently shut down and defueled plants. Therefore, the licensee requested an exemption from 10 CFR 140.11(a)(4) to permit a reduction in primary offsite liability insurance and to withdraw from participation in the industry retrospective rating plan.

III. Discussion

Pursuant to 10 CFR 140.8, ''Specific exemptions,'' the Commission may, upon application of any interested person or upon its own initiative, grant such exemptions from the requirements of the regulations in 10 CFR part 140 when the exemptions are authorized by law and are otherwise in the public interest. The NRC staff has reviewed the licensee's request for an exemption from 10 CFR 140.11(a)(4) and has concluded that the requested exemption is authorized by law and is otherwise in the public interest.

The Price Anderson Act of 1957 (PAA) requires that nuclear power reactor licensees have insurance to compensate the public for damages arising from a nuclear incident. Specifically, the PAA requires licensees of facilities with a ''rated capacity of 100,000 electrical kilowatts or more'' to maintain the maximum amount of primary offsite liability insurance commercially available (currently $450 million) and a specified amount of secondary insurance coverage (currently up to $131,056,000 per reactor). In the event of an accident causing offsite damages in excess of $450 million, each licensee would be assessed a prorated share of the excess damages, up to $131,056,000 per reactor, for a total of approximately $13 billion per nuclear incident. The NRC's regulations at 10 CFR 140.11(a)(4) implement these PAA insurance requirements and set forth the amount of primary and secondary insurance each power reactor licensee must have.

As noted above, the PAA requirements with respect to primary and secondary insurance and the implementing regulations at 10 CFR 140.11(a)(4) apply to licensees of facilities with a ''rated capacity of 100,000 electrical kilowatts or more.'' In accordance with 10 CFR 50.82(a)(2), the license for a power reactor no longer authorizes operation of the reactor or emplacement or retention of fuel into the reactor vessel upon the docketing of the certifications for permanent cessation of operations and permanent removal of fuel from the reactor vessel. Therefore, the reactor cannot be used to generate power.

Accordingly, a reactor that is undergoing decommissioning has no ''rated capacity.'' Thus, the NRC may take the reactor licensee out of the category of reactor licensees that are required to maintain the maximum available insurance and to participate in the secondary retrospective insurance pool.

The financial protection limits of 10 CFR 140.11(a)(4) were established to require a licensee to maintain sufficient insurance, as specified under the PAA, to satisfy liability claims by members of the public for personal injury, property damage, and the legal cost associated with lawsuits as the result of a nuclear accident at an operating reactor with a rated capacity of 100,000 kilowatts electric or greater. Thus, the insurance levels established by this regulation, as required by the PAA, were associated with the risks and potential consequences of an accident at an operating reactor with a rated capacity of 100,000 kilowatts electric or greater.

The legal and associated technical basis for granting exemptions from 10 CFR part 140 is set forth in SECY–93–127, ''Financial Protection Required of Licensees of Large Nuclear Power Plants During Decommissioning,'' dated May 10, 1993 (ADAMS Accession No. ML12257A628). The legal analysis underlying SECY–93–127 concluded that, upon a technical finding that lesser potential hazards exist after permanent cessation of power operations (and the reactor having no ''rated capacity''), the Commission has the discretion under the PAA to reduce the amount of insurance required of a licensee undergoing decommissioning.

As a technical matter, the fact that a reactor has permanently ceased power operations is not itself determinative as to whether a licensee may cease providing the offsite liability coverage required by the PAA and 10 CFR 140.11(a)(4). In light of the presence of freshly discharged irradiated fuel in the SFP at a recently shut down reactor, the potential for an offsite radiological release from a zirconium fire with consequences comparable in some respects to an operating reactor accident remains. That risk is very low at the time of reactor shutdown because of design provisions that prevent a significant reduction in coolant inventory in the SFP under normal and accident conditions and becomes no longer credible once the continual reduction in decay heat provides ample time to restore coolant inventory and permits air cooling in a drained SFP. After that time, the probability of a large offsite radiological release from a zirconium fire is negligible for permanently shutdown reactors, but the SFP is still operational and an inventory of radioactive materials still exists onsite. Therefore, an evaluation of the potential for offsite damage is necessary to determine the appropriate level of offsite insurance post shutdown, in accordance with the Commission's discretionary authority under the PAA

to establish an appropriate level of required financial protection for such permanently shutdown facilities.

The NRC staff has conducted an evaluation and concluded that, aside from the handling, storage, and transportation of spent fuel and radioactive materials for a permanently shutdown and defueled reactor, no reasonably conceivable potential accident exists that could cause significant offsite damage. During normal power reactor operations, the forced flow of water through the reactor coolant system (RCS) removes heat generated by the reactor. The RCS transfers this heat away from the reactor core by converting reactor feedwater to steam, which then flows to the main turbine generator to produce electricity. Most of the accident scenarios postulated for operating power reactors involve failures or malfunctions of systems that could affect the fuel in the reactor core, which in the most severe postulated accidents would involve the release of large quantities of fission products. With the permanent cessation of reactor operations at Pilgrim and the permanent removal of the fuel from the reactor core, such accidents are no longer possible. The reactor, RCS, and supporting systems no longer operate and have no function related to the storage of the irradiated fuel. Therefore, postulated accidents involving failure or malfunction of the reactor, RCS, or supporting systems are no longer applicable.

During reactor decommissioning, the principal radiological risks are associated with the storage of spent fuel onsite. On a case-by-case basis, licensees undergoing decommissioning have been granted permission to reduce the required amount of primary offsite liability insurance coverage from $450 million to $100 million and to withdraw from the secondary insurance pool. One of the technical criteria for granting the exemption is that the possibility of a design-basis event that could cause significant offsite damage has been eliminated.

The NRC staff performed an evaluation of the design-basis accidents for Pilgrim being permanently defueled as part of SECY–19–0078, ''Request by Entergy Nuclear Operations, Inc. for Exemptions from Certain Emergency Planning Requirements for the Pilgrim Nuclear Power Station,'' dated August 9, 2019 (ADAMS Accession No. ML18347A717).

ENOI has stated, and the NRC staff agrees, that while spent fuel remains in the SFP, the only postulated design-basis accident that would remain applicable to Pilgrim in the permanently defueled condition that could contribute a significant dose is a fuel handling accident (FHA) in the Reactor Building, where the SFP is located. For completeness, the NRC staff also evaluated the applicability of other design-basis accidents documented in the Pilgrim Updated Final Safety Analysis Report (UFSAR) (ADAMS Accession No. ML16083A494) to ensure that these accidents would not have consequences that could potentially exceed the 10 CFR 50.67 dose limits and Regulatory Guide 1.183, ''Alternative Radiological Source Terms for Evaluating Design Basis Accidents at Nuclear Power Reactors,'' dose acceptance criteria or approach the U.S. Environmental Protection Agency (EPA) early phase protective action guides (PAGs).

In the Pilgrim UFSAR, the licensee has determined that within 46 days after shutdown, the FHA doses would decrease to a level that would not warrant protective actions under the EPA early phase PAG framework, notwithstanding meeting the dose limit requirements under 10 CFR 50.67 and dose acceptance criteria under Regulatory Guide 1.183. The NRC staff notes that the doses from an FHA are dominated by the isotope Iodine-131. Pilgrim permanently ceased power operations on May 31, 2019. With 10 months of decay, the thyroid dose from an FHA would be negligible. After 10 months of decay, the only isotope remaining in significant amounts, among those postulated to be released in a design-basis FHA, would be Krypton-85. Since Krypton-85 primarily decays by beta emission, the calculated skin dose from an FHA analysis would make an insignificant contribution to the total effective dose equivalent (TEDE), which is the parameter of interest in the determination of the EPA early phase PAGs for sheltering or evacuation. The NRC staff concludes that the dose consequence from an FHA for the permanently shutdown Pilgrim would not approach the EPA early phase PAGs. Therefore, any offsite consequence from a design-basis radiological release is highly unlikely and, thus, a significant amount of offsite liability insurance coverage is not required.

The only beyond design-basis event that has the potential to lead to a significant radiological release at a permanently shutdown and defueled reactor is a zirconium fire. The zirconium fire scenario is a postulated, but highly unlikely, accident scenario that involves the loss of water inventory from the SFP resulting in a significant heatup of the spent fuel and culminating in substantial zirconium cladding oxidation and fuel damage. The probability of a zirconium fire scenario is related to the decay heat of the irradiated fuel stored in the SFP. Therefore, the risks from a zirconium fire scenario continue to decrease as a function of the time that Pilgrim has been permanently shut down.

In the analysis provided in Attachment 2, ''Calculation No. PNPS–EC–81416–M1418, Adiabatic Heatup Analysis for Drained Spent Fuel Pool,'' to the letter dated February 18, 2019 (ADAMS Accession No. ML19056A260), the licensee compared the conditions for the hottest fuel assembly stored in the SFP to a criterion proposed in SECY–99–168, ''Improving Decommissioning Regulations for Nuclear Power Plants,'' dated June 30, 1999 (ADAMS Accession No. ML12265A598), applicable to offsite emergency response for the unit in the decommissioning process. This criterion considers the time for the hottest assembly to heat up from 30 degrees Celsius (°C) to 900 °C adiabatically. If the heatup time is greater than 10 hours, then offsite emergency preplanning involving the plant is not necessary. Based on the limiting fuel assembly for decay heat and adiabatic heatup analysis presented in Attachment 2, at 10 months after permanent cessation of power operations (*i.e.,* 10 months of decay time), the time for the hottest fuel assembly to reach 900 °C is 10 hours after the assemblies have been uncovered. As stated in NUREG–1738, ''Technical Study of Spent Fuel Pool Accident Risk at Decommissioning Nuclear Power Plants,'' dated February 2001 (ADAMS Accession No. ML010430066), 900 °C is an acceptable temperature to use for assessing onset of fission product release under transient conditions to establish the critical decay time for determining the availability of 10 hours for deployment of mitigation equipment and, if necessary, for offsite agencies to take appropriate action to protect the health and safety of the public if fuel and cladding oxidation occurs in air.

The NRC staff reviewed the calculation to verify that important physical properties of materials were within acceptable ranges and the results were accurate. The NRC staff determined that physical properties were appropriate. Therefore, the NRC staff found that 10 months after permanent cessation of power operations, more than 10 hours would be available before a significant offsite release could begin. The NRC staff concluded that the adiabatic heatup calculation provided an acceptable method for determining the minimum

time available for deployment of mitigation equipment and, if necessary, implementing measures under a comprehensive general emergency plan.

In this regard, one technical criterion for relieving decommissioning reactor licensees from the insurance obligations applicable to an operating reactor is a finding that the heat generated by the SFP has decayed to the point where the possibility of a zirconium fire is highly unlikely.

This was addressed in SECY–93–127, where the NRC staff concluded that there was a low likelihood and reduced short-term public health consequences of a zirconium fire once a decommissioning plant's spent fuel has sufficiently decayed. In its Staff Requirements Memorandum, ''Financial Protection Required of Licensees of Large Nuclear Power Plants during Decommissioning,'' dated July 13, 1993 (ADAMS Accession No. ML003760936), the Commission approved a policy that authorized, through the exemption process, withdrawal from participation in the secondary insurance layer and a reduction in commercial liability insurance coverage to $100 million when a licensee is able to demonstrate that the spent fuel could be air-cooled if the SFP was drained of water.

The NRC staff has used this technical criterion to grant similar exemptions to other decommissioning reactors (*e.g.,* Maine Yankee Atomic Power Station, published in the **Federal Register** on January 19, 1999 (64 FR 2920); Zion Nuclear Power Station, published in the **Federal Register** on December 28, 1999 (64 FR 72700); Kewaunee Power Station, published in the **Federal Register** on March 24, 2015 (80 FR 15638); Crystal River Unit 3 Nuclear Generation Plant, published in the **Federal Register** on May 6, 2015 (80 FR 26100); and Oyster Creek Nuclear Generating Station, published in the **Federal Register** on December 28, 2018 (83 FR 67365)).

Additional discussions of other decommissioning reactor licensees that have received exemptions to reduce their primary insurance level to $100 million are provided in SECY–96–256, ''Changes to the Financial Protection Requirements for Permanently Shutdown Nuclear Power Reactors, 10 CFR 50.54(w) and 10 CFR 140.11,'' dated December 17, 1996 (ADAMS Accession No. ML15062A483). These prior exemptions were based on the licensee demonstrating that the SFP could be air-cooled consistent with the technical criterion discussed above.

The NRC staff has evaluated the issue of zirconium fires in SFPs and presented an independent evaluation of an SFP subject to a severe earthquake in NUREG–2161, ''Consequence Study of a Beyond-Design-Basis Earthquake Affecting the Spent Fuel Pool for a U.S. Mark l Boiling Water Reactor,'' dated September 2014 (ADAMS Accession No. ML14255A365). This evaluation concluded that, for a representative boiling-water reactor, fuel in a dispersed high-density configuration would be adequately cooled by natural circulation air flow within several months after discharge from a reactor if the pool was drained of water.

By letter dated July 30, 2019 (ADAMS Accession No. ML19211B509), ENOI provided a supplement to its exemption request addressing air-cooling of fuel in a drained SFP. In the attachment to this letter, the licensee compared Pilgrim fuel storage parameters with those used in NRC generic evaluations of fuel cooling included in NUREG/CR–6451, ''A Safety and Regulatory Assessment of Generic BWR [Boiling-Water Reactor] and PWR [Pressurized-Water Reactor] Permanently Shutdown Nuclear Power Plants,'' dated August 1997 (ADAMS Accession No. ML082260098). The analysis described in NUREG/CR–6451 determined that natural air circulation would adequately cool fuel that has decayed for 7 months after operation in a typical BWR. The licensee compared the post-shutdown fuel storage conditions with those assumed for the analysis presented in NUREG/CR–6451. The licensee found that the Pilgrim fuel storage configuration is nearly identical to the representative configuration used in the NUREG/CR–6451 analysis with respect to the fuel assembly size, the fuel storage pitch, the rack material, and the rack orifice size being larger than the BWR fuel assembly inlet nozzle size. Thus, the cooling air flow should be comparable. However, although the Pilgrim final cycle fuel operated at a lower power density, it achieved a higher total burnup than assumed for the NUREG/CR–6451 analysis. The licensee determined that the higher decay heat resulting from the increased burnup would be offset by the longer decay time (*i.e.,* 10 months) at the effective date of the requested exemption as compared to the decay time used in the NUREG/CR–6451 analysis (*i.e.,* 7 months), which results in a lower total decay heat rate. Therefore, at 10 months after permanent shutdown (*i.e.,* the effective date of the requested exemption), the NRC staff has reasonable assurance that fuel stored in the Pilgrim SFP would be adequately air-cooled in the unlikely event the SFP completely drained.

In SECY–00–0145, ''Integrated Rulemaking Plan for Nuclear Power Plant Decommissioning,'' dated June 28, 2000, and SECY–01–0100, ''Policy Issues Related to Safeguards, Insurance, and Emergency Preparedness Regulations at Decommissioning Nuclear Power Plants Storing Fuel in Spent Fuel Pools,'' dated June 4, 2001 (ADAMS Accession Nos. ML003721626 and ML011450420, respectively), the NRC staff discussed additional information concerning SFP zirconium fire risks at decommissioning reactors and associated implications for offsite insurance. Analyzing when the spent fuel stored in the SFP is capable of adequate air-cooling is one measure that demonstrates when the probability of a zirconium fire would be exceedingly low.

In addition, the licensee performed adiabatic heatup analyses in which a complete drainage of the SFP is combined with rearrangement of spent fuel rack geometry and/or the addition of rubble to the SFP; this type of analysis postulates that decay heat transfer from the spent fuel via conduction, convection, or radiation would be impeded. The licensee's adiabatic heatup analyses demonstrate that 10 months after the permanent cessation of operations, there would be at least 10 hours after the loss of all means of cooling (both air and/or water) before the spent fuel cladding would reach a temperature where the potential for a significant offsite radiological release could occur.

In the March 25, 2019, application, ENOI furnished the following information: ''Based on the length of time it would take for the adiabatic heat up to occur, there is ample time to respond to any partial drain down event that might cause such an occurrence by restoring SFP cooling or makeup, or providing SFP spray. As a result, the likelihood that such a scenario would progress to a zirconium fire is deemed not credible.''

In the NRC staff's evaluation contained in SECY–19–0078, the NRC staff assessed the ENOI accident analyses associated with the radiological risks from a zirconium fire at a permanently shut down and defueled Pilgrim site. For the highly unlikely beyond design-basis accident scenario where the SFP coolant inventory is lost in such a manner that all methods of heat removal from the spent fuel are no longer available, the NRC staff found that there will be a minimum of 10 hours from the initiation of the accident until the cladding reaches a temperature where offsite radiological release might occur. The NRC staff finds that 10 hours is sufficient time to support deployment of

mitigation equipment, consistent with plant conditions, to prevent the zirconium cladding from reaching a point of rapid oxidation.

The NRC staff has determined that the licensee's proposed reduction in primary offsite liability coverage to a level of $100 million and the licensee's proposed withdrawal from participation in the secondary insurance pool for offsite financial protection are consistent with the policy established in SECY–93–127 and subsequent insurance considerations resulting from zirconium fire risks, as discussed in SECY–00–0145 and SECY–01–0100. The NRC has previously determined in SECY–00–0145 that the minimum offsite financial protection requirement may be reduced to $100 million and that secondary insurance is not required once it is determined that the spent fuel in the SFP is no longer thermal-hydraulically capable of sustaining a zirconium fire based on a plant-specific analysis. In addition, the NRC staff notes that similar exemptions from these insurance requirements have been granted to other permanently shut down and defueled power reactors upon satisfactory demonstration that zirconium fire risk from the irradiated fuel stored in the SFP is of negligible concern.

A. The Exemption Is Authorized by Law

The PAA and its implementing regulations in 10 CFR 140.11(a)(4) require licensees of nuclear reactors that have a rated capacity of 100,000 kilowatts electric or more to have and maintain $450 million in primary financial protection and to participate in a secondary retrospective insurance pool. In accordance with 10 CFR 140.8, the Commission may grant exemptions from the regulations in 10 CFR part 140 as the Commission determines are authorized by law. The legal and associated technical basis for granting exemptions from 10 CFR part 140 are set forth in SECY–93–127. The legal analysis underlying SECY–93–127 concluded that, upon a technical finding that lesser potential hazards exist after permanent cessation of operations, the Commission has the discretion under the PAA to reduce the amount of insurance required of a licensee undergoing decommissioning.

Based on its review of the exemption request, the NRC staff concludes that the technical criteria for relieving Holtec Pilgrim and HDI from their existing primary and secondary insurance obligations have been met. As explained above, the NRC staff has concluded that no reasonably conceivable design-basis accident exists that could cause an offsite release greater than the EPA PAGs and, therefore, that any offsite consequence from a design-basis radiological release is highly unlikely and the need for a significant amount of offsite liability insurance coverage is unwarranted. Additionally, the NRC staff determined that, after 10 months decay, the fuel stored in the Pilgrim SFP will be capable of being adequately cooled by air in the highly unlikely event of pool drainage. Moreover, in the highly unlikely beyond design-basis accident scenario where the SFP coolant inventory is lost in such a manner that all methods of heat removal from the spent fuel are no longer available, the NRC staff has determined that at least 10 hours would be available and is sufficient time to support deployment of mitigation equipment, consistent with plant conditions, to prevent the zirconium cladding from reaching a point of rapid oxidation. Thus, the NRC staff concludes that the fuel stored in the Pilgrim SFP will have decayed sufficiently by the requested effective date for the exemption of 10 months after permanent cessation of power operations to support a reduction in the required insurance consistent with SECY–00–0145.

The NRC staff has determined that granting the licensee's proposed exemption will not result in a violation of the Atomic Energy Act of 1954, Section 170, or other laws, as amended, which require licensees to maintain adequate financial protection. Accordingly, consistent with the legal standard presented in SECY–93–127, under which decommissioning reactor licensees may be relieved of the requirements to carry the maximum amount of insurance available and to participate in the secondary retrospective premium pool where there is sufficient technical justification, the NRC staff concludes that the requested exemption is authorized by law.

B. The Exemption Is Otherwise in the Public Interest

The financial protection limits of 10 CFR 140.11 were established to require licensees to maintain sufficient offsite liability insurance to ensure adequate funding for offsite liability claims following an accident at an operating reactor. However, the regulation does not consider the reduced potential for and consequence of nuclear incidents at permanently shutdown and decommissioning reactors.

The basis provided in SECY–93–127, SECY–00–0145, and SECY–01–0100 allows licensees of decommissioning plants to reduce their primary offsite liability insurance and to withdraw from participation in the retrospective rating pool for deferred premium charges. As discussed in these documents, once the zirconium fire concern is determined to be negligible, possible accident scenario risks at permanently shutdown and defueled reactors are greatly reduced when compared to the risks at operating reactors and the associated potential for offsite financial liabilities from an accident are commensurately less. The licensee analyzed and the NRC staff confirmed that the risks of accidents that could result in an offsite radiological risk are minimal, thereby justifying the proposed reductions in offsite primary liability insurance and withdrawal from participation in the secondary retrospective rating pool for deferred premium charges.

Additionally, participation in the secondary retrospective rating pool could potentially have adverse consequences on the safe and timely completion of decommissioning. If a nuclear incident sufficient to trigger the secondary insurance layer occurred at another nuclear power plant, the licensee could incur financial liability of up to $131,056,000. However, because Pilgrim is permanently shut down, it cannot produce revenue from electricity generation sales to cover such a liability. Therefore, such liability if subsequently incurred could significantly affect the ability of the facility to conduct and complete timely radiological decontamination and decommissioning activities. In addition, as SECY–93–127 concluded, the shared financial risk exposure to the licensee is greatly disproportionate to the radiological risk posed by Pilgrim when compared to operating reactors. The reduced overall risk to the public at decommissioning power plants does not warrant that the licensee be required to carry full operating reactor insurance coverage after the requisite spent fuel cooling period has elapsed following final reactor shutdown. The licensee's proposed financial protection limits will maintain a level of liability insurance coverage commensurate with the risk to the public. These changes are consistent with previous NRC policy as discussed in SECY–00–0145 and exemptions approved for other decommissioning reactors. Thus, the underlying purpose of the regulations will not be adversely affected by the reductions in insurance coverage. Accordingly, an exemption from participation in the secondary insurance pool and a reduction in the primary insurance to $100 million, a value more in line with the potential consequences of accidents, would be in

the public interest in that this ensures that there will be adequate funds to address any of those consequences and helps to ensure the safe and timely decommissioning of the reactor.

Therefore, the NRC staff has concluded that an exemption from 10 CFR 140.11(a)(4), which would permit Holtec Pilgrim and HDI to lower the Pilgrim primary insurance levels and to withdraw from the secondary retrospective premium pool at the requested effective date of 10 months after permanent cessation of power operations, is in the public interest.

C. Environmental Considerations

The NRC's approval of an exemption from insurance or indemnity requirements belongs to a category of actions that the Commission, by rule or regulation, has declared to be a categorical exclusion after first finding that the category of actions does not individually or cumulatively have a significant effect on the human environment. Specifically, the exemption is categorically excluded from the requirement to prepare an environmental assessment or environmental impact statement in accordance with 10 CFR 51.22(c)(25).

Under 10 CFR 51.22(c)(25), granting of an exemption from the requirements of any regulation of Chapter I to 10 CFR is a categorical exclusion provided that: (i) There is no significant hazards consideration; (ii) there is no significant change in the types or significant increase in the amounts of any effluents that may be released offsite; (iii) there is no significant increase in individual or cumulative public or occupational radiation exposure; (iv) there is no significant construction impact; (v) there is no significant increase in the potential for or consequences from radiological accidents; and (vi) the requirements from which an exemption is sought involve surety, insurance, or indemnity requirements.

As the Director, Division of Operating Reactor Licensing, Office of Nuclear Reactor Regulation, I have determined that approval of the exemption request involves no significant hazards consideration, as defined in 10 CFR 50.92, because reducing a licensee's offsite liability requirements at Pilgrim does not: (1) Involve a significant increase in the probability or consequences of an accident previously evaluated; (2) create the possibility of a new or different kind of accident from any accident previously evaluated; or (3) involve a significant reduction in a margin of safety. The exempted financial protection regulation is unrelated to the operation of Pilgrim or site activities. Accordingly, there is no significant change in the types or significant increase in the amounts of any effluents that may be released offsite and no significant increase in individual or cumulative public or occupational radiation exposure. The exempted regulation is not associated with construction so there is no significant construction impact. The exempted regulation does not concern the source term (*i.e.,* potential amount of radiation in an accident) nor any activities conducted at the site. Therefore, there is no significant increase in the potential for, or consequences of, a radiological accident. In addition, there would be no significant impacts to biota, water resources, historic properties, cultural resources, or socioeconomic conditions in the region resulting from issuance of the requested exemption. The requirement for offsite liability insurance involves surety, insurance, or indemnity matters only.

Therefore, pursuant to 10 CFR 51.22(b) and 51.22(c)(25), no environmental impact statement or environmental assessment need be prepared in connection with the approval of this exemption request.

IV. Conclusions

Accordingly, the Commission has determined that, pursuant to 10 CFR 140.8, the exemption is authorized by law and is otherwise in the public interest. Therefore, the Commission hereby grants Holtec Pilgrim and HDI an exemption from the requirements of 10 CFR 140.11(a)(4) for Pilgrim. Pilgrim permanently ceased power operations on May 31, 2019. The exemption from 10 CFR 140.11(a)(4) permits Pilgrim to reduce the required level of primary financial protection from $450 million to $100 million and to withdraw from participation in the secondary layer of financial protection 10 months after permanent cessation of power operations.

The exemption is effective as of 10 months after permanent cessation of power operations.

Dated at Rockville, Maryland, this 6th day of January 2020.

For the Nuclear Regulatory Commission.

Craig G. Erlanger,

Director, Division of Operating Reactor Licensing, Office of Nuclear Reactor Regulation.

[FR Doc. 2020–00285 Filed 1–10–20; 8:45 am]

BILLING CODE 7590–01–P

RAILROAD RETIREMENT BOARD

Civil Monetary Penalty Inflation Adjustment

AGENCY: Railroad Retirement Board.

ACTION: Notice announcing updated penalty inflation adjustments for civil monetary penalties for 2020.

SUMMARY: As required by Section 701 of the Bipartisan Budget Act of 2015, entitled the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015, the Railroad Retirement Board (Board) hereby publishes its 2020 annual adjustment of civil penalties for inflation.

FOR FURTHER INFORMATION CONTACT: Marguerite P. Dadabo, Assistant General Counsel, Railroad Retirement Board, 844 North Rush Street, Chicago, IL 60611–1275, (312) 751–4945, TTD (312) 751–4701.

SUPPLEMENTARY INFORMATION: Section 701 of the Bipartisan Budget Act of 2015, Public Law 114–74 (Nov. 2, 2015), entitled the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (the 2015 Act), amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (28 U.S.C. 2461 note) (Inflation Adjustment Act) to require agencies to publish regulations adjusting the amount of civil monetary penalties provided by law within the jurisdiction of the agency not later than January 15th of every year.

For the 2020 annual adjustment for inflation of the maximum civil penalty under the Program Fraud Civil Remedies Act of 1986, the Board applies the formula provided by the 2015 Act and the Board's regulations at Title 20, Code of Federal Regulations, Part 356. In accordance with the 2015 Act, the amount of the adjustment is based on the percent increase between the Consumer Price Index (CPI–U) for the month of October preceding the date of the adjustment and the CPI–U for the October one year prior to the October immediately preceding the date of the adjustment. If there is no increase, there is no adjustment of civil penalties. The percent increase between the CPI–U for October 2019 and October 2018, as provided by Office of Management and Budget Memorandum M–20–05 (December 16, 2019) is 1.01764 percent. Therefore, the new maximum penalty under the Program Fraud Civil Remedies Act is $11,665 (the 2019 maximum penalty of $11,463 multiplied by 1.01764, rounded to the nearest dollar). The new minimum penalty under the False Claims Act is $11,665 (the 2019 minimum penalty of $11,463 multiplied by 1.01764, rounded to the

nearest dollar), and the new maximum penalty is $23,331 (the 2019 maximum penalty of $22,927 multiplied by 1.01764, rounded to the nearest dollar). The adjustments in penalties will be effective January 13, 2020.

Dated: January 8, 2020.

By Authority of the Board.

Stephanie Hillyard,

Secretary to the Board.

[FR Doc. 2020–00324 Filed 1–10–20; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release Nos. 33–10740; 34–87905; IA–5428; IC–33740]

Adjustments to Civil Monetary Penalty Amounts

AGENCY: Securities and Exchange Commission.

ACTION: Notice of annual inflation adjustment of civil monetary penalties.

SUMMARY: The Securities and Exchange Commission (the ''Commission'') is publishing this notice (the ''Notice'') pursuant to the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (the ''2015 Act''). This Act requires all agencies to annually adjust for inflation the civil monetary penalties that can be imposed under the statutes administered by the agency and publish the adjusted amounts in the **Federal Register**. This Notice sets forth the annual inflation adjustment of the maximum amount of civil monetary penalties (''CMPs'') administered by the Commission under the Securities Act of 1933, the Securities Exchange Act of 1934 (the ''Exchange Act''), the Investment Company Act of 1940, the Investment Advisers Act of 1940, and certain penalties under the Sarbanes-Oxley Act of 2002. These amounts are effective beginning on January 15, 2020, and will apply to all penalties imposed after that date for violations of the aforementioned statutes that occurred after November 2, 2015.

FOR FURTHER INFORMATION CONTACT: Stephen M. Ng, Senior Special Counsel, Office of the General Counsel, at (202) 551–7957, or Hannah W. Riedel, Senior Counsel, Office of the General Counsel, at (202) 551–7918.

SUPPLEMENTARY INFORMATION:

I. Background

This Notice is being published pursuant to the 2015 Act,[1] which amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (the ''Inflation Adjustment Act'').[2] The Inflation Adjustment Act previously had been amended by the Debt Collection Improvement Act of 1996 (the ''DCIA'')[3] to require that each federal agency adopt regulations at least once every four years that adjust for inflation the CMPs that can be imposed under the statutes administered by the agency. Pursuant to this requirement, the Commission previously adopted regulations in 1996, 2001, 2005, 2009, and 2013 to adjust the maximum amount of the CMPs that could be imposed under the statutes the Commission administers.[4]

The 2015 Act replaces the inflation adjustment formula prescribed in the DCIA with a new formula for calculating the inflation-adjusted amount of CMPs. The 2015 Act requires that agencies use this new formula to re-calculate the inflation-adjusted amounts of the penalties they administer on an annual basis and publish these new amounts in the **Federal Register** by January 15 of each year.[5] The Commission previously published the first annual adjustment required by the 2015 Act on January 6, 2017 (the ''2017 Adjustment'').[6] As part of the 2017 Adjustment, the Commission promulgated 17 CFR 201.1001(a) and Table I to Subsection 1001, which lists the penalty amounts for all violations that occurred on or before November 2, 2015. For violations occurring after November 2, 2015, Subsection 1001(b) provides that the applicable penalty amounts will be adjusted annually based on the formula set forth in the 2015 Act. Subsection 1001(b) further provides that these adjusted amounts will be published in the **Federal Register** and on the Commission's website. The Commission subsequently published annual adjustments on January 8, 2018 (the ''2018 Adjustment'')[7] and February 20, 2019 (''2019 Adjustment'').[8]

A CMP is defined in relevant part as any penalty, fine, or other sanction that: (1) Is for a specific amount, or has a maximum amount, as provided by federal law; and (2) is assessed or enforced by an agency in an administrative proceeding or by a federal court pursuant to federal law.[9] This definition applies to the monetary penalty provisions contained in four statutes administered by the Commission: The Securities Act, the Exchange Act, the Investment Company Act, and the Investment Advisers Act. In addition, the Sarbanes-Oxley Act provides the Public Company Accounting Oversight Board (the ''PCAOB'') authority to levy civil monetary penalties in its disciplinary proceedings pursuant to 15 U.S.C. 7215(c)(4)(D).[10] The definition of a CMP in the Inflation Adjustment Act encompasses such civil monetary penalties.[11]

II. Adjusting the Commission's Penalty Amounts for Inflation

This Notice sets forth the annual inflation adjustment required by the 2015 Act for all CMPs under the Securities Act, the Exchange Act, the Investment Company Act, and the Investment Advisers Act, and certain civil monetary penalties under the Sarbanes-Oxley Act.

Pursuant to the 2015 Act, the penalty amounts in the 2019 Adjustment are adjusted for inflation by increasing them by the percentage change between the Consumer Price Index for all Urban Consumers (''CPI–U'') for October 2018

[1] Public Law 114–74 Sec. 701, 129 Stat. 599–601 (Nov. 2, 2015), codified at 28 U.S.C. 2461 note.

[2] Public Law 101–410, 104 Stat. 890–892 (1990), codified at 28 U.S.C. 2461 note.

[3] Public Law 104–134, Title III, § 31001(s)(1), 110 Stat. 1321–373 (1996), codified at 28 U.S.C. 2461 note.

[4] *See* Release Nos. 33–7361, 34–37912, IA–1596, IC–22310, dated November 1, 1996 (effective December 9, 1996), previously found at 17 CFR 201.1001 and Table I to Subpart E of Part 201; Release Nos. 33–7946, 34–43897, IA–1921, IC–24846, dated January 31, 2001 (effective February 2, 2001), previously found at 17 CFR 201.1002 and Table II to Subpart E of Part 201; Release Nos. 33–8530, 34–51136, IA–2348, IC–26748, dated February 9, 2005 (effective February 14, 2005), previously found at 17 CFR 201.1003 and Table III to Subpart E of Part 201; Release Nos. 33–9009, 34–59449, IA–2845, IC–28635, dated February 25, 2009 (effective March 3, 2009), previously found at 17 CFR 201.1004 and Table IV to Subpart E of Part 201; and Release Nos. 33–9387, 34–68994, IA–3557, IC–30408, dated February 27, 2013 (effective March 5, 2013), previously found at 17 CFR 201.1005 and Table V to Subpart E of Part 201. The penalty amounts contained in these releases have now been consolidated into Table I to 17 CFR 201.1001.

[5] 28 U.S.C. 2461 note Sec. 4.

[6] Release Nos. 33–10276; 34–79749; IA–4599; IC–32414 (effective Jan. 18, 2017).

[7] Release Nos. 33–10451; 34–82455; IA–4842; IC–32963 (effective Jan. 15, 2018).

[8] Release Nos. 33–10604; 34–85118; IA–5111; IC–33373 (effective Jan. 15, 2019). The publication of the 2019 Adjustment in the **Federal Register** was delayed due to operation of the Antideficiency Act during the absence of an appropriations bill to fund federal government programs between December 22, 2018 and January 25, 2019.

[9] 28 U.S.C. 2461 note Sec. 3(2).

[10] 15 U.S.C. 7215(c)(4)(D).

[11] The Commission may by order affirm, modify, remand, or set aside sanctions, including civil monetary penalties, imposed by the PCAOB. *See* Section 107(c) of the Sarbanes-Oxley Act of 2002, 15 U.S.C. 7217. The Commission may enforce such orders in federal district court pursuant to Section 21(e) of the Exchange Act. As a result, penalties assessed by the PCAOB in its disciplinary proceedings are penalties ''enforced'' by the Commission for purposes of the Inflation Adjustment Act. *See Adjustments to Civil Monetary Penalty Amounts,* Release No. 33–8530 (Feb. 4, 2005) [70 FR 7606 (Feb. 14, 2005)].

and the October 2019 CPI–U.[12] OMB has provided its calculation of this multiplier (the ''CPI–U Multiplier'') to agencies.[13] The new penalty amounts are determined by multiplying the amounts in the 2019 Adjustment by the CPI–U Multiplier and then rounding to the nearest dollar.

For example, the CMP for certain insider trading violations by controlling persons under Exchange Act Section 21A(a)(3) [14] was readjusted for inflation as part of the 2019 Adjustment to $2,103,861. To determine the new CMP under this provision, the Commission multiplies this amount by the CPI–U Multiplier of 1.01764, and rounds to the nearest dollar. Thus, the new CMP for Exchange Act Section 21A(a)(3) is $2,140,973.

Below is the Commission's calculation of the new penalty amounts for the penalties it administers:

U.S. code citation	Civil monetary penalty description	2019 Adjustment penalty amounts	CPI–U multiplier	2020 Adjusted penalty amounts
15 U.S.C. 77h–1(g) (Securities Act Sec. 8A(g)).	For natural person	$8,671	1.01764	$8,824
	For any other person	86,718	1.01764	88,248
	For natural person/fraud	86,718	1.01764	88,248
	For any other person/fraud	433,591	1.01764	441,240
	For natural person/fraud/substantial losses or risk of losses to others or gains to self.	173,437	1.01764	176,496
	For any other person/fraud/substantial losses or risk of losses to others or gain to self.	838,275	1.01764	853,062
15 U.S.C. 77t(d) (Securities Act Sec. 20(d)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others.	947,130	1.01764	963,837
15 U.S.C. 78u(d)(3) (Exchange Act Sec. 21(d)(3)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others or gains to self.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others or gain to self.	947,130	1.01764	963,837
15 U.S.C. 78u–1(a)(3) (Exchange Act Sec. 21A(a)(3)).	Insider Trading—controlling person	2,103,861	1.01764	2,140,973
15 U.S.C. 78u–2 (Exchange Act Sec. 21B).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others.	947,130	1.01764	963,837
15 U.S.C. 78ff(b) (Exchange Act Sec. 32(b)).	Exchange Act/failure to file information documents, reports.	559	1.01764	569
15 U.S.C. 78ff(c)(1)(B) (Exchange Act Sec. 32(c)(1)(B)).	Foreign Corrupt Practices—any issuer	21,039	1.01764	21,410
15 U.S.C. 78ff(c)(2)(B) (Exchange Act Sec. 32(c)(2)(B)).	Foreign Corrupt Practices—any agent or stockholder acting on behalf of issuer.	21,039	1.01764	21,410
15 U.S.C. 80a–9(d) (Investment Company Act Sec. 9(d)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others or gains to self.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others or gain to self.	947,130	1.01764	963,837
15 U.S.C. 80a–41(e) (Investment Company Act Sec. 42(e)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384

[12] 28 U.S.C. 2461 note Sec. 5.

[13] Office of Management and Budget, *Implementation of Penalty Inflation Adjustments for 2020, Pursuant to the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015* (December 16, 2019), available at *https://www.whitehouse.gov/wp-content/uploads/2019/12/M-20-05.pdf*. This multiplier represents the percentage increase between the October 2018 CPI–U and the October 2019 CPI–U, plus 1.

[14] 15 U.S.C. 78u–1(a)(3).

U.S. code citation	Civil monetary penalty description	2019 Adjustment penalty amounts	CPI–U multiplier	2020 Adjusted penalty amounts
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others.	947,130	1.01764	963,837
15 U.S.C. 80b–3(i) (Investment Advisers Act Sec. 203(i)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others or gains to self.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others or gain to self.	947,130	1.01764	963,837
15 U.S.C. 80b–9(e) (Investment Advisers Act Sec. 209(e)).	For natural person	9,472	1.01764	9,639
	For any other person	94,713	1.01764	96,384
	For natural person/fraud	94,713	1.01764	96,384
	For any other person/fraud	473,566	1.01764	481,920
	For natural person/fraud/substantial losses or risk of losses to others.	189,427	1.01764	192,768
	For any other person/fraud/substantial losses or risk of losses to others.	947,130	1.01764	963,837
15 U.S.C. 7215(c)(4)(D)(i) (Sarbanes-Oxley Act Sec. 105(c)(4)(D)(i)).	For natural person	139,483	1.01764	141,943
	For any other person	2,789,675	1.01764	2,838,885
15 U.S.C. 7215(c)(4)(D)(ii) (Sarbanes-Oxley Act Sec. 105(c)(4)(D)(ii)).	For natural person	1,046,128	1.01764	1,064,582
	For any other person	20,922,558	1.01764	21,291,632

Pursuant to the 2015 Act and 17 CFR 201.1001, the adjusted penalty amounts in this Notice (and all penalty adjustments performed pursuant to the 2015 Act) apply to penalties imposed after the date the adjustment is effective for violations that occurred after November 2, 2015, the 2015 Act's enactment date. These penalty amounts supersede the amounts in the 2018 Adjustment.[15] For violations that occurred on or before November 2, 2015, the penalty amounts in Table I to 17 CFR 201.1001 continue to apply.[16]

By the Commission.

Dated: January 8, 2020.

Vanessa A. Countryman,

Secretary.

[FR Doc. 2020–00306 Filed 1–10–20; 8:45 am]

BILLING CODE 8011–01–P

[15] The penalty amounts in this Notice are being published in the **Federal Register** and will not be added to the Code of Federal Regulations in accordance with the 2015 Act and 17 CFR 201.1001(b). *See* 28 U.S.C. 2461 note Sec. 4(a)(2); 17 CFR 201.1001(b). In addition to being published in the **Federal Register**, the penalty amounts in this Notice will be made available on the Commission's website at *https://www.sec.gov/enforce/civil-penalties-inflation-adjustments.htm,* as detailed in 17 CFR 201.1001(b). This website also lists the penalty amounts for violations that occurred on or before November 2, 2015.

[16] 17 CFR 201.1001(a).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–87901; File No. SR–NYSEArca–2020–04]

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend the NYSE Arca Options Fee Schedule Regarding the Floor Broker Prepayment Program

January 7, 2020.

Pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 (''Act'')[2] and Rule 19b–4 thereunder,[3] notice is hereby given that on January 2, 2020, NYSE Arca, Inc. (''NYSE Arca'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend the NYSE Arca Options Fee Schedule (''Fee Schedule'') regarding the Floor Broker Prepayment Program. The Exchange proposes to implement the fee change effective January 2, 2020. The proposed rule change is available on the Exchange's website at *www.nyse.com,* at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to modify and extend the prepayment incentive program for Floor Broker organizations (each a ''Floor Broker'') which allows Floor Brokers to prepay certain annual costs in exchange for volume rebates, as set forth in the Fee Schedule (the ''FB Prepay Program'' or ''Program'').[4]

Pursuant to the current FB Prepay Program, the Exchange offers Floor Brokers a 10% discount on their ''Eligible Fixed Costs'' if such costs are prepaid in advance of the year (the ''10% Discount'')[5] and an opportunity to qualify for the Percentage Growth Incentive (the ''Growth Incentive''), which is designed to encourage Floor Brokers to increase their average daily volume (''ADV'') in billable manual contract sides by certain percentages (correlated with Tiers) as measured against (the greater of) one of two benchmarks.[6]

The Exchange proposes to make several changes to this Program, including to make it renewable annually, to remove the 10% Discount, and to offer an alternative annual fixed rebate amount if a participant qualifies for the Growth Incentive. Currently, if a Floor Broker qualifies for the Growth Incentive, it would be eligible for specified percentage reductions of its pre-paid annual fixed costs. The Exchange proposes to offer an alternative to receive a specified annual fixed rebate if a Floor Broker qualifies for the Growth Incentive. Participants that qualify would receive the greater of the two rebates. The Exchange also proposes to adjust the qualifying baseline volumes and benchmarks.

The Exchange proposes to implement the fee change effective January 2, 2020.

Background

The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.''[7]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[8] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[9]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. To respond to this competitive marketplace, the Exchange has established incentives for Floor Brokers, as such participants serve an important function in facilitating the execution of orders via open outcry, which promotes price discovery on the public markets. To the extent that these incentives succeed, the increased liquidity on the Exchange would result in enhanced market quality for all participants.

Proposed Rule Change

The Exchange proposes to modify the Floor Broker Prepayment Program in several ways. First, the Exchange proposes to remove reference to specific years and to add rule text making clear that the Program is renewable on an annual basis.[10] The Exchange also proposes to remove language regarding the 10% Discount, as that would no longer be included in the Program.[11] In addition, the Exchange proposes to expand the Growth Incentive to provide an annual fixed-rebate option.

Currently, to qualify for the Growth Incentive, the minimum threshold that a participant needs to exceed is the greater of: 11,000 contract sides in billable manual ADV; or 110% of the Floor Broker's total billable manual ADV in contract sides during the second half of 2017—*i.e.,* July through December 2017.[12]

The Exchange proposes to revise the minimum thresholds that a participant needs to exceed to qualify for the Growth Incentive as follows: 20,000 contract sides (up from 11,000) in billable manual ADV; or 105% of the Floor Broker's total billable manual ADV in contract sides (down from 110%) during the second half of 2017—*i.e.,* July through December 2017.[13] The Exchange believes that 20,000 ADV is a reasonable minimum threshold above which a participating Floor Broker would need to increase volume in order to qualify for the Growth Incentive given the increased options volume executed by Floor Brokers in the past year. The Exchange also notes that Floor Brokers that are new to the Exchange would be able to qualify for the Growth Incentive based on the minimum threshold of 20,000 contract sides. In addition, because Floor Broker volume has increased, the Exchange believes that Floor Brokers that previously participated in the Program would be able to achieve this proposed minimum

[4] *See* Fee Schedule, FLOOR BROKER FIXED COST PREPAYMENT INCENTIVE PROGRAM (the ''FB Prepay Program''), *available here, https://www.nyse.com/publicdocs/nyse/markets/arca-options/NYSE_Arca_Options_Fee_Schedule.pdf.*

[5] *See id.* (providing that Eligible Fixed Costs include: OTP Trading Participant Rights—Floor Broker; Floor Broker Order Capture Device- Market Data Fees; Floor Booths; Options Floor Access Fee; and Wire Services).

[6] The Percentage Growth Incentive excludes Customer volume, Firm Facilitation and Broker Dealer facilitating a Customer trades, and QCCs. Any volume calculated to achieve the Firm and Broker Dealer Monthly Fee Cap and the Limit of Fees on Options Strategy Executions, are likewise excluded from the Percentage Growth Incentive because fees on such volume is already capped and therefore does not increase billable manual volume. *See id.*

[7] *See* Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37499 (June 29, 2005) (S7–10–04) (''Reg NMS Adopting Release'').

[8] The OCC publishes options and futures volume in a variety of formats, including daily and monthly volume by exchange, *available here: https://www.theocc.com/market-data/volume/default.jsp.*

[9] Based on OCC data, *see id.,* the Exchange's market share in equity-based options declined from 9.57% for the month of January to 9.52% for the month of September.

[10] *See* proposed Fee Schedule, FLOOR BROKER FIXED COST PREPAYMENT INCENTIVE PROGRAM (the ''FB Prepay Program'') (including removing reference to specific years and adding references to Floor Brokers prepaying for the ''the following calendar year'' after committing thereto by ''the last business day of December in the current year''; being invoiced in January for Eligible Fixed Costs based on annualizing their Eligible Fixed Costs incurred in the previous November;'' and participants receiving their rebate ''in the following January.'' *See id.* For example, if a participating Floor Broker incurred $6,000 in Eligible Fixed Costs in November, that Floor Broker would be invoiced in January of the following year in the amount of $72,000 to prepay such costs for the entire year.

[11] *See* proposed Fee Schedule, FLOOR BROKER FIXED COST PREPAYMENT INCENTIVE PROGRAM (the ''FB Prepay Program''). For consistency, the Exchange would also remove reference to ''larger discounts'' as it related to the smaller 10% Discount and replace this reference with the word ''rebates.'' *See id.*

[12] *See* Fee Schedule, FLOOR BROKER FIXED COST PREPAYMENT INCENTIVE PROGRAM (the ''FB Prepay Program'').

[13] *See* proposed Fee Schedule, FLOOR BROKER FIXED COST PREPAYMENT INCENTIVE PROGRAM (the ''FB Prepay Program'').

threshold. The Exchange likewise believes it is appropriate to reduce the requisite percentage to meet the 2017 benchmark because it would make this alternative more achievable for Floor Brokers that do not meet the billable manual ADV threshold. The Exchange notes that the changes to the Program are designed to encourage those Floor Brokers that have previously enrolled in the Program to reenroll for the upcoming year as well as to attract Floor Brokers that have not yet participated.

Regardless of which benchmark a Floor Broker's growth is measured against, all Floor Brokers that aim to qualify for the Growth Incentive would be required to increase volume executed on the Exchange. The total annual rebate available for achieving each Tier would be the same regardless of whether the Floor Broker relied on the minimum (proposed) 20,000 ADV contract sides as the benchmark or 105% of the second half of 2017 volume.

The Exchange also proposes to add an option for a Floor broker to receive a fixed rebate instead of a percentage reduction of pre-paid annual fixed costs if it qualifies for the Growth Incentive. To reflect this new option, the Exchange proposes to add rule text providing that ''[e]ligible Floor Broker organizations are entitled to an annual rebate that is the greater of the 'Total Percentage Reduction of pre-paid annual Eligible Fixed Costs' or the 'Alternative Rebate' based upon the Percentage Growth Incentive Tier achieved, as set forth in the table below''.

As in prior years, the Exchange is proposing rebates based on the growth in ADV in contract sides, but proposes to modify (and make more achievable) the requisite Percentage Growth requirements to as low as 5% to achieve an annual rebate of 25% of prepaid Eligible Fixed Costs or $4,000/month, whichever is greater, to Growth Incentive as high as 150% to achieve an annual rebate of 100% Eligible Fixed Costs or $18,000/month (under new Tier 5), whichever is greater.[14] Just as the total percentage reduction increases as the Percentage Growth increases, the Exchange proposes that the annual Alternative Rebate, with fixed dollar amounts tied to each Tier, would also increase as the Percentage Growth increases. Participants that qualify for one of the Tiers would receive only the higher of the two potential rebates, paid annually.

The following table reflects the proposed changes (with deletions in brackets and new text italicized): [15]

FB PREPAYMENT PROGRAM INCENTIVES

[Based on *annual* ADV in contract sides *for the calendar year* (in 2019)]

Tier	Percentage growth incentive	Total percentage reduction of pre-paid annual eligible fixed costs [for 2019]	Alternative rebate
Tier 1	[30]*5*	[40]*25*	*$4,000/month.*
Tier 2	[65]*25*	[75]*50*	*$6,000/month.*
Tier 3	[100]*50*	[100*]*75*	*$8,000/month.*
Tier 4	*100*	*80*	*$14,000/month.*
Tier 5	*150*	*100*	*$18,000/month.*

Thus, as proposed, a participating Floor Broker would qualify for the proposed Growth Incentive by executing ADV growth in manual billable contract sides that is 5%, 25%, 50%, 100% or 150%, over the greater of (i) 20,000 contract sides ADV; or (ii) 105% of their ADV during the second half of 2017 (*i.e.,* July through December). Participants that qualify for Tiers 1, 2, 3, 4 or 5 would be eligible for 25%, 50%, 75%, 80% or 100% of their pre-paid annual Eligible Fixed costs, respectively. However, if the amount of the annual Alternative Rebate works out to be greater than the rebate available under the Growth Incentive program, the Floor Broker would be entitled to that amount.

Although this program relates to fixed costs, the Exchange believes the Program (as modified) would continue to incent Floor Brokers to increase their billable volume executed in open outcry on the Exchange, which would benefit all market participants by expanding liquidity and providing more trading opportunities, even to those market participants that have not committed to the Program. Regardless of which benchmark a participating Floor Broker's growth is measured against, all Floor Broker's that opt to participate would be required to increase volume executed on the Exchange in order to receive the enhanced discount. The Exchange cannot predict with certainty whether any Floor Brokers would avail themselves of this proposed fee change. However, all Floor brokers are eligible for this Program.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[16] in general, and furthers the objectives of Sections 6(b)(4) and (5) of the Act,[17] in particular, because it provides for the equitable allocation of reasonable dues, fees, and other charges among its members, issuers and other persons using its facilities and does not unfairly discriminate between customers, issuers, brokers or dealers.

The Proposed Rule Change Is Reasonable

The Exchange operates in a highly competitive market. The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its

[14] *See id.* The Exchange notes that new Tier 4 effectively replacing current Tier 3 in terms of growth requirement and potential rebate, as the Exchange has lowered (and made more achievable) proposed Tier 3. *See id.*

[15] Given that the annual Alternative Rebate will be available for all Tiers (and not just Tier 3 as is currently the case), the Exchange also proposes to delete the following language from the Fee Schedule as obsolete: ''*Participants in the FB Prepay Program that qualify for Tier 3 will be rebated the greater of 100% of their pre-paid annual Eligible Fixed Costs, or $10,000/month.'' *See id.*

[16] 15 U.S.C. 78f(b).

[17] 15 U.S.C. 78f(b)(4) and (5).

broader forms that are most important to investors and listed companies.'' [18]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[19] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[20]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. Stated otherwise, changes to exchange transaction fees can have a direct effect on the ability of an exchange to compete for order flow.

The Exchange believes the FB Prepay Program, as modified, is reasonable because the Program is optional and Floor Brokers can elect to participate or not. In addition, the Exchange is continuing to offer two alternative means to achieve the same enhanced rebate to ensure that Floor Brokers that are new to the Exchange (or Floor Brokers that did not execute more than 20,000 ADV in contract sides) could also participate in the Program. The Exchange believes that increasing one of the alternate requirements to 20,000 ADV is a reasonable minimum threshold above which a participating Floor Broker would need to increase volume in order to realize the proposed Growth Incentive because numerous Floor brokers exceeded this volume requirement in 2019, even though it was not required. Because Floor Brokers are already performing at this level, the Exchange believes it is reasonable to adjust the eligibility requirement for the Growth Incentive to match current performance levels. Having demonstrated an ability to meet this higher volume threshold, the Exchange is seeking to encourage Floor Brokers to sustain this volume threshold throughout the year. The Exchange also believes it is reasonable to use each Floor Broker's historical volume in the second half of 2017 as a benchmark against which to measure future growth to achieve the proposed Growth Incentive, and to lower from 110% to 105% the requisite increase over the Floor Broker's 2017 volume, because it makes the Growth Incentive more achievable and provides an opportunity for more Floor Brokers to qualify for the Growth Incentive Program.

The Exchange further believes that the proposed changes to add more tiers to the Growth Incentive is reasonable because it will provide greater opportunities to Floor Brokers to be eligible for one of the two rebates by providing lower thresholds to qualify. Overall, the proposed changes to the Growth Incentive program are designed to make the existing Tiers more achievable while adding new Tiers 4 and 5 to encourage increased executions by Floor Brokers on the Exchange, which activity (even with lower volume thresholds) would benefit all market participants.

The Exchange also believes it is reasonable to provide an annual alternative fixed rebate because it provides an option for Floor brokers to earn the higher of the percentage reduction rebate, or the fixed-rebate amount.

Moreover, the FB Prepay Program provides Floor Brokers the opportunity to receive rebates on its Eligible Fixed Costs that they otherwise would not receive, based on trading activity. Such rebates may encourage Floor Brokers to increase their billable volume executed in open outcry on the Exchange, which would benefit all market participants by expanding liquidity and providing more trading opportunities, even to non-Floor Broker market participants (including participating Floor Brokers who do not hit the volume thresholds).

Finally, to the extent the proposed change continues to attract greater volume and liquidity to the Exchange (including to the Floor), the Exchange believes the proposed change would improve the Exchange's overall competitiveness and strengthen its market quality for all market participants. In the backdrop of the competitive environment in which the Exchange operates, the proposed rule change is a reasonable attempt by the Exchange to increase the depth of its market and improve its market share relative to its competitors.

The Exchange cannot predict with certainty whether any Floor Brokers would avail themselves of this proposed fee change. However, all Floor brokers are eligible to participate in the Program.

The Proposed Rule Change Is an Equitable Allocation of Credits and Fees

The Exchange believes the proposed rule change is an equitable allocation of its fees and credits. The proposal is based on the amount and type of business transacted on the Exchange and Floor Brokers can opt to avail themselves of the Program or not, and to attempt to trade sufficient volume to achieve one of the Tiers, or not. All participating Floor Brokers have the ability to qualify for the same enhanced rebate under two alternatives means offered (*i.e.,* the greater of at least 20,000 contract sides in billable ADV or 105% of the Floor Broker's total billable manual ADV in the second half of 2017). The Exchange notes that the changes to the Program are designed to encourage those Floor Brokers that have previously enrolled in the Program to reenroll for the upcoming year as well as to attract Floor Brokers that have not yet participated.

Moreover, the proposed change applies to qualifying Floor Brokers equally and because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support.

To the extent that the proposed change continues to attract more participation in the programs of the Exchange, the increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to the Exchange thereby improving market-wide quality and price discovery.

The Proposed Rule Change Is Not Unfairly Discriminatory

The Exchange believes it is not unfairly discriminatory to modify the FB Prepayment program because the proposed modification would be available to all similarly-situated Floor Brokers on an equal and non-discriminatory basis.

The proposed modified Program is not unfairly discriminatory to non-Floor Brokers because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support. To the extent that the proposed change continues to

[18] *See* Reg NMS Adopting Release, *supra* note 7, at 37499.

[19] *See supra* note 8.

[20] Based on OCC data, *see supra* note 9, in 2019, the Exchange's market share in equity-based options declined from 9.57% for the month of January to 9.23% for the month of September.

attract more participation in the programs of the Exchange, the increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to the Exchange thereby improving market-wide quality and price discovery.

Moreover, the proposal is based on the amount and type of business transacted on the Exchange and Floor Broker organizations are not obligated to participate in the Program and, if they do, they are not obligated to try to achieve any of the Tiers.

To the extent that the proposed change attracts a variety of transactions to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to (the Floor of) the Exchange thereby improving market-wide quality and price discovery. The resulting increased volume and liquidity would provide more trading opportunities and tighter spreads to all market participants and thus would promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest.

Finally, the Exchange believes that it is subject to significant competitive forces, as described below in the Exchange's statement regarding the burden on competition.

B. Self-Regulatory Organization's Statement on Burden on Competition

In accordance with Section 6(b)(8) of the Act, the Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Instead, as discussed above, the Exchange believes that the proposed changes would encourage the submission of additional liquidity to a public exchange, thereby promoting market depth, price discovery and transparency and enhancing order execution opportunities for all market participants. As a result, the Exchange believes that the proposed change furthers the Commission's goal in adopting Regulation NMS of fostering integrated competition among orders, which promotes ''more efficient pricing of individual stocks for all types of orders, large and small.'' [21]

Intramarket Competition. The Exchange believes the proposed Program, as modified, should continue to encourage order flow to be directed to the (Floor of the) Exchange, which would enhance the quality of quoting and may increase the volumes of contracts trade on the Exchange. To the extent that there is an additional competitive burden on non-Floor Brokers, the Exchange believes that this is appropriate because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support.

To the extent that this function is achieved, all of the Exchange's market participants should benefit from the improved market liquidity. Enhanced market quality and increased transaction volume that results from the anticipated increase in order flow directed to the Exchange will benefit all market participants and improve competition on the Exchange.

Intermarket Competition. The Exchange believes that the proposed change could promote competition between the Exchange and other execution venues, by encouraging additional orders to be sent to the (Floor of the) Exchange for execution. The proposed adjustments to the Program are designed to make the incentives more achievable and to continue to encourage Floor Brokers to execute orders on the Floor of the Exchange, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads.

Given the robust competition for volume among options markets, many of which offer the same products, implementing programs to attract order flow, such as the proposed modification to the FB Prepayment Program, are consistent with the above-mentioned goals of the Act.

The Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues. In such an environment, the Exchange must continually review, and consider adjusting, its fees and credits to remain competitive with other exchanges. For the reasons described above, the Exchange believes that the proposed rule change reflects this competitive environment.

[21] *See* Reg NMS Adopting Release, *supra* note 7, at 37499.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change is effective upon filing pursuant to Section 19(b)(3)(A) [22] of the Act and subparagraph (f)(2) of Rule 19b–4 [23] thereunder, because it establishes a due, fee, or other charge imposed by the Exchange.

At any time within 60 days of the filing of such proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings under Section 19(b)(2)(B) [24] of the Act to determine whether the proposed rule change should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's internet comment form (*http://www.sec.gov/rules/sro.shtml*); or
- Send an email to *rule-comments@sec.gov.* Please include File Number SR–NYSEArca–2020–04 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090.

All submissions should refer to File Number SR–NYSEArca–2020–04. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (*http://www.sec.gov/*

[22] 15 U.S.C. 78s(b)(3)(A).

[23] 17 CFR 240.19b–4(f)(2).

[24] 15 U.S.C. 78s(b)(2)(B).

rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–NYSEArca–2020–04, and should be submitted on or before February 3, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[25]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–00262 Filed 1–10–20; 8:45 am]

BILLING CODE 8011–01–P

[25] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 33742; File No. 812–14940]

Kayne Anderson MLP/Midstream Investment Company, et al.

January 8, 2020.

AGENCY: Securities and Exchange Commission (''Commission'').

ACTION: Notice.

Notice of application for an order under sections 17(d) and 57(i) of the Investment Company Act of 1940 (the ''Act'') and rule 17d–1 under the Act to permit certain joint transactions otherwise prohibited by sections 17(d) and 57(a)(4) of the Act and rule 17d–1 under the Act.

SUMMARY OF APPLICATION: Applicants request an order to permit certain business development companies (''BDCs'') and closed-end management investment companies to co-invest in portfolio companies with each other and with certain affiliated investment funds and accounts.

APPLICANTS: Kayne Anderson MLP/Midstream Investment Company (''KYN''), Kayne Anderson Midstream/Energy Fund, Inc. (''KMF''), Kayne Anderson BDC, LLC (''KA BDC''), Kayne Anderson Income Strategies Fund (''KIF''), KA Credit Advisors, LLC (''KA Credit''), KA Fund Advisors, LLC (''KAFA''), Kayne Anderson Capital Advisors, L.P. (''KACALP''), Kayne Anderson Fund Advisors, LLC (''KAFAII''), Kayne Solutions Manager, L.P. (''KSM''), Kayne KS Credit GP, LLC (''KKSC''), Kayne Anderson Real Estate Debt Advisors III, LLC (''KAREDA''), Kayne Senior Credit III Manager, L.P. (''KSCIIIM''), Kayne Senior Credit IV Manager, L.P. (''KSCIVM'' and together with KA Credit, KAFA, KACALP, KAFAII, KSM, KKSC, KAREDA and KSCIIIM, the ''Existing Advisers''), Kayne Anderson Capital Income Partners (QP), L.P., Kayne Anderson Income Partners, L.P., Kayne Anderson Infrastructure Income Fund, L.P., Kayne Anderson Midstream Institutional Fund, L.P., Kayne Anderson MLP Fund, L.P., Kayne Anderson Real Assets Fund, L.P., Kayne Equity Yield Strategies, L.P., Kayne Global Infrastructure Fund, L.P., Kayne Renewable Energy Income Fund, L.P., KA Special K, L.P., Kayne Simplified Midstream, L.P., Kayne Anderson Real Estate Debt III, L.P., Kayne Senior Credit Fund III, L.P., Kayne Senior Credit III Offshore Fund, L.P., Kayne KS Credit Fund, L.P., Kayne Solutions Fund, L.P., Kayne Solutions Offshore Fund, L.P., Kayne Multiple Strategy Fund, L.P., KANTI (QP), L.P., Kayne Anderson Non-Traditional Investments, L.P., KARBO, L.P., Kayne Liquid Credit Fund, L.P., Kayne Solutions Mini-Master Fund, L.P., Kayne Senior Credit Funding III, LLC, Kayne Senior Credit Funding III Offshore, LLC, Kayne Senior Credit III Mini-Master Fund, L.P., Kayne Senior Credit Fund IV, L.P., Kayne Senior Credit IV Mini-Master Fund, L.P. and Kayne Senior Credit IV Offshore Fund, L.P. (together, ''Applicants'').

FILING DATES: The application was filed on August 15, 2018, and amended on April 3, 2019, July 1, 2019, September 6, 2019, November 15, 2019, and January 7, 2020.

HEARING OR NOTIFICATION OF HEARING: An order granting the requested relief will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on February 3, 2020, and should be accompanied by proof of service on applicants, in the form of an affidavit or, for lawyers, a certificate of service. Pursuant to rule 0–5 under the Act, hearing requests should state the nature of the writer's interest, any facts bearing upon the desirability of a hearing on the matter, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

ADDRESSES: Secretary, U.S. Securities and Exchange Commission, 100 F St. NE, Washington, DC 20549–1090. Applicants: 1800 Avenue of the Stars, Third Floor, Los Angeles, CA 90067.

FOR FURTHER INFORMATION CONTACT: Laura L. Solomon, Senior Counsel, at (202) 551–6915 or Kaitlin C. Bottock, Branch Chief, at (202) 551–6825 (Chief Counsel's Office, Division of Investment Management).

SUPPLEMENTARY INFORMATION: The following is a summary of the application. The complete application may be obtained via the Commission's website by searching for the file number, or for an applicant using the Company name box, at *http://www.sec.gov/search/search.htm* or by calling (202) 551–8090.

Introduction

1. The applicants request an order of the Commission under sections 17(d) and 57(i) and rule 17d–1 thereunder (the ''Order'') to permit, subject to the terms and conditions set forth in the application (the ''Conditions''), a Regulated Fund [1] and one or more other Regulated Funds and/or one or more Affiliated Funds [2] to enter into Co-

[1] ''Regulated Funds'' means KYN, KMF, KA BDC, KIF, the Future Regulated Funds and the BDC Downstream Funds (defined below). ''Future Regulated Fund'' means a closed-end management investment company (a) that is registered under the Act or has elected to be regulated as a BDC, (b) whose investment adviser is an Adviser, and (c) intends to participate in the Co-investment Program.

''Adviser'' means the Existing Advisers, including the Existing Relying Advisers (identified in Schedule B to the application), together with any future investment adviser that (i) controls, is controlled by or is under common control with KA Credit, KAFA, KACALP, or KAFAII, as applicable, (ii)(a) is registered as an investment adviser under the Investment Advisers Act of 1940 (''Advisers Act''), or (b) is a relying adviser of an investment adviser that is registered under the Advisers Act and that controls, is controlled by or is under common control with KA Credit, KAFA, KACALP or KAFAII, and (iii) is not a Regulated Fund or a subsidiary of a Regulated Fund.

[2] ''Affiliated Fund'' means any Existing Affiliated Fund (identified in Schedule A to the application), any Future Affiliated Fund, Existing KA Proprietary

Investment Transactions with each other. ''Co-Investment Transaction'' means any transaction in which a Regulated Fund (or its Wholly-Owned Investment Sub) participated together with one or more Affiliated Funds and/or one or more other Regulated Funds in reliance on the Order. Potential Co-Investment Transaction'' means any investment opportunity in which a Regulated Fund (or its Wholly-Owned Investment Sub) could not participate together with one or more Affiliated Funds and/or one or more other Regulated Funds (or its Wholly-Owned Investment Sub) without obtaining and relying on the Order.[3]

Applicants

2. KYN is a closed-end registered investment company incorporated in Maryland. KYN's Board[4] currently consists of eight directors, six of whom are Independent Directors.[5]

3. KMF is a closed-end registered investment company incorporated in Maryland. KMF's Board currently consists of eight directors, six of whom are Independent Directors.

4. KIF is a closed-end registered investment company and a Maryland statutory trust. KIF's Board currently consists of two directors.

5. KA BDC, a Delaware limited liability company, is an Affiliated Fund that intends to elect to be regulated as a BDC under the Act.[6] KA BDC's Board is comprised currently of one director.

6. KA Credit, a Delaware limited liability company that intends to register under the Advisers Act, would serve as the investment adviser to KA BDC and would serve as investment adviser to Future Regulated Funds that elected to be regulated as BDCs. KAFA, a Delaware limited liability company that is registered as an investment adviser under the Advisers Act, serves as investment adviser to each of KYN and KMF and certain Existing Affiliated Funds. KACALP a California limited partnership that is registered as an investment adviser under the Advisers Act, serves as investment adviser to certain of the Existing Affiliated Funds. KAFAII, a Delaware limited liability company that intends to register as an investment adviser under the Advisers Act, will serve as the investment adviser to KIF. KA Credit, KAFA, KACALP and KAFAII and their direct and indirect wholly or majority owned subsidiaries may hold various financial assets in a principal capacity (the ''Existing KA Proprietary Accounts'' and together with any Future KA Proprietary Account, the ''KA Proprietary Accounts'').

7. The Existing Affiliated Funds are the investment funds identified in Schedule A to the application. Applicants represent that each Existing Affiliated Fund is a separate and distinct legal entity and each would be an investment company but for section 3(c)(1) or 3(c)(7) of the Act or relies on rule 3a–7 under the Act.

8. The Existing Relying Advisers, identified in Schedule B to the application, each of which is a relying adviser of KAFA and/or KACALP serve as investment advisers for certain of the Existing Affiliated Funds.

9. Applicants state that a Regulated Fund may, from time to time, form one or more Wholly-Owned Investment Subs.[7] Such a subsidiary may be prohibited from investing in a Co-Investment Transaction with a Regulated Fund (other than its parent) or any Affiliated Fund because it would be a company controlled by its parent Regulated Fund for purposes of section 57(a)(4) and rule 17d–1. Applicants request that each Wholly-Owned Investment Sub be permitted to participate in Co-Investment Transactions in lieu of the Regulated Fund that owns it and that the Wholly-Owned Investment Sub's participation in any such transaction be treated, for purposes of the Order, as though the parent Regulated Fund were participating directly.

Applicants' Representations

A. Allocation Process

10. Applicants state that the Advisers are presented with numerous investment opportunities each year on behalf of their clients and must determine how to allocate those opportunities in a manner that, over time, is fair and equitable to all of their clients. Such investment opportunities may be Potential Co-Investment Transactions.

11. Applicants represent that they have established processes for allocating initial investment opportunities, opportunities for subsequent investments in an issuer and dispositions of securities holdings reasonably designed to treat all clients fairly and equitably. Further, applicants represent that these processes will be extended and modified in a manner reasonably designed to ensure that the additional transactions permitted under the Order will both (i) be fair and equitable to the Regulated Funds and the Affiliated Funds and (ii) comply with the Conditions.

12. Specifically, applicants state that the Advisers are organized and managed such that portfolio management teams (''Investment Teams''), responsible for evaluating investment opportunities and making investment decisions on behalf of clients are promptly notified of the opportunities. If the requested Order is granted, the Advisers will establish, maintain and implement policies and procedures reasonably designed to ensure that, when such opportunities arise, the Advisers to the relevant

Account, and Future KA Proprietary Account (each, as defined below). ''Future Affiliated Fund'' means any entity (a) whose investment adviser is an Adviser, (b) that either (i) would be an investment company but for section 3(c)(1), 3(c)(5)(C) or 3(c)(7) of the Act or (ii) relies on rule 3a–7 under the Act, (c) that intends to participate in the Co-Investment Program, and (d) that is not a BDC Downstream Fund. Applicants represent that no Existing Affiliated Fund is a BDC Downstream Fund. ''Future KA Proprietary Account'' means any direct or indirect, wholly- or majority-owned subsidiary of KACALP, or any other Adviser, that is formed in the future that, from time to time, may hold various financial assets in a principal capacity.

''BDC Downstream Fund'' means, with respect to any Regulated Fund that is a BDC, an entity (i) that the BDC directly or indirectly controls, (ii) that is not controlled by any person other than the BDC (except a person that indirectly controls the entity solely because it controls the BDC), (iii) that would be an investment company but for section 3(c)(1) or 3(c)(7) of the Act, (iv) whose investment adviser is an Adviser, and (v) that is not a Wholly-Owned Investment Sub (as defined below).

[3] All existing entities that currently intend to rely on the Order have been named as applicants and any existing or future entities that may rely on the Order in the future will comply with its terms and Conditions set forth in the application.

[4] ''Board'' means (i) with respect to a Regulated Fund other than a BDC Downstream Fund, the board of directors (or the equivalent) of the Regulated Fund and (ii) with respect to a BDC Downstream Fund, the Independent Party of the BDC Downstream Fund.

''Independent Party'' means, with respect to a BDC Downstream Fund, (i) if the BDC Downstream Fund has a board of directors (or the equivalent), the board or (ii) if the BDC Downstream Fund does not have a board of directors (or the equivalent), a transaction committee or advisory committee of the BDC Downstream Fund.

[5] ''Independent Director'' means a member of the Board of any relevant entity who is not an ''interested person'' as defined in 2(a)(19) of the Act. No Independent Director of a Regulated Fund (including any non-interested member of an Independent Party) will have a financial interest in any Co-Investment Transaction, other than indirectly through share ownership in one of the Regulated Funds.

[6] Section 2(a)(48) defines a BDC to be any closed-end investment company that operates for the purpose of making investments in securities described in section 55(a)(1) through 55(a)(3) and makes available significant managerial assistance with respect to the issuers of such securities.

[7] ''Wholly-Owned Investment Sub'' means an entity (i) that is wholly-owned by KA BDC or a Future Regulated Fund (with such Regulated Fund at all times holding, beneficially and of record, 100% of the voting and economic interests); (ii) whose sole business purpose is to hold one or more investments on behalf of such Regulated Fund; (iii) with respect to which such Regulated Fund's Board has the sole authority to make all determinations with respect to the entity's participation under the Conditions; and (iv) that would be an investment company but for section 3(c)(1) or 3(c)(7) of the Act.

Regulated Funds are promptly notified and receive the same information about the opportunity as any other Advisers considering the opportunity for their clients. In particular, consistent with Condition 1, if a Potential Co-Investment Transaction falls within the then-current Objectives and Strategies [8] and any Board-Established Criteria [9] of a Regulated Fund, the policies and procedures will require that the relevant Investment Team responsible for that Regulated Fund receive sufficient information to allow the Regulated Fund's Adviser to make its independent determination and recommendations under the Conditions.

13. The Adviser to each applicable Regulated Fund will then make an independent determination of the appropriateness of the investment for the Regulated Fund in light of the Regulated Fund's then-current circumstances. If the Adviser to a Regulated Fund deems the Regulated Fund's participation in such Potential Co-Investment Transaction to be appropriate, then it will formulate a recommendation regarding the proposed order amount for the Regulated Fund.

14. Applicants state that, for each Regulated Fund and Affiliated Fund whose Adviser recommends participating in a Potential Co-Investment Transaction, the applicable Investment Team will approve the investment and the investment amount. Applicants state further that the applicable Investment Team will notify the allocation committee that coordinates and facilitates an order submission process with a designated representative of each applicable Investment Team of a Regulated Fund and Affiliated Fund to the extent such investment is consistent with its Board-Established Criteria and/or falls within its then-current Objectives and Strategies. Prior to the External Submission (as defined below), each proposed order or investment amount may be reviewed and adjusted, in accordance with the applicable Advisers' written allocation policies and procedures, by both the allocation committee, consisting of legal, compliance, and operations personnel and/or applicable Investment Team of the Adviser (*e.g.,* public energy companies, or direct lending).[10] The order of a Regulated Fund or Affiliated Fund resulting from this process is referred to as its ''Internal Order.'' The Internal Order will be submitted for approval by the Required Majority of any participating Regulated Funds in accordance with the Conditions.[11]

15. If the aggregate Internal Orders for a Potential Co-Investment Transaction do not exceed the size of the investment opportunity immediately prior to the submission of the orders to the underwriter, broker, dealer or issuer, as applicable (the ''External Submission''), then each Internal Order will be fulfilled as placed. If, on the other hand, the aggregate Internal Orders for a Potential Co-Investment Transaction exceed the size of the investment opportunity immediately prior to the External Submission, then the allocation of the opportunity will be made pro rata on the basis of the size of the Internal Orders.[12] If, subsequent to such External Submission, the size of the opportunity is increased or decreased, or if the terms of such opportunity, or the facts and circumstances applicable to the Regulated Funds' or the Affiliated Funds' consideration of the opportunity, change, the participants will be permitted to submit revised Internal Orders in accordance with written allocation policies and procedures that the Advisers will establish, implement and maintain.[13]

B. Follow-On Investments

16. Applicants state that from time to time the Regulated Funds and Affiliated Funds may have opportunities to make Follow-On Investments [14] in an issuer in which a Regulated Fund and one or more other Regulated Funds and/or Affiliated Funds previously have invested.

17. Applicants propose that Follow-On Investments would be divided into two categories depending on whether the prior investment was a Co-Investment Transaction or a Pre-Boarding Investment.[15] If the Regulated Funds and Affiliated Funds had previously participated in a Co-Investment Transaction with respect to the issuer, then the terms and approval of the Follow-On Investment would be subject to the Standard Review Follow-Ons described in Condition 8. If the Regulated Funds and Affiliated Funds

[8] ''Objectives and Strategies'' means (i) with respect to any Regulated Fund other than a BDC Downstream Fund, its investment objectives and strategies, as described in its most current registration statement on Form N–2, other current filings with the Commission under the Securities Act of 1933 (the ''Securities Act'') or under the Securities Exchange Act of 1934, as amended, and its most current report to stockholders, and (ii) with respect to any BDC Downstream Fund, those investment objectives and strategies described in its disclosure documents (including private placement memoranda and reports to equity holders) and organizational documents (including operating agreements).

[9] ''Board-Established Criteria'' means criteria that the Board of a Regulated Fund may establish from time to time to describe the characteristics of Potential Co-Investment Transactions regarding which the Adviser to the Regulated Fund should be notified under Condition 1. The Board-Established Criteria will be consistent with the Regulated Fund's Objectives and Strategies. If no Board-Established Criteria are in effect, then the Regulated Fund's Adviser will be notified of all Potential Co-Investment Transactions that fall within the Regulated Fund's then-current Objectives and Strategies. Board-Established Criteria will be objective and testable, meaning that they will be based on observable information, such as industry/sector of the issuer, minimum EBITDA of the issuer, asset class of the investment opportunity or required commitment size, and not on characteristics that involve a discretionary assessment. The Adviser to the Regulated Fund may from time to time recommend criteria for the Board's consideration, but Board-Established Criteria will only become effective if approved by a majority of the Independent Directors. The Independent Directors of a Regulated Fund may at any time rescind, suspend or qualify its approval of any Board-Established Criteria, though applicants anticipate that, under normal circumstances, the Board would not modify these criteria more often than quarterly.

[10] The reason for any such adjustment to a proposed order amount will be documented in writing and preserved in the records of the Advisers.

[11] ''Required Majority'' means a required majority, as defined in section 57(o) of the Act. In the case of a Regulated Fund that is a registered closed-end fund, the Board members that make up the Required Majority will be determined as if the Regulated Fund were a BDC subject to section 57(o). In the case of a BDC Downstream Fund with a board of directors (or the equivalent), the members that make up the Required Majority will be determined as if the BDC Downstream Fund were a BDC subject to section 57(o). In the case of a BDC Downstream Fund with a transaction committee or advisory committee, the committee members that make up the Required Majority will be determined as if the BDC Downstream Fund were a BDC subject to section 57(o) and as if the committee members were directors of the fund.

[12] The Advisers will maintain records of all proposed order amounts, Internal Orders and External Submissions in conjunction with Potential Co-Investment Transactions. Each applicable Adviser will provide the Eligible Directors with information concerning the Affiliated Funds' and Regulated Funds' order sizes to assist the Eligible Directors with their review of the applicable Regulated Fund's investments for compliance with the Conditions.

''Eligible Directors'' means, with respect to a Regulated Fund and a Potential Co-Investment Transaction, the members of the Regulated Fund's Board eligible to vote on that Potential Co-Investment Transaction under section 57(o) of the Act (treating any registered investment company or series thereof as a BDC for this purpose).

[13] The Board of the Regulated Fund will then either approve or disapprove of the investment opportunity in accordance with Condition 2, 6, 7, 8 or 9, as applicable.

[14] ''Follow-On Investment'' means an additional investment in the same issuer, including, but not limited to, through the exercise of warrants, conversion privileges or other rights to purchase securities of the issuer.

[15] ''Pre-Boarding Investments'' are investments in an issuer held by a Regulated Fund as well as one or more Affiliated Funds and/or one or more other Regulated Funds that were acquired prior to participating in any Co-Investment Transaction: (i) In transactions in which the only term negotiated by or on behalf of such funds was price in reliance on one of the JT No-Action Letters (defined below); or (ii) in transactions occurring at least 90 days apart and without coordination between the Regulated Fund and any Affiliated Fund or other Regulated Fund.

have not previously participated in a Co-Investment Transaction with respect to the issuer but hold a Pre-Boarding Investment, then the terms and approval of the Follow-On Investment would be subject to the Enhanced-Review Follow-Ons described in Condition 9. All Enhanced Review Follow-Ons require the approval of the Required Majority. For a given issuer, the participating Regulated Funds and Affiliated Funds would need to comply with the requirements of Enhanced-Review Follow-Ons only for the first Co-Investment Transaction. Subsequent Co-Investment Transactions with respect to the issuer would be governed by the requirements of Standard Review Follow-Ons.

18. A Regulated Fund would be permitted to invest in Standard Review Follow-Ons either with the approval of the Required Majority under Condition 8(c) or without Board approval under Condition 8(b) if it is (i) a Pro Rata Follow-On Investment [16] or (ii) a Non-Negotiated Follow-On Investment.[17] Applicants believe that these Pro Rata and Non-Negotiated Follow-On Investments do not present a significant opportunity for overreaching on the part of any Adviser and thus do not warrant the time or the attention of the Board. Pro Rata Follow-On Investments and Non-Negotiated Follow-On Investments remain subject to the Board's periodic review in accordance with Condition 10.

C. Dispositions

19. Applicants propose that Dispositions [18] would be divided into two categories. If the Regulated Funds and Affiliated Funds holding investments in the issuer had previously participated in a Co-Investment Transaction with respect to the issuer, then the terms and approval of the Disposition would be subject to the Standard Review Dispositions described in Condition 6. If the Regulated Funds and Affiliated Funds have not previously participated in a Co-Investment Transaction with respect to the issuer but hold a Pre-Boarding Investment, then the terms and approval of the Disposition would be subject to the Enhanced Review Dispositions described in Condition 7. Subsequent Dispositions with respect to the same issuer would be governed by Condition 6 under the Standard Review Dispositions.[19]

20. A Regulated Fund may participate in a Standard Review Disposition either with the approval of the Required Majority under Condition 6(d) or without Board approval under Condition 6(c) if (i) the Disposition is a Pro Rata Disposition [20] or (ii) the securities are Tradable Securities [21] and the Disposition meets the other requirements of Condition 6(c)(ii). Pro Rata Dispositions and Dispositions of a Tradable Security remain subject to the Board's periodic review in accordance with Condition 10.

D. Delayed Settlement

21. Applicants represent that under the terms and Conditions of the application, all Regulated Funds and Affiliated Funds participating in a Co-Investment Transaction will invest at the same time, for the same price and with the same terms, conditions, class, registration rights and any other rights, so that none of them receives terms more favorable than any other. However, the settlement date for an Affiliated Fund in a Co-Investment Transaction may occur up to ten business days after the settlement date for the Regulated Fund, and vice versa. Nevertheless, in all cases, (i) the date on which the commitment of the Affiliated Funds and Regulated Funds is made will be the same even where the settlement date is not and (ii) the earliest settlement date and the latest settlement date of any Affiliated Fund or Regulated Fund participating in the transaction will occur within ten business days of each other.

E. Holders

22. Under Condition 15, if an Adviser, its principals, or any person controlling, controlled by, or under common control with the Adviser or its principals, and the Affiliated Funds (collectively, the ''Holders'') own in the aggregate more than 25 percent of the outstanding voting shares of a Regulated Fund (the ''Shares''), then the Holders will vote such Shares as directed by an independent third party when voting on matters specified in the Condition. Applicants believe that this Condition will ensure that the Independent Directors will act independently in evaluating Co-Investment Transactions, because the ability of the Adviser or its principals to influence the Independent Directors by a suggestion, explicit or implied, that the Independent Directors can be removed will be limited significantly. The Independent Directors shall evaluate and approve any independent party, taking into account

[16] A ''Pro Rata Follow-On Investment'' is a Follow-On Investment (i) in which the participation of each Affiliated Fund and each Regulated Fund is proportionate to its outstanding investments in the issuer or security, as appropriate, immediately preceding the Follow-On Investment, and (ii) in the case of a Regulated Fund, a majority of the Board has approved the Regulated Fund's participation in the pro rata Follow-On Investments as being in the best interests of the Regulated Fund. The Regulated Fund's Board may refuse to approve, or at any time rescind, suspend or qualify, its approval of Pro Rata Follow-On Investments, in which case all subsequent Follow-On Investments will be submitted to the Regulated Fund's Eligible Directors in accordance with Condition 8(c).

[17] A ''Non-Negotiated Follow-On Investment'' is a Follow-On Investment in which a Regulated Fund participates together with one or more Affiliated Funds and/or one or more other Regulated Funds (i) in which the only term negotiated by or on behalf of the funds is price and (ii) with respect to which, if the transaction were considered on its own, the funds would be entitled to rely on one of the JT No-Action Letters.

''JT No-Action Letters'' means SMC Capital, Inc., SEC No-Action Letter (pub. avail. Sept. 5, 1995), Massachusetts Mutual Life Insurance Company, SEC No-Action Letter (pub. avail. June 7, 2000) and Massachusetts Mutual Life Insurance Company, SEC No-Action Letter (pub. avail. July 28, 2000).

[18] ''Disposition'' means the sale, exchange or other disposition of an interest in a security of an issuer.

[19] However, with respect to an issuer, if a Regulated Fund's first Co-Investment Transaction is an Enhanced Review Disposition, and the Regulated Fund does not dispose of its entire position in the Enhanced Review Disposition, then before such Regulated Fund may complete its first Standard Review Follow-On in such issuer, the Eligible Directors must review the proposed Follow-On Investment not only on a stand-alone basis but also in relation to the total economic exposure in such issuer (*i.e.,* in combination with the portion of the Pre-Boarding Investment not disposed of in the Enhanced Review Disposition), and the other terms of the investments. This additional review would be required because such findings would not have been required in connection with the prior Enhanced Review Disposition, but they would have been required had the first Co-Investment Transaction been an Enhanced Review Follow-On.

[20] A ''Pro Rata Disposition'' is a Disposition (i) in which the participation of each Affiliated Fund and each Regulated Fund is proportionate to its outstanding investment in the security subject to Disposition immediately preceding the Disposition; and (ii) in the case of a Regulated Fund, a majority of the Board has approved the Regulated Fund's participation in pro rata Dispositions as being in the best interests of the Regulated Fund. The Regulated Fund's Board may refuse to approve, or at any time rescind, suspend or qualify, its approval of Pro Rata Dispositions, in which case all subsequent Dispositions will be submitted to the Regulated Fund's Eligible Directors.

[21] ''Tradable Security'' means a security that meets the following criteria at the time of Disposition: (i) It trades on a national securities exchange or designated offshore securities market as defined in rule 902(b) under the Securities Act; (ii) it is not subject to restrictive agreements with the issuer or other security holders; and (iii) it trades with sufficient volume and liquidity (findings as to which are documented by the Advisers to any Regulated Funds holding investments in the issuer and retained for the life of the Regulated Fund) to allow each Regulated Fund to dispose of its entire position remaining after the proposed Disposition within a short period of time not exceeding 30 days at approximately the value (as defined by section 2(a)(41) of the Act) at which the Regulated Fund has valued the investment.

its qualifications, reputation for independence, cost to the shareholders, and other factors that they deem relevant.

Applicants' Legal Analysis

1. Section 17(d) of the Act and rule 17d–1 under the Act prohibit participation by a registered investment company and an affiliated person in any ''joint enterprise or other joint arrangement or profit-sharing plan,'' as defined in the rule, without prior approval by the Commission by order upon application. Section 17(d) of the Act and rule 17d–1 under the Act are applicable to Regulated Funds that are registered closed-end investment companies.

2. Similarly, with regard to BDCs, section 57(a)(4) of the Act generally prohibits certain persons specified in section 57(b) from participating in joint transactions with the BDC or a company controlled by the BDC in contravention of rules as prescribed by the Commission. Section 57(i) of the Act provides that, until the Commission prescribes rules under section 57(a)(4), the Commission's rules under section 17(d) of the Act applicable to registered closed–end investment companies will be deemed to apply to transactions subject to section 57(a)(4). Because the Commission has not adopted any rules under section 57(a)(4), rule 17d–1 also applies to joint transactions with Regulated Funds that are BDCs.

3. Co-Investment Transactions are prohibited by either or both of rule 17d–1 and section 57(a)(4) without a prior exemptive order of the Commission to the extent that the Affiliated Funds and the Regulated Funds participating in such transactions fall within the category of persons described by rule 17d–1 and/or section 57(b), as applicable, vis-à-vis each participating Regulated Fund. Each of the participating Regulated Funds and Affiliated Funds may be deemed to be affiliated persons vis-à-vis a Regulated Fund within the meaning of section 2(a)(3) by reason of common control because (i) the Existing Advisers to Affiliated Funds manage, and may be deemed to control, each of the Existing Affiliated Funds and any other Affiliated Fund will be managed by, and may be deemed to be controlled by an Adviser to Affiliated Funds; (ii) KACALP is the investment adviser to, and may be deemed to control, various Affiliated Funds and KACALP controls the other Existing Advisers to Regulated Funds, and may be deemed to control any Future Regulated Fund, (iii) each BDC Downstream Fund will be deemed to be controlled by its BDC parent and/or its BDC parent's investment adviser; and (iv) the Advisers to Affiliated Funds and the Advisers to Regulated Funds are under common control. Thus, each of the Affiliated Funds could be deemed to be a person related to the Regulated Funds, including any BDC Downstream Fund, in a manner described by section 57(b) and related to the other Regulated Funds in a manner described by rule 17d–1; and therefore the prohibitions of rule 17d–1 and section 57(a)(4) would apply respectively to prohibit the Affiliated Funds from participating in Co-Investment Transactions with the Regulated Funds. In addition, because the KA Proprietary Accounts are controlled by KACALP and, therefore, may be under common control with the Existing Advisers other than KACALP, any future Advisers, and any Future Regulated Funds, the KA Proprietary Accounts could be deemed to be persons related to the Regulated Funds (or a company controlled by the Regulated Funds) in a manner described by section 57(b) and also prohibited from participating in the Co-Investment Program.

4. In passing upon applications under rule 17d–1, the Commission considers whether the company's participation in the joint transaction is consistent with the provisions, policies, and purposes of the Act and the extent to which such participation is on a basis different from or less advantageous than that of other participants.

5. Applicants state that in the absence of the requested relief, in many circumstances the Regulated Funds would be limited in their ability to participate in attractive and appropriate investment opportunities. Applicants state that, as required by rule 17d–1(b), the Conditions ensure that the terms on which Co-Investment Transactions may be made will be consistent with the participation of the Regulated Funds being on a basis that it is neither different from nor less advantageous than other participants, thus protecting the equity holders of any participant from being disadvantaged. Applicants further state that the Conditions ensure that all Co-Investment Transactions are reasonable and fair to the Regulated Funds and their shareholders and do not involve overreaching by any person concerned, including the Advisers. Applicants state that the Regulated Funds' participation in the Co-Investment Transactions in accordance with the Conditions will be consistent with the provisions, policies, and purposes of the Act and would be done in a manner that is not different from, or less advantageous than, that of other participants.

Applicants' Conditions

Applicants agree that the Order will be subject to the following Conditions:

1. *Identification and Referral of Potential Co-Investment Transactions.*

(a) The Advisers will establish, maintain and implement policies and procedures reasonably designed to ensure that each Adviser is promptly notified of all Potential Co-Investment Transactions that fall within the then-current Objectives and Strategies and Board–Established Criteria of any Regulated Fund the Adviser manages.

(b) When an Adviser to a Regulated Fund is notified of a Potential Co-Investment Transaction under Condition 1(a), the Adviser will make an independent determination of the appropriateness of the investment for the Regulated Fund in light of the Regulated Fund's then-current circumstances.

2. *Board Approvals of Co-Investment Transactions*

(a) If the Adviser deems a Regulated Fund's participation in any Potential Co-Investment Transaction to be appropriate for the Regulated Fund, it will then determine an appropriate level of investment for the Regulated Fund.

(b) If the aggregate amount recommended by the Advisers to be invested in the Potential Co-Investment Transaction by the participating Regulated Funds and any participating Affiliated Funds, collectively, exceeds the amount of the investment opportunity, the investment opportunity will be allocated among them pro rata based on the size of the Internal Orders, as described in section III.A.1.b. of the application. Each Adviser to a participating Regulated Fund will promptly notify and provide the Eligible Directors with information concerning the Affiliated Funds' and Regulated Funds' order sizes to assist the Eligible Directors with their review of the applicable Regulated Fund's investments for compliance with these Conditions.

(c) After making the determinations required in Condition 1(b) above, each Adviser to a participating Regulated Fund will distribute written information concerning the Potential Co-Investment Transaction (including the amount proposed to be invested by each participating Regulated Fund and each participating Affiliated Fund) to the Eligible Directors of its participating Regulated Fund(s) for their consideration. A Regulated Fund will enter into a Co-Investment Transaction with one or more other Regulated Funds or Affiliated Funds only if, prior to the Regulated Fund's participation in the

Potential Co-Investment Transaction, a Required Majority concludes that:

(i) The terms of the transaction, including the consideration to be paid, are reasonable and fair to the Regulated Fund and its equity holders and do not involve overreaching in respect of the Regulated Fund or its equity holders on the part of any person concerned;

(ii) the transaction is consistent with:

(A) The interests of the Regulated Fund's equity holders; and

(B) the Regulated Fund's then-current Objectives and Strategies;

(iii) the investment by any other Regulated Fund(s) or Affiliated Fund(s) would not disadvantage the Regulated Fund, and participation by the Regulated Fund would not be on a basis different from, or less advantageous than, that of any other Regulated Fund(s) or Affiliated Fund(s) participating in the transaction; provided that the Required Majority shall not be prohibited from reaching the conclusions required by this Condition 2(c)(iii) if:

(A) The settlement date for another Regulated Fund or an Affiliated Fund in a Co-Investment Transaction is later than the settlement date for the Regulated Fund by no more than ten business days or earlier than the settlement date for the Regulated Fund by no more than ten business days, in either case, so long as: (x) The date on which the commitment of the Affiliated Funds and Regulated Funds is made is the same; and (y) the earliest settlement date and the latest settlement date of any Affiliated Fund or Regulated Fund participating in the transaction will occur within ten business days of each other; or

(B) any other Regulated Fund or Affiliated Fund, but not the Regulated Fund itself, gains the right to nominate a director for election to a portfolio company's board of directors, the right to have a board observer or any similar right to participate in the governance or management of the portfolio company so long as: (x) The Eligible Directors will have the right to ratify the selection of such director or board observer, if any; (y) the Adviser agrees to, and does, provide periodic reports to the Regulated Fund's Board with respect to the actions of such director or the information received by such board observer or obtained through the exercise of any similar right to participate in the governance or management of the portfolio company; and (z) any fees or other compensation that any other Regulated Fund or Affiliated Fund or any affiliated person of any other Regulated Fund or Affiliated Fund receives in connection with the right of one or more Regulated Funds or Affiliated Funds to nominate a director or appoint a board observer or otherwise to participate in the governance or management of the portfolio company will be shared proportionately among any participating Affiliated Funds (who may, in turn, share their portion with their affiliated persons) and any participating Regulated Fund(s) in accordance with the amount of each such party's investment; and

(iv) the proposed investment by the Regulated Fund will not involve compensation, remuneration or a direct or indirect [22] financial benefit to the Advisers, any other Regulated Fund, the Affiliated Funds or any affiliated person of any of them (other than the parties to the Co-Investment Transaction), except (A) to the extent permitted by Condition 14, (B) to the extent permitted by section 17(e) or 57(k), as applicable, (C) indirectly, as a result of an interest in the securities issued by one of the parties to the Co-Investment Transaction, or (D) in the case of fees or other compensation described in Condition 2(c)(iii)(B)(z).

3. *Right to Decline.* Each Regulated Fund has the right to decline to participate in any Potential Co-Investment Transaction or to invest less than the amount proposed.

4. *General Limitation.* Except for Follow-On Investments made in accordance with Conditions 8 and 9 below,[23] a Regulated Fund will not invest in reliance on the Order in any issuer in which a Related Party has an investment.[24]

5. *Same Terms and Conditions.* A Regulated Fund will not participate in any Potential Co-Investment Transaction unless (i) the terms, conditions, price, class of securities to be purchased, date on which the commitment is entered into and registration rights (if any) will be the same for each participating Regulated Fund and Affiliated Fund and (ii) the earliest settlement date and the latest settlement date of any participating Regulated Fund or Affiliated Fund will occur as close in time as practicable and in no event more than ten business days apart. The grant to one or more Regulated Funds or Affiliated Funds, but not the respective Regulated Fund, of the right to nominate a director for election to a portfolio company's board of directors, the right to have an observer on the board of directors or similar rights to participate in the governance or management of the portfolio company will not be interpreted so as to violate this Condition 5, if Condition 2(c)(iii)(B) is met.

6. *Standard Review Dispositions.*

(a) *General.* If any Regulated Fund or Affiliated Fund elects to sell, exchange or otherwise dispose of an interest in a security and one or more Regulated Funds and Affiliated Funds have previously participated in a Co-Investment Transaction with respect to the issuer, then:

(i) The Adviser to such Regulated Fund or Affiliated Fund [25] will notify each Regulated Fund that holds an investment in the issuer of the proposed Disposition at the earliest practical time; and

(ii) the Adviser to each Regulated Fund that holds an investment in the issuer will formulate a recommendation as to participation by such Regulated Fund in the Disposition.

(b) *Same Terms and Conditions.* Each Regulated Fund will have the right to participate in such Disposition on a proportionate basis, at the same price and on the same terms and conditions as those applicable to the Affiliated Funds and any other Regulated Fund.

(c) *No Board Approval Required.* A Regulated Fund may participate in such a Disposition without obtaining prior approval of the Required Majority if:

(i) (A) The participation of each Regulated Fund and Affiliated Fund in such Disposition is proportionate to its then-current holding of the security (or securities) of the issuer that is (or are) the subject of the Disposition; [26] (B) the

[22] For example, procuring the Regulated Fund's investment in a Potential Co-Investment Transaction to permit an affiliate to complete or obtain better terms in a separate transaction would constitute an indirect financial benefit.

[23] This exception applies only to Follow-On Investments by a Regulated Fund in issuers in which that Regulated Fund already holds investments.

[24] ''Related Party'' means (i) any Close Affiliate and (ii) in respect of matters as to which any Adviser has knowledge, any Remote Affiliate. ''Close Affiliate'' means the Advisers, the Regulated Funds, the Affiliated Funds and any other person described in Section 57(b) (after giving effect to Rule 57b–1) in respect of any Regulated Fund (treating any registered investment company or series thereof as a BDC for this purpose) except for limited partners included solely by reason of the reference in Section 57(b) to Section 2(a)(3)(D). ''Remote Affiliate'' means any person described in Section 57(e) in respect of any Regulated Fund (treating any registered investment company or series thereof as a BDC for this purpose) and any limited partner holding 5% or more of the relevant limited partner interests that would be a Close Affiliate but for the exclusion in that definition.

[25] Any KA Proprietary Account that is not advised by an Adviser is itself deemed to be an Adviser for purposes of Conditions 6(a)(i), 7(a)(i), 8(a)(i) and 9(a)(i).

[26] In the case of any Disposition, proportionality will be measured by each participating Regulated Fund's and Affiliated Fund's outstanding

Continued

Board of the Regulated Fund has approved as being in the best interests of the Regulated Fund the ability to participate in such Dispositions on a pro rata basis (as described in greater detail in the application); and (C) the Board of the Regulated Fund is provided on a quarterly basis with a list of all Dispositions made in accordance with this Condition; or

(ii) each security is a Tradable Security and (A) the Disposition is not to the issuer or any affiliated person of the issuer; and (B) the security is sold for cash in a transaction in which the only term negotiated by or on behalf of the participating Regulated Funds and Affiliated Funds is price.

(d) *Standard Board Approval.* In all other cases, the Adviser will provide its written recommendation as to the Regulated Fund's participation to the Eligible Directors and the Regulated Fund will participate in such Disposition solely to the extent that a Required Majority determines that it is in the Regulated Fund's best interests.

7. *Enhanced Review Dispositions.*

(a) *General.* If any Regulated Fund or Affiliated Fund elects to sell, exchange or otherwise dispose of a Pre-Boarding Investment in a Potential Co-Investment Transaction and the Regulated Funds and Affiliated Funds have not previously participated in a Co-Investment Transaction with respect to the issuer:

(i) The Adviser to such Regulated Fund or Affiliated Fund will notify each Regulated Fund that holds an investment in the issuer of the proposed Disposition at the earliest practical time;

(ii) the Adviser to each Regulated Fund that holds an investment in the issuer will formulate a recommendation as to participation by such Regulated Fund in the Disposition; and

(iii) the Advisers will provide to the Board of each Regulated Fund that holds an investment in the issuer all information relating to the existing investments in the issuer of the Regulated Funds and Affiliated Funds, including the terms of such investments and how they were made, that is necessary for the Required Majority to make the findings required by this Condition.

(b) *Enhanced Board Approval.* The Adviser will provide its written recommendation as to the Regulated Fund's participation to the Eligible Directors, and the Regulated Fund will participate in such Disposition solely to the extent that a Required Majority determines that:

(i) The Disposition complies with Condition 2(c)(i), (ii), (iii)(A), and (iv).

(ii) the making and holding of the Pre-Boarding Investments were not prohibited by section 57 or rule 17d–1, as applicable, and records the basis for the finding in the Board minutes.

(c) *Additional Requirements:* The Disposition may only be completed in reliance on the Order if:

(i) *Same Terms and Conditions.* Each Regulated Fund has the right to participate in such Disposition on a proportionate basis, at the same price and on the same terms and Conditions as those applicable to the Affiliated Funds and any other Regulated Fund;

(ii) *Original Investments.* All of the Affiliated Funds' and Regulated Funds' investments in the issuer are Pre-Boarding Investments;

(iii) *Advice of counsel.* Independent counsel to the Board advises that the making and holding of the investments in the Pre-Boarding Investments were not prohibited by section 57 (as modified by rule 57b–1) or rule 17d–1, as applicable;

(iv) *Multiple Classes of Securities.* All Regulated Funds and Affiliated Funds that hold Pre-Boarding Investments in the issuer immediately before the time of completion of the Co-Investment Transaction hold the same security or securities of the issuer. For the purpose of determining whether the Regulated Funds and Affiliated Funds hold the same security or securities, they may disregard any security held by some but not all of them if, prior to relying on the Order, the Required Majority is presented with all information necessary to make a finding, and finds, that: (x) Any Regulated Fund's or Affiliated Fund's holding of a different class of securities (including for this purpose a security with a different maturity date) is immaterial [27] in amount, including immaterial relative to the size of the issuer; and (y) the Board records the basis for any such finding in its minutes. In addition, securities that differ only in respect of issuance date, currency, or denominations may be treated as the same security; and

(v) *No control.* The Affiliated Funds, the other Regulated Funds and their affiliated persons (within the meaning of section 2(a)(3)(C) of the Act), individually or in the aggregate, do not control the issuer of the securities (within the meaning of section 2(a)(9) of the Act).

8. *Standard Review Follow-Ons.*

(a) *General.* If any Regulated Fund or Affiliated Fund desires to make a Follow-On Investment in an issuer and the Regulated Funds and Affiliated Funds holding investments in the issuer previously participated in a Co-Investment Transaction with respect to the issuer:

(i) The Adviser to each such Regulated Fund or Affiliated Fund will notify each Regulated Fund that holds securities of the portfolio company of the proposed transaction at the earliest practical time; and

(ii) the Adviser to each Regulated Fund that holds an investment in the issuer will formulate a recommendation as to the proposed participation, including the amount of the proposed investment, by such Regulated Fund.

(b) *No Board Approval Required.* A Regulated Fund may participate in the Follow-On Investment without obtaining prior approval of the Required Majority if:

(i) (A) The proposed participation of each Regulated Fund and each Affiliated Fund in such investment is proportionate to its outstanding investments in the issuer or the security at issue, as appropriate,[28] immediately preceding the Follow-On Investment; and (B) the Board of the Regulated Fund has approved as being in the best interests of the Regulated Fund the ability to participate in Follow-On Investments on a pro rata basis (as described in greater detail in the application); or

(ii) it is a Non-Negotiated Follow-On Investment.

(c) *Standard Board Approval.* In all other cases, the Adviser will provide its written recommendation as to the Regulated Fund's participation to the Eligible Directors and the Regulated Fund will participate in such Follow-On Investment solely to the extent that a Required Majority makes the

investment in the security in question immediately preceding the Disposition.

[27] In determining whether a holding is ''immaterial'' for purposes of the Order, the Required Majority will consider whether the nature and extent of the interest in the transaction or arrangement is sufficiently small that a reasonable person would not believe that the interest affected the determination of whether to enter into the transaction or arrangement or the terms of the transaction or arrangement.

[28] To the extent that a Follow-On Investment opportunity is in a security or arises in respect of a security held by the participating Regulated Funds and Affiliated Funds, proportionality will be measured by each participating Regulated Fund's and Affiliated Fund's outstanding investment in the security in question immediately preceding the Follow-On Investment using the most recent available valuation thereof. To the extent that a Follow-On Investment opportunity relates to an opportunity to invest in a security that is not in respect of any security held by any of the participating Regulated Funds or Affiliated Funds, proportionality will be measured by each participating Regulated Fund's and Affiliated Fund's outstanding investment in the issuer immediately preceding the Follow-On Investment using the most recent available valuation thereof.

determinations set forth in Condition 2(c). If the only previous Co-Investment Transaction with respect to the issuer was an Enhanced Review Disposition the Eligible Directors must complete this review of the proposed Follow-On Investment both on a stand-alone basis and together with the Pre-Boarding Investments in relation to the total economic exposure and other terms of the investment.

(d) *Allocation.* If, with respect to any such Follow-On Investment:

(i) The amount of the opportunity proposed to be made available to any Regulated Fund is not based on the Regulated Funds' and the Affiliated Funds' outstanding investments in the issuer or the security at issue, as appropriate, immediately preceding the Follow-On Investment; and

(ii) the aggregate amount recommended by the Advisers to be invested in the Follow-On Investment by the participating Regulated Funds and any participating Affiliated Funds, collectively, exceeds the amount of the investment opportunity, then the Follow-On Investment opportunity will be allocated among them pro rata based on the size of the Internal Orders, as described in section III.A.1.b. of the application.

(e) *Other Conditions.* The acquisition of Follow-On Investments as permitted by this Condition will be considered a Co-Investment Transaction for all purposes and subject to the other Conditions set forth in the application.

9. *Enhanced Review Follow-Ons.*

(a) *General.* If any Regulated Fund or Affiliated Fund desires to make a Follow-On Investment in an issuer that is a Potential Co-Investment Transaction and the Regulated Funds and Affiliated Funds holding investments in the issuer have not previously participated in a Co-Investment Transaction with respect to the issuer:

(i) The Adviser to each such Regulated Fund or Affiliated Fund will notify each Regulated Fund that holds securities of the portfolio company of the proposed transaction at the earliest practical time;

(ii) the Adviser to each Regulated Fund that holds an investment in the issuer will formulate a recommendation as to the proposed participation, including the amount of the proposed investment, by such Regulated Fund; and

(iii) the Advisers will provide to the Board of each Regulated Fund that holds an investment in the issuer all information relating to the existing investments in the issuer of the Regulated Funds and Affiliated Funds, including the terms of such investments and how they were made, that is necessary for the Required Majority to make the findings required by this Condition.

(b) *Enhanced Board Approval.* The Adviser will provide its written recommendation as to the Regulated Fund's participation to the Eligible Directors, and the Regulated Fund will participate in such Follow-On Investment solely to the extent that a Required Majority reviews the proposed Follow-On Investment both on a stand-alone basis and together with the Pre-Boarding Investments in relation to the total economic exposure and other terms and makes the determinations set forth in Condition 2(c). In addition, the Follow-On Investment may only be completed in reliance on the Order if the Required Majority of each participating Regulated Fund determines that the making and holding of the Pre-Boarding Investments were not prohibited by section 57 (as modified by rule 57b–1) or rule 17d–1, as applicable. The basis for the Board's findings will be recorded in its minutes.

(c) *Additional Requirements.* The Follow-On Investment may only be completed in reliance on the Order if:

(i) *Original Investments.* All of the Affiliated Funds' and Regulated Funds' investments in the issuer are Pre-Boarding Investments;

(ii) *Advice of counsel.* Independent counsel to the Board advises that the making and holding of the investments in the Pre-Boarding Investments were not prohibited by section 57 (as modified by rule 57b–1) or rule 17d–1, as applicable;

(iii) *Multiple Classes of Securities.* All Regulated Funds and Affiliated Funds that hold Pre-Boarding Investments in the issuer immediately before the time of completion of the Co-Investment Transaction hold the same security or securities of the issuer. For the purpose of determining whether the Regulated Funds and Affiliated Funds hold the same security or securities, they may disregard any security held by some but not all of them if, prior to relying on the Order, the Required Majority is presented with all information necessary to make a finding, and finds, that: (x) Any Regulated Fund's or Affiliated Fund's holding of a different class of securities (including for this purpose a security with a different maturity date) is immaterial in amount, including immaterial relative to the size of the issuer; and (y) the Board records the basis for any such finding in its minutes. In addition, securities that differ only in respect of issuance date, currency, or denominations may be treated as the same security; and

(iv) *No control.* The Affiliated Funds, the other Regulated Funds and their affiliated persons (within the meaning of section 2(a)(3)(C) of the Act), individually or in the aggregate, do not control the issuer of the securities (within the meaning of section 2(a)(9) of the Act).

(d) *Allocation.* If, with respect to any such Follow-On Investment:

(i) The amount of the opportunity proposed to be made available to any Regulated Fund is not based on the Regulated Funds' and the Affiliated Funds' outstanding investments in the issuer or the security at issue, as appropriate, immediately preceding the Follow-On Investment; and

(ii) the aggregate amount recommended by the Advisers to be invested in the Follow-On Investment by the participating Regulated Funds and any participating Affiliated Funds, collectively, exceeds the amount of the investment opportunity, then the Follow-On Investment opportunity will be allocated among them pro rata based on the size of the Internal Orders, as described in section III.A.1.b. of the application.

(e) *Other Conditions.* The acquisition of Follow-On Investments as permitted by this Condition will be considered a Co-Investment Transaction for all purposes and subject to the other Conditions set forth in the application.

10. *Board Reporting, Compliance and Annual Re-Approval*

(a) Each Adviser to a Regulated Fund will present to the Board of each Regulated Fund, on a quarterly basis, and at such other times as the Board may request, (i) a record of all investments in Potential Co-Investment Transactions made by any of the other Regulated Funds or any of the Affiliated Funds during the preceding quarter that fell within the Regulated Fund's then-current Objectives and Strategies and Board-Established Criteria that were not made available to the Regulated Fund, and an explanation of why such investment opportunities were not made available to the Regulated Fund; (ii) a record of all Follow-On Investments in and Dispositions of investments in any issuer in which the Regulated Fund holds any investments by any Affiliated Fund or other Regulated Fund during the prior quarter; and (iii) all information concerning Potential Co-Investment Transactions and Co-Investment Transactions, including investments made by other Regulated Funds or Affiliated Funds that the Regulated Fund considered but declined to participate in, so that the Independent Directors, may determine whether all Potential Co-Investment

Transactions and Co-Investment Transactions during the preceding quarter, including those investments that the Regulated Fund considered but declined to participate in, comply with the Conditions.

(b) All information presented to the Regulated Fund's Board pursuant to this Condition will be kept for the life of the Regulated Fund and at least two years thereafter, and will be subject to examination by the Commission and its staff.

(c) Each Regulated Fund's chief compliance officer, as defined in rule 38a–1(a)(4), will prepare an annual report for its Board each year that evaluates (and documents the basis of that evaluation) the Regulated Fund's compliance with the terms and Conditions of the application and the procedures established to achieve such compliance. In the case of a BDC Downstream Fund that does not have a chief compliance officer, the chief compliance officer of the BDC that controls the BDC Downstream Fund will prepare the report for the relevant Independent Party.

(d) The Independent Directors (including the non-interested members of each Independent Party) will consider at least annually whether continued participation in new and existing Co-Investment Transactions is in the Regulated Fund's best interests.

11. *Record Keeping.* Each Regulated Fund will maintain the records required by section 57(f)(3) of the Act as if each of the Regulated Funds were a BDC and each of the investments permitted under these Conditions were approved by the Required Majority under section 57(f).

12. *Director Independence.* No Independent Director (including the non-interested members of any Independent Party) of a Regulated Fund will also be a director, general partner, managing member or principal, or otherwise be an ''affiliated person'' (as defined in the Act) of any Affiliated Fund.

13. *Expenses.* The expenses, if any, associated with acquiring, holding or disposing of any securities acquired in a Co-Investment Transaction (including, without limitation, the expenses of the distribution of any such securities registered for sale under the Securities Act) will, to the extent not payable by the Advisers under their respective advisory agreements with the Regulated Funds and the Affiliated Funds, be shared by the Regulated Funds and the participating Affiliated Funds in proportion to the relative amounts of the securities held or being acquired or disposed of, as the case may be.

14. *Transaction Fees.*[29] Any transaction fee (including break-up, structuring, monitoring or commitment fees but excluding brokerage or underwriting compensation permitted by section 17(e) or 57(k)) received in connection with any Co-Investment Transaction will be distributed to the participants on a pro rata basis based on the amounts they invested or committed, as the case may be, in such Co-Investment Transaction. If any transaction fee is to be held by an Adviser pending consummation of the transaction, the fee will be deposited into an account maintained by the Adviser at a bank or banks having the qualifications prescribed in section 26(a)(1), and the account will earn a competitive rate of interest that will also be divided pro rata among the participants. None of the Advisers, the Affiliated Funds, the other Regulated Funds or any affiliated person of the Affiliated Funds or the Regulated Funds will receive any additional compensation or remuneration of any kind as a result of or in connection with a Co-Investment Transaction other than (i) in the case of the Regulated Funds and the Affiliated Funds, the pro rata transaction fees described above and fees or other compensation described in Condition 2(c)(iii)(B)(z), (ii) brokerage or underwriting compensation permitted by section 17(e) or 57(k) or (iii) in the case of the Advisers, investment advisory compensation paid in accordance with investment advisory agreements between the applicable Regulated Fund(s) or Affiliated Fund(s) and its Adviser.

15. *Independence.* If the Holders own in the aggregate more than 25 percent of the Shares of a Regulated Fund, then the Holders will vote such Shares as directed by an independent third party when voting on (1) the election of directors; (2) the removal of one or more directors; or (3) any other matter under either the Act or applicable State law affecting the Board's composition, size or manner of election.

For the Commission, by the Division of Investment Management, under delegated authority.

Jill M. Peterson,

Assistant Secretary.

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BILLING CODE 8011–01–P

[29] Applicants are not requesting and the Commission is not providing any relief for transaction fees received in connection with any Co-Investment Transaction.

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–87903; File No. SR–NYSEAMER–2020–02]

Self-Regulatory Organizations; NYSE American LLC; Notice of Filing and Immediate Effectiveness of Proposed Change To Amend the NYSE American Options Fee Schedule Regarding the Floor Broker Prepayment Program

January 7, 2020.

Pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 (''Act'')[2] and Rule 19b–4 thereunder,[3] notice is hereby given that on January 2, 2020, NYSE American LLC (''NYSE American'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend the NYSE American Options Fee Schedule (''Fee Schedule'') regarding the Floor Broker Prepayment Program. The Exchange proposes to implement the fee change effective January 2, 2020. The proposed change is available on the Exchange's website at *www.nyse.com,* at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to modify and extend the prepayment incentive program for Floor Broker organizations (each a ''Floor Broker'') which allows Floor Brokers to prepay certain annual costs in exchange for volume rebates, as set forth in the Fee Schedule (the ''FB Prepay Program'' or ''Program'').[4] The Exchange also plans to eliminate the Floor Broker Volume Rebate Program (the ''FB Volume Rebate'') as duplicative and superfluous in light of the proposed changes to the FB Prepay Program.[5]

Pursuant to the current FB Prepay Program, the Exchange offers Floor Brokers a 10% discount on their ''Eligible Fixed Costs'' if such costs are prepaid in advance of the year (the ''10% Discount'')[6] and an opportunity to qualify for the Percentage Growth Incentive (the ''Growth Incentive''), which is designed to encourage Floor Brokers to increase their average daily volume (''ADV'') in billable manual contract sides by certain percentages (correlated with Tiers) as measured against (the greater of) one of two benchmarks.[7]

The Exchange proposes to make several changes to this Program, including to make it renewable annually, to remove the 10% Discount, and to offer an alternative annual fixed rebate amount if a participant qualifies for the Growth Incentive. Currently, if a Floor Broker qualifies for the Growth Incentive, it would be eligible for specified percentage reductions of its pre-paid annual fixed costs. The Exchange proposes to offer an alternative to receive a specified annual fixed rebate if a Floor Broker qualifies for the Growth Incentive. Participants that qualify would receive the greater of the two rebates. The Exchange also proposes to adjust the qualifying baseline volumes and benchmarks.

In addition, the FB Volume Rebate offers Floor Brokers the opportunity to qualify for a $5,000 rebate each month that the Floor Broker increases its ADV by a certain percentage over one of two benchmarks. Given the proposed changes to the FB Prepay Program, the Exchange proposes to eliminate (as duplicative) the FB Volume Rebate Program as discussed further herein.

The Exchange proposes to implement the fee change effective January 2, 2020.

Background

The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.''[8]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[9] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[10]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. To respond to this competitive marketplace, the Exchange has established incentives for Floor Brokers, as such participants serve an important function in facilitating the execution of orders via open outcry, which promotes price discovery on the public markets. To the extent that these incentives succeed, the increased liquidity on the Exchange would result in enhanced market quality for all participants.

Proposed Rule Change

The Exchange proposes to modify the Floor Broker Prepayment Program in several ways. First, the Exchange proposes to remove reference to specific years and to add rule text making clear that the Program is renewable on an annual basis.[11] The Exchange also proposes to remove language regarding the 10% Discount, as that would no longer be included in the Program.[12] In addition, the Exchange proposes to expand the Growth Incentive to provide an annual fixed-rebate option.

Currently, to qualify for the Growth Incentive, the minimum threshold that a participant needs to exceed is the greater of: 11,000 contract sides in billable manual ADV; or 110% of the Floor Broker's total billable manual ADV in contract sides during the second half of 2017—*i.e.,* July through December 2017.[13]

The Exchange proposes to revise the minimum thresholds that a participant needs to exceed to qualify for the Growth Incentive as follows: 20,000 contract sides (up from 11,000) in billable manual ADV; or 105% of the

[4] *See* Fee Schedule, Section I.E.1, Floor Broker Fixed Cost Prepayment Incentive Program (the ''FB Prepay Program''), *available here, https://www.nyse.com/publicdocs/nyse/markets/american-options/NYSE_American_Options_Fee_Schedule.pdf.*

[5] *See id.,* Fee Schedule, Section I.E.2 Floor Broker Volume Rebate Program (the ''FB Volume Rebate''). Given the plans to remove the FB Volume Rebate, the Exchange proposes a technical change to remove reference to ''Floor Broker Programs'' in the Table of Contents, as well as in the body of the Fee Schedule to re-number the FB Prepay Program as Section I.E., which would add clarity and transparency to the Fee Schedule.

[6] *See id.* (providing that Eligible Fixed Costs include: Section III.A. Monthly ATP Fees; Section III.B. Floor Access Fee; and Section IV. Monthly Floor Communication, Connectivity, Equipment and Booth or Podia Fees, specifically: Login, Transport Charges, Booth Premises, Telephone Service, Cellular Phones, Booth Telephone System—Line Charge, Booth Telephone System—Single line phone jack and data jack, and Wire Services).

[7] The Percentage Growth Incentive excludes Customer volume, Firm Facilitation trades and QCCs. Any volume calculated to achieve the Firm and Broker Dealer Monthly Fee Cap and the Limit of Fees on Options Strategy Executions, are likewise excluded from the Percentage Growth Incentive because fees on such volume is already capped and therefore does not increase billable manual volume. *See id.*

[8] *See* Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37499 (June 29, 2005) (S7–10–04) (''Reg NMS Adopting Release'').

[9] The OCC publishes options and futures volume in a variety of formats, including daily and monthly volume by exchange, *available here: https://www.theocc.com/market-data/volume/default.jsp.*

[10] Based on OCC data, *see id.,* the Exchange's market share in equity-based options declined from 9.82% for the month of January to 7.86% for the month of September.

[11] *See* proposed Fee Schedule, Section I.E., Floor Broker Fixed Cost Prepayment Incentive Program (the ''FB Prepay Program'') (including removing reference to specific years and adding references to Floor Brokers prepaying for the ''the following calendar year'' after committing thereto by ''the last business day of December in the current year''; being invoiced in January for Eligible Fixed Costs based on annualizing their Eligible Fixed Costs incurred in the previous November;'' and participants receiving their rebate ''in the following January.'' *See id.* For example, if a participating Floor Broker incurred $6,000 in Eligible Fixed Costs in November, that Floor Broker would be invoiced in January of the following year in the amount of $72,000 to prepay such costs for the entire year.

[12] *See id.* For consistency, the Exchange would also remove reference to ''larger discounts'' as it related to the smaller 10% Discount and replace this reference with the word ''rebates.'' *See id.*

[13] *See* Fee Schedule, Section I.E.2 Floor Broker Volume Rebate Program (the ''FB Volume Rebate'').

Floor Broker's total billable manual ADV in contract sides (down from 110%) during the second half of 2017—*i.e.,* July through December 2017.[14] The Exchange believes that 20,000 ADV is a reasonable minimum threshold above which a participating Floor Broker would need to increase volume in order to qualify for the Growth Incentive given the increased options volume executed by Floor Brokers in the past year. The Exchange also notes that Floor Brokers that are new to the Exchange would be able to qualify for the Growth Incentive based on the minimum threshold of 20,000 contract sides. In addition, because Floor Broker volume has increased, the Exchange believes that Floor Brokers that previously participated in the Program would be able to achieve this proposed minimum threshold. The Exchange likewise believes it is appropriate to reduce the requisite percentage to meet the 2017 benchmark because it would make this alternative more achievable for Floor Brokers that do not meet the billable manual ADV threshold. The Exchange notes that the changes to the Program are designed to encourage those Floor Brokers that have previously enrolled in the Program to reenroll for the upcoming year as well as to attract Floor Brokers that have not yet participated.

Regardless of which benchmark a Floor Broker's growth is measured against, all Floor Brokers that aim to qualify for the Growth Incentive would be required to increase volume executed on the Exchange. The total annual rebate available for achieving each Tier would be the same regardless of whether the Floor Broker relied on the minimum (proposed) 20,000 ADV contract sides as the benchmark or 105% of the second half of 2017 volume.

The Exchange also proposes to add an option for a Floor broker to receive a fixed rebate instead of a percentage reduction of pre-paid annual fixed costs if it qualifies for the Growth Incentive. To reflect this new option, the Exchange proposes to add rule text providing that ''[e]ligible Floor Broker organizations are entitled to an annual rebate that is the greater of the 'Total Percentage Reduction of pre-paid annual Eligible Fixed Costs' or the 'Alternative Rebate' based upon the Percentage Growth Incentive Tier achieved, as set forth in the table below''.

As in prior years, the Exchange is proposing rebates based on the growth in ADV in contract sides, but proposes to modify (and make more achievable) the requisite Percentage Growth requirements to as low as 5% to achieve an annual rebate of 10% of prepaid Eligible Fixed Costs or $2,000/month, whichever is greater, to Growth Incentive as high as 100% to achieve an annual rebate of 100% Eligible Fixed Costs or $16,000/month (under new Tier 4), whichever is greater.[15] Just as the total percentage reduction increases as the Percentage Growth increases, the Exchange proposes that the annual Alternative Rebate, with fixed dollar amounts tied to each Tier, would also increase as the Percentage Growth increases. Participants that qualify for one of the Tiers would receive only the higher of the two potential rebates, paid annually.

The following table reflects the proposed changes (with deletions in brackets and new text italicized):[16]

FB PREPAYMENT PROGRAM INCENTIVES

[Based on *annual* ADV in contract sides *for the calendar year* (in 2019)]

Tier	Percentage growth incentive	Total Percentage Reduction of pre-paid annual Eligible Fixed Costs [for 2019]	Alternative Rebate
Tier 1	[30]*5*	[40%]*10*	*$2,000/month.*
Tier 2	[65]*30*	[75]*50*	*$4,000/month.*
Tier 3	[100]*50*	[100*]*80*	*$8,000/month.*
Tier 4	*100*	*100*	*$16,000/month.*

Thus, as proposed, a participating Floor Broker would qualify for the proposed Growth Incentive by executing ADV growth in manual billable contract sides that is 5%, 30%, 50%, or 100%, over the greater of (i) 20,000 contract sides ADV; or (ii) 105% of their ADV during the second half of 2017 (*i.e.,* July through December). Participants that qualify for Tiers 1, 2, 3, or 4 would be eligible for 10%, 50%, 80% or 100% of their pre-paid annual Eligible Fixed costs, respectively. However, if the amount of the annual Alternative Rebate works out to be greater than the rebate available under the Growth Incentive program, the Floor Broker would be entitled to that amount.

The Exchange also proposes to eliminate the Floor Broker Volume Rebate, as it is now duplicative following the modifications to the FB Prepayment Program.[17] In particular, proposed Tier 3 of the FB Prepay Program requires the same level of growth as the FB Volume Rebate and a greater potential rebate. Both programs require the greater of 20,000 contract sides or a level of trading as compared to a prior period that is the same or greater than volume during that period. The Exchange notes, however, that the FB Volume Rebate uses the second half of 2018 volume as the prior volume benchmark whereas the proposed FB Prepay Program uses the second half of 2017 volume. The Exchange believes the similarities in the program—both in terms of incentives and potential rebates—obviate the need to keep both programs. Thus, the Exchange proposes to delete as superfluous (and duplicative) the FB Volume Rebate.

Although the FB Prepay Program relates to fixed costs, the Exchange believes the Program (as modified) would continue to incent Floor Brokers to increase their billable volume executed in open outcry on the Exchange, which would benefit all market participants by expanding liquidity and providing more trading

[14] *See* proposed Fee Schedule, Section I.E., Floor Broker Fixed Cost Prepayment Incentive Program (the ''FB Prepay Program'').

[15] *See id.* The Exchange notes that new Tier 4 effectively replacing current Tier 3 in terms of growth requirement and potential rebate, as the Exchange has lowered (and made more achievable) proposed Tier 3. *See id.*

[16] Given that the annual Alternative Rebate will be available for all Tiers (and not just Tier 3 as is currently the case), the Exchange also proposes to delete the following language from the Fee Schedule as obsolete: ''*Participants in the FB Prepay Program that qualify for Tier 3 will be rebated the greater of 100% of their pre-paid annual Eligible Fixed Costs, or $10,000/month.'' *See id.*

[17] *See id.*

opportunities, even to those market participants that have not committed to the Program. Regardless of which benchmark a participating Floor Broker's growth is measured against, all Floor Broker's that opt to participate would be required to increase volume executed on the Exchange in order to receive the enhanced discount. The Exchange cannot predict with certainty whether any Floor Brokers would avail themselves of this proposed fee change. However, all Floor brokers are eligible for this Program.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[18] in general, and furthers the objectives of Sections 6(b)(4) and (5) of the Act,[19] in particular, because it provides for the equitable allocation of reasonable dues, fees, and other charges among its members, issuers and other persons using its facilities and does not unfairly discriminate between customers, issuers, brokers or dealers.

The Proposed Rule Change Is Reasonable

The Exchange operates in a highly competitive market. The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.'' [20]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[21] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[22]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. Stated otherwise, changes to exchange transaction fees can have a direct effect on the ability of an exchange to compete for order flow.

The Exchange believes the FB Prepay Program, as modified, is reasonable because the Program is optional and Floor Brokers can elect to participate or not. In addition, the Exchange is continuing to offer two alternative means to achieve the same enhanced rebate to ensure that Floor Brokers that are new to the Exchange (or Floor Brokers that did not execute more than 20,000 ADV in contract sides) could also participate in the Program. The Exchange believes that increasing one of the alternate requirements to 20,000 ADV is a reasonable minimum threshold above which a participating Floor Broker would need to increase volume in order to realize the proposed Growth Incentive because numerous Floor brokers exceeded this volume requirement in 2019, even though it was not required. Because Floor Brokers are already performing at this level, the Exchange believes it is reasonable to adjust the eligibility requirement for the Growth Incentive to match current performance levels. Having demonstrated an ability to meet this higher volume threshold, the Exchange is seeking to encourage Floor Brokers to sustain this volume threshold throughout the year. The Exchange also believes it is reasonable to use each Floor Broker's historical volume in the second half of 2017 as a benchmark against which to measure future growth to achieve the proposed Growth Incentive, and to lower from 110% to 105% the requisite increase over the Floor Broker's 2017 volume, because it makes the Growth Incentive more achievable and provides an opportunity for more Floor Brokers to qualify for the Growth Incentive Program.

The Exchange further believes that the proposed changes to add an additional tier to the Growth Incentive is reasonable because it will provide greater opportunities to Floor Brokers to be eligible for one of the two rebates by providing lower thresholds to qualify. Overall, the proposed changes to the Growth Incentive program are designed to make the existing Tiers more achievable while adding new Tier 4 (which has same threshold percentage as existing Tier 3) to encourage increased executions by Floor Brokers on the Exchange, which activity (even with lower volume thresholds) would benefit all market participants.

The Exchange also believes it is reasonable to provide an annual alternative fixed rebate because it provides an option for Floor brokers to earn the higher of the percentage reduction rebate, or the fixed-rebate amount.

Moreover, the FB Prepay Program provides Floor Brokers the opportunity to receive rebates on its Eligible Fixed Costs that they otherwise would not receive, based on trading activity. Such rebates may encourage Floor Brokers to increase their billable volume executed in open outcry on the Exchange, which would benefit all market participants by expanding liquidity and providing more trading opportunities, even to non-Floor Broker market participants (including participating Floor Brokers who do not hit the volume thresholds).

Finally, to the extent the proposed change continues to attract greater volume and liquidity to the Exchange (including to the Floor), the Exchange believes the proposed change would improve the Exchange's overall competitiveness and strengthen its market quality for all market participants. In the backdrop of the competitive environment in which the Exchange operates, the proposed rule change is a reasonable attempt by the Exchange to increase the depth of its market and improve its market share relative to its competitors.

The Exchange cannot predict with certainty whether any Floor Brokers would avail themselves of this proposed fee change. However, all Floor brokers are eligible to participate in the Program.

The proposed technical change to re-number the Table of Contents as well as the body of the Fee Schedule in light of the removal of the FB Volume Rebate program is reasonable as it would add clarity and transparency to the Fee Schedule.

The Proposed Rule Change Is an Equitable Allocation of Credits and Fees

The Exchange believes the proposed rule change is an equitable allocation of its fees and credits. The proposal is based on the amount and type of business transacted on the Exchange and Floor Brokers can opt to avail themselves of the Program or not, and to attempt to trade sufficient volume to achieve one of the Tiers, or not. All

[18] 15 U.S.C. 78f(b).

[19] 15 U.S.C. 78f(b)(4) and (5).

[20] *See* Reg NMS Adopting Release, *supra* note 8, at 37499.

[21] *See supra* note 9.

[22] Based on OCC data, *see supra* note 10, in 2019, the Exchange's market share in equity-based options declined from 9.82% for the month of January to 7.86% for the month of September.

participating Floor Brokers have the ability to qualify for the same enhanced rebate under two alternatives means offered (*i.e.,* the greater of at least 20,000 contract sides in billable ADV or 105% of the Floor Broker's total billable manual ADV in the second half of 2017). The Exchange notes that the changes to the Program are designed to encourage those Floor Brokers that have previously enrolled in the Program to reenroll for the upcoming year as well as to attract Floor Brokers that have not yet participated.

Moreover, the proposed change applies to qualifying Floor Brokers equally and because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support.

To the extent that the proposed change continues to attract more participation in the programs of the Exchange, the increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to the Exchange thereby improving market-wide quality and price discovery.

The Proposed Rule Change Is Not Unfairly Discriminatory

The Exchange believes it is not unfairly discriminatory to modify the FB Prepayment program because the proposed modification would be available to all similarly-situated Floor Brokers on an equal and non-discriminatory basis.

The proposed modified Program is not unfairly discriminatory to non-Floor Brokers because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support. To the extent that the proposed change continues to attract more participation in the programs of the Exchange, the increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to the Exchange thereby improving market-wide quality and price discovery.

Moreover, the proposal is based on the amount and type of business transacted on the Exchange and Floor Broker organizations are not obligated to participate in the Program and, if they do, they are not obligated to try to achieve any of the Tiers.

To the extent that the proposed change attracts a variety of transactions to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to (the Floor of) the Exchange thereby improving market-wide quality and price discovery. The resulting increased volume and liquidity would provide more trading opportunities and tighter spreads to all market participants and thus would promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest.

Finally, the Exchange believes that it is subject to significant competitive forces, as described below in the Exchange's statement regarding the burden on competition.

B. Self-Regulatory Organization's Statement on Burden on Competition

In accordance with Section 6(b)(8) of the Act, the Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Instead, as discussed above, the Exchange believes that the proposed changes would encourage the submission of additional liquidity to a public exchange, thereby promoting market depth, price discovery and transparency and enhancing order execution opportunities for all market participants. As a result, the Exchange believes that the proposed change furthers the Commission's goal in adopting Regulation NMS of fostering integrated competition among orders, which promotes ''more efficient pricing of individual stocks for all types of orders, large and small.'' [23]

Intramarket Competition. The Exchange believes the proposed Program, as modified, should continue to encourage order flow to be directed to the (Floor of the) Exchange, which would enhance the quality of quoting and may increase the volumes of contracts trade on the Exchange. To the extent that there is an additional competitive burden on non-Floor Brokers, the Exchange believes that this is appropriate because Floor Brokers serve an important function in facilitating the execution of orders via open outcry, which as a price-improvement mechanism, the Exchange wishes to encourage and support.

To the extent that this function is achieved, all of the Exchange's market participants should benefit from the improved market liquidity. Enhanced market quality and increased transaction volume that results from the anticipated increase in order flow directed to the Exchange will benefit all market participants and improve competition on the Exchange.

The proposed technical change to re-number the Table of Contents as well as the body of the Fee Schedule in light of the removal of the FB Volume Rebate program is not designed to impact competition but instead should add clarity and transparency to the Fee Schedule.

Intermarket Competition. The Exchange believes that the proposed change could promote competition between the Exchange and other execution venues, by encouraging additional orders to be sent to the (Floor of the) Exchange for execution. The proposed adjustments to the Program are designed to make the incentives more achievable and to continue to encourage Floor Brokers to execute orders on the Floor of the Exchange, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads.

Given the robust competition for volume among options markets, many of which offer the same products, implementing programs to attract order flow, such as the proposed modification to the FB Prepayment Program, are consistent with the above-mentioned goals of the Act.

The Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues. In such an environment, the Exchange must continually review, and consider adjusting, its fees and credits to remain competitive with other exchanges. For the reasons described above, the Exchange believes that the proposed rule change reflects this competitive environment.

[23] *See* Reg NMS Adopting Release, *supra* note 8, at 37499.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change is effective upon filing pursuant to Section 19(b)(3)(A) [24] of the Act and subparagraph (f)(2) of Rule 19b–4 [25] thereunder, because it establishes a due, fee, or other charge imposed by the Exchange.

At any time within 60 days of the filing of such proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings under Section 19(b)(2)(B) [26] of the Act to determine whether the proposed rule change should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's internet comment form (*http://www.sec.gov/rules/sro.shtml*); or
- Send an email to *rule-comments@sec.gov.* Please include File Number SR–NYSEAMER–2020–02 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090.

All submissions should refer to File Number SR–NYSEAMER–2020–02. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (*http://www.sec.gov/rules/sro.shtml*). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–NYSEAMER–2020–02, and should be submitted on or before February 3, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[27]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–00264 Filed 1–10–20; 8:45 am]

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[24] 15 U.S.C. 78s(b)(3)(A).

[25] 17 CFR 240.19b–4(f)(2).

[26] 15 U.S.C. 78s(b)(2)(B).

[27] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–87902; File No. SR–NYSEAMER–2020–01]

Self-Regulatory Organizations; NYSE American LLC; Notice of Filing and Immediate Effectiveness of Proposed Change To Amend the NYSE American Options Fee Schedule Regarding Fees Charged Under the Market Maker Sliding Scale

January 7, 2020.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (''Act'') [2] and Rule 19b–4 thereunder,[3] notice is hereby given that, on January 2, 2020, NYSE American LLC (''NYSE American'' or ''Exchange'') filed with the Securities and Exchange Commission (''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend the NYSE American Options Fee Schedule (''Fee Schedule'') regarding fees charged under the Market Maker Sliding Scale. The Exchange proposes to implement the fee change effective January 2, 2020. The proposed change is available on the Exchange's website at *www.nyse.com,* at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to modify certain of the fees charged under the Market Maker Sliding Scale program, as described in more detail below.

Section I.C. of the Fee Schedule sets forth the Sliding Scale of transaction fees charged to NYSE American Options Market Makers (referred to as Market Makers herein), which fees decrease upon the Market Maker trading certain minimum (increasing) monthly volume thresholds as expressed in five tiers (the ''MM Sliding Scale'').[4] The MM Sliding

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

[4] *See* Fee Schedule, Section I.C., NYSE American Options Market Maker Sliding Scale—Electronic, *available here, https://www.nyse.com/publicdocs/nyse/markets/american-options/NYSE_American_Options_Fee_Schedule.pdf* (excluding any volumes attributable to QCC trades, CUBE Auctions, and Strategy Execution Fee Caps, as these transactions are subject to separate pricing described in Fee Schedule Sections I.F., I.G., and I.J., respectively). The thresholds are based on a Market Makers' volume transacted Electronically as a percentage of

Continued

Scale offers different rates depending on whether volume is make or take [5] and offers reduced rates for Market Makers that participate in the Exchange's Prepayment Programs, per Section I.D. of the Fee Schedule.[6] The Exchange proposes to modify (increase) the MM Siding Scale per contract rate in some of the tiers for Market Makers enrolled in the Prepayment Program, but will not be changing any aspect of the Prepayment Program or the volume thresholds required to qualify for each MM Sliding Scale tier.[7]

The Exchange proposes to implement the fee change effective January 2, 2020.

Background

The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.'' [8]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[9] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[10]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. To respond to this competitive marketplace, the Exchange has already established incentives to encourage Market Makers to provide liquid and active markets on the Exchange, including by offering the MM Sliding Scale and Prepayment Programs. Market Makers that would like to receive a more favorable per contract rate under the MM Sliding Scale have the option to commit to the Exchange's Prepayment Program, which commitment increases liquidity on the Exchange to the benefit of all market participants. The Exchange provides Market Makers with the flexibility to join annually or at various points in the year to encourage broader participation. While the proposed change would increase certain MM Sliding Scale fees for Market Makers that have prepaid, the Exchange nonetheless believes that the (still lower and) reduced MM Sliding Scale fees would continue to encourage Market Makers to increase their participation, thereby improving the quoted markets and attracting more order flow trading volume to the Exchange. To the extent that these incentives succeed, the increased liquidity on the Exchange would result in enhanced market quality for all participants.

Proposed Rule Change

The Exchange proposes to modify the per contract rate for Market Makers enrolled in the Prepayment Program and that qualify for tiers 2, 3 or 4, as shown in the table below (with current rates in brackets and proposed rates italicized), but will not be changing tiers 1 or 5, nor the volume thresholds required to qualify for any MM Sliding Scale tier: [11]

Tier	Market Maker electronic ADV as a % of TCADV	Prepayment Program participant rates	
		Rate per contract for non-take volume	Rate per contract for take volume
1	0.00% to 0.20%	$0.22	$0.24
2	>0.20% to 0.65%	[$0.17] 0.18	[$0.20] 0.22
3	>0.65% to 1.40%	[0.08] 0.09	[0.11] 0.13
4	>1.40% to 2.00%	[0.05] 0.06	[0.08] 0.10
5	>2.00%	0.03	0.06

The Exchange believes that the modified rates (while increased) still reflect a significant reduction in overall transaction rates for participants in one of the Prepayment Programs. Thus, the Exchange believes that the (still lower and) reduced MM Sliding Scale fees would continue to encourage Market Makers to increase their participation, thereby improving the quoted markets and attracting more order flow trading volume to the Exchange. To the extent that these incentives succeed, the increased liquidity on the Exchange would result in enhanced market

total industry Customer equity and Exchange Traded Fund options volumes as reported by the Options Clearing Corporation (the ''OCC''). *See* OCC Monthly Statistics Reports, available here, *http://www.theocc.com/webapps/monthly-volume-reports. See also* Fee Schedule, Key Terms and Definitions, TCADV (defining TCADV as ''Total Industry Customer equity and ETF option average daily volume. TCADV includes OCC calculated Customer volume of all types, including Complex Order transactions and QCC transactions, in equity and ETF options'').

[5] For purposes of the Sliding Scale, ''all eligible volume that does not remove liquidity'' would be considered non-take volume; whereas any volume that removes liquidity would be considered take volume.'' *See* Fee Schedule, Section I.C., note 1. For example, any Market Maker transaction that interacts with resting liquidity is take volume.

[6] The Exchange offers Market Makers the opportunity to prepay a portion of certain transactions costs in exchange for reduced rates under the MM Sliding Scale program as well as enabling such Market Makers to qualify their Affiliated OFP or Appointed OFP, if any, to earn enhanced credits under the American Customer Engagement (''ACE'') Program per Section I.E. of the Fee Schedule. *See* Fee Schedule, Section I.D., *supra* note 4 (describing 1 Year Prepayment Program and Balance of the Year Program). *See also* Fee Schedule, Section I.E. (setting forth the ACE Program).

[7] *See* proposed Fee Schedule, Section I.C., NYSE American Options Market Maker Sliding Scale—Electronic. *See also* Fee Schedule, Section I.D. (Prepayment Program).

[8] *See* Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37499 (June 29, 2005) (S7–10–04) (''Reg NMS Adopting Release'').

[9] The OCC publishes options and futures volume in a variety of formats, including daily and monthly volume by exchange, *available here: https://www.theocc.com/market-data/volume/default.jsp.*

[10] Based on OCC data, *see id.,* the Exchange's market share in equity-based options declined from 9.82% for the month of January to 7.86% for the month of September.

[11] The Exchange notes that this table does not include the tiered MM Sliding Scale rates for participants that are not enrolled in a Prepayment Program. *See* Fee Schedule, Section I.C. (setting forth the rate per contract for non-take and take volume for non-Prepayment participants, based on tier).

quality for all participants. The Exchange notes that it is not modifying the rates for Tiers 1 or 5 because it believes those rates are appropriate and should continue to attract liquidity to the Exchange. In particular, Tier 1 has no minimum volume threshold and thus operates as a base tier, which any Market Maker doing business on the Exchange can achieve; whereas Tier 5 is the highest MM Sliding Scale tier and the Exchange wants to keep the rate the same so as to continue to encourage those Market Makers that already qualify for the tier to continue to execute sufficient volume to achieve this highest perk (*i.e.,* lower per contract pricing).

The Exchange believes that the Market Makers that would like to receive a more favorable per contract rate under the MM Sliding Scale have the option to commit the Exchange's Prepayment Program, which commitment increases liquidity on the Exchange to the benefit of all market participants. The Exchange notes that Market Makers serve a crucial role in the options markets by providing liquidity to facilitate market efficiency and functioning. The Exchange provides Market Makers with the flexibility to join annually or at various points in the year to encourage broader participation. The proposed fees, although increased, are still less expensive for participants in the Prepayment Program and therefore the Exchange believes that the Prepayment Program and MM Sliding Scale would continue to encourage Market Makers to commit to directing their order flow to the Exchange in exchange for reduced rates, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads.

The Exchange's fees are constrained by intermarket competition, as Market Makers can register on any or all of the 16 options exchanges. Thus, ATP Holders that are also members of other exchanges have a choice of where they register and operate as Market Makers. The proposed fees, although increased, are still less expensive for participants in the Prepayment Program and therefore the Exchange believes that the Prepayment Program and MM Sliding Scale would continue to encourage Market Makers to commit to directing their order flow to the Exchange in exchange for reduced rates, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads. The Exchange notes that all market participants stand to benefit from increased transaction volume, which promotes market depth, facilitates tighter spreads and enhances price discovery, and may lead to a corresponding increase in order flow from other market participants.

The Exchange cannot predict with certainty whether any Market Makers would avail themselves of this proposed fee change, particularly because the deadline for Market Makers to sign up for the Prepayment Program for 2020 is not until the end of 2019. Moreover, Market Makers may be registered on other options exchanges and may choose to post orders and quotes to those exchanges based on available incentives.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[12] in general, and furthers the objectives of Sections 6(b)(4) and (5) of the Act,[13] in particular, because it provides for the equitable allocation of reasonable dues, fees, and other charges among its members, issuers and other persons using its facilities and does not unfairly discriminate between customers, issuers, brokers or dealers.

The Proposed Rule Change Is Reasonable

The Exchange operates in a highly competitive market. The Commission has repeatedly expressed its preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, the Commission highlighted the importance of market forces in determining prices and SRO revenues and, also, recognized that current regulation of the market system ''has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.'' [14]

There are currently 16 registered options exchanges competing for order flow. Based on publicly-available information, and excluding index-based options, no single exchange has more than 16% of the market share of executed volume of multiply-listed equity and ETF options trades.[15] Therefore, no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in the third quarter of 2019, the Exchange had less than 10% market share of executed volume of multiply-listed equity & ETF options trades.[16]

The Exchange believes that the ever-shifting market share among the exchanges from month to month demonstrates that market participants can shift order flow, or discontinue or reduce use of certain categories of products, in response to fee changes. Accordingly, competitive forces constrain options exchange transaction fees. Stated otherwise, changes to exchange transaction fees can have a direct effect on the ability of an exchange to compete for order flow.

Market Makers that would like to receive a more favorable per contract rate under the MM Sliding Scale have the option to commit the Exchange's Prepayment Program, which commitment increases liquidity on the Exchange to the benefit of all market participants. The Exchange provides Market Makers with the flexibility to join annually or at various points in the year to encourage broader participation. The proposed fees, although increased, are still less expensive for participants in the Prepayment Program and therefore the Exchange believes that the Prepayment Program and MM Sliding Scale would continue to encourage Market Makers to commit to directing their order flow to the Exchange in exchange for reduced rates, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads. Further, the proposed Sliding Scale rates are competitive with fees charged by other exchanges and are designed to attract (and compete for) order flow to the Exchange, which provides a greater opportunity for trading by all market participants.[17]

Finally, to the extent the proposed change continues to attract greater volume and liquidity to the Exchange, the Exchange believes the proposed change would improve the Exchange's overall competitiveness and strengthen its market quality for all market participants. In the backdrop of the competitive environment in which the

[12] 15 U.S.C. 78f(b).

[13] 15 U.S.C. 78f(b)(4) and (5).

[14] *See* Reg NMS Adopting Release, *supra* note 8, at 37499.

[15] *See supra* note 9.

[16] Based on OCC data, *see supra* note 10, in 2019, the Exchange's market share in equity-based options declined from 9.82% for the month of January to 7.86% for the month of September.

[17] *See, e.g.,* Cboe Exchange, Inc. (''Cboe'') fee schedule, Liquidity Provider Sliding Scale Prepayment, *available here: https://www.cboe.com/publish/feeschedule/CBOEFeeSchedule.pdf.* The Exchange further notes that other options exchanges similarly differentiate fees based on maker-taker activity. *See, e.g.,* MIAX Options fee schedule, at p.1, *available here: https://www.miaxoptions.com/sites/default/files/fee_schedule-files/MIAX_Options_Fee_Schedule_12052019.pdf* (''Market Maker Sliding Scale'').

Exchange operates, the proposed rule change is a reasonable attempt by the Exchange to increase the depth of its market and improve its market share relative to its competitors.

The Exchange cannot predict with certainty whether any Market Makers would avail themselves of this proposed fee change, particularly because the deadline for Market Makers to sign up for the Prepayment Program for 2020 is not until the end of 2019. Moreover, Market Makers may be registered on other options exchanges and may choose to post orders and quotes to those exchanges based on available incentives.

The Proposed Rule Change Is an Equitable Allocation of Credits and Fees

The Exchange believes the proposed rule change is an equitable allocation of its fees and credits. The proposal is based on the amount and type of business transacted on the Exchange and Market Makers can opt to avail themselves of the Prepayment program or not, and to attempt to trade sufficient monthly volume to achieve one of the MM Sliding Scale tiers, or not. Moreover, the Prepayment Program—which is tied to the proposed fee changes—is designed to encourage Market Makers to commit capital to the Exchange as a demonstration of long term participation on the Exchange as a primary execution venue. To the extent that the proposed change continues to attract more participation in the programs of the Exchange, the increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed rule change would improve market quality for all market participants on the Exchange and, as a consequence, attract more order flow to the Exchange thereby improving market-wide quality and price discovery.

The Proposed Rule Change Is Not Unfairly Discriminatory

The Exchange believes it is not unfairly discriminatory to modify the MM Sliding Scale because the proposed modification would be available to all similarly-situated market participants on an equal and non-discriminatory basis.

The proposed modified MM Sliding Scale rates are not unfairly discriminatory because Market Makers that would like to receive a more favorable per contract rate under the Sliding Scale have the option to commit to one of the Prepayment Programs, which commitment increases liquidity on the Exchange to the benefit of all market participants. Moreover, all Market Makers would be subject to the differing rates depending on whether eligible volume is make or take volume.

The proposal is based on the amount and type of business transacted on the Exchange and Market Maker organizations are not obligated to try to achieve any of the MM Sliding Scale tiers, even if they participate in the Prepayment Program (that latter program also being optional to Market Makers). In addition, Market Maker organizations have increased obligations with respect to trading on the Exchange, and the Exchange believes that the proposed fees, although increased, are still less expensive for participants in the Prepayment Program and therefore the Exchange believes that the Prepayment Program and MM Sliding Scale would continue to encourage Market Makers to commit to directing their order flow to the Exchange in exchange for reduced rates, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads. To the extent that the proposed change attracts a variety of transactions to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for order execution thereby improving market-wide quality and price discovery. The resulting increased volume and liquidity would provide more trading opportunities and tighter spreads to all market participants and thus would promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest.

Finally, the Exchange believes that it is subject to significant competitive forces, as described below in the Exchange's statement regarding the burden on competition.

B. Self-Regulatory Organization's Statement on Burden on Competition

In accordance with Section 6(b)(8) of the Act, the Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Instead, as discussed above, the Exchange believes that the proposed changes would encourage the submission of additional liquidity to a public exchange, thereby promoting market depth, price discovery and transparency and enhancing order execution opportunities for all market participants. As a result, the Exchange believes that the proposed change furthers the Commission's goal in adopting Regulation NMS of fostering integrated competition among orders, which promotes ''more efficient pricing of individual stocks for all types of orders, large and small.'' [18]

Intramarket Competition. The proposed change is designed to continue to attract order flow to the Exchange by offering competitive rates based on increased volumes on the Exchange, which would enhance the quality of quoting and may increase the volumes of contracts trade on the Exchange. To the extent that there is an additional competitive burden on non-NYSE American Market Makers, the Exchange believes that this is appropriate because Market Makers have heightened obligations that other market participants do not and the proposal should incent market participants to direct additional order flow to the Exchange, and thus provide additional liquidity that enhances the quality of its markets and increases the volume of contracts traded here. To the extent that this purpose is achieved, all of the Exchange's market participants should benefit from the improved market liquidity. Enhanced market quality and increased transaction volume that results from the anticipated increase in order flow directed to the Exchange will benefit all market participants and improve competition on the Exchange.

Intermarket Competition. The Exchange believes that the proposed change, which is consistent with the goals of the MM Sliding Scale Program by providing reduced per contract rates for Market Makers in the Preypayment [sic] Program, could promote competition between the Exchange and other execution venues, by encouraging additional orders to be sent to the Exchange for execution. The proposed adjustments to the MM Sliding Scale fees are designed to continue to encourage Market Makers to commit to directing their order flow to the Exchange, which would increase volume and liquidity, to the benefit of all market participants by providing more trading opportunities and tighter spreads. Further, the proposed Sliding Scale rates are competitive with fees charged by other exchanges and are designed to attract (and compete for) order flow to the Exchange, which provides a greater opportunity for trading by all market participants.[19]

[18] *See* Reg NMS Adopting Release, *supra* note 8, at 37499.

[19] *See supra* note 17 (regarding Cboe's Liquidity Provider Sliding Scale Prepayment).

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change is effective upon filing pursuant to Section 19(b)(3)(A) [20] of the Act and subparagraph (f)(2) of Rule 19b–4 [21] thereunder, because it establishes a due, fee, or other charge imposed by the Exchange.

At any time within 60 days of the filing of such proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings under Section 19(b)(2)(B) [22] of the Act to determine whether the proposed rule change should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's internet comment form (*http://www.sec.gov/rules/sro.shtml*); or
- Send an email to *rule-comments@sec.gov.* Please include File Number SR–NYSEAMER–2020–01 on the subject line.

Paper Comments

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090.

All submissions should refer to File Number SR–NYSEAMER–2020–01. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (*http://www.sec.gov/rules/sro.shtml*). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–NYSEAMER–2020–01, and should be submitted on or before February 3, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[23]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–00263 Filed 1–10–20; 8:45 am]

BILLING CODE 8011–01–P

[20] 15 U.S.C. 78s(b)(3)(A).

[21] 17 CFR 240.19b–4(f)(2).

[22] 15 U.S.C. 78s(b)(2)(B).

[23] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

Sunshine Act Meetings

TIME AND DATE: 2:00 p.m. on Wednesday, January 15, 2020.

PLACE: The meeting will be held at the Commission's headquarters, 100 F Street NE, Washington, DC 20549.

STATUS: This meeting will be closed to the public.

MATTERS TO BE CONSIDERED: Commissioners, Counsel to the Commissioners, the Secretary to the Commission, and recording secretaries will attend the closed meeting. Certain staff members who have an interest in the matters also may be present.

In the event that the time, date, or location of this meeting changes, an announcement of the change, along with the new time, date, and/or place of the meeting will be posted on the Commission's website at *https://www.sec.gov.*

The General Counsel of the Commission, or his designee, has certified that, in his opinion, one or more of the exemptions set forth in 5 U.S.C. 552b(c)(3), (5), (6), (7), (8), 9(B) and (10) and 17 CFR 200.402(a)(3), (a)(5), (a)(6), (a)(7), (a)(8), (a)(9)(ii) and (a)(10), permit consideration of the scheduled matters at the closed meeting.

The subject matters of the closed meeting will consist of the following topics:

Institution and settlement of injunctive actions;

Institution and settlement of administrative proceedings;

Resolution of litigation claims; and

Other matters relating to enforcement proceedings.

At times, changes in Commission priorities require alterations in the scheduling of meeting agenda items that may consist of adjudicatory, examination, litigation, or regulatory matters.

CONTACT PERSON FOR MORE INFORMATION: For further information; please contact Vanessa A. Countryman from the Office of the Secretary at (202) 551–5400.

Dated: January 8, 2020.

Vanessa A. Countryman,

Secretary.

[FR Doc. 2020–00373 Filed 1–9–20; 11:15 am]

BILLING CODE 8011–01–P

DEPARTMENT OF STATE

[Public Notice:10999]

Notice of Determinations; Culturally Significant Objects Imported for Exhibition—Determinations: ''Millet and Modern Art: From Van Gogh to Dalí'' Exhibition

SUMMARY: Notice is hereby given of the following determinations: I hereby determine that certain objects to be included in the exhibition ''Millet and Modern Art: From Van Gogh to Dalí'' imported from abroad for temporary exhibition within the United States, are of cultural significance. The objects are imported pursuant to loan agreements with the foreign owners or custodians. I also determine that the exhibition or display of the exhibit objects at the Saint Louis Art Museum, St. Louis, Missouri, from on or about February 16, 2020, until on or about May 17, 2020, and at possible additional exhibitions or venues yet to be determined, is in the national interest. I have ordered that Public Notice of these determinations be published in the **Federal Register**.

FOR FURTHER INFORMATION CONTACT: Chi D. Tran, Paralegal Specialist, Office of the Legal Adviser, U.S. Department of State (telephone: 202–632–6471; email: *section2459@state.gov*). The mailing address is U.S. Department of State, L/PD, SA–5, Suite 5H03, Washington, DC 20522–0505.

SUPPLEMENTARY INFORMATION: The foregoing determinations were made pursuant to the authority vested in me by the Act of October 19, 1965 (79 Stat. 985; 22 U.S.C. 2459), Executive Order 12047 of March 27, 1978, the Foreign Affairs Reform and Restructuring Act of 1998 (112 Stat. 2681, *et seq.*; 22 U.S.C. 6501 note, *et seq.*), Delegation of Authority No. 234 of October 1, 1999, and Delegation of Authority No. 236–3 of August 28, 2000.

Marie Therese Porter Royce,

Assistant Secretary, Educational and Cultural Affairs, Department of State.

[FR Doc. 2020–00408 Filed 1–10–20; 8:45 am]

BILLING CODE 4710–05–P

DEPARTMENT OF TRANSPORTATION

Office of the Secretary

[Docket No. DOT–OST–2020–0003]

Agency Information Collection Activities: Request for Comments; Renewal of a Previously Approved Information Collection: U.S. Department of Transportation, Individual Complaint of Employment Discrimination Form

AGENCY: Office of the Secretary, U.S. Department of Transportation.

ACTION: Notice and request for comments.

SUMMARY: In accordance with the Paperwork Reduction Act of 1995, this notice announces that the U.S. Department of Transportation (DOT) will forward the Information Collection Request (ICR) abstracted below to the Office of Management and Budget (OMB) for renewal of a previously approved collection. The ICR describes the nature of the information collection and its expected cost and burden hours. The OMB approved the form in 2017 with its renewal required by January 31, 2020. The **Federal Register** Notice with a 60-day comment period soliciting comments on the form renewal was published on November 1, 2019 [FR Vol. 84, No. 212, page 58830]. No comments were received.

DATES: Comments on this notice must be received by February 12, 2020.

FOR FURTHER INFORMATION CONTACT: Beverly Onwubere, Associate Director, Equal Employment Opportunity (EEO) Complaints and Investigations Division (S–34), U.S. Department of Transportation, Departmental Office of Civil Rights, W78–316, 1200 New Jersey Avenue SE, Washington, DC 20590, 202–366–5988 (office), *beverly.onwubere@dot.gov.*

SUPPLEMENTARY INFORMATION:

Title: Individual Compliant of Employment Discrimination Form.

Form Number: DOT–F 1050–8.

OMB Control Number: 2105–0556.

Type of Request: Renewal of a previously approved collection.

Abstract: The DOT will utilize the form to collect information necessary to process EEO discrimination complaints filed by individuals who are Federal employees, former employees or applicants for employment with the Department. These complaints are processed in accordance with the U.S. Equal Employment Opportunity Commission's regulations, Title 29, Code of Federal Regulations, Part 1614, as amended. The DOT will use the form to: (a) Request requisite information from the applicant for processing his/her EEO discrimination complaint; and (b) obtain information to identify an individual or his or her attorney or other representative, if appropriate. An applicant's filing of an EEO discrimination complaint is solely voluntary. The DOT estimates that it takes an applicant approximately one hour to complete the form.

Affected Public: Federal employees, former employees, or applicants for employment with the Department.

Estimated Number of Respondents: 100 per year.

Estimated Total Annual Estimated Burden: 100 hours.

Frequency of Collection: An individual's filing of an EEO complaint is solely voluntary.

ADDRESSES: Send comments regarding the burden estimate, including suggestions for reducing the burden, to the Office of Management and Budget, Attention: Desk Officer for the Office of the Secretary of Transportation, 725 17th Street NW, Washington, DC 20503. Comments are invited on: Whether the proposed collection of information is necessary for the proper performance of the functions of the Department, including whether the information will have practical utility; the accuracy of the Department's estimate of the burden of the proposed information collection; ways to enhance the quality, utility and clarity of the information to be collected; and ways to minimize the burden of the collection of information on respondents, including the use of automated collection techniques or other forms of information technology. All responses to this notice will be summarized and included in the request for Office of Management and Budget approval. All comments will also become a matter of public record.

Authority: The Paperwork Reduction Act of 1995; 44 U.S.C. Chapter 35, as amended; and 49 CFR 1:48.

Issued in Washington, DC, on January 7, 2020.

Charles E. James, Sr.,

Director, Departmental Office of Civil Rights, U.S. Department of Transportation.

BILLING CODE 4910–9X–P

OMB No:

PAPERWORK REDUCTION ACT BURDEN STATEMENT

Under the Paperwork Act of 1995, no persons are required to respond to a collection of information unless it displays valid OMB control number. The public reporting burden for this voluntary collection of information is estimated to average 1 hour per response. If you wish to comment on the accuracy of the estimate or make suggestions for reducing this burden, please direct your comments to the U.S. Department of Transportation, Departmental Office of Civil Rights, S-34, 1200 New Jersey Avenue, SE., Washington, DC 20590

U.S. Department of Transportation

INDIVIDUAL COMPLAINT OF EMPLOYMENT DISCRIMINATION FORM INSTRUCTIONS

(*Read the following instructions carefully before you complete this form.*)
(*Please complete all items on the complaint form.*)

GENERAL: This form should be used only if you, as an applicant for employment with the Department of Transportation, or as a present or former Department of Transportation employee:

1) believe you have been discriminated against because of your **race, color, religion, sex** (gender, sexual harassment, pregnancy, sexual orientation, gender identity, or transgender status), **national origin, age** (40 years or older at the time of the event giving rise to your claim), **physical or mental disability, equal pay/compensation**, **genetic information**, or believe that you have been **retaliated** against for participating in activities covered under the Equal Employment Opportunity statutes; **and**

2) have presented the matter for informal resolution to an EEO Counselor within **45-calendar days** of the event giving rise to your claim, or within **45-calendar days** of first becoming aware of the alleged discrimination.

IMPORTANT NOTE: In certain situations, the information provided in Part III of the attached complaint form may be used in lieu of an affidavit in the investigation of your complaint. Accordingly, the information you provide in this part should be brief, clear, and complete.

WHEN TO FILE: In accordance with 29 C.F.R. § 1614.106, your formal complaint must be filed within **15-calendar days** of the date you received the Notice of Right to File a Discrimination Complaint form from your EEO Counselor. You must sign and date your complaint. If you are represented **by an attorney**, the attorney may sign the complaint on your behalf.

These time limits may be extended: **1)** if you show that you were not notified of the time limits and were not otherwise aware of them, or **2)** if you were prevented by circumstances beyond your control from submitting the matter within the time limits, or **3)** for other reasons considered sufficient by the Department.

REPRESENTATION: You may have a representative of your own choosing at all stages of the processing of your complaint. However, your representative will be disqualified if such representation would conflict with the official or collateral duties of the representative. No EEO Counselor or EEO Officer may serve as a representative. *(Your representative need not be an attorney, but only an attorney representative may sign the complaint on your behalf.)*

WHERE TO FILE: The complaint should be filed with the Associate Director, Equal Employment Opportunity Complaints and Investigations Division (S-34), Departmental Office of Civil Rights, 1200 New Jersey Avenue, S.E., W76-401, Washington, DC 20590. Filing instructions are contained in the Notice of Right to File a Discrimination Complaint form which was provided by your EEO Counselor. Keep a copy of the completed complaint form for your records.

(PLEASE ALSO READ THE PRIVACY ACT STATEMENT ON THE REVERSE SIDE)

PRIVACY ACT STATEMENT

1. **FORM NUMBER/TITLE DATE**: Department of Transportation Form Number 1050-8, Individual Complaint of Employment Discrimination with the Department of Transportation.

2. **AUTHORITY**: 42 U.S.C. 2000e; 29 U.S.C. 633a; PL 95-062 as amended; 5 U.S.C. 1303 and 1304; 5 C.F.R. 5.2 and 5.3; 29 C.F.R. 1614.105 and 1614.107; and Executive Order 11478, as amended.

3. **PRINCIPAL PURPOSES**: The purpose of this complaint form, whether recorded initially on the form or taken from a letter from the Complainant, is to record the filing of a formal written complaint of employment discrimination with the Department of Transportation on the grounds of race, color, religion, sex (gender, sexual harassment, pregnancy, sexual orientation, gender identity, or transgender status), national origin, age, physical or mental disability, genetic information, or reprisal, and to reach a decision on the complaint. Information provided on this form will be used by the Department of Transportation to determine whether the complaint was timely filed and whether the claims in the complaint are within the purview of 29 C.F.R. Part 1614, and to provide a factual basis for investigation of the complaint.

4. **ROUTINE USES**: Other disclosures may be:

   a. to respond to a request from a Member of Congress regarding the status of the complaint or appeal;
   b. to respond to a court subpoena and/or to refer to a district court in connection with a civil suit;
   c. to disclose information to authorized officials or personnel to adjudicate a complaint or appeal;
   d. to disclose information to another Federal agency or to a court or third party in litigation when the Government is party to a suit before the court.

5. **WHETHER DISCLOSURE IS MANDATORY OR VOLUNTARY, AND EFFECT ON INDIVIDUAL BY NOT PROVIDING INFORMATION**: Formal complaints of employment discrimination must be in writing, signed by the Complainant (or attorney representative), and must identify the parties and action or policy at issue. Failure to comply may result in the Department of Transportation dismissing the complaint. It is not mandatory that this form be used to provide the requested information.

DETACH AND KEEP THIS PAGE WHEN YOU FILE YOUR COMPLAINT

ONE DOT Working Better Together DEPARTMENT OF TRANSPORTATION

INDIVIDUAL COMPLAINT OF EMPLOYMENT DISCRIMINATION WITH THE DEPARTMENT OF TRANSPORTATION

FOR OFFICE USE ONLY

DEPARTMENT CASE NUMBER

FILING DATE

PART I COMPLAINANT IDENTIFICATION INFORMATION

1. Name (Last, First, Middle Initial):

2. Telephone/Fax (Include Area Code):

Home: Fax:

Work: Fax:

E-Mail:

3. Present Home Address (You must notify the Departmental Office of Civil Rights of any changes to your address while the complaint is pending, or your complaint may be dismissed):

Street Address

City State Zip Code

4. If you are a *current* or *former* employee of the Federal government, list your most recent title, series, and grade.

Title Series Grade

5. Name and Address of Organization Where You Work (If a Department of Transportation Employee):

Office and Staff Symbol:

Street Address:

City: State: Zip Code:

6. Employment Status in Relation to this Complaint:

☐ **Applicant** ☐ **Probationary** ☐ **Career/Career Conditional**

☐ **Former Employee**

Date Last Employed at Department

☐ **Retired**

Date of Retirement

☐ **Other**

Specify

7. I certify that all of the statements made in this complaint are true, complete, and correct to the best of my knowledge and belief.

Signature of Complainant or ATTORNEY Representative **Date**

PART II DESIGNATION OF REPRESENTATIVE

8. You may represent yourself in this complaint or you may choose someone to represent you. Your representative does not have to be an attorney. You may change your designation of a representative at a later date, but you must notify the Departmental Office of Civil Rights immediately in writing of any change, and you must include the same information requested in this Part.

"I hereby designate _____ (Please Print Name) to serve as my representative during the course of this complaint. I understand that my representative is authorized to act on my behalf.

9. Representative's Mailing Address:

Firm/Organization

Street Address

City State Zip Code

10. Representative's Employer (If Federal Agency):

11. Representative's Telephone/Fax (Include Area Code):

Telephone: Fax:

12. SIGNATURE of Complainant (or ATTORNEY) **DATE**

PART III ALLEGED DISCRIMINATORY ACTIONS

13. Name and Address of Agency/office that took the action at issue (if different than item 5.)

Office and Organizational Component

Street Address

City State Zip Code

14. If your complaint involves non-selection for a position, please complete the following:

Position Title Series Grade

Vacancy Announcement No. Date Learned of Non-selection

15. Mark below ONLY the basis(es) you believe were relied on to take the actions described in #17.

- ☐ Race (Specify) _____
- ☐ Color (State Complexion) _____
- ☐ Religion (Specify) _____
- ☐ Sex (Gender, Sexual Harassment, Pregnancy, Sexual Orientation, Gender Identity, or Transgender Status) _____
- ☐ National Origin (Specify) _____
- ☐ Age (Date of Birth) _____
- ☐ Mental Disability (Specify) _____
- ☐ Physical Disability (Specify) _____
- ☐ Equal Pay/Compensation (Specify) _____
- ☐ Genetic Information (Specify) _____
- ☐ Retaliation (Date(s) of prior EEO Activity) _____

16. Mark below ONLY the claim(s) you believe were relied on to take the actions described in #17.

☐	1. Appointment/Hire	☐	14. Reassignment A. Denied B. Directed
☐	2. Assignment Of Duties	☐	15. Reasonable Accommodation – Disability
☐	3. Awards	☐	16. Reinstatement
☐	4. Conversion To Full-Time	☐	17. Religious Accommodation
☐	5. Disciplinary Action A. Demotion B. Reprimand C. Suspension D. Termination E. Other	☐	18. Retirement
☐	6. Duty Hours	☐	19. Sex Stereotyping (LGBT-related discrimination only)
☐	7. Evaluation/Appraisal	☐	20. Telework
☐	8. Examination/Test	☐	21. Termination
☐	9. Harassment A. Non-Sexual B. Sexual C. Hostile Work Environment (non-sexual) D. Hostile Work Environment (sexual)	☐	22. Terms/Conditions Of Employment

☐	10. Medical Examination	☐	23. Time And Attendance
☐	11. Pay Including Overtime	☐	24. Training
☐	12. Performance Evaluation/ Appraisal	☐	25. Other
☐	13. Promotion/Non-Selection		

17. (A) Describe the action taken against you that you believe was discriminatory; (B) Give the date the action occurred, and the name of each person responsible for the action; (C) Describe how you were treated differently than other employees or applicants because of your race, color, religion, sex (gender, sexual harassment, pregnancy, sexual orientation, gender identity, or transgender status), national origin, age (40 years or older), disability (mental and/or physical), genetic information, or in retaliation for your participation in the EEO complaint process or opposition to alleged discriminatory practices; (D) indicate what harm, if any, came to you in your work situation as a result of this action. (You may attach extra sheets.)

18. What remedial or corrective action are you seeking?

PART IV EEO COUNSELOR CONTACT

19. When did the most recent discriminatory event occur?

Month Day Year

20. When did you first become aware of the alleged discrimination?

Month Day Year

21. When did you contact an EEO Counselor?

Month Day Year

22. Did you discuss ALL actions raised in item 17 with an EEO Counselor? ☐ YES ☐ NO
(If no, explain on attached sheet)

23. Name and Telephone number of EEO Counselor

Name Telephone No.

24. When did you receive your Notice of Right to File a Discrimination Complaint?

Month Day Year

25. On this same matter, have you filed a grievance or appeal under:

- Negotiated Grievance procedures ☐ YES ☐ NO
- Agency grievance procedure ☐ YES ☐ NO
- MSPB appeal procedure ☐ YES ☐ NO

If you filed a grievance or appeal, provide date filed, case number, and present status.

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Part II

Department of the Treasury

Internal Revenue Service

26 CFR 1

Investing in Qualified Opportunity Funds; Final Rule

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9889]

RIN 1545–BP04

Investing in Qualified Opportunity Funds

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains final regulations governing the extent to which taxpayers may elect the Federal income tax benefits provided by section 1400Z–2 of the Internal Revenue Code (Code) with respect to certain equity interests in a qualified opportunity fund (QOF). The final regulations address the comments received in response to the two notices of proposed rulemaking issued under section 1400Z–2 and provide additional guidance for taxpayers eligible to elect to temporarily defer the inclusion in gross income of certain gains if corresponding amounts are invested in certain equity interests in QOFs, as well as guidance on the ability of such taxpayers to exclude from gross income additional gain recognized after holding those equity interests for at least 10 years. The final regulations also address various requirements that must be met for an entity to qualify as a QOF, including requirements that must be met for an entity to qualify as a qualified opportunity zone business. The final regulations affect entities that self-certify as QOFs and eligible taxpayers that make investments, whether qualifying or non-qualifying, in such entities.

DATES:

Effective date: The final regulations contained in this document are effective on March 13, 2020.

Applicability dates: See **SUPPLEMENTARY INFORMATION.**

FOR FURTHER INFORMATION CONTACT: Concerning section 1400Z–2 and these regulations generally, Alfred H. Bae, (202) 317–7006, or Kyle C. Griffin, (202) 317–4718, of the Office of Associate Chief Counsel (Income Tax and Accounting); concerning issues related to C corporations and consolidated groups, Jeremy Aron-Dine, (202) 317–6848, or Sarah Hoyt, (202) 317–5024, of the Office of Associate Chief Counsel (Corporate); concerning issues related to gains from financial contracts, REITs, or RICs, Andrea Hoffenson or Pamela Lew, (202) 317–7053, of the Office of Associate Chief Counsel (Financial Institutions and Products); concerning issues related to investments by foreign persons, Eric Florenz, (202) 317–6941, or Milton Cahn (202) 317–6937, of the Office of Associate Chief Counsel (International); concerning issues related to partnerships, S corporations or trusts, Marla Borkson, Sonia Kothari, or Vishal Amin, at (202) 317–6850, and concerning issues related to estates and gifts, Leslie Finlow or Lorraine Gardner, at (202) 317–6859, of the Office of Associate Chief Counsel (Passthroughs and Special Industries). These numbers are not toll-free numbers.

SUPPLEMENTARY INFORMATION:

Background

This document amends the Income Tax Regulations (26 CFR part 1) by adding final regulations under section 1400Z–2 of the Code. Section 13823 of Public Law 115–97, 131 Stat. 2054 (December 22, 2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA), added sections 1400Z–1 and 1400Z–2 to the Code. Section 1400Z–1 addresses the designation of population census tracts located in the 50 states, U.S. territories, and the District of Columbia as qualified opportunity zones (QOZs). See Notice 2018–48, 2018–28 I.R.B. 9, and Notice 2019–42, 2019–29 I.R.B. 352, for the list of population census tracts designated as QOZs (each, a QOZ designation notice).

Section 1400Z–2 provides two main Federal income tax benefits to eligible taxpayers that make longer-term investments of new capital in one or more designated QOZs through QOFs and qualified opportunity zone businesses. The first main Federal income tax benefit provided by section 1400Z–2 is the ability of an eligible taxpayer, upon the making of a valid election, to defer until as late as December 31, 2026, the inclusion in gross income of certain gains that would otherwise be recognized in a taxable year if the taxpayer invests a corresponding amount of such gain in a qualifying investment in a QOF within a 180-day statutory period. The eligible taxpayer may potentially exclude 10 percent of such deferred gain from gross income if the eligible taxpayer holds the qualifying investment in the QOF for at least five years. See section 1400Z–2(b)(2)(B)(iii). An additional five percent of such gain may potentially be excluded from gross income if the eligible taxpayer holds that qualifying investment for at least seven years. See section 1400Z–2(b)(2)(B)(iv). The second main Federal income tax benefit provided by section 1400Z–2 is the ability for the eligible taxpayer, upon the making of a separate valid election, to exclude from gross income any appreciation on the eligible taxpayer's qualifying investment in the QOF if the eligible taxpayer holds the qualifying investment for at least 10 years. See section 1400Z–2(c).

On October 29, 2018, the Department of the Treasury (Treasury Department) and the IRS published a notice of proposed rulemaking (REG–115420–18) in the **Federal Register** (83 FR 54279) containing a first set of proposed regulations under section 1400Z–2 (October 2018 proposed regulations). The October 2018 proposed regulations addressed the type of gain that is eligible for deferral by eligible taxpayers, the timing by which eligible taxpayers must invest amounts in QOFs corresponding to the gains to be deferred, and the manner in which eligible taxpayers could make deferral elections of any gains. The October 2018 proposed regulations also provided rules for the self-certification of QOFs, valuation of QOF assets, and general guidance on the requirements for a corporation or partnership to be a qualified opportunity zone business, including providing that the term ''substantially all'' as used in section 1400Z–2(d)(3)(A)(i) means at least 70 percent. The Treasury Department and the IRS received 180 written and electronic comments responding to the October 2018 proposed regulations. A public hearing on the October 2018 proposed regulations was held on February 14, 2019.

A second notice of proposed rulemaking (REG–120186–18) was published in the **Federal Register** (84 FR 18652) on May 1, 2019, containing additional proposed regulations under section 1400Z–2 (May 2019 proposed regulations). The May 2019 proposed regulations updated portions of the October 2018 proposed regulations to address various issues, including: The definition of the term ''substantially all'' in each of the various places the term appears in section 1400Z–2; transactions resulting in the inclusion under section 1400Z–2(a)(1)(B) and (b) of eligible gain that an eligible taxpayer elected to defer under section 1400Z–2(a); the treatment of leased property used by a QOF or qualified opportunity zone business; the use of qualified opportunity zone business property in the QOZ; the sourcing of gross income to the qualified opportunity zone business; and the ''reasonable period'' for a QOF to reinvest proceeds from the sale of qualifying assets without paying the penalty imposed by section 1400Z–2(f)(1). The Treasury Department and

the IRS received 127 written and electronic comments responding to the May 2019 proposed regulations. A public hearing on the May 2019 proposed regulations was held on July 9, 2019.

The October 2018 proposed regulations and the May 2019 proposed regulations are collectively referred to in this Treasury decision as the ''proposed regulations.'' All comments received on the proposed regulations are available at *www.regulations.gov* or upon request.

The preamble to the May 2019 proposed regulations stated that the Treasury Department and the IRS would schedule tribal consultation with officials of governments of Federally recognized Indian tribes (Indian tribal governments) before finalizing the proposed regulations to obtain additional input, within the meaning of the Treasury Department's Tribal Consultation Policy (80 FR 57434, September 23, 2015), in accordance with Executive Order 13175, ''Consultation and Coordination with Indian tribal governments'' (65 FR 67249, November 6, 2000), on the ability of entities organized under the law of an Indian tribe to be QOFs or qualified opportunity zone businesses, whether any additional guidance may be needed regarding the ability of QOFs or qualified opportunity zone businesses to lease tribal government Federal trust lands or leased real property located on such lands, and any other tribal implications of the proposed regulations. This tribal consultation took place via telephone on October 21, 2019 (Consultation) (see part VI. of the Special Analyses for additional discussion).

After full consideration of all comments received on the proposed regulations, including comments received from the Consultation, and the testimony heard at both public hearings, this Treasury decision adopts the proposed regulations with modifications in response to such comments and testimony, as described in the Summary of Comments and Explanation of Revisions following this Background.

For dates of applicability, see §§ 1.1400Z2(a)–1, 1.1400Z2(b)–1, 1.1400Z2(c)–1, 1.1400Z2(d)–1, 1.1400Z2(d)–2, 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 set forth in this document, which provide that the final regulations set forth in §§ 1.1400Z2(a)–1 through 1.1400Z2(d)–2, 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 are generally applicable for taxable years beginning after March 13, 2020. With respect to the portion of a taxpayer's first taxable year ending after December 21, 2017 that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, taxpayers may choose either (1) to apply the final regulations set forth in §§ 1.1400Z2(a)–1 through 1.1400Z2(d)–2, 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 contained in this document, if applied in a consistent manner for all such taxable years, or (2) to rely on each section of proposed §§ 1.1400Z2(a)–1 through 1.1400Z2(g)–1, except for proposed § 1.1400Z2(c)–1, contained in the notice of proposed rulemaking documents published on October 29, 2018, and on May 1, 2019, in the **Federal Register** (83 FR 54279; 84 FR 18652), but only if relied upon in a consistent manner for all such taxable years. Taxpayers relying on each section of proposed §§ 1.1400Z2(a)–1 through 1.1400Z2(g)–1, except for proposed § 1.1400Z2(c)–1, contained in the notice of proposed rulemaking documents published on October 29, 2018, and on May 1, 2019, in the **Federal Register** (83 FR 54279; 84 FR 18652), must apply § 1.1400Z2(c)–1 of the final regulations contained in this document with respect to any elections made under section 1400Z–2(c).

Summary of Comments and Explanation of Revisions

I. Overview

The final regulations set forth in §§ 1.1400Z2(a)–1 through 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 (section 1400Z–2 regulations) retain the basic approach and structure of the proposed regulations, with certain revisions. The Treasury Department and the IRS have refined and clarified certain aspects of the proposed regulations in these final regulations to make the rules easier to follow and understand. Specifically, proposed § 1.1400Z2(d)–1 has been split into two separate sections: §§ 1.1400Z2(d)–1 and 1.1400Z2(d)–2. Further, the Treasury Department and the IRS have combined duplicative rules regarding QOFs and qualified opportunity zone businesses, and have added defined terms to allow the reader to more intuitively grasp the meaning of the numerous provisions cross-referenced in the final regulations.

This Summary of Comments and Explanation of Revisions discusses those revisions as well as comments received in response to each of §§ 1.1400Z2(a)–1 through 1.1400Z2(g)–1 of the proposed regulations (proposed §§ 1.1400Z2(a)–1 through 1.1400Z2(g)–1). The rules proposed in the October 2018 proposed regulations and the May 2019 proposed regulations are explained in greater detail in the Explanation of Provisions sections of the preambles to each set of proposed regulations.

II. Comments on and Changes to Proposed § 1.1400Z2(a)–1

Proposed § 1.1400Z2(a)–1 prescribed rules regarding the election to defer gains under section 1400Z–2(a)(1), including rules regarding which taxpayers are eligible to make the election, which gains are eligible for deferral, and the method by which eligible taxpayers may make deferral elections. This part II describes the revisions made to proposed § 1.1400Z2(a)–1 based on the comments received on those proposed rules, including revisions to the definition of eligible gain and revisions to the rules applying the statutory 180-period and other requirements with regard to the making of a qualifying investment in a QOF.

A. Definitions and Related Operating Rules

1. Eligible Gain

Proposed § 1.1400Z2(a)–1(b)(2) generally provided that an amount of gain would be eligible for deferral under section 1400Z–2(a) if the gain (i) is treated as a capital gain for Federal income tax purposes that would be recognized for Federal income tax purposes before January 1, 2027, if section 1400Z–2(a)(1) did not apply to defer recognition of the gain; and (ii) did not arise from a sale or exchange with a related person within the meaning of section 1400Z–2(e)(2) (eligible gain). This part II.A.1. describes the comments received on various aspects of the proposed definition of eligible gain and explains the revisions, based on those comments, adopted by § 1.1400Z2(a)–1(b)(11) of the final regulations.

a. Gains From Section 1231 Property

Proposed § 1.1400Z2(a)–1(b)(2)(iii) of the May 2019 proposed regulations provided that the only gain arising from property used in the taxpayer's trade or business (section 1231 property) eligible for deferral under section 1400Z–2(a)(1) was ''capital gain net income'' for a taxable year, which was defined as the amount by which the capital gains arising from all of a taxpayer's section 1231 property exceeded all of the taxpayer's losses from section 1231 property for a taxable year. The Treasury Department and the IRS have reconsidered this approach based on the numerous comments received on this aspect of the May 2019 proposed regulations.

i. Section 1231 Generally

Section 1231 governs the character of a taxpayer's gains or losses with respect to section 1231 property not otherwise characterized by section 1245 or 1250. Section 1231(b) defines ''section 1231 property'' generally as depreciable or real property that is used in the taxpayer's trade or business and held for more than one year, subject to enumerated exceptions (for example, property held by the taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business).

Under section 1231(a)(1), if a taxpayer's aggregate gains from each sale and exchange (each gain, a section 1231 gain) during the taxable year exceed the taxpayer's aggregate losses from each sale and exchange (each loss, a section 1231 loss), the taxpayer's section 1231 gains and section 1231 losses are treated as long-term capital gains and long-term capital losses, respectively. However, if the aggregate section 1231 gains do not exceed the aggregate section 1231 losses (that is, the aggregate amount of section 1231 gains equals or is less than the aggregate amount of section 1231 losses), those gains and losses are not treated as gains and losses from sales or exchanges of capital assets (that is, they are treated as ordinary income and ordinary losses). See sections 64, 1221, 1222, and 1231(a)(2) of the Code.

Several provisions of the Code may apply to limit the long-term capital treatment otherwise potentially provided under section 1231(a)(1). For example, prior to the aggregation of section 1231 gains and losses under section 1231(a), the recapture rules of sections 1245 and 1250 must be applied on an asset-by-asset basis. Section 1245, which applies to sales, exchanges, or dispositions of depreciable tangible and intangible property, characterizes any gain recognized as ordinary income (as defined in section 64) to the extent depreciation or amortization has been allowed or allowable with respect to that property. Section 1250 provides a similar ''pre-aggregation'' recapture rule with regard to sales, exchanges, or dispositions of depreciable real property that is not section 1245 property, and it characterizes as ordinary income (as defined in section 64) any gain recognized in excess of straight line depreciation.

Section 1231(c), on the other hand, sets forth a ''post-aggregation'' recapture provision, requiring the net section 1231 gain for any taxable year to be treated as ordinary income to the extent that such gain does not exceed the non-recaptured net section 1231 losses. Non-recaptured net section 1231 losses are net section 1231 losses for the five most recent preceding taxable years of the taxpayer that have not yet been recaptured. However, section 1231(c)(5), provides that the principles of section 1231(a)(4) apply for purposes of section 1231(c). Under section 1231(a)(4), to determine whether gains exceed losses for the section 1231(a) character determination, section 1231 gains are included only if and to the extent that they are taken into account in computing gross income, and section 1231 losses are included only if and to the extent that they are taken into account in computing taxable income.

Essentially, the operation of the ''pre-aggregation'' recapture rules under sections 1245 and 1250, as well as the ''post-aggregation'' recapture rule under section 1231(c), requires a gain recognized with respect to section 1231 property potentially to be treated as ordinary income, even if that gain otherwise would have been characterized differently under section 1231(a) in the absence of such recapture rules.

Section 64 defines the term ''ordinary income'' for purposes of subtitle A of the Code (subtitle A), which includes sections 1231, 1245, 1250, and 1400Z–2, to include ''any gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b),'' and provides further that ''[a]ny gain from the sale or exchange of property which is treated or considered, under other provisions of this subtitle, as 'ordinary income' shall be treated as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b).'' See for example, sections 1231(c), 1245, and 1250; see also §§ 1.1245–1(a)(1), 1.1245–1(b)(2), 1.1250–1(a)(1), 1.1250–1(b)(1), and 1.1250–1(c)(1).

ii. Comments on Treatment of Section 1231 Property

Commenters suggested that the gross amount of section 1231 gain realized from sales or exchanges of section 1231 property should be eligible gain, provided that such gain is determined to be capital gain at the end of the taxable year by taking into account all section 1231 gains and section 1231 losses. Some commenters also recommended that the 180-day period for investment begin on the date of the sale or exchange that gives rise to a section 1231 gain instead of at the end of the taxable year. Many of the commenters recognized that, because section 1231(a)(1) requires a netting process to determine whether section 1231 gains and losses are capital in character, investors might not be certain if any of the section 1231 gain invested from sales or exchanges before the end of the taxable year is capital in character. Therefore, several commenters suggested that gross section 1231 gains be eligible for investment on the date of the sale or exchange, contingent on such gains being capital in character as determined by the netting process at the end of the taxable year. Under this approach, if the section 1231 gains invested in a QOF during a taxable year are determined not to be capital in character because section 1231 gains for the year do not exceed section 1231 losses, the section 1231 gains invested that year would constitute an investment that does not qualify for deferral under section 1400Z–2(a)(1) (a non-qualifying investment).

In the alternative, many commenters recommended an election to permit a taxpayer to begin the 180-day period for section 1231 gains on the last day of the taxable year. This election would accommodate the needs of taxpayers who are unable to determine whether section 1231 gains will be capital in character until all transactions involving section 1231 property have been completed for a taxable year. As a model for this elective approach, commenters referred to proposed § 1.1400Z2(a)–1(c)(2)(iii)(B), which permits a partner to elect to align its 180-day period with that of the partnership, that is, the date of the sale or exchange giving rise to such gain.

Commenters observed that because gain that is deferred under section 1400Z–2 would not be taken into account in computing gross income until recognized, pursuant to section 1231(a)(4), any deferred gains would be excluded from the section 1231(a) character determination. As a result, taxpayers could ensure that section 1231 gains do not exceed section 1231 losses for a taxable year under section 1231(a) by investing the excess of gains realized from the sale or exchange of section 1231 property over the losses from those sales, thus, rendering all section 1231 losses, that otherwise would be capital in character, ordinary in character. However, commenters noted that section 1231(a)(4) gives rise to a circularity issue if applied in this manner. If the only section 1231 gains that are eligible for deferral under section 1400Z–2 are capital character section 1231 gains, then, if a taxpayer invests an amount of section 1231 gains in a QOF such that the character determination under section 1231(a) produces ordinary character gains and

losses for a taxable year, then all section 1231 gains in that taxable year would not be eligible gains. Therefore, in light of the application of section 1231(a)(4), a taxpayer could only defer an amount of section 1231 gains such that even after subtracting deferred gains, the remaining non-deferred section 1231 gains for the taxable year would still exceed section 1231 losses. In many cases, this excess amount would be substantially less than the gross amount of section 1231 gains realized from the sale or exchange section 1231 property for the taxable year. To resolve both the issue of shifting the character of otherwise capital character section 1231 losses to ordinary character section 1231 losses and the circularity issue described previously, a commenter suggested treating section 1231 gains deferred under section 1400Z–2 as if they were ''taken into account in computing gross income'' for purposes of section 1231(a)(4). Under such a rule, even if the full amount of section 1231 gains that are capital in character were deferred under section 1400Z–2, section 1231 gains would still exceed section 1231 losses and both section 1231 gains and losses would retain their capital character after the application of section 1231(a).

Several commenters also requested additional rules with respect to the application of the rules of section 1231(c) (described earlier) to deferred section 1231 gain. Commenters suggested a rule providing that deferred section 1231 gain to the extent of non-recaptured net section 1231 losses be treated as ordinary income when those gains are recognized rather than in the year of gain deferral. In some instances, this approach may require a taxpayer to account for its non-recaptured net section 1231 losses for a period longer than the five most recent taxable years section 1231(c) requires. A commenter suggested that the extension of the recapture period be accomplished by means of an election by the taxpayer at the time any section 1231 gain is deferred under section 1400Z–2. In electing to defer section 1231 gain, a taxpayer also would elect to extend the section 1231(c) recapture period to the longer of the statutory five-year period or the taxable year that includes December 31, 2026. Alternatively, some commenters asked that section 1231(c) not apply at all to deferred section 1231 gains.

One commenter also noted that the term ''capital gain net income'' already is defined in section 1222(9), and that its separate definition and use in the section 1400Z–2 regulations might lead to confusion.

In response to these comments, the final regulations provide that eligible gains that may be deferred pursuant to section 1400Z–2(a)(1)(A) and the section 1400Z–2 regulations include gains from the sale or exchange of property described in section 1231(b) not required to be characterized as ordinary income by sections 1245 or 1250 (qualified section 1231 gains), regardless of whether section 1231(a) (without regard to section 1231(a)(4)) would determine those gains to be capital or ordinary in character. As noted earlier, section 64 provides that gains from the sale or exchange of section 1231 property generally are not considered ordinary income for purposes of subtitle A, although recaptured income under section 1245 or 1250 would be ordinary income under section 64.

However, the final regulations do not set forth a special rule to address the application of section 1231(a)(4) for purposes of applying section 1400Z–2 and the section 1400Z–2 regulations. Thus, section 1231(a)(4) applies to eligible section 1231 gains deferred pursuant to section 1400Z–2(a)(1)(A) as it would under similar deferral provisions, such as sections 453 and 1031. That is, unless a section 1231 gain (as defined in section 1231(a)(3)(A)) is taken into account in computing gross income in a taxable year, section 1231(a)(4) does not include that gain in calculating whether section 1231 gains exceed section 1231 losses under section 1231(a)(1) for the taxable year.

Additionally, these final regulations do not alter the statutory application of the section 1231(c) recapture of net ordinary loss. Therefore, if a deferral election with respect to an eligible section 1231 gain is made in year 1, any non-recaptured net section 1231 losses from the five most recent taxable years that precede year 1 apply to recapture as ordinary income in year 1 any net section 1231 gain that has not been deferred in year 1. In other words, the section 1231(c) amount that would have applied to the eligible section 1231 gain absent a deferral election and corresponding investment in a QOF is not an attribute associated with the deferred eligible section 1231 gain that is taken into account in applying section 1231 in the ultimate year in which the deferred gain is included in income under section 1400Z–2(b) and the section 1400Z–2 regulations. Instead, when deferred eligible section 1231 gain is subsequently included in income on December 31, 2026, or on an earlier date as a result of an inclusion event, section 1231(c) will recapture net section 1231 gain in the year of inclusion by taking into account non-recaptured section 1231 losses only from the five most recent taxable years preceding the taxable year of inclusion.

Unlike the net approach of the proposed regulations, the final regulations adopt a gross approach to eligible section 1231 gains without regard to any section 1231 losses. In addition, under the final regulations, the character of eligible section 1231 gains, other than as gains arising from the sale or exchange of section 1231 property, is not determined until the taxable year such gains are taken into account in computing gross income pursuant to section 1231(a)(4). Accordingly, the term ''capital gain net income'' used in the proposed regulations is no longer applicable when referring to the amount of any gain from the sale or exchange of section 1231 property that is eligible for deferral under section 1400Z–2(a)(1)(A) and the section 1400Z–2 regulations.

The Treasury Department and the IRS have determined that a gross approach that does not apply section 1231(a) and (c) (gross approach) to determine eligible gain from the sale or exchange of section 1231 property is consistent with the long-standing rules of section 64, and is appropriate due to the complexity of applying section 1231 to deferred gains generally. Moreover, limiting eligible gain from the sale or exchange of section 1231 property to an amount less than the net section 1231 gains for a taxable year would impose a significant administrative burden on persons that are required to report the recognition of such gains during the taxable year under Federal income tax accounting principles (eligible taxpayers). Similarly, a gross approach to determine eligible section 1231 gains eliminates complexity and uncertainty in determining eligible gain for partnerships and S corporations that are eligible taxpayers.

As discussed in part II.A.3.a. of this Summary of Comments and Explanation of Revisions, because eligible gains include the gross amount of eligible section 1231 gains unreduced by section 1231 losses regardless of character, it is not necessary for an investor to wait until the end of the taxable year to determine whether any eligible section 1231 gains are eligible gains. As a consequence, the final regulations provide that the 180-day period for investing an amount with respect to an eligible section 1231 gain for which a deferral election is to be made begins on the date of the sale or exchange that gives rise to the eligible section 1231 gain.

b. Character of Eligible Gain

Section 1400Z–2(a)(1)(A) provides that if a taxpayer has ''gain from the sale to, or exchange with, an unrelated person of any property held by the taxpayer,'' the taxpayer may elect to exclude from gross income for the taxable year the aggregate amount of such gain invested by the taxpayer in a QOF during the 180-day period beginning on the date of such sale or exchange. The Treasury Department and the IRS considered whether ''gain'' eligible for deferral under section 1400Z–2 should include both gain from the disposition of a capital asset as well as gain treated as ordinary income under subtitle A.

As noted in part II.A.1.a, section 64 of the Code provides generally that for purposes of subtitle A, the term ''ordinary income'' includes any gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b). Any gain from the sale or exchange of property which is treated or considered, under other provisions of subtitle A, as ''ordinary income'' shall be treated as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b). Thus, for purposes of subtitle A, including section 1400Z–2, section 64 defines gains treated as ordinary income as categorically different from gains from the sale or exchange of capital assets or section 1231 property.

In this regard, proposed § 1.1400Z2(a)–1(b)(2)(i) as contained in the October 2018 proposed regulations provided that an amount of gain is an ''eligible gain,'' and thus is eligible for deferral under section 1400Z–2(a), if the gain is treated as a capital gain for Federal income tax purposes. In addition, the May 2019 proposed regulations provided that the only gain arising from section 1231 property eligible for deferral under section 1400Z–2(a)(1) was ''capital gain net income'' for a taxable year, which was defined as the amount by which the capital gains arising from all of a taxpayer's section 1231 property exceeded all of the taxpayer's losses from section 1231 property for a taxable year.

Based on the statutory text of section 1400Z–2(a)(1)(A), several commenters requested that the final regulations permit taxpayers to treat both capital gains and ordinary gains (that is, gains treated as ordinary income) as eligible gains. For example, commenters requested that gain from property used in a trade or business required to be characterized as ordinary income, such as recapture income under section 1231(c) or 1245(a), should be permitted to be invested in a QOF.

After consideration of the language, structure and purpose of section 1400Z–2 as a whole, the Treasury Department and the IRS have determined that it would be inconsistent with section 64 and the statutory framework of section 1400Z–2 to extend the meaning of the term ''gain'' in section 1400Z–2(a)(1) to gain required to be treated as ordinary income under subtitle A, including section 1245 gain. The interpretation of the Treasury Department and the IRS of the text and structure of the statute is confirmed by the legislative history, which explicitly identifies ''capital gains'' as the gains that are eligible for deferral. See H.R. Rep. No. 115–466, at 537–540 (Dec. 15, 2017) (Conference Report).

Accordingly, the Treasury Department and the IRS have retained in the final regulations the general rule set forth in the proposed regulations that limits eligible gains to gains treated as capital gains for Federal income tax purposes. For purposes of section 1400Z–2(a)(1), eligible gains generally include gains from the disposition of capital assets as defined in section 1221(a), gains from the disposition of property described in section 1231(b), and income treated as capital gain under any provision of the Code, such as capital gain dividends distributed by certain corporations. For this purpose, both long-term capital gain and short-term capital gain may be determined to be eligible gain under the section 1400Z–2 regulations. However, consistent with section 64, any gain required to be treated as ordinary income under subtitle A, such as section 1245 recapture income, is not eligible gain.

In that regard, one commenter suggested that, unlike other investors in QOFs, existing residents of a QOZ should be provided a special accommodation not available to other eligible taxpayers—such residents should be permitted to invest any gain, regardless of character, in QOFs and elect to defer the corresponding amounts in accordance with section 1400Z–2. The Treasury Department and the IRS have determined that neither the statutory language nor legislative history of section 1400Z–2 supports different treatment for residents of QOZs regarding the deferral of eligible gains. Section 1400Z–2 references the term ''taxpayer,'' which section 7701(a)(14) defines as ''any person subject to any internal revenue tax.'' In turn, section 7701(a)(1) defines the term ''person'' to include ''an individual, a trust, estate, partnership, association, company or corporation.''

The Treasury Department and the IRS have determined that construction of the term ''taxpayer'' in accordance with section 7701(a)(14) would be consistent with the language and purpose of section 1400Z–2 as a whole, and therefore would give effect to the intent of Congress. Moreover, disparate treatment of eligible taxpayers residing in QOZs and those who do not is not warranted given that the statute equally incents investment in QOZs by any taxpayer, including those that have historically invested in businesses operated within QOZs and those that have not. Accordingly, the section 1400Z–2 regulations do not adopt the comment recommending special treatment for residents of QOZs to invest ordinary income, including gain required to be treated as ordinary income under subtitle A, in QOFs.

c. Gain From Sales of Capital Assets, Unreduced by Any Losses

One commenter also requested clarification that the deferral election under section 1400Z–2(a)(1) applies to the gross amount of gain treated as capital gain unreduced by losses. The proposed regulations generally provided that in the case of gain from the sale of a capital asset as defined under section 1221, the full amount of capital gain from that sale or exchange, unreduced by any losses, is eligible gain that generally may be invested during the 180-day period beginning on the date of the sale or exchange of the property giving rise to the gain.

The section 1400Z–2 regulations retain the general rule of the proposed regulations providing that the full amount of gain that would be recognized from the sale or exchange of a capital asset as defined under section 1221, unreduced by any losses, is eligible gain and therefore eligible taxpayers do not have to net a gain from a section 1221 capital asset against the sum of the taxpayer's losses from section 1221 capital assets. Thus, if a capital gain is realized by an eligible taxpayer during a taxable year, section 1400Z–2 and the section 1400Z–2 regulations generally do not require that any losses reduce the amount of the gain that may be an eligible gain.

However, gain that otherwise may qualify as a capital gain may be required to be recharacterized or redetermined by other provisions of the Code. For example, sections 1245 and 1250 may require gain that potentially could be characterized as capital in nature to instead be treated as ordinary income ''notwithstanding any other provision of

this subtitle,'' referring to subtitle A, which includes section 1400Z–2. Consistent with section 64, if a provision of the Code requires the character of a potential capital gain to be recharacterized, redetermined, or treated as ordinary income for purposes of subtitle A, such gain cannot be, and is not, treated as other than ordinary income under the Code, and therefore is not eligible gain for purposes of section 1400Z–2 and the section 1400Z–2 regulations. See §§ 1.1245–1(a)(1), 1.1245–1(b)(2), 1.1250–1(a)(1), 1.1250–1(b)(1), and 1.1250–1(c)(1).

d. Gains From Sales to, or Exchanges of Property With, a QOF or Qualified Opportunity Zone Business

The October 2018 proposed regulations provided that eligible gain does not include gain from the sale to, or the exchange of property with, a person that is related to the taxpayer within the meaning of section 1400Z–2(e)(2). Section 1400Z–2(d)(2)(D) and the May 2019 proposed regulations provided that qualified opportunity zone business property that a QOF owns must be acquired by the QOF by purchase from an unrelated party. As a result, property that is purchased by a QOF from a related party, as well as property that is contributed to a QOF in a transfer to which section 351 or section 721(a) applies, is not qualified opportunity zone business property.

Commenters have requested confirmation that eligible gain includes gain arising from the sale to, or the exchange of property with, a QOF if the amount of the gain is later invested in that QOF. Commenters similarly have requested confirmation that gain from the sale to, or the exchange of property with, a qualified opportunity zone business is eligible for investment into the QOF that owns the qualified opportunity zone business. Relatedly, commenters have requested that the final regulations provide that a sale to, or an exchange of property with, a QOF or qualified opportunity zone business, followed by an investment of the amount of the sales proceeds into the QOF, would not be characterized as a purchase from a related party for purposes of section 1400Z–2(d)(2)(D).

One commenter expressed concern that, if a taxpayer sold property to an unrelated QOF and then invested the amount of the sales proceeds in the same QOF, that sequence of transactions could be characterized under circular cash flow principles as if the taxpayer contributed the property directly to the QOF (and each transfer of the amount of the sales proceeds would be disregarded for Federal income tax purposes). If this construct applied, the acquired property would not qualify as qualified opportunity zone business property.

The Treasury Department and the IRS agree that generally applicable Federal income tax principles would require this result if, under the facts and circumstances, the consideration paid by the QOF or by a qualified opportunity zone business returns to its initial source as part of the overall plan. See Rev. Rul. 83–142, 1983–2 C.B. 68; Rev. Rul. 78–397, 1978–2 C.B. 150. Under the step transaction doctrine and circular cash flow principles, the circular movement of the consideration in such a transaction would be disregarded for Federal income tax purposes, including for purposes of section 1400Z–2 and the section 1400Z–2 regulations. Thus, the transaction would be treated for Federal income tax purposes as a transfer of property to the purchasing QOF for an interest therein or, if applicable, as a transfer of property to a QOF for an interest therein followed by a transfer of such property by the QOF to the purchasing qualified opportunity zone business.

Accordingly, an eligible taxpayer's gain from a sale to or an exchange of property with an unrelated QOF (acquiring QOF), as part of a plan that includes the investment of the consideration received by the eligible taxpayer back into the acquiring QOF, is not eligible gain to the eligible taxpayer because the transaction would not be characterized as a sale or exchange to an unrelated person for Federal income tax purposes. Similarly, an eligible taxpayer's gain from a sale to or an exchange of property with an unrelated qualified opportunity zone business (acquiring qualified opportunity zone business) is not eligible gain to the eligible taxpayer if the sale occurs as part of a plan that includes (i) the investment of the consideration received by the eligible taxpayer back into the QOF that owns the acquiring qualified opportunity zone business, followed by (ii) the contribution by the QOF of that consideration to the qualified opportunity zone business. Furthermore, because the transaction is not treated as a ''purchase'' of tangible property by the qualified opportunity zone business from an unrelated party, the newly acquired property will not qualify as qualified opportunity zone business property under section 1400Z–2(d)(2)(D).

The Treasury Department and the IRS also note that, if an eligible taxpayer sells property to, or exchanges property with, an unrelated qualified opportunity zone business as part of a plan that includes the investment of the consideration by the taxpayer back into the QOF that owns the acquiring qualified opportunity zone business, the transaction potentially may be recast or recharacterized as a non-qualifying investment even if the QOF retains the consideration (rather than transferring the consideration to the qualified opportunity zone business). See § 1.1400Z2(f)–1(c)(1). See also part II.D (discussing the transfer of property for a qualifying investment) and part VI.A (discussing the applicability of the step transaction doctrine) of this Summary of Comments and Explanation of Revisions.

e. Gain Not Subject to Federal Income Tax

The Treasury Department and the IRS received comments regarding the scope of the term ''eligible gain'' with respect to gains realized by persons that generally are not subject to Federal income tax with respect to those gains, such as persons that are not United States persons under section 7701(a)(30) (foreign persons) or that are entities generally exempt from tax under the Code. Some commenters suggested that an eligible gain should include all realized capital gains, including gains that are not subject to Federal income tax. However, other commenters stated that permitting deferral elections with respect to gains that are not subject to Federal income tax would be inappropriate because section 1400Z–2 is premised on the assumption that a person could make qualified investments in a QOF only with respect to amounts of capital gains for which taxation is deferred.

The Treasury Department and the IRS have determined that eligible taxpayers generally should be able to make an election under section 1400Z–2(a)(1) and the section 1400Z–2 regulations only for capital gains that would be subject to tax under subtitle A before January 1, 2027 (subject to Federal income tax) but for the making of a valid deferral election under section 1400Z–2(a)(1) and the section 1400Z–2 regulations. Section 1400Z–2 defers the time when eligible gains are included in income, and there would not be any taxable income to defer for a gain that is not subject to Federal income tax. This approach ensures that both United States persons and foreign persons may be eligible for the Federal income tax benefits of section 1400Z–2 under the same conditions. Moreover, particularly with respect to foreign persons, the lack of any requirement that a gain be subject to Federal income tax would make it difficult for the IRS to verify the extent to which the amount being invested in

a QOF was, in fact, with respect to a capital gain.

Accordingly, the final regulations clarify that deferral of a gain under section 1400Z–2(a)(1) and the section 1400Z–2 regulations generally is available only for capital gain that would be subject to Federal income tax but for the making of a valid deferral election under section 1400Z–2(a)(1) and the section 1400Z–2 regulations. Thus, for example, a deferral election may generally be made by nonresident alien individuals and foreign corporations with respect to an item of capital gain that is effectively connected with a U.S. trade or business. Further, individual bona fide residents of U.S. territories who are United States persons may generally make a deferral election with respect to an item of capital gain that is derived from sources outside their territory of residence. Similarly, an organization that is subject to the unrelated business income tax imposed by section 511 may generally make a deferral election with respect to an item of capital gain to the extent the item would be included in computing the organization's unrelated business taxable income (such as under the unrelated debt-financed income rules).

In contrast, an eligible taxpayer who is not a United States person within the meaning of section 7701(a)(30), or who is treated as a resident of another country for purposes of an applicable income tax treaty (foreign eligible taxpayer), should not be able to elect to defer an item of capital gain if, in the taxable year in which such gain is includible, the item is treated as exempt from Federal income tax under a provision of an applicable income tax treaty (for example, capital gain that is effectively connected with a U.S. trade or business but is not attributable to a permanent establishment of the taxpayer within the United States). To prevent foreign eligible taxpayers from taking inconsistent positions with respect to treaty benefits in the taxable year of deferral and the taxable year of inclusion, the final regulations provide that a foreign eligible taxpayer cannot make a deferral election under section 1400Z–2(a) and the section 1400Z–2 regulations with respect to an eligible gain unless the foreign eligible taxpayer irrevocably waives, in accordance with forms and instructions, any treaty benefits that would exempt that gain from Federal income tax at the time of inclusion pursuant to an applicable U.S. income tax convention.

In the event that forms and instructions have not yet been published incorporating the treaty waiver requirement for a foreign eligible taxpayer for the taxable year that the deferral election applies to, the final regulations require the attachment of a written statement to waive such treaty benefits. Eligible taxpayers other than foreign eligible taxpayers will only be required to make this treaty waiver if and to the extent required in forms and publications.

The Treasury Department and the IRS have determined that it would be unduly burdensome to require a partnership to determine the extent to which a capital gain would be, but for a deferral election by the partnership under section 1400Z–2(a) and the section 1400Z–2 regulations, subject to Federal income tax by its direct or indirect partners because partnerships do not generally have sufficient information about the tax treatment and positions of their partners to perform this analysis. Thus, in the case of partnerships, the final regulations provide an exception to the general requirement that gain be subject to Federal income tax in order to constitute eligible gain.

The Treasury Department and the IRS are aware that foreign persons who are not subject to Federal income tax may plan to enter into transactions including, but not limited to, the use of partnerships formed or availed of to circumvent the rule generally requiring eligible gains to be subject to Federal income tax. Therefore, under an anti-abuse rule added in § 1.1400Z2(f)–1(c)(2), a partnership formed or availed of with a significant purpose of avoiding of avoiding the requirement in § 1.1400Z2(a)–1(b)(11)(i)(B) that eligible gains be subject to Federal income tax will be disregarded, in whole or in part to prevent the creation of a qualifying investment by the partnership with respect to any partner that would not otherwise satisfy the requirement of that paragraph. The anti-abuse rule may apply even if some of the partners in the partnership are subject to Federal income tax. See § 1.1400Z2(f)–1(c)(3)(i) and (ii), *Examples 1 and 2.*

Finally, in response to comments expressing uncertainty as to whether persons who do not or cannot make a valid deferral election for eligible gains nevertheless may invest in QOFs, the Treasury Department and the IRS note that nothing in section 1400Z–2 or the section 1400Z–2 regulations prevents persons who do not have eligible gains from investing in QOFs. Thus, Indian tribal governments, and tax-exempt organizations that invest amounts other than items of capital gain that would be included in computing their unrelated business taxable income, may invest in a QOF to the extent otherwise permitted by law or regulation. However, those investments will not qualify for the Federal income tax benefits under section 1400Z–2 or the section 1400Z–2 regulations. That is, those investments are not qualifying investments described in section 1400Z–2(e)(1)(A)(i).

f. Measuring Gain From Sales or Exchanges of Virtual Currency

Section 1400Z–2 and the proposed regulations clearly provide that eligible gain is gain that has been realized pursuant to a sale or exchange. One commenter identified a potential obstacle in calculating the eligible gain from sales or exchanges of certain types of digital assets, including virtual currency. The commenter expressed concern that the vast majority of digital assets could not directly be exchanged for traditional types of money. The commenter explained that these digital assets first must be converted into other digital assets in taxable transactions before ultimately being sold for the type of currency that would be invested in a QOF. The commenter expressed concern that gain or loss from these intermediate transactions in which a digital asset is exchanged for another digital asset may not necessarily be tracked in detail. Thus, the commenter requested a separate rule for these digital assets under which eligible gain would be calculated by reference to the basis of the original digital asset and to the actual proceeds received in the ultimate transaction that converts an intermediate digital asset to money or property that would be invested in a QOF.

Notice 2014–21, 2014–16 I.R.B. 938 provides that convertible virtual currency is property for Federal income tax purposes, and that general Federal income tax principles applicable to property transactions apply to transactions involving convertible virtual currency. Section 1400Z–2(a) applies to gain that, absent a deferral election, would be included in the taxpayer's gross income. To determine the amount of such gain, the taxpayer must know the basis of the property, regardless of the type of such property. If the amount invested in a QOF exceeds the amount of eligible gain, then the taxpayer will have a non-qualifying investment for the amount of gain invested in excess of eligible gain invested in the QOF and a qualifying investment for the amount of eligible gain invested in the QOF (mixed-funds investment). Taxpayers selling digital assets are not prevented from investing eligible gain generated from the sale into a QOF simply because one digital asset must be converted into another type of

asset before the taxpayer can convert its assets into U.S. dollars. Therefore, the Treasury Department and the IRS decline to adopt the commenter's request for a special rule for digital assets.

g. Gain From a Section 1256 Contract or a Position Part of an Offsetting-Positions Transaction

The preamble to the October 2018 proposed regulations explained that the Treasury Department and the IRS considered allowing deferral under section 1400Z–2(a)(1) for a net amount of capital gain related to a straddle (as defined in section 1092(c)(1)) after the disposition of all positions in the straddle, but concluded that such a rule would pose significant administrative burdens. Proposed § 1.1400Z2(a)–1(b)(2)(iv) provided that, if a capital gain is from a position that is or has been part of an offsetting-positions transaction, the gain is not eligible for deferral under section 1400Z–2(a)(1). For this purpose, an offsetting-positions transaction generally is a transaction in which a taxpayer has substantially diminished the taxpayer's risk of loss from holding one position with respect to personal property by holding one or more other positions with respect to personal property (whether or not of the same kind) and includes positions with respect to personal property that is not actively traded.

Proposed § 1.1400Z2(a)–1(b)(2)(iii)(A) provided that the only gain arising from section 1256 contracts that is eligible for deferral under section 1400Z–2(a)(1) is capital gain net income from all of a taxpayer's section 1256 contracts for a taxable year. Additionally, proposed § 1.1400Z2(a)–1(b)(2)(iii)(B) provided that, if at any time during the taxable year, any of the taxpayer's section 1256 contracts were part of an offsetting-positions transaction and any other position in that transaction was not a section 1256 contract, then no gain from any section 1256 contract is an eligible gain with respect to that taxpayer in that taxable year.

Two commenters expressed concern about the application of the offsetting-positions transaction rule in the October 2018 proposed regulations to positions that are not part of a straddle under section 1092. One commenter stated that the IRS did not adequately describe its policy concerns when extending the offsetting-positions transaction rule beyond the scope of section 1092. The second commenter argued that a taxpayer is permitted to recognize losses while deferring gains by continuing to hold an asset that is not actively traded, and that allowing deferral under section 1400Z–2(a)(1) would be no different than having the taxpayer continue to hold its gain position. The Treasury Department and the IRS appreciate the concerns expressed regarding the extension of the proposed offsetting-positions transaction rule to transactions that are not straddles under section 1092 and the final regulations do not include the provisions that applied to transactions that are not straddles under section 1092.

Two commenters expressed concern that the proposed offsetting-positions transaction rule excluded gains from a position that, at any time, had been part of an offsetting-positions transaction, including offsetting-positions transactions that occurred many years ago. The commenters recommended either deleting the phrase ''or has been'' or limiting application of that phrase to permit deferral of capital gain from an offsetting-positions transaction if there is no offsetting position on or after the enactment of the TCJA. The Treasury Department and the IRS have concluded that the rule should not exclude gains that have, at any time, been part of an offsetting position but should instead exclude gains based on whether an offsetting position was in existence during a limited time period. Limiting the application of the straddle rules to situations in which there was an offsetting position on or after the date of the enactment of the TCJA would, in future years, require taxpayers and the IRS to look back over an extended period of time. This requirement could result in significant administrative burdens without serving a significant tax policy purpose. As a result, the Treasury Department and the IRS have revised the limitation on the use of gains from a straddle to net gain from a position that was either part of a straddle during the taxable year or part of a straddle in a prior taxable year if a loss from that straddle is carried over under section 1092(a)(1)(B) to the taxable year.

One commenter suggested that, in the context of a straddle, the deferral under section 1400Z–2(a)(1) of gain from the disposition of a position in a straddle would not permit the current recognition of an otherwise suspended loss from an offsetting position in the straddle. The commenter also recognized, however, that it might be overly generous for a taxpayer investing in a QOF to eliminate 15 percent of the taxpayer's deferred gain (assuming that the taxpayer holds that QOF interest for seven years by December 31, 2026), if the taxpayer was also permitted ultimately to recognize all of its suspended loss from the offsetting straddle position. The commenter suggested a rule eliminating any suspended loss in the same proportion as any elimination of gain in one or more offsetting positions.

The Treasury Department and the IRS have determined that there would be significant administrative burdens for taxpayers and the IRS in tracking specific gains deferred under section 1400Z–2(a)(1) for the purpose of determining whether and when some or all of a deferred straddle loss might ultimately become deductible. In addition, the Treasury Department and the IRS have determined that the tracking of deferred losses for multiple taxable years after the positions in the straddle have been disposed of and a potential proportional elimination of a suspended loss, years after the suspension, would create additional complexity and administrative burdens for both taxpayers and the IRS. The final regulations therefore provide a general rule that net gain from positions that are or, as described previously, in certain circumstances have recently been part of a straddle, are not eligible for deferral under section 1400Z–2(a)(1).

Another commenter suggested that, absent a clearly articulated policy concern with permitting deferral of net gain from a straddle, the Treasury Department and the IRS should consider eliminating or minimizing the scope of capital gains subject to the prohibition in the proposed regulations. The Treasury Department and the IRS have concluded that, in certain circumstances, deferral of net gain from a straddle does not present significant policy concerns or unreasonable administrative burdens for taxpayers and the IRS. Under the final regulations, if during the taxable year: (i) A position was covered by an identification under section 1092 or 1256(d), (ii) no gain or loss with respect to any position that was part of the identified straddle remains unrecognized at the end of the taxable year (other than gain that would be recognized but for deferral under section 1400Z–2(a)(1)), (iii) none of the positions in the identified straddle were part of any other straddle during the taxable year, and (iv) none of the positions in the identified straddle were part of a straddle in a previous taxable year from which a loss was carried over to the taxable year under section 1092(a)(1)(B), then the net gain during the taxable year from positions that were part of the identified straddle is not prevented from being an eligible gain. Net gain from an identified straddle during the taxable year is equal to the excess of the capital gains recognized for Federal income tax

purposes in the taxable year, determined without regard to section 1400Z–2(a)(1), over the sum of the capital losses and net ordinary losses from all positions that were part of the straddle, including capital gains and losses from section 1256 contracts and other positions marked to market on the last business day of the taxable year or upon transfer or termination and annual account net gain from positions in a mixed straddle account.

The final regulations clarify that, if a taxpayer identifies a straddle under section 1092(a)(2), the taxpayer must adjust basis in accordance with section 1092(a)(2)(A)(ii) and (iii) when determining the net gain during the taxable year from positions that were part of the straddle. The net gain realized during the taxable year that is deferred under section 1400Z–2(a)(1) is not treated as unrecognized gain for purposes of determining whether a loss from a position in the straddle is deferred under section 1092(a)(3)(A)(ii).

A commenter suggested that the provision in the October 2018 proposed regulations disqualifying all gains from section 1256 contracts if at any time during the taxable year, any of the taxpayer's section 1256 contracts were part of an offsetting-positions transaction and any other position in that transaction was not a section 1256 contract be revised to limit the disqualification to the specific type of offsetting-positions transaction identified by the Treasury Department and the IRS. In response to this comment, under the final regulations net gain during the taxable year from section 1256 contracts that were not part of a straddle is not prevented from being eligible gain.

The final regulations also provide that additional exceptions to the general rule may be provided in guidance published in the Internal Revenue Bulletin. The Treasury Department and the IRS request comments on whether there are other situations that might warrant an exception from the general rule that net gain from a position that was either part of a straddle during the taxable year or part of a straddle in a prior year if a loss from that straddle is carried over under section 1092(a)(1)(B) to the taxable year is not eligible gain.

2. Eligible Interests

Proposed § 1.1400Z2(a)–1(b)(3) provided that an eligible interest in a QOF must be an equity interest issued by a QOF, and that eligible interests do not include debt instruments as defined in section 1275(a)(1) and § 1.1275–1(d). One commenter requested clarification with respect to debt instruments issued by a QOF or a potential investor. The commenter set forth a fact pattern in which an eligible taxpayer lends money to a QOF prior to the sale of property that generates eligible gain. After the sale of the property, the taxpayer essentially transfers its creditor position in the loan to the QOF. The commenter requested confirmation that such an arrangement would result in a qualifying investment in a QOF. Determination of the tax treatment of the arrangement described previously would require a debt-equity analysis based on a careful examination of all relevant facts and circumstances and Federal income tax principles apart from those found in section 1400Z–2 and these regulations. Accordingly, such an analysis would exceed the scope of these regulations.

The commenter also described a second fact pattern in which an eligible taxpayer issues a promissory note to the QOF in exchange for an interest in the QOF. The commenter requested clarification as to whether such an exchange would give rise to an amount invested in the QOF. A taxpayer can make an investment in a QOF by contributing cash or property. The contribution of a promissory note, however, is inconsistent with the policy of the section 1400Z–2 statute to incentivize investments in QOZs, and is beyond the scope of these regulations. The Treasury Department and the IRS have determined that a taxpayer should not receive the benefits under section 1400Z–2 merely by promising to pay, and thereby invest in a QOZ, in the future. As such, the Treasury Department and the IRS decline to adopt this comment.

3. 180-Day Investment Requirement

a. Section 1231 Gains

As discussed in part II.A.1.a. of this Summary of Comments and Explanation of Revisions, proposed § 1.1400Z2(a)–1(b)(2)(iii) of the May 2019 proposed regulations provided that the 180-day period for investment with respect to capital gain net income from section 1231 property for a taxable year began on the last day of the taxable year without regard to the date of any particular disposition of section 1231 property.

The Treasury Department and the IRS have received numerous comments regarding the ''capital gain net income'' approach of the May 2019 proposed regulations. In response to the May 2019 proposed regulations, taxpayers and practitioners consistently have emphasized that the year-long character testing period under section 1231 often can frustrate a taxpayer's ability to defer gains resulting from sales or exchanges of section 1231 property. Unlike typical transactions that result in ordinary or capital gain upon their completion, taxpayers generally lack the ability to determine whether section 1231 gain from a sale or exchange of section 1231 property will be capital in character until the completion of all sales or exchanges of section 1231 property during a taxable year. See generally section 1231(a), (c) (describing taxable-year-based determination). However, to defer recognition under section 1400Z–2(a), taxpayers must invest eligible gain within a 180-day period that begins on the date on which the taxpayer otherwise would have recognized that gain (180-day investment requirement). See section 1400Z–2(a)(1)(A) (setting forth the 180-day investment requirement). Accordingly, commenters have recommended a wide spectrum of approaches to integrate the rules of section 1231 with section 1400Z–2, including approaches that would (i) modify the timing of the section 1231 calculation (including recapture), the start of the 180-day period, or both; or (ii) allow for immediate investment of gross section 1231 gains to be treated as eligible gains if those gains are determined to be capital at the end of the taxable year.

As described in part II.A.1.a. of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have determined that a ''gross approach'' solely with regard to eligible section 1231 gains (without regard to any section 1231 losses) would eliminate unnecessary barriers to potential QOF investors. Specifically, the final regulations provide that eligible gains include gains from the sale or exchange of property described in section 1231(b) not required to be characterized as ordinary income by section 1245 or 1250 (eligible section 1231 gains), regardless of whether section 1231(a) (without regard to section 1231(a)(4)) would determine those gains to be capital or ordinary in character. This approach will eliminate significant complexity, as well as uncertainty in determining eligible gain for partnerships and S corporations that are eligible taxpayers. Importantly, although the determination under section 1231(a) of the character of an eligible section 1231 gain would ordinarily occur at the end of a taxable year, that section 1231(a) determination is not necessary to determine whether that gain is eligible for deferral under section 1400Z–2 and the section 1400Z–2 regulations. Because status as an

eligible gain relies on facts that are known at the time of a sale or exchange, the 180-day period for an eligible taxpayer to invest an amount with respect to an eligible section 1231 gain begins on the date of the sale or exchange giving rise to the gain rather than at the end of the taxable year. Therefore, an investor can invest an amount with respect to an eligible section 1231 gain from a sale or exchange of section 1231 property and have certainty as to the amount of the qualifying investment on the date the investment is made. Finally, allowing the 180-day period to begin on the date of the sale, exchange, or other disposition that gives rise to the eligible section 1231 gain accelerates both capital infusion into a QOZ and allows an investor to invest eligible proceeds from dispositions of section 1231 property as soon as any such funds are available to invest.

b. RIC and REIT Capital Gain Dividends

Several commenters noted that the application of the 180-day investment requirement to real estate investment trust (REIT) capital gain dividends may preclude some shareholders from making qualifying investments in QOFs because REIT capital gain dividends are based on the net capital gain of the REIT during the relevant taxable year of the REIT. In other words, REITs determine that a dividend, or part thereof, is eligible for capital gain dividend status after the REIT's taxable year has ended, when the REIT can compute net capital gain for the year. Thus, a shareholder may receive a dividend during the year but may not receive the designation that the dividend is a capital gain dividend until after the REIT's taxable year has ended. To facilitate investment in QOZs, commenters requested that the 180-day investment requirement apply beginning on the last day of the REIT's taxable year, rather than the date on which the shareholder receives a dividend, thereby providing a 180-day period after the shareholder has notice of the dividend's capital gain designation. In the alternative, some commenters proposed beginning the 180-day period for investment of REIT capital gain dividends on the date that is 30 days after the close of the REIT's taxable year. Commenters also noted that the same concerns apply to regulated investment company (RIC) capital gain dividends and maintained that the 180-day period should be the same for both RIC and REIT capital gain dividends.

The Treasury Department and the IRS seek to facilitate the ability of RIC and REIT shareholders to make qualifying investments in QOFs that result from capital gain dividends received during a taxable year. However, because shareholders may not have the same taxable year as the RIC or REIT in which they are invested, these final regulations provide that the 180-day period for RIC or REIT capital gain dividends generally begins at the close of the shareholder's taxable year in which the capital gain dividend would otherwise be recognized by the shareholder. To ensure that RIC and REIT shareholders do not have to wait until the close of their taxable year to invest capital gain dividends received during the taxable year, these final regulations provide that shareholders may elect to begin the 180-day period on the day each capital gain dividend is paid. The 180-day period for undistributed capital gain dividends, however, begins on either the last day of the shareholder's taxable year in which the dividend would otherwise be recognized or the last day of the RIC or REIT's taxable year, at the shareholder's election. Regardless of the 180-day period applicable to its capital gain dividends, the aggregate amount of a shareholder's eligible gain with respect to capital gain dividends received from a RIC or a REIT in a taxable year cannot exceed the aggregate amount of capital gain dividends that the shareholder receives as reported or designated by that RIC or that REIT for the shareholder's taxable year. Any excess investments will be treated under the final regulations as non-qualifying investments.

c. Installment Sales

Commenters requested clarification regarding the application of the 180-day investment requirement to gains recognized in an installment sale pursuant to the installment method under section 453. See section 453(c) (defining the term ''installment method''). Section 453(a) provides generally that income from an installment sale must be taken into account for purposes of the Code under the installment method. In general, the installment method allows taxpayers to report gain from a sale of property in the taxable year or years during which payments are received rather than in the year of the sale. Commenters expressed concern that, for taxpayers who are considering investing the gain from an installment sale in a QOF, it is not clear whether (i) there is a single 180-day period for all income from the installment sale that begins on the date and year of the sale (for example, March 15, 2020), or (ii) there are multiple 180-day periods, each beginning in the year during which a payment is received and income is recognized under the installment method.

To provide flexibility to these types of potential investors in QOZs, the Treasury Department and the IRS have included in these final regulations a rule that accommodates both of the potential options described by the commenters previously. Specifically, the final regulations allow an eligible taxpayer to elect to choose the 180-day period to begin on either (i) the date a payment under the installment sale is received for that taxable year, or (ii) the last day of the taxable year the eligible gain under the installment method would be recognized but for deferral under section 1400Z–2. As a result, if the taxpayer defers gain from multiple payments under an installment sale, there might be multiple 180-day periods, or a single 180-day period at the end of the taxpayer's taxable year, depending upon taxpayer's election.

One commenter also requested confirmation that only capital gain realized with respect to an installment sale that occurred after the effective date of section 1400Z–2 (that is, December 22, 2017) should be eligible gain. The Treasury Department and the IRS have determined that it would be inconsistent with the general rule for eligible gains in the final regulations, as well as installment sale case law, to exclude from the definition of eligible gains any capital gains recognized by an eligible taxpayer under the installment method, regardless of whether the installment sale occurred before the effective date of section 1400Z–2. Accordingly, the Treasury Department and the IRS decline to adopt this comment.

d. Special 180-Day Period for Partners, S Corporation Shareholders, and Trust Beneficiaries

The May 2019 proposed regulations provided that, for purposes of the 180-Day Investment Requirement, the period during which a partner must invest an amount equal to the partner's eligible gains in the partner's distributive share generally begins on the last day of the partnership taxable year in which the partner's allocable share of the partnership's eligible gain is taken into account under section 706(a). However, if a partnership does not elect to defer all of its eligible gain, the partner may elect to treat the partner's own 180-day period regarding the partner's distributive share of that gain as being the same as the partnership's 180-day period.

Several commenters requested an additional special rule for application of the 180-day investment requirement

with regard to partners in a partnership, shareholders in an S corporation, and beneficiaries of a trust. These commenters highlighted that owners of flow-through entities experience information delays regarding the Federal income tax consequences of transactions taken by such entities due to the ordinary course timing of Schedule K–1 issuances. As a result of this delay in receiving information necessary to determine the existence of eligible gain, commenters contended that partners in a partnership, shareholders in an S corporation, and beneficiaries of a trust should have an additional option to commence the 180-day period upon the due date of the entity's tax return.

The Treasury Department and the IRS agree with the commenters' suggestions. As a result, the final regulations provide partners of a partnership, shareholders of an S corporation, and beneficiaries of decedents' estates and non-grantor trusts with the option to treat the 180-Day period as commencing upon the due date of the entity's tax return, not including any extensions. However, the Treasury Department and the IRS have determined that similar rules for a grantor trust are not necessary because the grantor is treated as the owner of the grantor trust's property for Federal income tax purposes. Therefore, the final regulations set forth different rules applicable to the grantor.

4. Additional Deferral of Previously Invested Gains

Section 1400Z–2(a)(2)(A) provides that no deferral election under section 1400Z–2(a)(1) may be made with respect to a sale or exchange if an election previously made with respect to the sale or exchange is in effect. In proposed § 1.1400Z2(a)–1(b)(4)(ii)(D), Example 4 (Proposed Example 4), a taxpayer disposed of its entire qualifying investment in a QOF in 2025 in a transaction that constituted an event described in proposed § 1.1400Z(b)–1(c) (inclusion event) and recognized gain as a result. In the example, the taxpayer wanted to defer the amount of gain from the inclusion transaction by making another qualifying investment. The example concluded that the gain recognized due to the inclusion event may be invested in either the original QOF or a different QOF within 180 days of the inclusion event in order to make a new deferral election under section 1400Z–2. The preamble to the May 2019 proposed regulations explained that, upon disposition of that QOF interest, deferring an inclusion otherwise mandated by section 1400Z–2(a)(1)(B) is permitted only if the taxpayer has disposed of the entire initial investment because section 1400Z–2(a)(2)(A) expressly prohibits the making of a deferral election under section 1400Z–2(a)(1) with respect to a sale or exchange if an election previously made with respect to the same sale or exchange remains in effect.

A commenter requested that gain from an inclusion event in which a taxpayer disposes of less than its entire investment in a QOF be eligible for the deferral election under section 1400Z–2(a)(1). The commenter asserted that gain arising from an inclusion event, whether representing all or part of the initially deferred gain, represents new gain that should be eligible for deferral under section 1400Z–2(a).

The Treasury Department and the IRS agree with the commenter. The final regulations adopt the position that gain arising from an inclusion event is eligible for deferral under section 1400Z–2(a) even though the taxpayer retains a portion of its qualifying investment after the inclusion event. Although such gain relates in part to gain from a sale or exchange for which there was a prior election in effect, it is no longer subject to that prior election within the meaning of section 1400Z–2(a)(2)(A) as soon as the inclusion event triggers an income inclusion. Therefore, if an inclusion event relates only to a portion of a taxpayer's qualifying investment in the QOF, (i) the deferred gain that otherwise would be required to be included in income (inclusion gain amount) may be invested in a different QOF, and (ii) the taxpayer may make a deferral election under section 1400Z–2(a) with respect to the inclusion gain amount, so long as taxpayer satisfies all requirements for a deferral election on the inclusion gain amount. To satisfy the requirements under section 1400Z–2(a) and § 1.1400Z2(a)–1(b)(11)(iv), the eligible taxpayer must treat the inclusion gain amount to be deferred as if it were originally realized as a result of the inclusion event. In addition, the eligible taxpayer must meet all other requirements to defer gain under section 1400Z–2. See section 1400Z–2(a)(1) and § 1.1400Z2(a)–1(b)(11)(i)(C) (gain that arises from a sale or exchange of property with a related person is not eligible gain); section 1400Z–2(a)(2)(B) (election may not be made for gain arising after December 31, 2026). Consistent with Proposed Example 4, included in these regulations as § 1.1400Z2(a)–1(b)(7)(iv)(D), the 180-day period for the inclusion gain amount begins on the date of the inclusion event, and the holding period for the second QOF investment begins on the date that an amount corresponding to the inclusion gain amount is invested in the second QOF. See § 1.1400Z2(a)–1(b)(7)(iv), *Example 4.*

A commenter also requested clarification as to whether additional gain deferral under section 1400Z–2(a)(1)(A), as in Proposed Example 4, is permitted for gain included due to the operation of section 1400Z–2(b)(1)(B), which requires the full amount of gain that was deferred under section 1400Z–2(a)(1)(A), reduced by the amount of gain previously included under proposed § 1.1400Z2(b)–1(b) (remaining deferred gain) to be included in income in the taxable year of the eligible taxpayer that includes December 31, 2026. The commenter explained that the ability to reinvest gains required to be included in income under section 1400Z–2(b) would facilitate liquidity and capital mobility for investors. Moreover, in the event that additional gain deferral is permitted after a taxable year that includes December 31, 2026, the commenter requested clarification regarding the effect of such an additional gain deferral election on items including the proper amount includible as well as the amount of deferred gain that may be reinvested for the benefits of the election under section 1400Z–2(c).

Proposed Example 4 only illustrated that a taxpayer may invest gain that otherwise would be included pursuant to section 1400Z–2(b)(1)(A) upon the complete disposition of a QOF interest prior to December 31, 2026 (that is, an inclusion event), where the amount of that gain is reinvested in any QOF during the 180-day period beginning on the date of the inclusion event. No inferences should be drawn regarding gains from dispositions after December 31, 2026, because deferral of any gain from such dispositions is expressly prohibited by section 1400Z–2(a)(2)(B). Section 1400Z–2(b)(1) provides that all gain to which section 1400Z–2(a)(1)(A) deferral applies must be included in income in the taxable year that includes the earlier of the date on which a QOF investment is sold or exchanged or December 31, 2026. Further, section 1400Z–2(a)(2)(B) provides that no deferral election may be made under section 1400Z–2(a)(1) with respect to any sale or exchange after December 31, 2026. Accordingly, the statutory language of section 1400Z–2 clearly states, and therefore the section 1400Z–2 regulations provide, that (i) the ability to defer eligible gains pursuant to section 1400Z–2(a)(1)(A) is not permitted with respect to a gain arising after December 31, 2026, and (ii) no additional deferral of any gain is permitted if such gain is required to be

included in gross income under section 1400Z–2(b)(1)(B).

5. Qualifying Investment

Section 1400Z–2 provides Federal income tax benefits to an eligible taxpayer that makes an equity investment in a QOF described in section 1400Z–2(e)(1)(A)(i) (that is, a qualifying investment) if the qualifying investment is held for the various statutorily prescribed holding periods. For example, in the case of an eligible taxpayer that maintains a qualifying investment for seven years, the eligible taxpayer's basis in the qualifying investment will be increased by a total amount equal to 15 percent of the amount of the taxpayer's deferred gain. See section 1400Z–2(b)(2)(B)(iii) and (iv) (providing for basis increases of 10 and five percent, respectively). With respect to a qualifying investment that is sold or exchanged after being held by the eligible taxpayer for at least 10 years, if the eligible taxpayer makes an election under section 1400Z–2(c), the basis of the qualifying investment will be increased to an amount equal to the fair market value of that investment on the date on which it is sold or exchanged. See section 1400Z–2(c).

In the May 2019 proposed regulations, the Treasury Department and the IRS specified transactions that would cause the inclusion in gross income of an eligible taxpayer's gain that had been deferred under section 1400Z–2(a)(1)(B) and (b). Defined as an ''inclusion event,'' each of these transactions ''would reduce or terminate the QOF investor's direct (or, in the case of partnerships, indirect) qualifying investment for Federal income tax purposes or (in the case of distributions) would constitute 'cashing out' of the QOF investor's qualifying investment. . . . It is necessary to treat such [distributive] transactions as inclusion events to prevent taxpayers from 'cashing out' a qualifying investment in a QOF without including in gross income any amount of their deferred gain.'' See May 2019 proposed regulations, Explanation of Provisions, part VII.A.

As indicated in the first sentence of part VII.E. (Transfers of Property by Gift or by Reason of Death) and elsewhere in the Explanation of Provisions in the May 2019 proposed regulations, the termination of a direct interest in a qualifying investment that resulted in an inclusion event terminated the status of an investment in a QOF as a qualifying investment '' [f]or purposes of sections 1400Z–2(b) and (c).'' This is because the statutory text of each of section 1400Z–2(a), (b), (c), and (e)(1) focuses on one holding period of ''the taxpayer'' tested at various points during a period of at least 10 years.

The May 2019 proposed regulations excepted certain enumerated dispositions of qualifying investments from treatment as inclusion events to provide for business flexibility for QOFs or qualified opportunity zone businesses. However, those exceptions were premised upon the requirement that the same eligible taxpayer generally be treated as continuing to hold the same interest in the QOF, and thereby continue to bear the Federal income tax liability associated with holding the interest, such as by reason of section 381 or section 704(c). This degree of identity of taxpayer is fundamentally different (and more demanding) than a mere ''step in the shoes'' concept based on whether the transferee of the interest can tack the holding period and basis of the transferor. Accordingly, the May 2019 proposed regulations treated, among other transactions, gifts and section 351 exchanges as inclusion events because, in each instance, (i) the initial eligible taxpayer had severed the direct investment interest in the QOF and (ii) the transferee taxpayer was not treated for Federal income tax purposes either as the same taxpayer as the initial eligible taxpayer or as a successor taxpayer. This is true even though in each such case, the acquiring taxpayer's basis and holding period for purposes of determining gain or loss may be identical to that of the taxpayer that made the initial investment in the QOF. See id., parts VII.E (regarding gifts) and VII.G (regarding section 351 exchanges).

Commenters have requested clarification of the treatment of investments in QOFs under section 1400Z–2(c) that have been disposed of by gift, in section 351 exchanges, and in other transactions treated as inclusion events. For the foregoing reasons, the final regulations clarify that transactions described as inclusion events result in a reduction or termination of a qualifying investment's status as a qualifying investment to the extent of the reduction or termination, except as otherwise provided in § 1.1400Z2(b)–1(c) or other provisions of the section 1400Z–2 regulations. See part IV.C of this Summary of Comments and Explanation of Revisions. Moreover, the reduction or termination of that status applies for purposes of section 1400Z–2(c) as well as section 1400Z–2(a)(1)(B) and (b). An inclusion event is a transaction that reduces or terminates the QOF investor's direct (or, in the case of partnerships, indirect) qualifying investment for Federal income tax purposes or, in the case of distributions, constitutes a ''cashing out'' of the eligible taxpayer's qualifying investment in the QOF. For that reason and to that extent, the taxpayer holding the reduced investment in the QOF after the inclusion event no longer possesses a qualifying investment. Thus, the benefits provided under section 1400Z–2(c) generally are available only to a taxpayer that not only makes an equity investment in a QOF described in section 1400Z–2(e)(1)(A)(i) (that is, a qualifying investment), but also then continuously maintains that qualifying investment throughout statutorily prescribed holding periods.

However, consistent with that rationale, the May 2019 proposed regulations did not treat as an inclusion event a gift by the taxpayer to a grantor trust of which the taxpayer is the deemed owner because, for Federal income tax purposes, the owner of the grantor trust is treated as the owner of the trust's property and thus of the qualifying investment in its QOF. See id., part VII.E. See also id., part VII.F.1 (providing a similar exception regarding section 381 transactions based on a statutory successor taxpayer concept). Accordingly, eligibility for benefits under section 1400Z–2 in these limited instances would be maintained.

The Treasury Department and the IRS have received several comments requesting clarification that qualifying investments include interests received in a transfer by reason of death that is not an inclusion event. In the case of a decedent, section 1400Z–2(e)(3) provides a special rule requiring amounts recognized under section 1400Z–2, if not properly includible in the gross income of the decedent, to be includible in gross income as provided by section 691. In that specific case, the beneficiary that receives the qualifying investment has the obligation to include the deferred gain in gross income in the event of any subsequent inclusion event, including for example, any further disposition by that recipient. See id., part VII.E. In other words, unlike an inclusion event contemplated by the general rules of section 1400Z–2(b), the obligation to include the original taxpayer investor's deferred gain in income travels with that taxpayer's qualifying investment to the beneficiary. Accordingly, the May 2019 proposed regulations excepted transfers of a qualifying investment to the deceased owner's estate, as well as distributions by the estate, from the definition of ''inclusion event.'' *See id.,* part VII.E.

As indicated in part VII.E. of the Explanation of Provisions of the May 2019 proposed regulations, the Treasury Department and the IRS have

determined that interests received in a transfer by reason of death continue to be a qualifying investment in the hands of the beneficiary for purposes of section 1400Z–2(c). As described earlier, sections 691 and 1400Z–2(e)(2) require such a transfer to not give rise to an inclusion event because the beneficiary is treated as a successor to the original eligible taxpayer that made the qualifying investment (that is, the beneficiary ''steps into the shoes'' of the original taxpayer investor with regard to both the benefits of the qualifying investment and the obligation to ultimately include the original taxpayer's deferred gain into the beneficiary's income). As a result, the Treasury Department and the IRS have determined that a qualifying investment received by a beneficiary in a transfer by reason of death should continue to be a qualifying investment in the hands of the beneficiary for purposes of section 1400Z–2(b) and (c).

The Treasury Department and the IRS have also received a comment suggesting that the final regulations should permit QOFs to make loans to qualified opportunity zone businesses and treat as qualifying investments the debt instruments arising from such loans. Confirmation of the tax treatment of such debt instruments as qualifying investments (that is, equity investments in a QOF) would require a debt-equity analysis based on a careful examination of all relevant facts and circumstances and Federal income tax principles apart from those found in section 1400Z–2 and the section 1400Z–2 regulations. Such an analysis would exceed the scope of these regulations. As a result, the final regulations do not adopt the commenter's suggestion.

B. Making an Investment for Purposes of an Election Under Section 1400Z–2(a)

1. Acquisition of an Eligible Interest From a Person Other Than a QOF

Proposed § 1.1400Z2(a)–1(b)(9)(iii) permitted a taxpayer to make a deferral election under section 1400Z–2(a)(1)(A) for an eligible interest acquired from a person other than a QOF. Commenters asked whether the transferor of that eligible interest needed to have made an election under section 1400Z–2(a) prior to the taxpayer's acquisition. Commenters also asked whether the acquirer must have realized eligible gain within the 180-day period prior to the acquisition of the eligible interest in order for acquisition of that interest to support a deferral election under section 1400Z–2(a)(1)(A) with respect to the eligible gain. Additionally, commenters requested confirmation regarding whether shares or partnership interests in a pre-existing entity that becomes a QOF pursuant to proposed § 1.1400Z2(d)–1(a)(3) become eligible interests when the pre-existing corporation or partnership becomes a QOF.

The final regulations do not require the transferor to have made a prior election under section 1400Z–2(a) for the acquirer of an eligible interest to make such an election. Further, for interests in entities that existed before the enactment of section 1400Z–2, if such entities become QOFs pursuant to § 1.1400Z2(d)–1(a)(3), then the interests in those entities, even though not qualifying investments in the hands of a transferor, are eligible interests that may (i) be acquired by an investor and (ii) result in a qualifying investment of the acquirer if the acquirer has eligible gain and the acquisition was during the 180-day period with respect to that gain.

2. Eligibility of Built-In Gain for Deferral

One commenter requested confirmation that the built-in gain of a REIT, a RIC, or an S corporation potentially subject to corporate-level tax under section 1374 or § 1.337(d)–7 is eligible for deferral under section 1400Z–2. To the extent the built-in gain is an eligible gain, an election under section 1400Z–2 may be made for such gain of a REIT, a RIC, or an S corporation. If such election is made, the amount of such gain will not be included in the calculation of the entity's net recognized built-in gain (as defined in section 1374(d)(2)) in the year of deferral. Similarly, if a deferral election is made with respect to an eligible gain that, absent the deferral election, would constitute a recognized built-in gain (RBIG) within the meaning of section 382(h)(2)(A) or section 1374(d)(3), the amount of such eligible gain deferred as a result of a qualifying investment in a QOF is not taken into account as RBIG in the year of deferral.

3. Grantor Trusts

A commenter pointed out that the rule in proposed § 1.1400Z2(a)–1(c)(3) does not achieve the proper result for grantor trusts that do not make the deferral election but distribute the deferred gain to a trust beneficiary other than the deemed owner of the trust. The commenter pointed out that the proposed rule should not apply to grantor trusts because the deemed owner of the trust is liable for the Federal income tax on the gain regardless of whether that gain is distributed currently to a trust beneficiary other than the deemed owner. The commenter also requested clarification that either the grantor trust recognizing the gain or the deemed owner of that trust is eligible to both make the deferral election and make a qualifying investment, regardless of whether the grantor trust distributes the gain to the deemed owner or to any other person. The Treasury Department and the IRS agree with the commenter and have made the requested adjustments in the final regulations.

C. Identification of Disposed Interests in a QOF

Under the May 2019 proposed regulations, if a taxpayer held interests in a QOF with identical rights (for example, equivalent shares of stock in a QOF corporation) that were acquired on different days, and if the taxpayer disposed of less than all of those interests on a single day, the taxpayer was required to use the first-in-first-out (FIFO) method to identify which interests were disposed of for certain specified purposes, such as determining the character and other attributes of the deferred gain that is included as a result of the disposition. In circumstances in which the FIFO method did not provide a complete answer, taxpayers were required to use a pro-rata method. In requesting comments as to whether methods other than the FIFO method and the pro-rata method should be used, the Treasury Department and the IRS stipulated that any such methods must both provide certainty as to which fungible interest a taxpayer disposes of and allow taxpayers to comply easily with the requirements of section 1400Z–2(a)(1)(B) and (b) that certain dispositions of an interest in a QOF cause deferred gain be included in a taxpayer's income.

In response, commenters requested that taxpayers be permitted to specifically identify the QOF interests that are sold or otherwise disposed of, and they recommended that the final regulations adopt rules similar to those in § 1.1012–1(c). Under such rules, a taxpayer would be required to use the FIFO method only if the taxpayer fails to adequately identify which shares were disposed of.

The Treasury Department and the IRS agree that specific identification should be permitted for dispositions of interests in QOF corporations. Thus, the final regulations permit taxpayers to employ the rules and principles of § 1.1012–1(c) to specifically identify the QOF stock that is sold or otherwise disposed. If a taxpayer fails to adequately identify which QOF shares are disposed of, then the FIFO identification method applies. If, after application of the FIFO method, a taxpayer is treated as having disposed

of less than all of its investment interests that the taxpayer acquired on one day and the investments vary in its characteristics, then the pro-rata method will apply to the remainder.

However, the final regulations do not extend this specific identification methodology to the disposition of interests in a QOF partnership because, under Federal income tax law, a partnership interest represents an undivided, unitary interest in all of the partnership assets and liabilities. Other than in the case of a mixed-funds investment in a QOF partnership, where the section 1400Z–2 statute mandates a division of partnership interests, the final regulations do not adopt the commenters' recommendation because it would broaden the complexities associated with dividing partnership interests into separate components with associated assets and liabilities.

In addition, the final regulations make it clear that if a taxpayer is required to include in income some or all of a previously deferred gain, the gain so included has the same attributes that the gain would have had if the recognition of gain had not been deferred under section 1400Z–2. The final regulations generally provide that forms, instructions, and other administrative guidance control in determining which deferred gains are associated with particular interests in QOFs. However, the final regulations also provide that, to the extent that such guidance does not clearly associate an investment in a QOF with an amount of deferred gain, an ordering rule applies that permits taxpayers to determine how to associate investments in QOFs with particular deferred gains.

D. Property Transferred in Exchange for a Qualifying Investment Is Not Qualified Opportunity Zone Business Property

The May 2019 proposed regulations clarify that taxpayers may transfer property other than cash to a QOF in exchange for a qualifying investment. A commenter asked whether property that is purchased in a QOZ and contributed to a QOF could be qualified opportunity zone business property, or whether such property would be excluded automatically because it is not purchased by the QOF. The commenter further asked why taxpayers are permitted to contribute property to a QOF in exchange for a qualifying investment if the property cannot be qualified opportunity zone business property.

Taxpayers are permitted to transfer property to a QOF in exchange for a qualifying investment because the statute does not preclude taxpayers from investing in a QOF in this manner and because permitting such transfers is not inconsistent with the policies underlying section 1400Z–2. As the commenter noted, property that is contributed to a QOF cannot be qualified opportunity zone business property because qualified opportunity zone business property must be purchased by a QOF. See section 1400Z–2(d)(2)(D)(i)(I). The QOF may retain the contributed property among its assets that are not qualified opportunity zone property, or it may sell the property and use the proceeds to acquire qualified opportunity zone property in accordance with section 1400Z–2(d) and the section 1400Z–2 regulations.

E. Amount Invested in a QOF Partnership for Purposes of Section 1400Z–2(a)(1)(A)

The May 2019 proposed regulations contained two rules that, if either were applicable, would reduce the amount of a taxpayer's qualifying investment.

First, proposed § 1.1400Z2(a)–1(b)(11)(ii)(A)(*1*) provided that, to the extent the transfer of property to a QOF partnership is characterized other than as a contribution (for example, a transfer that is characterized as a disguised sale under section 707), the transfer is not an investment within the meaning of section 1400Z–2(a)(1)(A) (section 1400Z–2(a)(1)(A) investment). The Treasury Department and the IRS confirm that the reference to the disguised sale regulations under section 707 is intended to provide an existing analytical framework and rules applicable to transfers of property to a QOF partnership to determine whether the transfer is a contribution for purposes of making a qualifying investment. All guidance under section 707 that otherwise would be applicable, including any exception, applies. In particular, § 1.707–4(b)(2) (relating to operating cash flow distributions) applies to transfers to and distributions from a QOF partnership. Therefore, to the extent a transfer of property is characterized as a sale under the existing section 707 framework, there is no contribution and section 1400Z–2 would not apply to the transfer. These final regulations do not modify section 707 or the regulations in this part under section 707.

Second, proposed § 1.1400Z2(a)–1(b)(11)(ii)(A)(*2*) provided that, to the extent proposed § 1.1400Z2(a)–1(b)(11)(ii)(A)(*1*) did not apply, the transfer to the partnership would not be treated as a section 1400Z–2(a)(1)(A) investment to the extent the partnership makes a distribution to the partner and the transfer to the partnership and the distribution would be recharacterized as a disguised sale under section 707 if (i) any cash contributed were non-cash property, and (ii) in the case of a distribution by the partnership to which § 1.707–5(b) (relating to debt-financed distributions) applies, the partner's share of liabilities is zero. The Treasury Department and the IRS received comments asking for clarification of the application of proposed § 1.1400Z2(a)–1(b)(11)(ii)(A)(*2*) and confirmation that the regulations under section 707, including the exceptions to the disguised sale rules, apply in determining whether a contribution, in whole or part, is treated as part of a disguised sale. In particular, commenters asked how debt-financed distributions should be treated and requested confirmation that operating cash flow distributions would not be presumed to be a part of a disguised sale.

The Treasury Department and the IRS note that, even if a contribution were not recharacterized as a disguised sale under section 707 and the regulations in this part under section 707, the amount of the qualifying investment is reduced under the modified application of the section 707 disguised sale rules in § 1.1400Z2(a)–1(c)(6)(iii)(A)(*2*). This provision adopts the rule contained in the May 2019 proposed regulations without change. However, in making the qualifying investment determination under this rule, the other exceptions to the disguised sale rules still would apply. For example, a distribution by the partnership would not reduce the amount of the qualifying investment to the extent the operating cash flow distribution exception of § 1.707–4(b) applied.

Commenters also requested clarification regarding the Federal income tax consequences of distributions by an ''overfunded'' QOF partnership carried out to eliminate the amount of excess cash invested therein. Commenters explained that, in this situation, an eligible taxpayer would contribute a cash amount in excess of the amount that the QOF partnership desires to invest and, within the same year, the QOF partnership distributes the excess cash back to the eligible taxpayer. The final regulations provide an example clarifying and illustrating the application of the rules. The later distribution by the QOF partnership would be tested under the normal distribution rules for purposes of determining whether there is an inclusion event. For QOF partnerships, there would be an inclusion event to the extent the distribution exceeds the

partner's outside basis in its qualifying investment. Although the basis in the qualifying investment is initially zero, that basis may be increased by the partner's share of debt and net income.

F. At-Risk Basis

One commenter requested clarification that investors get at-risk basis for their qualifying investments. The May 2019 proposed regulations did not address whether a taxpayer has at-risk basis in its qualifying investment. Thus, the commenter stated that there is uncertainty under the May 2019 proposed regulations as to whether investors' capital contributions will give rise to at-risk basis under section 465 even though taxpayers must take zero basis in their qualifying investments.

Section 465 generally provides that a taxpayer shall be considered ''at risk'' for an activity with respect to amounts including the amount of money and the adjusted basis of other property contributed by the taxpayer to the activity. The Treasury Department and the IRS note that a taxpayer's amount at risk generally is determined by reference to the amount of money and the basis of property contributed, not to the basis of the interest received in exchange for the property. Additionally, section 465 and the regulations in this part under section 465 provide the necessary guidance for this determination. As a result, the Treasury Department and the IRS have determined that the commenter's requested clarification exceeds the scope of the section 1400Z–2 regulations.

G. Withholding Tax and FIRPTA

The Treasury Department and the IRS received comments regarding the application of withholding tax regimes within the context of section 1400Z–2(a). For example, a commenter requested that a foreign taxpayer engaging in a sale subject to withholding under section 1445(a) (imposing a 15 percent withholding tax as part of the Foreign Investment in Real Property Tax Act (FIRPTA)) be able to provide a certificate or other form of documentation to avoid withholding on the basis of the taxpayer's intention to invest the resulting gain in a QOF pursuant to a deferral election under section 1400Z–2(a)(1). Another commenter requested an exemption from withholding when a person enters into an agreement with the IRS to pay the tax when the deferred gain is included under section 1400Z–2(a)(1)(B) and (b), similar to when a gain recognition agreement is ''triggered'' under section 367 and the regulations in this part under section 367. The Treasury Department and the IRS continue to consider this comment and other matters related to the mechanics of applying section 1400Z–2 in the context of a sale subject to withholding tax.

The final regulations clarify that section 1400Z–2 is not a ''nonrecognition provision'' for purposes of section 897(e) and § 1.897–6T. See § 1.1400Z2(a)–1(e). A non-recognition provision is defined in section 897(e)(3) as any provision of the Code for ''not recognizing gain or loss.'' Similarly, § 1.897–6T(a)(2) defines a non-recognition provision as any Code provision ''which provides that gain or loss shall not be recognized.'' Pursuant to section 897(e)(1) and § 1.897–6T(a)(1), nonrecognition provisions generally do not apply upon the exchange of a U.S. real property interest in a transaction subject to FIRPTA unless the asset received in exchange is also a U.S. real property interest. The Treasury Department and the IRS have determined that section 1400Z–2 is not a nonrecognition provision for purposes of section 897(e) and § 1.897–6T because an election under that provision generally defers, rather than prevents altogether, the recognition of gain. By deferring gain recognition, section 1400Z–2 is fundamentally different from the provisions identified as nonrecognition provisions in § 1.897–6T(a)(2), such as sections 332, 351, 721, and 1031.

III. Comments on and Changes to Proposed § 1.1400Z2(b)–1

Proposed § 1.1400Z2(b)–1 provided rules regarding the inclusion in income of gain deferred under section 1400Z–2(a)(1)(A), including rules regarding which events trigger the inclusion of deferred gain, how much gain is included, and the effects of these events on the investor's basis and holding period in its qualifying investment.

A. General Rule Regarding Inclusion Events

Proposed § 1.1400Z2(b)–1(c)(1) generally provided that, except as otherwise provided in proposed § 1.1400Z2(b)–1(c), certain events (that is, inclusion events) result in the inclusion of gain under proposed § 1.1400Z2(b)–1(b) if and to the extent that: (i) A taxpayer's transfer of a qualifying investment reduces the taxpayer's equity interest in the qualifying investment; (ii) a taxpayer receives property in a transaction treated as a distribution for Federal income tax purposes, regardless of whether the receipt reduces the taxpayer's ownership of the QOF; or (iii) a taxpayer claims a worthlessness deduction with respect to its qualifying investment. Proposed § 1.1400Z2(b)–1(c)(2) through (15) then provided specific rules for certain types of transactions that are or are not treated as inclusion events.

The Treasury Department and the IRS received several comments and questions regarding the general rule set forth in proposed § 1.1400Z2(b)–1(c)(1). For example, one commenter asked whether the phrase ''the following events'' refers to the items in proposed § 1.1400Z2(b)–1(c)(2) through (15) or whether the phrase instead refers to the items in proposed § 1.1400Z2(b)–1(c)(1)(i) through (iii). Another commenter stated that the general rule in proposed § 1.1400Z2(b)–1(c)(1)(i) could be read to suggest that there is no inclusion event so long as a taxpayer retains an equity interest, whether direct or indirect, in a qualifying investment after a transfer, even though the preamble to the May 2019 proposed regulations indicated that any reduction in a taxpayer's direct interest in a qualifying investment is an inclusion event, other than in the case of partnerships. Yet another commenter asserted that the specific rules in proposed § 1.1400Z2(b)–1(c)(2) through (15) appear to cover all potentially relevant transactions and therefore the purpose of the general rule seems unclear. As a result, commenters recommended that the Treasury Department and the IRS clarify or eliminate the general rule.

As explained in the preamble to the May 2019 proposed regulations, proposed § 1.1400Z2(b)–1(c) reflected the general principle that, except as otherwise provided, an inclusion event results from: A transfer of a qualifying investment, to the extent the transfer reduces the taxpayer's direct equity interest; the receipt of a distribution on or with respect to a qualifying investment, which constitutes an impermissible ''cashing out'' of the taxpayer's qualifying investment; or the claim of a worthlessness deduction (under section 165(g) or otherwise) in respect of a qualifying investment. Proposed § 1.1400Z2(b)–1(c)(1) set forth these principles as a general rule, and proposed § 1.1400Z2(b)–1(c)(2) through (15) provided elaborations of, and exceptions to, the general rule. The Treasury Department and the IRS did not intend the general rule to suggest that a taxpayer may avoid an inclusion event by retaining an indirect interest in a QOF, and the specific rules clearly indicated that a transfer that reduces a

taxpayer's direct interest is an inclusion event except as otherwise provided.

These final regulations retain the general rule in proposed § 1.1400Z2(b)–1(c)(1). However, this general rule has been clarified in response to the foregoing comments. In addition to the changes described in this part III, the specific rules in § 1.1400Z2(b)–1(c)(2) through (c)(15) have been clarified as necessary.

These final regulations also clarify that if a QOF is decertified, either through the QOF's voluntary self-decertification or an involuntary decertification, such decertification is an inclusion event that terminates the qualifying investment status of the taxpayer's interest in the QOF.

A commenter also requested clarification as to whether an inclusion event terminates the application of section 1400Z–2 to an interest in a QOF. In some cases, an inclusion event may be the result of a transfer of the qualifying investment that reduces or terminates the owner's interest in the QOF, but in other cases it may not (for example, a distribution from a QOF C corporation subject to section 301(c)(3)). Thus, the commenter argued that the occurrence of an inclusion event is not the appropriate test for determining whether an interest in a QOF ceases to be a qualifying investment eligible for the basis adjustments under section 1400Z–2(b).

As discussed in part II.A.5 of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have determined that an inclusion event generally results in a reduction or termination of a qualifying investment's status as a qualifying investment to the extent of the reduction or termination for purposes of section 1400Z–2(a)(1)(B), (b), and (c). However, the Treasury Department and the IRS agree that certain types of inclusion events (namely, certain distributions) do not terminate a taxpayer's qualifying investment. See part IV.C of this Summary of Comments and Explanation of Revisions.

The Treasury Department and the IRS also recognize that the language in proposed § 1.1400Z2(b)–1(g)(2), which provided that ''[t]he increases in basis under section 1400Z–2(b)(2)(B)(iii) and (iv) only apply to that portion of the qualifying investment that has not been subject to previous gain inclusion under section 1400Z–2(b)(2)(A),'' could be read to suggest that all inclusion events cause interests in a QOF to cease to be qualifying investments. In other words, by restricting the five-year and seven-year basis increases to qualifying investments that have ''not been subject to previous gain inclusion,'' proposed § 1.1400Z2(b)–1(g)(2) appeared to exclude any qualifying investment that has been subject to any inclusion event, even if substantial amounts of deferred gain remain.

The Treasury Department and the IRS have determined that qualifying investments that have been subject to inclusion events should continue to be eligible for the five-year and seven-year basis increases to the extent deferred gain has not yet been recognized at the time of these basis increases. For example, if a taxpayer invests $100x of eligible gain in a QOF corporation and the corporation subsequently makes a section 301(c)(3) distribution of $20x with respect to the taxpayer's qualifying investment, the taxpayer still should be eligible to receive a five-year basis increase of $8x (10 percent of its remaining deferred gain of $80x) and a seven-year basis increase of $4x (five percent of its remaining deferred gain of $80x). Section 1.1400Z2(b)–1(g)(2) of the final regulations has been modified accordingly.

B. Transactions Treated as Distributions for Federal Income Tax Purposes

1. Overview

Proposed § 1.1400Z2(b)–1(c)(1)(ii) generally provided that, except as otherwise provided in proposed § 1.1400Z2(b)–1(c), an inclusion event occurs if and to the extent a taxpayer receives property in a transaction that is treated as a distribution for Federal income tax purposes, regardless of whether the receipt reduces the taxpayer's ownership of the QOF. Proposed § 1.1400Z2(b)–1(c)(8) modified this general rule by providing that a distribution of property by a QOF C corporation with respect to a qualifying investment, including a distribution of stock that is treated as a distribution of property to which section 301 applies under section 305(b), is an inclusion event only to the extent section 301(c)(3) applies to the distribution. In the preamble to the May 2019 proposed regulations, the Treasury Department and the IRS requested comments on the proposed treatment of distributions to which section 305(b) applies.

In turn, proposed § 1.1400Z2(b)–1(c)(9) generally provided that a redemption described in section 302(d) by a QOF C corporation is an inclusion event with respect to the full amount of the distribution. However, if the QOF C corporation is wholly and directly owned by a single shareholder (or by members of a single consolidated group), the section 302(d) redemption is an inclusion event only to the extent section 301(c)(3) applies.

2. Section 302(d) Redemptions

Commenters made several recommendations with respect to the foregoing rules. For example, commenters questioned the treatment of dividend-equivalent redemptions in the May 2019 proposed regulations. One commenter acknowledged that a section 302(d) redemption reduces a taxpayer's direct equity interest, but the commenter recommended treating such redemptions in the same manner as section 301 distributions for purposes of section 1400Z–2 because section 302 treats such redemptions as distributions rather than as sales or exchanges. The commenter further recommended that section 302(d) redemptions in which each shareholder surrenders a pro rata percentage of its shares not be treated as inclusion events. Another commenter recognized that requiring an inclusion event only upon a complete redemption of a shareholder's qualifying investment would enable taxpayers to avoid taxation by retaining even a small amount of qualifying QOF stock, but the commenter still questioned why a partial redemption should cause acceleration. Both commenters recommended that section 302(d) redemptions and section 301 distributions be treated similarly for purposes of section 1400Z–2, with the exception of complete redemptions, which would be an inclusion event to the extent of the full amount of the distribution.

As noted in the foregoing comments, a redemption transaction reduces a taxpayer's direct qualifying investment in a QOF, regardless of whether such transaction is treated as a dividend for Federal income tax purposes. The Treasury Department and the IRS have determined that the general treatment of section 302(d) redemptions as section 301 distributions for Federal income tax purposes should not override the general requirement that QOF shareholders must retain their direct qualifying investment in a QOF corporation in order to retain the benefits of section 1400Z–2. See section 1400Z–2(b)(1)(A) (''Gain to which subsection (a)(1)(B) applies shall be included in income in the taxable year which includes . . . the date on which such investment is sold or exchanged . . .''). As a result, the Treasury Department and the IRS have determined that it would be inappropriate to treat such redemptions in the same manner as section 301 distributions for purposes of section 1400Z–2.

However, in certain circumstances, a reduction in a taxpayer's qualifying investment by virtue of a section 302(d) redemption is meaningless. For example, if a wholly owned QOF C corporation partially redeems its sole shareholder, the shareholder will continue to wholly own the QOF C corporation after the redemption. Similarly, if a QOF C corporation redeems its single outstanding class of stock from all shareholders on a pro rata basis, each QOF shareholder will retain the same proportionate interest in the QOF after the partial redemption.

As a result, the final regulations generally continue to treat dividend-equivalent redemptions by QOF C corporations as inclusion events with respect to the full amount of the distribution, with an exception for redemptions by wholly owned QOF C corporations, which are inclusion events only to the extent section 301(c)(3) applies. The Treasury Department and the IRS agree with the commenter that an additional exception should be created for pro rata section 302(d) redemptions, so long as the QOF C corporation has only one class of stock outstanding. The final regulations have been modified to treat such redemptions in the same manner as redemptions by wholly owned QOF C corporations. In other words, an inclusion event occurs only to the extent section 301(c)(3) applies. Similarly, with respect to QOF S corporations, the final regulations continue to treat dividend-equivalent redemptions as inclusion events to the extent that the distributed property has a fair market value in excess of the shareholder's basis, including any basis adjustments under section 1400Z–2(b)(2)(B)(iii) and (iv). See part III.E.2.a of this Summary of Comments and Explanation of Revisions.

3. Section 305 Distributions and Section 306 Redemptions

A commenter agreed with the treatment of section 305(b) distributions in the May 2019 proposed regulations—namely, that such distributions should be included as distributions subject to the rule in proposed § 1.1400Z2(b)–1(c)(8). However, the commenter further recommended that the final regulations address the treatment of stock received in a section 305(a) distribution with respect to qualifying QOF stock. When a corporation distributes its own stock to its shareholders, section 305(a) provides that the shareholders do not include the distribution in gross income. The basis of the new stock received and of the stock with respect to which the distribution is made (old stock) is determined by allocating the basis of the old stock between the old stock and the new stock in proportion to the respective fair market values of the old stock and the new stock on the date on which the new stock is distributed, and the holding period for the new stock is the same as the holding period for the old stock. See § 1.307–1(a) (regarding allocation of basis) and section 1223(4) (regarding determination of holding period). The commenter requested clarification that the new stock received in a section 305(a) distribution with respect to qualifying QOF stock is also qualifying QOF stock, with the remaining deferred gain being allocated pro rata between the old stock and the new stock, and with the holding period for the new stock being the same as the holding period for the old stock. The Treasury Department and the IRS agree with the commenter's recommendation, and the final regulations have been modified accordingly.

The commenter also requested clarification regarding the treatment of redemptions of section 306 stock. Section 306 stock generally includes stock, other than common stock, that was received tax-free in certain transactions by the shareholder disposing of such stock, including a stock dividend under section 305(a), a corporate reorganization described in section 368(a), or a distribution or exchange to which section 355 (or so much of section 356 as relates to section 355) applied. See section 306(c). Section 306(a)(2) provides that, if a shareholder disposes of its section 306 stock in a redemption, the amount realized is treated as a distribution of property to which section 301 applies. The commenter recommended that such a redemption be subject to the rules for section 301 distributions in proposed § 1.1400Z2(b)–1(c)(8).

The Treasury Department and the IRS agree that the final regulations should address the treatment of section 306(a)(2) redemptions. For the reasons discussed in part III.B.2 of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have determined that section 306(a)(2) redemptions should be treated in the same manner as dividend-equivalent redemptions for purposes of section 1400Z–2. The final regulations have been modified accordingly.

4. Distributions Subject to Section 1059

A commenter recommended that qualifying investments in QOF C corporations be excluded from the application of section 1059. Alternatively, the commenter requested confirmation that (1) the recognition of gain under section 1059(a)(2) would result in an inclusion event to the extent of that gain, and (2) the ordering rule in proposed § 1.1400Z2(b)–1(g)(1)(ii), which applied to basis increases under section 1400Z–2(b)(2)(B)(ii), also would apply to such inclusion event.

The commenter contended that, in many instances, the policy concerns underlying section 1059, as described by the commenter, would not be applicable to distributions made by a QOF C corporation. However, an example in the commenter's analysis illustrated that the concerns underlying section 1059 are present any time a QOF corporation has earnings and profits (E&P) predating the date on which a qualifying investment is made. The Treasury Department and the IRS have determined that, to the extent consistent with the application of section 1400Z–2, and unless provided otherwise by the section 1400Z–2 regulations, the rules of subchapter C apply with respect to a QOF C corporation. The commenter's analysis did not set forth any statutory authority under section 1400Z–2 or subchapter C for not applying section 1059 to distributions from a QOF C corporation. As a result, the Treasury Department and the IRS have determined that section 1059 should apply to a QOF C corporation, and the final regulations do not adopt the commenter's primary recommendation.

However, the Treasury Department and the IRS agree with the commenter's alternative recommendation that the recognition of gain under section 1059(a)(2) should result in an inclusion event to the extent of that gain, and that the ordering rule in proposed § 1.1400Z2(b)–1(g)(1)(ii) should apply to such inclusion event. The final regulations have been modified accordingly.

C. Reorganizations of QOF Corporations

1. Overview

Proposed § 1.1400Z2(b)–1(c)(10) generally provided that, if the assets of a QOF corporation are acquired in a qualifying section 381 transaction, and if the acquiring corporation is a QOF within a prescribed period of time after the acquisition, the transaction would not be an inclusion event. The proposed regulations included this rule because, after the transaction, the taxpayer would have retained a direct qualifying investment in an acquiring QOF that is a successor to the transferor QOF under section 381. The proposed regulations defined the term ''qualifying section 381 transaction'' to mean an acquisitive asset reorganization described in section

381(a)(2), with certain enumerated exceptions. See proposed § 1.1400Z2(b)–1(a)(2)(xx).

However, if a QOF shareholder received boot in a qualifying section 381 transaction with respect to the shareholder's qualifying investment, the taxpayer would have an inclusion event because the taxpayer would have reduced its direct qualifying investment in the QOF or cashed out part of its investment. For this purpose, the term ''boot'' means money or other property that section 354 or 355 does not permit to be received without the recognition of gain. Under the May 2019 proposed regulations, if the taxpayer realizes a gain on the transaction, the amount that gives rise to the inclusion event is the amount of gain under section 356 that is not treated as a dividend under section 356(a)(2). If the taxpayer realizes a loss on the transaction, the amount that gives rise to the inclusion event is an amount equal to the fair market value of the boot received. If a single taxpayer or members of a single consolidated group wholly own both the target QOF and the acquiring QOF, the boot is treated as if it were distributed from the QOF in a separate section 301 transaction and is only taxable to the extent section 301(c)(3) applies.

In turn, proposed § 1.1400Z2(b)–1(c)(12) generally provided that, if a QOF corporation engages in a recapitalization transaction described in section 368(a)(1)(E) (recapitalization), or if a QOF shareholder engages in a stock-for-stock exchange described in section 1036 (section 1036 exchange), and if the transaction does not have the result of decreasing the shareholder's proportionate interest in the QOF corporation, the transaction is not an inclusion event. However, any property or boot received by the shareholder in the transaction is treated as property or boot to which section 301 or section 356 applies, as determined under general Federal income tax principles. Proposed § 1.1400Z2(b)–1(c)(8) or (10), respectively, then determined the extent to which the receipt of such property or boot triggers an inclusion event. Moreover, if the transaction decreases the shareholder's proportionate qualifying investment in the QOF corporation, the shareholder has an inclusion event equal to the amount of the reduction in fair market value of the shareholder's qualifying QOF stock.

2. Proposed Treatment of Recapitalizations and Section 1036 Exchanges

Several commenters recommended that a single inclusion event rule be applied to qualifying section 381 transactions, recapitalizations, and section 1036 exchanges. One commenter argued that, if a taxpayer's proportionate interest were reduced in a recapitalization or in a section 1036 exchange, the taxpayer either would have received actual consideration (that is, boot) in the transaction or would be deemed to have received boot in the transaction under general Federal income tax principles. See, for example, Rev. Rul. 74–269, 1974–1 C.B. 87. Another commenter argued that a reduction in a shareholder's proportionate interest by virtue of the QOF's issuance of new stock to a new investor should not be treated as an inclusion event, and that a reduction in the shareholder's interest by virtue of the shareholder's receipt of non-stock consideration should be covered by the boot rules for reorganizations. Thus, the commenters argued that recapitalizations and section 1036 exchanges should be governed by the same rules that govern qualifying section 381 transactions.

The Treasury Department and the IRS agree with many of the foregoing comments. For example, the Treasury Department and the IRS agree that the reduction of a shareholder's proportionate interest in a QOF through a recapitalization should not be treated as an inclusion event unless the shareholder receives, or is deemed to receive, boot in the transaction. Thus, a shareholder should not have an inclusion event by virtue of the QOF's issuance of qualifying QOF stock to a new investor. The Treasury Department and the IRS also agree that the rules for recapitalizations and section 1036 exchanges should be modified to mirror more closely the rules for qualifying section 381 transactions. The final regulations reflect these determinations. However, the final regulations retain separately numbered rules for reorganizations, and for recapitalizations and section 1036 exchanges.

3. Receipt of Boot

Commenters also recommended simplifying the proposed rules regarding boot. For example, one commenter recommended eliminating the special rule for the receipt of boot from a wholly owned QOF in proposed § 1.1400Z2(b)–1(c)(10)(i)(C)(*2*) and subjecting qualifying section 381 transactions, recapitalizations, and section 1036 exchanges to a single rule similar to proposed § 1.1400Z2(b)–1(c)(10)(i)(C)(*1*) (the general rule regarding the receipt of boot by QOF shareholder in a qualifying section 381 transaction). Another commenter questioned the disparate treatment of boot in reorganizations depending on whether gain or loss is realized.

The Treasury Department and the IRS agree with commenters that the proposed rules regarding the receipt of boot should be simplified. Accordingly, the final regulations adopt a single rule for the receipt of boot in a qualifying section 381 transaction. Under this rule, a taxpayer is treated as disposing of a portion of its qualifying investment equal to the portion of total consideration received in the transaction with respect to the taxpayer's qualifying investment that consists of boot. For example, if a QOF engages in a merger that is a qualifying section 381 transaction, and if 10 percent of the consideration received by a QOF shareholder, as measured by fair market value, consists of boot, the QOF shareholder is treated as having disposed of 10 percent of its qualifying investment. This rule applies regardless of whether the QOF shareholder recognizes gain or loss on the transaction, and regardless of whether the QOF is wholly owned.

For property or boot received in recapitalizations or section 1036 exchanges, the final regulations provide that the property or boot is treated as property or boot to which section 301 or section 356(a) or (c) applies, as determined under general Federal income tax principles. The receipt of property to which section 301 applies is an inclusion event only to the extent section 301(c)(3) applies. The receipt of boot to which section 356(a) or (c) applies is subject to the single rule for the receipt of boot in a qualifying section 381 transaction.

If a taxpayer receives boot with respect to its qualifying investment in a qualifying section 355 transaction, as defined in proposed § 1.1400Z2(b)–1(a)(2)(xix), and if section 356(a) applies to the transaction, the receipt of boot also is subject to the single rule for the receipt of boot in a qualifying section 381 transaction. In turn, if a taxpayer receives boot with respect to its qualifying investment in a qualifying section 355 transaction, and if section 356(b) applies to the transaction, the receipt of boot is an inclusion event only to the extent section 301(c)(3) applies.

4. Treatment of the Surviving or Acquiring Corporation as a QOF

A commenter also requested clarification that, in the event of mergers, consolidations, share exchanges, asset acquisitions, and conversions in which the acquiring or surviving enterprise is a QOF, such

acquiring or surviving enterprise continues to be a QOF.

Whether the surviving or acquiring corporation after a merger, consolidation, share exchange, or asset acquisition continues to be a QOF depends on whether the surviving or acquiring corporation satisfies the requirements of section 1400Z–2(d) and the section 1400Z–2 regulations. Therefore, the final regulations do not adopt the commenter's recommended clarification. For a discussion of conversions of QOF partnerships to QOF corporations, see part III.E.1 of this Summary of Comments and Explanation of Revisions.

D. Reorganizations of QOF Shareholders

Proposed § 1.1400Z2(b)–1(c)(10)(ii) generally provided that a transfer of a QOF shareholder's assets in a qualifying section 381 transaction (qualifying owner reorganization) is not an inclusion event, except to the extent the QOF shareholder transfers less than all of its qualifying investment in the transaction, because the section 381 successor to the QOF shareholder retains a direct qualifying investment in the QOF. In other words, the section 381 successor is treated as the historic QOF shareholder and therefore no disposition of the direct qualifying investment in the QOF has occurred. Based on the same rationale, proposed § 1.1400Z2(b)–1(c)(2)(ii)(B) provided that the transfer of a QOF shareholder's qualifying investment in a complete liquidation under section 332 is not an inclusion event to the extent section 337(a) applies (qualifying owner liquidation). Special rules applied to S corporations that are shareholders of a QOF, and generally tracked the rules of subchapter C described previously, to the extent consistent with the rules of subchapter S. See proposed § 1.1400Z2(b)–1(c)(7).

Proposed § 1.1400Z2(b)–1(d)(1) and (2) contained special rules for qualifying section 381 transactions in which the target corporation was a QOF immediately before the acquisition and the acquiring corporation is a QOF immediately after the acquisition. For purposes of section 1400Z–2(b)(2)(B) and 1400Z–2(c), the May 2019 proposed regulations provided that the holding period for the QOF stock relinquished by a taxpayer is ''tacked'' onto the holding period of the QOF stock received in the transaction, and any qualified opportunity zone property transferred by the transferor QOF to the acquiring QOF in connection with the transaction does not lose its status as qualified opportunity zone property solely as a result of the transfer. However, the May 2019 proposed regulations did not provide similar rules for qualifying owner reorganizations or liquidations. As a result, one commenter requested that a ''tacked'' holding period be expressly provided for a QOF shareholder's qualifying investment in such transactions. Another commenter requested a rule for qualifying owner liquidations and reorganizations similar to proposed § 1.1400Z2(b)–1(c)(6)(ii)(C), which generally provided that the resulting partnership after certain partnership mergers or consolidations is subject to section 1400Z–2 and the section 1400Z–2 regulations to the same extent as the original partnership before the transaction.

The Treasury Department and the IRS agree that a ''tacking'' rule should apply to stock of a QOF shareholder after a qualifying owner reorganization or liquidation. Section 1.1400Z2(b)–1(d)(1)(ii) of the final regulations has been modified accordingly.

E. Partnerships, S Corporations, and Trusts

1. Inclusion Events for QOF Partnerships

Proposed § 1.1400Z2(b)–1(c)(6)(i) provided inclusion rules for QOF partnerships and partnerships that directly or indirectly own interests in QOFs. These rules applied to transactions involving any direct or indirect partner of a QOF to the extent of the partner's share of any eligible gain. Proposed § 1.1400Z2(b)–1(c)(6)(ii)(B) provided that a contribution by a QOF owner of its direct or indirect partnership interest in a qualifying investment to a partnership is not an inclusion event to the extent the transaction is governed by section 721(a), provided the transfer does not cause a termination of a QOF partnership, or of the direct or indirect owner of a QOF, under section 708(b)(1).

The Treasury Department and the IRS received several comments on whether certain transactions involving QOF partnerships should be considered inclusion events. One commenter requested clarification of proposed § 1.1400Z2(b)–1(c)(6)(iii), which provided that a distribution of property by a QOF partnership to a partner is an inclusion event if the distributed property has a fair market value in excess of the partner's basis in its qualifying investment, and that similar rules apply to distributions involving tiered partnerships. The final regulations provide that, for amounts relating to a partner's qualifying investment, a distribution by a QOF partnership to a partner is an inclusion event to the extent the distribution is of cash or property with a fair market value in excess of the partner's outside basis in the QOF partnership. However, with respect to distributions by a partnership that owns a QOF, such distribution will only be an inclusion event for the indirect QOF owner if the distribution is a liquidating distribution.

The commenter suggested that such a distribution should not be an inclusion event to the extent the partner in the QOF ultimately would be allocated the gain recognized upon the distribution. The commenter also requested an exception from inclusion event treatment for section 731 distributions of a QOF interest by an upper-tier partnership to the extent the distribution is to the partner that made the initial qualifying investment in the QOF. The Treasury Department and the IRS decline to adopt these recommendations. Under the rules in subchapter K of chapter 1 of subtitle A (subchapter K), a distribution of property with a fair market value in excess of basis reduces a partner's equity interest in the partnership. Such a reduction is an inclusion event and is economically the same as an investor cashing out its investment or reducing its equity investment in the QOF.

One commenter also requested that a contribution of an interest in a partnership that holds a direct interest in a QOF partnership to another partnership not be considered an inclusion event. This transaction was addressed by proposed § 1.1400Z2(b)–1(c)(6)(ii)(B), which applied to contributions under section 721(a) by a QOF owner, including a QOF partner. See proposed § 1.1400Z2(b)–1(a)(2)(xii), which defined a QOF partner as a person that directly owns a qualifying investment in a QOF partnership or a person that owns such a qualifying investment through equity interests solely in one or more partnerships. The final regulations clarify that the rule in proposed § 1.1400Z2(b)–1(c)(6)(ii)(B) applies to any QOF owner that contributes its qualifying QOF stock or direct or indirect partnership interest in a qualifying investment to a partnership in a transaction governed by section 721(a).

Another commenter requested that the list of inclusion events exclude not only section 721 contributions, but also the merger of a fund formed as a REIT into another REIT. The commenter recommended that the final regulations clarify and expand the scope of the permitted transactions under the rules for inclusion. The Treasury Department and the IRS decline to adopt this

suggestion but note that the exceptions to inclusion event treatment applicable to QOF C corporations, such as the exception for qualifying section 381 transactions, also apply to RICs and REITs.

Proposed § 1.1400Z2(b)–1(c)(6)(ii)(C) provided that a merger or consolidation of a partnership holding a qualifying investment, or of a partnership holding an interest in such partnership solely through one or more partnerships, with another partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event. A commenter noted that the May 2019 proposed regulations did not explicitly provide that a merger of a QOF partnership into another partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event, even if the acquiring partnership is a QOF immediately after the merger.

The Treasury Department and the IRS adopt the comment in part. The Treasury Department and the IRS have determined that the rule in § 1.1400Z2(b)–1(c)(6)(iii) of the May 2019 proposed regulations, which provided that a QOF partnership distribution with a fair market value in excess of the distributee partner's basis is an inclusion event, should be modified in the case of certain mergers or consolidations under section 708(b)(2)(A).

The final regulations provide that, in the case of an assets-over merger or consolidation of a QOF partnership with another QOF partnership in a transaction to which section 708(b)(2)(A) applies, the fair market value of property distributed in the merger or consolidation is reduced by the fair market value of the partnership interest received in the merger or consolidation for purposes of determining whether there has been an inclusion event. Therefore, the transaction will not be an inclusion event to a partner that receives only a partnership interest in the resulting partnership. However, there will be an inclusion event to the extent that a partner receives other property that exceeds that partner's basis in the partnership.

Additionally, the final regulations provide that a merger or consolidation of a QOF partnership with another QOF partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event under § 1.1400Z2(b)–1(c)(2)(i), which provides that there is an inclusion event if a QOF ceases to exist for Federal income tax purposes. The resulting partnership becomes subject to section 1400Z–2 and the section 1400Z–2 regulations to the same extent that the terminated partnership was so subject prior to the transaction, and must allocate and report any gain inclusion under section 1400Z–2(b) to the same extent and to the same partners that the terminated partnership would have been required to allocate and report those items prior to the transaction.

A commenter also requested clarification that any partnership distribution of property pursuant to a division governed by § 1.708–1(d) is not an inclusion event, provided the taxpayer's beneficial interest in a QOF has not changed and all deferred gain still would be recognized by the same taxpayer. Several other commenters requested that pro-rata divisions of QOF partnerships into two or more QOF partnerships pursuant to section 708 not be treated as inclusion events, provided the amount of a taxpayer's equity interest in its qualifying investment remains the same.

The Treasury Department and the IRS decline to adopt a general rule excluding divisions as inclusion events because divisions may result in deemed distributions arising from debt shifts, as well as distributions in excess of basis, which may result in gain recognition under the subchapter K rules. Additionally, as described in part IV.E.4 of this Summary of Comments and Explanation of Revisions, the final regulations expand the rule of proposed § 1.1400Z2(c)–1(b)(2)(ii) to provide that, with the exception of gain from the sale of inventory in the ordinary course of business, all gain from the sale of property by a QOF partnership or by a qualified opportunity zone business that is a partnership is eligible for exclusion as long as the qualifying investment in the QOF has been held for at least 10 years. This change to proposed § 1.1400Z2(c)–1(b)(2)(ii) may minimize the need for divisions of QOF partnerships as a way to dispose of certain assets.

One commenter also asked that a distribution by a QOF partnership of its net cash flow, measured on an annual basis by reference to taxable income, plus depreciation deductions, not constitute an inclusion event. The Treasury Department and the IRS decline to adopt this recommendation because allowing such distributions in excess of the QOF partner's basis would add significant complexity, requiring the tracing of distributions of net cash flow proceeds versus cash from other sources.

One commenter asked why proposed § 1.1400Z2(b)–1(c)(6) used the phrase ''eligible gain.'' Proposed § 1.1400Z2(b)–1(c)(6) stated, in relevant part, that ''the inclusion rules of this paragraph (c) apply to transactions involving any direct or indirect partner of the QOF to the extent of such partner's share of eligible gain of the QOF.'' The commenter further noted that proposed § 1.1400Z2(b)–1(c)(6) used this phrase three times, and the inclusion of that phrase seemed inappropriate.

The Treasury Department and the IRS confirm that ''eligible gain'' was the intended term in proposed § 1.1400Z2(b)–1(c)(6). Eligible gain is a defined term in proposed § 1.1400Z2(a)–1(b)(2), and generally refers to gain that is eligible to be deferred under section 1400Z–2(a). The term is further defined in § 1.1400Z2(a)–1(b)(11) of the final regulations. In addition, proposed § 1.1400Z2(b)–1(c)(6) provided special rules relating to inclusion events for partners and partnerships, and used the defined term ''eligible gain'' to reference the amount of gain deferred under section 1400Z–2(a) that is required to be included in income upon the occurrence of certain inclusion events.

Proposed § 1.1400Z2(b)–1(c)(7)(iv) provided special rules regarding inclusion events for conversions of S corporations to partnerships or disregarded entities. Otherwise, the May 2019 proposed regulations did not expressly address whether a QOF's change in classification, such as from a partnership to a corporation, is an inclusion event. A commenter recommended that the conversion of a QOF from a partnership to a corporation for Federal tax purposes be treated as neither an inclusion event nor a disposition of a qualifying investment for purposes of the election in section 1400Z–2(c).

The Treasury Department and the IRS note that, if a partnership elects under § 301.7701–3(c)(1)(i) to be classified as an association, under § 301.7701–3(g)(1)(i) the partnership is deemed to contribute all of its assets and liabilities to the association in exchange for stock and to liquidate immediately thereafter. See also Rev. Rul. 2004–59, 2004–1 C.B. 1050 (applying the same treatment to a partnership that converts to a corporation under a state law formless conversion statute). As provided in proposed § 1.1400Z2(b)–1(c)(2)(i), a taxpayer generally has an inclusion event for all of its qualifying investment if the QOF ceases to exist for Federal income tax purposes, and no specific rule in proposed § 1.1400Z2(b)–1(c) provides an exception for liquidations of QOF partnerships. Thus, the conversion of a partnership to a corporation would be an inclusion event. No change has been made to the

final regulations with respect to this comment.

2. Inclusion Events for QOF S Corporations

a. General Principle of Section 1371(a)

The May 2019 proposed regulations relied upon the principle set forth in section 1371(a), which provides that the rules of subchapter C of chapter 1 of subtitle A (subchapter C) applicable to C corporations and their shareholders apply to S corporations and their shareholders, except to the extent inconsistent with the provisions of subchapter S. In such instances, S corporations and their shareholders are subject to the specific rules of subchapter S. For example, similar to rules applicable to QOF partnerships, a distribution of property to which section 1368 applies by a QOF S corporation is an inclusion event to the extent that the distributed property has a fair market value in excess of the shareholder's basis, including any basis adjustments under section 1400Z–2(b)(2)(B)(iii) and (iv). In addition, the rules set forth in the May 2019 proposed regulations regarding redemptions, liquidations, and reorganizations of QOF C corporations and QOF C corporation shareholders apply equally to QOF S corporations and QOF S corporation shareholders to the extent consistent with the rules of subchapter S. For example, because the stock of an S corporation cannot be held by a C corporation, no exception is provided for a liquidation or upstream asset reorganization of an S corporation investor in a QOF.

However, the May 2019 proposed regulations also reflect that flow-through principles under subchapter S apply to S corporations when the application of subchapter C would be inconsistent with subchapter S. For example, under the May 2019 proposed regulations, if an inclusion event were to occur with respect to deferred gain of an S corporation that is an investor in a QOF, the shareholders of the S corporation would include the gain pro rata in their respective taxable incomes. See section 1366(a)(1)(A). Consequently, those S corporation shareholders would increase their bases in their S corporation stock at the end of the taxable year during which the inclusion event occurred. See section 1367(a)(1)(A). Pursuant to the S corporation distribution rules set forth in section 1368, the S corporation shareholders would receive future distributions from the S corporation tax-free to the extent of the deferred gain amount included in income and included in stock basis. If the S corporation has accumulated E&P, the S corporation's accumulated adjustments account would be increased by the same amount as the increase in stock basis to ensure the shareholders' tax-free treatment of the future distributions. See section 1368(c), (e)(1).

b. Specific Inclusion Event Rules for S Corporations

The May 2019 proposed regulations also set forth specific rules for S corporations to provide certainty to taxpayers regarding the application of particular provisions under section 1400Z–2. Regarding section 1400Z–2(b)(1)(A), the May 2019 proposed regulations clarified that a conversion of an S corporation that holds a qualifying investment in a QOF to a C corporation (or a conversion of a C corporation to an S corporation) is not an inclusion event because the interests held by each shareholder of the C corporation or S corporation, as appropriate, would remain unchanged with respect to the corporation's qualifying investment in a QOF. For mixed-funds investments in a QOF S corporation described in section 1400Z–2(e)(1), if different blocks of stock are created for otherwise qualifying investments to track basis in these qualifying investments, the May 2019 proposed regulations made clear that the separate blocks would not be treated as different classes of stock for purposes of S corporation eligibility under section 1361(b)(1).

The Treasury Department and the IRS received favorable comments regarding the reliance of the May 2019 proposed regulations upon the principle set forth in section 1371(a). In addition, commenters provided favorable comments regarding the foregoing rules, which the Treasury Department and the IRS drafted in accordance with that principle. As a result, the final regulations adopt those rules without modification.

c. Elimination of 25-Percent Aggregate Ownership Change Rule

The May 2019 proposed regulations set forth a special rule that, solely for purposes of section 1400Z–2, an S corporation's qualifying investment in a QOF would be treated as disposed of if there is a greater-than-25 percent aggregate change in ownership of the S corporation (25-percent aggregate ownership change rule). Under that rule, upon a greater-than-25 percent aggregate change in ownership, the S corporation would have an inclusion event for all of the S corporation's remaining deferred gain, and neither section 1400Z–2(b)(2)(B)(iii) or (iv), nor section 1400Z–2(c), would apply to the S corporation's qualifying investment after that date. In proposing the 25-percent aggregate ownership change rule, the Treasury Department and the IRS attempted to ''balance the status of the S corporation as the owner of the qualifying investment with the desire to preserve the incidence of the capital gain inclusion and income exclusion benefits under section 1400Z–2.'' Section VII.D.3 of the preamble to the May 2019 proposed regulations.

The Treasury Department and the IRS have received comments from the taxpayer and practitioner communities critical of the 25-percent aggregate ownership change rule. In particular, commenters have emphasized that the proposed rule conflicts with the stated purpose of inclusion events under section 1400Z–2, which is to ''prevent taxpayers from 'cashing out' a qualifying investment in a QOF without including in gross income any amount of their deferred gain.'' Section VII.A of the preamble to the May 2019 proposed regulations. In addition, commenters have noted that subchapter S of the Code already contains provisions, such as section 1377, that achieve more effectively the ''balance'' intended through the proposed 25-percent aggregate ownership change rule.

As previously stated, for purposes of the Code, including section 1400Z–2, the rules of subchapter C apply to an S corporation and its shareholders unless inconsistent with subchapter S. See section 1371(a). For example, if an S corporation investor in a QOF were to have an inclusion event regarding the S corporation's qualifying investment, the rules of subchapter S would apply to ensure that the shareholders of the S corporation would include the resulting gain pro rata in their respective taxable incomes and increase their bases in their S corporation stock at the end of the taxable year during which the inclusion event occurred. See generally section 1366. However, neither subchapter S nor section 1400Z–2 provides that the disposition of any stock held by a shareholder of an S corporation should cause an inclusion event under section 1400Z–2 for a qualifying investment held by the S corporation in a QOF (that is, should be treated as a disposition by the S corporation). Rather, the rules of subchapter S indicate the opposite, as evidenced by the ability for S corporation shareholders to dispose of their stock without affecting the S corporation's tax-free treatment resulting from a like-kind exchange of one of its assets. See generally section 1031. The Treasury Department and the

IRS have determined that, like a C corporation investor in a QOF C corporation, an S corporation investor should not have an inclusion event for its qualifying investment solely as the result of a disposition of shares by one of its shareholders, regardless of the disposition's magnitude.

Furthermore, the Treasury Department and the IRS have determined that the proposed 25-percent aggregate ownership change rule does not achieve its stated purpose of balancing the status of the S corporation as the owner of the qualifying investment while directing capital gain inclusion to the proposed rule's intended parties (that is, the S corporation's shareholders, upon an inclusion event). See section VII.D.3 of the May 2019 proposed regulations. Indeed, the Treasury Department and the IRS note that the proposed rule conflicts with section 1377, the longstanding provision in subchapter S that governs the allocation of items of income among S corporation shareholders.

Under section 1377(a)(1), each shareholder's pro rata share of any item for any tax year generally equals the sum of the amounts determined for the shareholder by (1) assigning an equal portion of the item to each day of the tax year, and then (2) dividing that portion pro rata among the shares outstanding on that day, per share, per day. As an exception for terminations of a shareholder's interest, section 1377(a)(2) permits an S corporation and the affected shareholders (that is, the remaining shareholders of the S corporation at the time of the termination) to agree to a ''closing of the books'' of the S corporation and allocate the S corporation's items of income among those shareholders based on their ownership before and after the termination (that is, treat the taxable year as two taxable years, the first of which ends on the date of the termination). As highlighted by one commenter, in the absence of a ''closing of the books'' election, the inclusion of capital gain resulting from an inclusion event will be allocated pro rata among all of the S corporation's shareholders as of the end of the S corporation's taxable year, rather than to those shareholders who were shareholders at the time the S corporation invested its deferred capital gain in its QOF. In other words, the allocation rules of section 1377 do not operate to match S corporation items to specific shareholders. For these reasons, the Treasury Department and the IRS agree with the comments received and have removed the proposed 25-percent aggregate ownership change rule from the final regulations.

d. Contributions of QOF Investments to a Partnership

With respect to the contribution of a qualifying investment to an upper-tier partnership or the acquisition of an interest in an upper-tier partnership by another person, one commenter requested that forward section 704(c) and reverse section 704(c) principles apply to ensure that deferred gains, or any built-in gains on the QOF interest, are allocable to the proper taxpayers and that appropriate basis adjustments are made. The Treasury Department and the IRS agree that forward section 704(c) and reverse section 704(c) principles, which otherwise would apply, also apply in this context.

In addition, several commenters requested that the final regulations provide greater flexibility in the structuring of investments in QOF partnerships by allowing investors to use master-feeder structures and similar structures such as aggregator funds. The commenters noted that proposed § 1.1400Z2(b)–1(c)(6)(ii)(B) permitted a QOF owner to contribute its direct or indirect interest in a QOF partnership to another partnership under certain circumstances in a transaction governed by section 721(a) without the transfer being treated as an inclusion event. The final regulations decline to incorporate that comment because it is inconsistent with the statute. Specifically, section 1400Z–2(a)(1)(A) requires an eligible taxpayer to make an investment in a QOF within 180 days of the sale or exchange that gave rise to the eligible gain in order for the taxpayer to have made a qualifying investment.

The final regulations clarify that, when a QOF partner contributes its qualifying investment to a transferee partnership in a section 721 transaction, the transferee partnership is the party that recognizes the deferred gain and is eligible for the five- and seven-year basis adjustments. However, the transferee partnership must allocate all such amounts to the contributing partner, applying the principles of section 704(c). The contributing partner no longer will be eligible to make the elections under section 1400Z–2(c) and § 1.1400Z2(c)–1(b)(2). Instead, the transferee partnership will be the sole person eligible to make these elections, and the elections will apply to all partners in the transferee partnership for that tax year.

e. Mixed-Funds Investments in QOF Partnerships

Proposed § 1.1400Z2(b)–1(c)(6)(iv) provided that a partner that holds a mixed-funds investment in a QOF partnership (mixed-funds partner) is treated as holding separate interests in the QOF partnership—a qualifying investment and a non-qualifying investment—solely for purposes of section 1400Z–2. Under proposed § 1.1400Z2(b)–1(c)(6)(iv)(B), all section 704(b) allocations of income, gain, loss, and deduction, all section 752 allocations of debt, and all distributions made to a mixed-funds partner were treated as made to the separate interests based on the allocation percentages of the interests, which generally were determined based on the relative capital contributions attributable to the qualifying investment and the non-qualifying investment. However, if a partner received a profits interest in the partnership in exchange for services, the May 2019 proposed regulations provided that the profits interest was a non-qualifying investment and that the allocation percentage for the profits interest was based on the highest share of residual profits the mixed-funds partner would receive with respect to that interest.

The Treasury Department and the IRS received a number of comments advocating different methods of allocating section 704(b) items, debt, and distributions between qualifying and non-qualifying investments in a mixed-funds investment. For example, one commenter requested that taxpayers be allowed to treat partnership distributions as made disproportionately to non-qualifying investments to minimize the likelihood that a distribution will cause a qualifying investment to be considered sold or exchanged. Another commenter requested that all debt be allocated to the non-qualifying investment. One commenter also recommended that gain on the sale of property by a QOF partnership be treated as attributable to the non-qualifying investment and qualifying investment based on each investment's share of section 704(b) gain with respect to the property.

The Treasury Department and the IRS decline to adopt these comments because the recommended changes would (i) increase the complexities in determining the items attributable to qualifying and non-qualifying investments comprising a mixed-funds investment, and (ii) be significantly more difficult to administer for both taxpayers and the IRS. The Treasury Department and the IRS have

determined that the approach in the May 2019 proposed regulations is the most straightforward option, and the option that minimizes administrable burden, for determining allocation percentages for qualifying and non-qualifying investments. Therefore, the final regulations retain the rule in the May 2019 proposed regulations and continue to determine allocation percentages based on relative capital contributions.

Commenters generally agreed with the rule in proposed § 1.1400Z2(a)–1(b)(9)(ii) that profits interests received for services should not be treated as qualifying investments. However, a number of commenters requested changes to the rule for calculating allocation percentages in the case of a profits interest received for services. One commenter highlighted that the proposed rule could result in a profits interest holder receiving an allocation percentage that is higher than its actual share of residual profits. Another commenter recommended that the allocation percentage for a profits interest be determined by comparing the profits received by the service provider with those derived by another significant partner that does not provide services to the QOF partnership. Yet another commenter requested that the final regulations incorporate the definition of ''applicable partnership interest'' under section 1061. This commenter recommended that the final regulations provide that the highest share of residual profits that a partner holding the mixed-funds investment would receive with respect to an ''applicable partnership interest'' would be determined by the highest share of residual profits less a reasonable return on the partner's capital interest, based on consideration of all facts and circumstances at the time of the receipt of the interest.

The Treasury Department and the IRS decline to adopt any of these comments because the approach in proposed § 1.1400Z2(b)–1(c)(6)(iv) is simpler and more administrable. The final regulations require a partner who receives a profits interest for services as part of a mixed-funds investment in a QOF partnership to determine the allocation percentage of the profits interest based on the share of residual profits that the mixed-funds partner would receive from the partnership. In addition, the final regulations provide that, if the residual share provided in the partnership agreement is not reasonably likely to apply, then that share will be disregarded in determining allocation percentages, and the allocation percentage for the profits interest will be the final share of profits provided in the partnership agreement that is likely to apply.

f. QSST and ESBT Conversions

A commenter requested clarification as to whether a conversion from a qualified subchapter S trust (QSST) to an electing small business trust (ESBT), and vice versa, falls within the exceptions to an inclusion event. The final regulations confirm that neither type of conversion is an inclusion event if the person who is both the deemed owner of the portion of the ESBT holding the qualifying investment and the QSST beneficiary is the person taxable on the income from the qualifying investment both before and after the conversion. For this purpose, § 1.1361–1(j)(8) is deemed not to apply because the conversion of a QSST to an ESBT differs from a disposition of the QSST asset where there is recognition of gain on the asset. However, there will be an inclusion event upon conversion if the qualifying investment is in the grantor portion of the ESBT and the ESBT's deemed owner is a nonresident alien.

g. Holding Periods

One commenter suggested clarifying how the principles of proposed § 1.1400Z2(b)–1(d)(1) and (2), which provided rules for holding periods for QOF investments, would be applied to partnership transactions described in proposed § 1.1400Z2(b)–1(c)(6)(ii), such as section 721(a) contributions and section 708(b)(2)(A) mergers or consolidations.

Proposed § 1.1400Z2(b)–1(d)(3) allowed the holding period of qualifying investments transferred in non-inclusion events listed in proposed § 1.1400Z2(b)–1(c)(6)(ii) to tack onto the holding period of the transferor under section 1223(1). The final regulations retain this provision. Under § 1.1400Z2(b)–1(d)(1), the holding period of the transferee partnership will include the holding period of the contributing partner.

h. Special Amount Includible Rule for Partnerships and S Corporations

Proposed § 1.1400Z2(b)–1(e)(4) provided that, for inclusion events involving partnerships and S corporations, the amount includible is equal to the percentage of the qualifying QOF partnership or QOF S corporation interest disposed of, multiplied by the lesser of (1) the remaining deferred gain less the five-year and seven-year basis adjustments; or (2) the gain that would be recognized by the partner or shareholder if the interest were sold in a fully taxable transaction for its then fair market value.

Section 1400Z–2(b)(2)(A) provides that the amount of gain included in gross income under section 1400Z–2(a)(1)(A) is the excess of (i) the lesser of the amount of gain excluded under paragraph (1) of that section or the fair market value of the investment as determined as of the date described in paragraph (1), over (ii) the taxpayer's basis in the investment.

Several commenters requested that the special amount includible rule for partnerships and S corporations be changed to follow the statutory language in section 1400Z–2(b)(2)(A). Commenters acknowledged that the special amount includible rule was intended to prevent taxpayers from avoiding the recognition of deferred gain upon an inclusion event when the fair market value of their qualifying investment has diminished due to debt-financed deductions or distributions. However, these commenters emphasized that the special amount includible rule creates inequitable results for debt-financed losses attributable to periods before December 31, 2026, as compared to debt-financed losses incurred after this date. Certain commenters also suggested that this rule has adversely affected the ability to develop low-income housing tax credit projects and other community development properties in QOZs.

The Treasury Department and the IRS have determined that the proposed special amount includible rule for partnerships and S corporations conforms to the underlying intent of the capital gain deferral allowed under section 1400Z–2. Thus, the Treasury Department and the IRS decline to adopt this request, and the final regulations retain the special amount includible rule for partnerships and S corporations found in proposed § 1.1400Z2(b)–1(e)(4). Further, although the final regulations do not limit the combining (commonly referred to as ''twinning'') of other tax incentives with the benefits provided by section 1400Z–2, the creation of special rules in this regard exceeds the scope of section 1400Z–2 and the section 1400Z–2 regulations.

3. Grantor Trusts

Proposed § 1.1400Z2(b)–1(c)(5)(i) provided that a taxpayer's transfer of its qualifying investment in a QOF to a grantor trust of which the taxpayer is the deemed owner was not an inclusion event for purposes of section 1400Z–2(b)(1) and proposed § 1.1400Z2(b)–1(c). One commenter asked whether a gift to a ''defective grantor trust'' would be an

inclusion event. The Treasury Department and the IRS note that a defective grantor trust is a grantor trust for Federal income tax purposes, so its funding does not change the conclusion that the transfer is not an inclusion event under section 1400Z–2. In each situation, the deemed owner of the grantor trust's property for Federal income tax purposes (that is, the taxpayer) would be treated as maintaining a direct qualifying investment in the QOF for Federal income tax purposes. See part II.A.5 of this Summary of Comments and Explanation of Revisions (describing rationale for not treating such transfers as inclusion events).

Another commenter stated that proposed § 1.1400Z2(b)–1(c)(5)(ii), which addressed inclusion events related to grantor trusts, was too broad because the proposed rule applied to ''a change in the status of a grantor trust.'' The commenter noted that this language could be read to apply to a taxpayer that owned a QOF investment and was the deemed owner of a grantor trust, regardless of whether the grantor trust itself held a QOF investment. The Treasury Department and the IRS agree with this comment. Accordingly, the final regulations clarify that the provision applies to a change in the status of a grantor trust owning a qualifying investment in a QOF.

A commenter also requested clarification that non-gift transactions between a grantor trust and its deemed owner that are not recognition events for Federal income tax purposes are not inclusion events, and that such transactions do not start a new holding period for purposes of section 1400Z. In such transactions, the deemed owner of the trust continues, for Federal income tax purposes, to be the taxpayer liable for the Federal income tax on the qualifying investment. Thus, the Treasury Department and the IRS have determined that, like transfers by the deemed owner to the grantor trust, these transactions (including transfers from the grantor trust to its deemed owner) are not inclusion events.

F. Transfers of Property by Gift or by Reason of Death, or Incident to Divorce

1. Gifts

The May 2019 proposed regulations provided that a transfer by gift of a qualifying investment in a QOF is an inclusion event for purposes of section 1400Z–2(b)(1) and proposed § 1.1400Z2(b)–1(c). One commenter asserted that a donor's gift of a qualifying investment in a QOF should not be considered a sale or exchange for purposes of section 1400Z–2, provided that the gift otherwise is not treated as a taxable disposition for Federal income tax purposes.

As noted in the preamble to the May 2019 proposed regulations, section 1400Z–2(b)(1) does not directly address non-sale or exchange dispositions, such as gifts and bequests. However, the Conference Report provides that, under section 1400Z–2(b)(1), the ''deferred gain is recognized on the earlier of the date on which the [qualifying] investment is disposed of or December 31, 2026.'' See Conference Report at 539 (indicating that continued gain recognition deferral requires the taxpayer to maintain directly the taxpayer's qualifying investment).

Section 1400Z–2 requires the deferred Federal income tax on capital gains to be paid by the taxpayer who incurred that gain and reinvested an amount up to the amount of the net proceeds from the sale into the qualifying investment in the QOF. The only exception is the recognition under section 691 of a decedent's deferred gain that is not properly includible in the decedent's gross income. The Treasury Department and the IRS have concluded that (i) no authority exists to impose the donor's deferred capital gains tax liability on the donee of the qualifying investment, and therefore (ii) the Federal income tax on the deferred gain must be collected from the donor at the time of the gift of the qualifying investment. Accordingly, the final regulations continue to provide that a gift of the qualifying investment in a QOF is an inclusion event. In addition, consistent with the discussion in part VII.E. of the Explanation of Provisions to the May 2019 proposed regulations, the final regulations provide that the interest received by the donee is no longer a qualifying investment in a QOF as a result of the inclusion event, and thus the donee is not eligible to make an election under section 1400Z–2(c) to adjust the basis of the interest in the QOF to fair market value.

2. Death

The May 2019 proposed regulations generally provided that a transfer of a qualifying investment by reason of the taxpayer's death is not an inclusion event. See proposed § 1.1400Z2(b)–1(c)(4)(ii) (enumerating the sole exceptions to that general rule). One commenter noted that the recipient of a deceased owner's qualifying investment may not have the liquidity to pay the deferred tax on the gain the decedent invested in the QOF upon an inclusion event as of December 31, 2026. The commenter requested that the final regulations permit an election to treat death as an inclusion event, thereby making the decedent's estate liable for the payment of the deferred tax, or grant the recipient a further deferral until the recipient's disposition of the qualifying investment.

The Treasury Department and the IRS note that, if a decedent who dies after 2026 had not disposed of the qualifying investment prior to December 31, 2026, it is possible that even the decedent could have faced such a liquidity problem. In light of the statute's clear direction that the deferral be terminated no later than December 31, 2026, the final regulations provide no election to a decedent's estate to treat death as an inclusion event or provide further deferral to a person inheriting the qualifying investment as a result of the deceased owner's death.

One commenter also requested clarification regarding the application of section 691 to the recipient of the qualifying investment by reason of the death of the owner. In response, the final regulations provide that the tax on the decedent's deferred gain is the liability of the person in receipt of that interest from the decedent at the time of an inclusion event.

3. Transactions Between Spouses or Incident to Divorce

A commenter requested that transfers between spouses or incident to divorce, as described in section 1041, be excepted from the definition of an inclusion event. Although those transactions are nonrecognition events for Federal income tax purposes, a transfer of the qualifying investment in such a transaction constitutes a disposition of that interest for purposes of section 1400Z–2(a)(1)(B) and (b). Therefore, the final regulations in § 1.1400Z2(b)–1(c)(3)(ii) clarify that a transfer described in section 1041 is an inclusion event. Accordingly, the transferor's deferred gain is recognized, and the transferee's interest in the QOF no longer is a qualifying investment.

G. Basis Adjustments

1. Adjustments to Basis of Qualifying QOF Stock

Under section 1400Z–2(b)(2)(B)(ii) and proposed § 1.1400Z2(b)–1(g), a taxpayer's basis in its qualifying investment is increased by the amount of gain recognized upon an inclusion event or on December 31, 2026. Proposed § 1.1400Z2(b)–1(g) also provided additional rules regarding the timing and amount of basis adjustments under section 1400Z–2(b)(2)(B)(ii).

Commenters requested clarification as to how the section 1400Z–2(b)(2)(B)(ii) basis adjustments should be made if a taxpayer disposes of less than all of its qualifying QOF stock or if less than all of its qualifying QOF stock is redeemed by the QOF corporation. If an investor has a qualifying investment with $0 basis and a corresponding $100 of deferred gain, and if the investor were to sell its entire qualifying investment for $100, the investor would recognize $100 of deferred gain, increase its basis in the qualifying investment by $100, and then recognize $0 of gain under section 1001 on the sale of the qualifying investment. If the investor were to sell half of its investment for $50 instead, the investor would recognize $50 of deferred gain under proposed § 1.1400Z2(b)–1(e)(1) and then increase its basis in its qualifying investment by $50. However, it is unclear under the May 2019 proposed regulations whether the $50 basis increase should be applied to the shares that were sold, to the shares that were retained, or to both the sold and the retained shares proportionally.

A commenter recommended that the section 1400Z–2(b)(2)(B)(ii) basis increase be made only to those specific shares that trigger the inclusion event. In the foregoing example, if the $50 basis adjustment were made solely to the sold shares, the investor would recognize $50 of the deferred gain on the disposition of such shares and $0 of gain under section 1001, and the investor would continue to have $50 of deferred gain and $0 of basis in the retained shares. In contrast, if all or a proportionate amount of the section 1400Z–2(b)(2)(B)(ii) basis increase were made to the retained shares, the investor would recognize $50 of deferred gain plus an additional $50 or $25 of gain, respectively, under section 1001. Thus, the investor would recognize more gain than the amount realized in the transaction. Moreover, the retained portion of the investment still would be associated with $50 of deferred gain. Although the taxpayer would have a basis of either $50 or $25 in its retained stock, the taxpayer could end up recognizing gain in excess of the amount of deferred gain if the qualifying investment appreciates sufficiently—an outcome that is contrary to the express language of the statute. See section 1400Z–2(b)(2)(A).

Similarly, commenters recommended that, in the case of a dividend-equivalent redemption of qualifying QOF stock owned by a sole shareholder of a QOF corporation, the section 1400Z–2(b)(2)(B)(ii) basis increase for any section 301(c)(3) gain or 1059(a)(2) gain be made only to the redeemed shares.

The Treasury Department and the IRS agree with the commenters that, if a shareholder of a QOF corporation sells less than all of its qualifying QOF stock, the section 1400Z–2(b)(2)(B)(ii) basis increase should be made only to those specific shares that are sold. The final regulations have been revised accordingly. Otherwise, issues relating relating to the treatment of basis upon a redemption are beyond the scope of the final regulations. The Treasury Department and the IRS continue to study such issues. See REG–143686–07, 84 FR 11686 (March 28, 2019).

2. Basis Adjustments to QOF Partnership Interests and QOF S Corporation Stock

a. General Application of Five-Year and Seven-Year Basis Increases

A commenter noted that the May 2019 proposed regulations, unlike the preamble, did not specifically provide that the five-year and seven-year basis increases to a qualifying investment are basis for all purposes of the Code, and recommended that the final regulations confirm this result. The Treasury Department and the IRS agree with this comment. Accordingly, the final regulations in § 1.1400Z2(b)–1(g)(4)(ii) and (g)(5)(i) specifically provide that five-year and seven-year basis adjustments to a qualifying investment in a partnership or S corporation described in section 1400Z–2(b)(2)(B)(iii) and (iv) and section 1400Z–2(c) are basis for all purposes of the Code, including for purposes of suspended losses under sections 704(d) and 1366(d).

b. Specific Stock Basis Rules for S Corporations

The May 2019 proposed regulations provided that, if an S corporation is an investor in a QOF, the S corporation must adjust the basis of its qualifying investment in the manner set forth for C corporations in proposed § 1.1400Z2(b)–1(g), except as otherwise provided in those proposed regulations. This rule does not affect adjustments to the basis of any other asset of the S corporation. The S corporation shareholder's pro-rata share of any recognized deferred capital gain at the S corporation level will be separately stated under section 1366 and will adjust the shareholders' stock basis under section 1367. In addition, the May 2019 proposed regulations made clear that any adjustment to the basis of an S corporation's qualifying investment under section 1400Z–2(b)(2)(B)(iii) or (iv) or section 1400Z–2(c) will not (1) be separately stated under section 1366, and (2) adjust the shareholders' stock basis under section 1367 until the date on which an inclusion event with respect to the S corporation's qualifying investment occurs. If a basis adjustment under section 1400Z–2(b)(2)(B)(ii) is made as a result of an inclusion event, then the basis adjustment will be made before determining the other tax consequences of the inclusion event.

The Treasury Department and the IRS received favorable comments regarding the foregoing rules, which the Treasury Department and the IRS drafted in accordance with the principle of section 1371(a), as discussed in part III.E.2.a of this Summary of Comments and Explanation of Revisions. As a result, the final regulations adopt these rules without modification.

3. Basis Adjustments by Reason of Death

Several commenters requested clarification regarding the basis of a qualifying investment in the hands of a deceased owner's heir, legatee, or beneficiary. More specifically, commenters requested clarification as to whether the basis adjustment under section 1014 would apply less the amount of unrecognized gain.

If the decedent's investment in a QOF exceeded the gain the decedent elected to defer under section 1400Z–2(a), the investment is a mixed-funds investment that is treated as two separate investments—a qualifying investment subject to section 1400Z–2, and a non-qualifying investment to which section 1400Z–2 is inapplicable. See section 1400Z–2(e)(1). Proposed § 1.1400Z2(a)–1(b)(11)(i)(D) identified the basis of the non-qualifying investment as the taxpayer's total basis in the QOF less the basis of the qualifying investment, in each case determined without the zero-basis rule and without any other basis adjustment provided for in section 1400Z–2(b)(2)(B). In general, this amount equals the taxpayer's total investment in the QOF less the amount of gain invested on which the capital gains tax was deferred.

Because section 1400Z–2 is inapplicable to the non-qualifying investment, the recipient's basis in the non-qualifying investment on the death of the owner is governed by section 1014. As with other income in respect of a decedent, the estate tax value is not reduced by the liability for the deferred income tax.

However, section 1400Z–2(b)(2)(B) applies with regard to the recipient's basis in the qualifying investment. This section provides that the basis of the qualifying investment is zero, with

specified increases for gain recognized at the time of an inclusion event and for qualifying investments held for at least five or seven years. This provision governs without regard to section 1014. Because a taxpayer's basis in its qualifying investment is zero except as otherwise provided in section 1400Z–2(b)(2)(B) and section 1400Z–2(c) (which concerns qualifying investments held for at least 10 years), the Treasury Department and the IRS have determined that section 1014 does not apply to adjust the basis of an inherited qualifying investment to its fair market value as of the deceased owner's death.

H. Earnings and Profits

A commenter requested guidance regarding the E&P consequences of section 1400Z–2 and the section 1400Z–2 regulations. Specifically, the commenter recommended that any increase to E&P as a result of gain deferred under section 1400Z–2 be deferred until such gain is included in income upon either an inclusion event or December 31, 2026.

As noted by the commenter, section 312(f)(1) provides that gain or loss realized on the sale or other disposition of property by a corporation increases or decreases the E&P of such corporation, but only to the extent the realized gain or loss was recognized in computing taxable income under the law applicable to the year in which such sale or disposition was made. Section 1400Z–2 and the section 1400Z–2 regulations enable a taxpayer to defer recognition of an eligible gain in the year the eligible gain was realized. As a result, the amount of gain so deferred does not increase the taxpayer's E&P in the year of realization. See section 312(f)(1). When the gain eventually is included in income upon an inclusion event or on December 31, 2026, the taxpayer's E&P will be increased. See § 1.312–6(b). The Treasury Department and the IRS have determined that section 312 and the regulations in this part under section 312 provide this result in their current form, and therefore no additional rules are necessary. However, the examples set forth in § 1.1400Z2(b)–1(g)(3) have been revised to illustrate the application of the existing E&P rules within the context of section 1400Z–2.

The commenter also recommended that the amount of basis adjustments resulting from the application of section 1400Z–2(b)(2)(B)(iii) and (iv) and section 1400Z–2(c) should be treated as tax-exempt income that causes an increase to E&P under § 1.312–6(b). Section 1.312–6(b) provides that, among other items, income exempted from Federal income tax by statute is entered into the computation of E&P for a particular period. The basis increases under section 1400Z–2(b)(2)(B)(iii) and (iv) exempt from tax under subtitle A those gains that are deferred under section 1400Z–2(a). Similarly, the election under section 1400Z–2(c) potentially exempts from tax under subtitle A those gains that are attributable to the appreciation of QOF investments. Therefore, these basis increases are tax-exempt income for purposes of computing E&P and will increase the E&P of the taxpayer at the time such increases are made. As noted previously, the Treasury Department and the IRS have determined that section 312 and the regulations in this part under section 312 provide this result in their current form and that no additional rules are necessary.

One commenter further asserted that § 1.312–6(b) should not apply to income that is exempt from tax as a result of the basis increases under section 1400Z–2 in order to facilitate passing the benefits of a REIT's qualifying investments to the REIT's shareholders. See part IX.B of this Summary of Comments and Explanation of Revisions. However, the Treasury Department and the IRS have determined that section 312 and § 1.312–6(b) appropriately apply to income that is exempt from tax under subtitle A as a result of these basis increases. Thus, the final regulations have not been revised in response to this comment.

I. Voluntary Inclusion; Applicable Tax Rate

A commenter requested that a QOF investor be permitted to voluntarily recognize the full amount of deferred gain in a taxable year of the investor's choosing prior to the statutorily required year of inclusion under section 1400Z–2(b)(1), and at the Federal income tax rate applicable to the chosen recognition year. The investor would remain fully invested in the QOF, and therefore the basis increases at the five-year mark and seven-year mark, as well as the basis adjustment to fair market value after 10 years, still would be available with regard to the taxpayer's qualifying investment. If the investor meets the requirements for one or more of these basis adjustments, the investor could request a refund of the tax paid on the appropriate amount of the gain in a prior year.

According to the commenter, voluntary gain recognition prior to the statutorily provided year of inclusion would accomplish two purposes. First, the investor could eliminate the risk that the tax rate under subtitle A in the statutorily required year of inclusion would be significantly higher than in the year of voluntary inclusion. Second, the investor would possess the flexibility to pay a tax liability in a year during which the investor is certain to have available the necessary amount of funds.

The Treasury Department and the IRS do not adopt the commenter's recommendation. Section 1400Z–2(b) specifies two events upon which an investor's deferred gain under section 1400Z–2(a)(1) may be included in income. First, deferred gain is included in income upon the occurrence of an inclusion event as explained further in these regulations in § 1.1400Z2(b)–1. Second, deferred gain is included on December 31, 2026. It is not contemplated under the statute or legislative history that a taxpayer may choose to include deferred gain in income at another time and continue to remain invested in a QOF. Accordingly, if a taxpayer wishes to include deferred gain in income, it may cause the occurrence of an inclusion event, with the effect that the investor's ownership of the QOF would terminate for all purposes, including the basis adjustment to fair market value under section 1400Z–2(c).

Another commenter inquired whether the proper Federal income tax rate to apply to the gain recognized pursuant to section 1400Z–2(b)(1) is the Federal income tax rate at the time of the investment and deferral election, or the Federal income tax rate in the taxable year of inclusion. The May 2019 proposed regulations provided that, if section 1400Z–2(a)(1)(B) and (b) require a taxpayer to include in income some or all of a previously deferred gain, the gain so included has the same attributes in the taxable year of inclusion that it would have had if tax had not been deferred. Thus, if the Federal income tax rate were considered an ''attribute'' of the gain, the rate applicable in the year of deferral arguably would apply to gain recognized under section 1400Z–2(b)(1).

Although the May 2019 proposed regulations provided rules for the tax attributes of the amount deferred in the year of inclusion, the May 2019 proposed regulations did not discuss the Federal income tax rates for the year of inclusion. The final regulations clarify that gain recognized pursuant to section 1400Z–2(b)(1) and the section 1400Z–2 regulations is subject to taxation at the applicable Federal income tax rates for the year of inclusion, not of the year of deferral.

J. Availability of Basis Adjustments Under Section 1400Z–2(b)(2)(B)(iii) and (iv)

Section 1400Z–2(b) provides that gain deferred under section 1400Z–2(a)(1)(A) is included in income in the taxable year that includes the earlier of the date on which the QOF investment was sold or exchanged or December 31, 2026. Therefore, in order to be eligible for both the five-year and seven-year basis increases under section 1400Z–2(b)(2)(B)(iii) and (iv), respectively, a taxpayer must invest eligible gain in a qualifying investment no later than December 31, 2019. Eligibility solely for the five-year basis increase requires an investment of eligible gain no later than December 31, 2021. Commenters requested that the statutory inclusion date be postponed to December 31, 2027 or December 31, 2028 to provide investors additional time to consider investing in a QOF, and still receive the benefit of the five- and seven-year basis increases with the benefit of final regulatory guidance.

The Treasury Department and the IRS note that the December 31, 2026, date is mandated by statute, and that there is no indication that Congress intended a later inclusion date. Therefore, the final regulations do not adopt this recommendation.

Another commenter requested confirmation that the inclusion dates in section 1400Z–2(b)(1) do not apply to the five-year and seven-year basis increases under section 1400Z–2(b)(2)(B)(iii) and (iv). As a consequence, a qualifying investment would be eligible for these basis increases regardless of whether the full amount of deferred gain has been recognized, and regardless of when the qualifying investment is made.

As discussed in parts III.A and III.I of this Summary of Comments and Explanation of Revisions, the basis adjustments provided by section 1400Z–2(b)(2)(B)(iii) and (iv) are based on an eligible taxpayer's remaining deferred gain. Moreover, section 1400Z–2(b)(1) clearly requires all deferred gain to be taken into account no later than December 31, 2026. After that date, there will be no remaining deferred gain to be excluded from Federal income tax as a result of the five- or seven-year basis adjustments. As a consequence of the commenter's recommendation, the five- and seven-year basis increases would operate not only to exclude a portion of the deferred gain from Federal income tax, but also to exclude a portion of subsequent appreciation in the value of a qualifying investment from Federal income tax. The Treasury Department and the IRS have determined that the statutory text of section 1400Z–2 does not adequately support the commenter's recommendation, and have clarified the final regulations.

In addition, a commenter requested that the five-year and seven-year basis increases under section 1400Z–2(b)(2)(B) be elective rather than automatic, based on the commenter's position that an investor should be allowed to choose to recognize deferred gain that otherwise would be eliminated due to those basis increases. The statute and legislative history do not indicate that the basis increases under section 1400Z–2(b)(2)(B) operate at the taxpayer's option once the requisite five- and seven-year holding periods have been met. Accordingly, the Treasury Department and the IRS decline to adopt this recommendation.

K. Commencement of the Holding Period for a QOF Investment

In *Examples 1* and *7* in proposed § 1.1400Z2(b)–1(f), the holding period for a qualifying investment in a QOF begins on the date on which the qualifying investment is acquired rather than on the day after the date of its acquisition. One commenter noted that, under Rev. Rul. 70–598, 1970–2 C.B. 168, and general Federal income tax principles, the holding period for a capital asset begins on the day after the acquisition of the asset.

The Treasury Department and the IRS acknowledge the divergence between (i) the day on which the holding period of a qualifying investment begins, and (ii) the day on which the holding period for a capital asset ordinarily would begin. However, the Treasury Department and the IRS have determined that no provision of the Code, nor any Federal income tax principle, requires conformity in this context. As a result, the final regulations do not modify the date on which the holding period for a qualifying investment commences.

L. QOF Exit and Reinvestment

Commenters requested that the final regulations provide a rule that would permit an investor to dispose of its entire interest in a qualifying investment and reinvest the resulting proceeds in another QOF within a short period of time, such as 180 days. Under this rule, the investor would be permitted to tack the holding period of the disposed qualifying investment onto the new qualifying investment for purposes of the five-year, seven-year, and ten-year basis adjustments under section 1400Z–2(a)(2)(B)(iii) and (iv) and section 1400Z–2(c), respectively. This rule would allow an investor to disinvest in a particular QOF as long as the investor remains invested in QOFs, in the aggregate, for the requisite holding periods. One commenter indicated that such a rule would expose investors to a lower risk of loss, which would facilitate investments in professionally managed QOFs from a wider variety of consumer-type investors.

The Treasury Department and the IRS acknowledge the additional investment flexibility that would be provided through adoption of the commenters' recommendation. However, the Treasury Department and the IRS have found no support for this recommendation in the statutory text of section 1400Z–2 or its underlying legislative history. As a result, the final regulations do not incorporate the commenters' recommendation. With regard to the effect of specific transactions on the holding period of a qualifying investment for purposes of the basis adjustments under sections 1400Z–2(a)(2)(B)(iii) and (iv) and 1400Z–2(c), the final regulations provide taxpayers with provisions that address specific inclusion events.

IV. Comments on and Changes to Proposed § 1.1400Z2(c)–1

Section 1400Z–2(c) provides that in the case of any investment held by the taxpayer for at least 10 years and with respect to which the taxpayer makes an election under section 1400Z–2(c), the basis of such property will be equal to the fair market value of such investment on the date that the investment is sold or exchanged. Proposed § 1.1400Z2(c)–1 set forth proposed rules concerning the election under section 1400Z–2(c), including special rules for QOF partnerships and QOF S corporations.

A. Gain Exclusion for Asset Sales by QOFs and Qualified Opportunity Zone Businesses

Proposed § 1.1400Z2(c)–1(b)(2)(ii)(A)(*1*) provided that an investor in a QOF partnership or a QOF S corporation may elect to exclude some, or all, of the capital gain arising from the QOF's sale of qualified opportunity zone business property upon satisfaction of the 10-year holding period in section 1400Z–2(c). A commenter requested guidance regarding a fact pattern in which a QOF that has been held for the requisite 10-year holding period owns multiple qualified opportunity zone businesses. Specifically, the commenter requested confirmation that the gain from each separate disposition of interests in qualified opportunity zone businesses,

after a 10-year holding period of a qualifying investment, qualifies for the basis adjustment and potential gain exclusion under section 1400Z–2(c).

The Treasury Department and the IRS agree that, in the case of a QOF partnership or QOF S corporation, the disposition of QOF assets, including interests in qualified opportunity zone businesses, may qualify for the election under section 1400Z–2(c) if the qualifying investment in the QOF partnership or QOF S corporation meets the 10-year holding period of section 1400Z–2(c), notwithstanding the disposal of interests in qualified opportunity zone businesses at different times. A rule that requires a single disposition of all QOF assets in order to qualify for the benefits under section 1400Z–2(c) would provide an incentive for QOFs and their investors to dispose of a qualified opportunity zone business at a time when, in the absence of section 1400Z–2(c), such a disposition would not be made for reasons unrelated to section 1400Z–2. The final regulations permit interests in qualified opportunity zone businesses to be disposed of at different times. This rule provides taxpayers flexibility consistent with the principle that the economic success of the QOF and the qualified opportunity zone businesses should be the overriding concern when an investor decides whether to dispose of an interest in a qualified opportunity zone business.

One commenter also requested clarification regarding the application of section 1400Z–2(c) to a disposition of assets at less than fair market value, including situations in which the property sold is government-owned or low-income housing. If an investment is held for at least 10 years by a QOF and a taxpayer makes an election under section 1400Z–2(c), then the basis of the investment is equal to fair market value on the date that the investment is sold or exchanged. Proposed § 1.1400Z2(c)–1(b)(2)(ii)(A)(*1*) applied the basis adjustment rule in section 1400Z–2(c) to the disposition of assets by a QOF partnership. Under general Federal income tax principles, the fair market value of property will generally be equal to the actual sales price of such property when a buyer and seller are unrelated. Fair market value under section 1400Z–2(c) is consistent with these principles. Therefore, in a disposition of assets of a QOF to an unrelated party where the taxpayer makes a valid election under section 1400Z–2(c), the relevant fair market value of the assets generally would be the sale price. In a disposition of assets to a related party, the fair market value for purposes of section 1400Z–2(c) would be determined with consideration of the principles of section 482.

B. Application of Section 1400Z–2(c) Election to Certain Gain

Commenters asked whether taxpayers may make an election under section 1400Z–2(c) with respect to section 301(c)(3) gain or section 731 gain on a qualifying investment. The Treasury Department and the IRS have determined that an election under section 1400Z–2(c) should be available for gain resulting from section 301(c)(3), section 731(a), section 1059(a)(2), or section 1368(b)(2) or (c)(3) on a qualifying investment because such gain is treated as gain from the sale or exchange of property for Federal income tax purposes.

C. Inclusion Events

As discussed in part III of this Summary of Comments and Explanation of Revisions, proposed § 1.1400Z2(b)–1(c) provided rules regarding various events that trigger the inclusion of deferred gain under section 1400Z–2(b) and proposed § 1.1400Z2(b)–1(b). Commenters requested guidance as to whether, and to what extent, such inclusion events, as well as events that occur after December 31, 2026, also would cause a qualifying investment to lose eligibility for the election under section 1400Z–2(c) and proposed § 1.1400Z2(c)–1. Specifically, commenters asked whether an inclusion event with respect to gain under section 301(c)(3) would preclude an election under section 1400Z–2(c). See proposed § 1.1400Z2(b)–1(c)(8) and related provisions in proposed § 1.1400Z2(b)–1(c)(9) through (12).

As discussed in part II.A.5 of this Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have determined that an inclusion event generally would cause a qualifying investment to lose eligibility for the election under section 1400Z–2(c) and § 1.1400Z2(c)–1. However, the Treasury Department and the IRS have determined that gain resulting from section 301(c)(3), section 731(a), section 1059(a)(2), or section 1368(b)(2) or (c)(3) should not preclude a taxpayer from making a subsequent election under section 1400Z–2(c) for its qualifying investment. Therefore, a QOF C corporation shareholder or QOF S corporation shareholder is eligible to make an election under section 1400Z–2(c) for a qualifying investment regardless of the extent to which the shareholder has received distributions subject to section 301(c)(3), section 1059(a)(2), or section 1368(b)(2) or (c)(3) with respect to such investment. Similarly, in the case of inclusion events under § 1.1400Z2(b)–1(c)(6)(iii) (partnership distributions) and § 1.1400Z2(b)–1(c)(7)(ii) (distributions by QOF S corporation), the section 1400Z–2(c) election continues to be available to a partner or S corporation shareholder, respectively, as long as the QOF owner continues to hold a qualifying investment in the QOF partnership or QOF S corporation, despite the distribution that caused an inclusion event. The final regulations have been modified accordingly.

Commenters also recommended that an ordering rule similar to proposed § 1.1400Z2(b)–1(g)(1)(ii) be applied to the election under section 1400Z–2(c), so that such a basis increase would occur immediately before determining the results under section 301(c) and section 1059(a). The final regulations adopt such a rule.

D. QOF REIT Capital Gain Dividends Identified With a Date

Proposed § 1.1400Z2(c)–1(e) provided rules for QOF REITs to identify capital gain dividends with a date so that some shareholders could elect to receive the amount of such dividends tax-free under section 1400Z–2(c). One commenter recommended that the term ''QOF RIC'' be added throughout the final regulations alongside all references to QOF REITs to ensure that the regulations apply equally to QOF RICs and QOF REITs.

The Treasury Department and the IRS understand that a Business Development Company (BDC) that is a RIC may qualify as a QOF. The Treasury Department and the IRS have determined that, if a RIC meets the qualifications for, and elects to be, a QOF RIC, that entity and its shareholders should receive the same treatment under these regulations as a QOF REIT and its shareholders. This change is reflected in the final regulations. The proportionality rule for QOF REITs identifying a capital gain dividend with a date in the May 2019 proposed regulations was proposed under the authority granted to the Secretary under section 857(g)(2). The Treasury Department and the IRS apply a similar proportionality requirement to RICs (see Rev. Rul. 89–81, 1989–1 C.B. 226), and thus have maintained the proportionality rule for both QOF RICs and QOF REITs identifying capital gain dividends with a date.

E. Special Rules for QOF Partnerships and QOF S Corporations

1. Section 1400Z–2(c) Election by Transferee Partnership

The transferee partnership of a qualifying investment in a QOF partnership, following a section 721(a) contribution (including those resulting from a merger of QOF partnerships), provided there is no inclusion event, is eligible to make the section 1400Z–2(c) election to exclude from gross income gains and losses from the disposition of property held by a QOF (other than gains and losses from the sale of inventory in the ordinary course of a business), so long as the 10-year holding period requirement is satisfied. See § 1.1400Z2(b)–1(d)(1)(ii) (transferee partnership has a tacked holding period). The final regulations clarify this rule and provide reporting requirements for the transferee partnership in making the section 1400Z–2(c) election.

2. Basis Adjustment Amount on the Sale of a Qualifying Investment

Proposed § 1.1400Z2(c)–1(b)(2)(i) provided that, if a taxpayer sells or exchanges a qualifying investment in a QOF partnership that has been held for at least 10 years, and the taxpayer makes the election described in section 1400Z–2(c), the basis of the partnership interest is adjusted to an amount equal to the fair market value of the interest, including debt. The Treasury Department and the IRS received comments asking for clarification of the phrase ''including debt'' in the proposed rule. Specifically, commenters requested a rule that more clearly states that the basis of the partnership interest is adjusted to an amount equal to the net fair market value of the QOF partnership interest plus the partner's share of debt. One commenter suggested that a ''gross fair market value'' rule would encourage QOF partnerships to borrow money and distribute the proceeds, which could increase debt within QOZs while reducing cash amounts held by QOF partnerships, potentially exacerbating the plight of the economically distressed communities. In addition, several commenters asked for clarification that the fair market value of the QOF partnership interest cannot be less than the partner's allocable share of non-recourse debt, consistent with section 7701(g).

The Treasury Department and the IRS agree with the commenters that clarification is needed. Accordingly, the final regulations clarify that the basis of the partnership interest is adjusted to an amount equal to its net fair market value, plus the partner's share of partnership debt relating to that interest, so that the partner would recognize no gain or loss on a sale or exchange of the qualifying QOF partnership interest after at least 10 years. The final regulations also state that the fair market value cannot be less than the partner's allocable share of non-recourse debt. In addition, the final regulations note that, in the case of a sale or exchange of qualifying S corporation shares, the basis is adjusted to an amount equal to the fair market value of the shares immediately prior to the sale or exchange.

3. Adjustment to Basis of QOF Partnership Assets on Sale of a Qualifying Investment

Proposed § 1.1400Z2(c)–1(b)(2)(i) provided that, if a taxpayer's basis is adjusted under section 1400Z–2(c), the bases of the QOF partnership assets also are adjusted immediately prior to the sale or exchange. The adjustment is calculated in a manner similar to a section 743(b) adjustment as if the transferor partner had purchased its interest in the QOF partnership for an amount of cash equal to the fair market value of the partnership interest immediately prior to the sale or exchange, assuming that a valid section 754 election had been in place. The Treasury Department and the IRS received comments asking for clarification that (i) the assets of lower-tier partnerships also should be adjusted pursuant to this rule, (ii) no actual section 754 election is required, and (iii) generally applicable guidance issued pursuant to sections 743(b) and 754 applies in this context.

The Treasury Department and the IRS agree with the commenters that clarification is needed. Accordingly, the final regulations clarify that the adjustment applies to any partnerships directly or indirectly owned, solely through one or more partnerships (tiered partnerships), by the QOF partnership, whether or not an actual section 754 election is in place for any of the partnerships. Guidance issued pursuant to sections 743(b) and 754 applies as it would outside of the context of section 1400Z–2. Further, because section 1400Z–2(c) is designed to result in no gain or loss to the transferor QOF partner, the final regulations provide that, to the extent the existing rules of sections 743(b) and 755 operate in a manner that results in recognition of gain or loss on the transaction, the basis adjustments are to be made to the extent necessary to eliminate any such gain or loss.

4. Sales or Exchanges of Property by QOF Partnerships and QOF S Corporations

The May 2019 proposed regulations provided that, if a QOF partnership or QOF S corporation disposes of qualified opportunity zone property after a taxpayer is treated as holding its qualifying investment in the QOF partnership or QOF S corporation for 10 years, the taxpayer may make an election to exclude from gross income some or all of the capital gain arising from the disposition. The Treasury Department and the IRS received comments requesting that, in addition to capital gain from the sales of qualified opportunity zone property by a QOF, capital gain from the sales of property by a qualified opportunity zone business that is held in partnership form should be eligible for exclusion as long as the qualifying investment in the QOF has been held for 10 years. The final regulations adopt this recommendation for QOF partnerships and QOF S corporations.

Commenters also requested that all types of gains and losses, including gains and losses from the sales of inventory, section 1231 gains and losses, and depreciation recapture, be eligible for exclusion under this special election for QOF partnerships and QOF S corporations. Other commenters suggested that the exclusion election should apply to all gains and losses of QOF partnerships or QOF S corporations other than gains and losses from the sales of inventory in the ordinary course of business. The final regulations adopt the recommendation to exclude ordinary course inventory sales from the exclusion election.

The final regulations set forth two requirements for the QOF partnership or QOF S corporation and the taxpayer when the taxpayer wishes to make an election to exclude gains and losses upon sales of assets other than inventory sold in the ordinary course of a trade or business by the QOF. First, the taxpayer must make the election for each taxable year in which it wishes to exclude the QOF's gains and losses from all sales and exchanges of assets. This election may be made regardless of whether the taxpayer has made an election for any prior taxable year. The election will apply to all gains and losses, other than gains and losses from sales of inventory in the ordinary course of business, of the QOF partnership or QOF S corporation for that taxable year, including any gains and losses from a lower-tier partnership. The election must be made by the taxpayer on the applicable form filed with its Federal

tax return for the year in which the sale or exchange occurs.

The second requirement is designed to eliminate future section 1400Z–2 benefits attributable to the reinvestment of proceeds from asset sales for which gain and loss is not recognized under section 1400Z–2. Under this provision, and solely for purposes of determining the amount of a QOF owner's qualifying investment and non-qualifying investment, the QOF is treated as distributing to each electing QOF owner its share of net proceeds from the asset sales on the last day of the QOF's tax year. For a QOF S corporation, such deemed distributions and recontributions will have no Federal income tax consequence other than the adjustment of the respective values of qualifying and non-qualifying investments in a QOF S corporation. For example, such deemed distributions will have no impact on an accumulated adjustments account of a QOF S corporation, and will not be treated as a disproportionate distribution of a QOF S corporation.

For a QOF partner that holds a mixed-funds investment, any distribution will be allocated to the separate interests of the QOF partner pursuant to § 1.1400Z2(b)–1(c)(6)(iv)(B). This rule provides that any distribution will be allocated proportionately between the qualifying and non-qualifying investments of the partner. Immediately after the deemed distribution, the distributee QOF owner is treated as recontributing the amount received in exchange for a non-qualifying investment.

In determining the post-contribution qualifying investment and non-qualifying investment of a QOF partnership, the QOF partnership is required to value each interest based on the underlying value of the partnership's assets, determined in accordance with the principles of § 1.704–1(b)(2)(iv) at the end of its taxable year. For this purpose, the amount of the net proceeds from an asset sale is equal to the amount realized from the sale, less any indebtedness included in the amount realized that would constitute a qualified liability under § 1.707–5(a)(6) if property subject to the debt had been contributed to a lower-tier partnership. An actual distribution of sales proceeds within 90 days of that asset sale will reduce the amount of the deemed distribution and deemed recontribution.

In determining the post-contribution qualifying investment and non-qualifying investment of a QOF S corporation, the QOF S corporation is required to value each interest based on the underlying value of the QOF S corporation's assets. For this purpose, the amount of the net proceeds from an asset sale is equal to the amount realized from the sale, less any indebtedness included in the amount realized that would constitute a qualified liability under the principles of § 1.707–5(a)(6). An actual distribution of sales proceeds within 90 days of that asset sale will reduce the amount of the deemed distribution and deemed recontribution.

F. Controlled Foreign Corporations

A commenter requested that a United States shareholder investor in a QOF that is a controlled foreign corporation (CFC) organized in a U.S. territory be permitted to make section 1400Z–2(c) elections with respect to assets sold by the CFC, thereby eliminating any subpart F income or tested income resulting from these transactions. The commenter analogized this treatment to rules in proposed § 1.1400Z2(c)–1(b)(2)(ii) providing that, in certain cases, the owners of a QOF partnership or QOF S corporation can make a section 1400Z–2(c) election with respect to their distributive or pro rata shares of capital gain from the QOF's disposition of assets.

However, the rules for income inclusions with respect to CFCs are not analogous to those for partnerships or S corporations. Unlike partnerships and S corporations, CFCs are not treated as flow-through entities for purposes of the Code. Additionally, in contrast with partnerships and S corporations, only certain U.S. taxpayer owners of CFCs (United States shareholders) are required to have current income inclusions with respect to CFCs, and these United States shareholders are required to currently include in gross income only certain income earned by a CFC (for example, subpart F income). These rules effectuate the policies underlying the subpart F and global intangible low-taxed income under section 951A(a) (GILTI) regimes—to prevent United States shareholders from deferring or eliminating U.S. tax on certain income by earning such income through CFCs. Such policies generally are not applicable to partnerships and S corporations, which generally are treated as flow-through entities for purposes of the Code. See H.R. Rep. No. 1447 at 57–58 (1962); S. Rep. No. 1881 at 78–80 (1962); S. Comm. on the Budget, Reconciliation Recommendations Pursuant to H. Con. Res. 71, S. Print No. 115–20, at 370 (2017).

As opaque entities, CFCs are more analogous to domestic C corporations than to partnerships or S corporations because the income of CFCs and domestic C corporations may be subject to U.S. taxation when earned (at the United States shareholder-level in the case of a CFC) and also when distributed as a dividend to U.S. taxpayer shareholders. This result with respect to domestic C corporations is not changed by section 1400Z–2, which does not permit a shareholder of a domestic QOF C corporation to make a section 1400Z–2(c) election with respect to either the QOF C corporation's capital gains from sales of assets or dividends distributed to such shareholder, unless section 1059(a)(2) applies to such dividends. Allowing this benefit for United States shareholders of QOFs that are CFCs organized in a U.S. territory would thus provide an unwarranted advantage to shareholders of QOF C corporations organized under the laws of U.S. territories compared to shareholders of QOF C corporations organized under the laws of the 50 states or the District of Columbia. The Treasury Department and the IRS have determined that there is no statutory or policy basis for such disparate treatment. Accordingly, the comment is not adopted. A comment with respect to QOFs that are passive foreign investment companies (within the meaning of section 1297(a)) is rejected for similar reasons.

G. Permitting Elections Through December 31, 2047

The October 2018 proposed regulations preserved the ability of taxpayers to make an election under section 1400Z–2(c) until December 31, 2047. The Treasury Department and the IRS requested comments on whether some other period would better align with taxpayers' economic interests and the purposes of the statute, and whether alternative approaches would be appropriate. For example, the preamble to the October 2018 proposed regulations noted the possibility of allowing for an automatic basis step-up immediately before the end of 2047. The Treasury Department and the IRS will continue to consider the appropriateness of such an approach, including ways to address how best to value investments in QOFs absent a sale or exchange between unrelated persons by December 31, 2047.

V. Comments on and Changes To Proposed § 1.1400Z2(d)–1

Section 1400Z–2(d) sets forth requirements that an entity classified for Federal income tax purposes as a partnership or corporation must satisfy to qualify as a QOF or as a qualified

opportunity zone business that is owned, in whole or in part, by one or more QOFs.

Section 1400Z–2(d)(1) defines a QOF as a partnership or corporation that (i) is organized for the purpose of investing in ''qualified opportunity zone property'' (other than another qualified opportunity fund), and (ii) must hold at least 90 percent of its assets in qualified opportunity zone property, determined by the average of the percentage of qualified opportunity zone property held in the entity as measured on two semiannual testing dates (90-percent investment standard). Section 1400Z–2(d)(2) defines the term ''qualified opportunity zone property'' to mean property directly held by a QOF that consists of (i) stock in a corporation that is qualified opportunity zone stock, (ii) partnership interests that are qualified opportunity zone partnership interests, or (iii) tangible property that is qualified opportunity zone business property.

A QOF's directly held interest in a partnership or corporation will be treated as a qualified opportunity zone partnership interest or qualified opportunity zone stock, and thus qualified opportunity zone property, for purposes of the 90-percent investment standard if the interest or stock satisfies the requirements set forth in section 1400Z–2(d)(2)(B) or (C), as applicable. First, the QOF must have acquired the interest or stock from the partnership or corporation, respectively, solely in exchange for cash after December 31, 2017. Second, at the time of issuance of the interest or stock, as well as during substantially all of the QOF's holding period for such interest or stock, the entity must qualify as a ''qualified opportunity zone business'' (or, if newly formed, must have been organized for such purpose).

Section 1400Z–2(d)(2)(D) provides that tangible property will be treated as qualified opportunity zone business property if the tangible property is used in a trade or business of the QOF and satisfies three general requirements. First, the QOF must have acquired the tangible property after December 31, 2017 (post–2017 acquired tangible property) from a person that is not related (as defined in section 179(d)(2), and modified by section 1400Z–2(e)(2)) and not a member of the same controlled group (as defined in section 179(d)(2)(B) and (d)(7)) in a transaction resulting in the QOF holding the tangible property with other than a transferred basis (within the meaning of section 7701(a)(43)) or with a section 1014 basis (post-2017 acquisition requirement). Second, the original use of the post-2017 acquired tangible property in the QOZ must begin with the QOF (original use requirement), or the QOF must substantially improve the post–2017 acquired tangible property (substantial improvement requirement). Third, during substantially all of the QOF's holding period for such post–2017 acquired tangible property, substantially all of the use of post–2017 acquired tangible property has been in a QOZ. Under section 1400Z–2(d)(2)(D)(ii), the substantial improvement requirement is met only if, during any 30-month period beginning after the date of acquisition of the post–2017 acquired tangible property, there are ''additions to basis with respect to such property'' held by the QOF that, in the aggregate, exceed the adjusted basis of the post–2017 acquired tangible property held by the QOF as of the beginning of that 30-month period.

Section 1400Z–2(d)(3)(A) defines the term ''qualified opportunity zone business'' as a trade or business (other than an enumerated ''sin business'' under section 144(c)(6)(B)) that meets each of the following two requirements. First, substantially all of the tangible property owned or leased in connection with the trade or business must be qualified opportunity zone business property. See section 1400Z–2(d)(3)(A)(i). Second, the trade or business must satisfy the following requirements provided in paragraphs (2), (4), and (8) of section 1397C(b): (i) At least 50 percent of the total gross income of such entity must be derived from the active conduct of the trade or business in the QOZ (50-percent gross income requirement); (ii) a substantial portion of the intangible property of such entity must be used in the active conduct of the trade or business in the QOZ; and (iii) less than five percent of the average of the aggregate unadjusted bases of the property of such entity must be attributable to nonqualified financial property (NQFP and five-percent NQFP limitation, respectively). See section 1400Z–2(d)(3)(A)(ii).

Proposed § 1.1400Z2(d)–1, introduced in the October 2018 proposed regulations and expanded in the May 2019 proposed regulations, provided guidance for applying each of the provisions of section 1400Z–2(d). In general, the proposed regulations addressed (i) QOF self-certification procedures, (ii) valuation methods for determining satisfaction of the 90-percent investment standard, (iii) how various types of property can qualify as qualified opportunity zone property, including qualified opportunity zone business property, and (iv) how trades or businesses can satisfy the requirements for qualifying as qualified opportunity zone businesses. The Treasury Department and the IRS have received numerous comments regarding the proposed rules set forth in proposed § 1.1400Z2(d)–1. The remainder of this part V discusses those comments in the order of the rules set forth in proposed § 1.1400Z2(d)–1 and describes the changes in the final regulations in response to those comments.

A. Certification of an Entity as a QOF

1. Consideration of Revisions to QOF Self-Certification Requirements

Section 1400Z–2(e)(4)(A) directs the Treasury Department and the IRS to prescribe regulations for the certification of QOFs for purposes of section 1400Z–2. In order to facilitate the certification process and minimize the information collection burden placed on taxpayers, proposed § 1.1400Z2(d)–1(a)(1) generally permits any taxpayer that is a corporation or partnership for Federal income tax purposes to self-certify as a QOF, provided that the entity is eligible to self-certify. Proposed § 1.1400Z2(d)–1(a)(1)(i) permits the Commissioner of Internal Revenue (Commissioner) to determine the time, form, and manner of the self-certification in IRS forms and instructions or guidance published in the Internal Revenue Bulletin.

In this regard, the Commissioner has determined that self-certification must be reported annually on a timely filed Form 8996. Form 8996 requires the taxpayer to certify that, for the first period during which an entity will certify as a QOF, the QOF must include in its organizing documents (1) a statement of the purpose of investing in qualified opportunity zone property (as required by section 1400Z–2(d)(1)) by the end of the first QOF year, and (2) a description of the qualified opportunity zone business that a QOF expects to engage in, either directly or indirectly through a lower-tier operating entity.

The Treasury Department and the IRS received several comments regarding the certification process outlined in the proposed regulations. Several commenters requested that the requirements set forth in Form 8996 be incorporated into the final regulations. Other commenters recommended that the final regulations require individuals who manage the QOFs (fund managers) to certify that they have not been indicted or convicted of fraud, embezzlement, or theft, similar to requirements under section 45D of the Code for the New Markets Tax Credit program. One commenter recommended the use of licensing procedures for fund managers similar to those used in the

Small Business Investment Company (SBIC) licensure program administered by the Small Business Administration. Other commenters recommended that QOF certification require the QOF to receive a letter of support from the local government of the QOZ in which the QOF will operate.

Several commenters also recommended that the final regulations require a taxpayer to identify, at the time of QOF certification, the QOF's intended community development outcomes and objectives. For example, one commenter requested that, as part of the QOF certification process, a QOF must certify that the QOF will create quality jobs for low-income individuals, develop affordable housing, and achieve other beneficial community outcomes. To facilitate the ability of a QOF to make such certification, one commenter suggested that the final regulations provide a safe harbor for certification for a QOF that undergoes an independent, third-party verification (similar to the SBIC's annual third-party impact assessment) to establish that the QOF meets the needs of the community, fund managers, and investors.

The Treasury Department and the IRS appreciate the commenters' recommendations regarding QOF certification. In developing the proposed regulations, as well as Form 8996, the Treasury Department and the IRS intended to strike a balance between providing taxpayers with a flexible and efficient process for organizing QOFs, while ensuring that investments in such vehicles will be properly directed toward the economic development of low-income communities. The suggested recommendations, while potentially helpful for directing such investment and limiting abuse, likely would present numerous obstacles for potential QOF investors and ultimately reduce, rather than increase, the total amount of investment in low-income communities. As a result, the final regulations do not adopt the commenters' recommendations. However, the Treasury Department and the IRS will consider these comments in the event that additional guidance on QOF certification is warranted.

2. Consideration of Indian Tribal Governments and Corporations as Eligible Entities To Certify as QOFs

Several commenters requested that Indian tribal governments and corporations organized under Indian tribal laws should be included in the definition of entities eligible to be a QOF. Proposed § 1.1400Z2(d)–1(e)(1) provided that, if an entity is not organized in one of the 50 states, the District of Columbia, or the U.S. territories, it is ineligible to be a QOF. Similarly, proposed § 1.1400Z2(d)–1(e)(2) provided that, if an entity is not organized in one of the 50 states, the District of Columbia, or the U.S. territories, an equity interest in the entity is neither qualified opportunity zone stock nor a qualified opportunity zone partnership interest. The Treasury Department and the IRS have determined that, for purposes of both proposed § 1.1400Z2(d)–1(e)(1) and (2), an entity ''organized in'' one of the 50 states includes an entity organized under the law of a Federally recognized Indian tribe if the entity's domicile is located in one of the 50 states or the District of Columbia. Such entity satisfies the requirement in section 1400Z–2(d)(2)(B)(i) and (C) that qualified opportunity zone stock be stock in a domestic corporation, and a qualified opportunity zone partnership interest be an interest in a domestic partnership. See section 7701(a)(4) (defining the term ''domestic'').

The Treasury Department and the IRS appreciate the sovereignty of Indian tribal governments. However, an entity eligible to be a QOF must be subject to Federal income tax, including the penalty imposed by section 1400Z–2(f)(1) where a QOF fails to meet the 90-percent investment standard, regardless of the laws under which the entity is established or organized. No individual who participated in the Consultation disagreed with the position that an entity organized under the law of an Indian tribal government is eligible to be a QOF, if the entity's domicile is located in one of the 50 states or the District of Columbia, but that such entity would be subject to Federal income tax. Accordingly, the Treasury Department and IRS affirm these positions and incorporate a reference to entities organized under the law of an Indian tribal government in the definition of the term ''eligible entity.''

3. QOF Decertification Rules and Federal Income Tax Consequences

In the October 2018 proposed regulations, the Treasury Department and the IRS announced an intention to publish additional guidance regarding QOF decertification. See 83 FR 54283 (September 29, 2018). Comments were received on this topic, including comments requesting a mechanism to permit a QOF to self-decertify, as well as comments requesting guidance on the ability of the IRS to decertify a QOF. The Treasury Department and the IRS have included in the final regulations a provision to allow a QOF to self-decertify. This rule specifies that self-decertification becomes effective at the beginning of the month following the month specified by the taxpayer. The month specified by the taxpayer must not be earlier than the month in which the taxpayer files its self-decertification. For example, if a QOF wishes to decertify on May, the earliest date that the QOF could be decertified would be June 1st, provided that all applicable procedures were followed.

The Treasury Department and the IRS are developing additional instructions regarding QOF self-decertification including instructions regarding the time, form, and manner of QOF self-decertification. Additionally, the Treasury Department and the IRS continue to consider the circumstances under which involuntary decertification of a QOF would be warranted, and intend to propose guidance regarding those circumstances. As noted in part III.A. of this Summary of Comments and Explanation of Revisions, the final regulations include a rule providing that the decertification of a QOF, whether voluntary or involuntary, is an inclusion event for eligible taxpayers that hold a qualifying investment in that QOF. See § 1.1400Z2(b)–1(c)(15).

4. Entities That Are Not QOFs During the First Month of Their Taxable Year

Under proposed § 1.1400Z2(d)–1(a)(2), an entity may become a QOF during a month that is not the first month of the QOF's taxable year. Several commenters suggested that the Treasury Department and the IRS provide additional detail and clarification regarding this proposed rule. One commenter suggested that the final regulations permit QOFs to select as the QOF's first six-month period testing date either (i) the corresponding day of the month that is six months after the date of certification, or (ii) the last day of a month that is not more than six months after that certification date. Another commenter requested confirmation that the term ''month'' means a period of time between the same dates in successive calendar months in order to provide a consistent measuring period. A commenter also asserted that the first six-month period testing date should fall on the last day of that first six-month period, even if that period ends later than the end of the taxable year. The Treasury Department and the IRS will consider adding clarifying language to the Instructions to the Form 8996, ''Qualified Opportunity Fund,'' to address these comments.

5. Qualification of Existing Entities as QOFs or Qualified Opportunity Zone Businesses

Section 1400Z–2(d)(1) provides, in relevant part, that a QOF is ''any investment vehicle which is organized as a corporation or a partnership for the purpose of investing in qualified opportunity zone property.'' Accordingly, the statute does not indicate whether such partnership or corporation must be newly formed or could be a preexisting entity. Likewise, neither the definition of the term ''qualified opportunity zone partnership interest'' nor the definition of the term ''qualified opportunity zone stock'' explicitly states that the partnership or corporation may be a preexisting entity. See section 1400Z–2(d)(2)(B)(i), (C). Several commenters have requested confirmation as to whether existing entities could qualify as QOFs or qualified opportunity zone businesses. In addition, one commenter inquired as to whether preexisting entities could use an adjusted tax basis for valuing assets purchased before 2018 to improve the ability for such entities to qualify as QOFs.

The Treasury Department and the IRS have addressed these comments in the final regulations. The final regulations confirm that preexisting entities are not barred from qualifying as QOFs or qualified opportunity zone businesses. Like newly formed partnerships and corporations, however, the final regulations require preexisting entities to satisfy all requirements applicable to QOFs under section 1400Z–2 and the section 1400Z–2 regulations.

To value assets acquired prior to 2018, the final regulations provide that preexisting entities must use either (i) the applicable financial statement valuation method set forth in § 1.1400Z2(d)–1(b)(3) of the final regulations, if the QOF has an applicable financial statement within the meaning of § 1.475(a)–4(h) (AFS), or (ii) the alternative valuation method set forth in § 1.1400Z2(d)–1(b)(4) of the final regulations. Under the applicable financial statement valuation method, the value of each asset that is owned or leased by a QOF is the value of that asset as reported on the QOF's AFS for the relevant reporting period (rather than the adjusted tax basis of the asset). Under the alternative valuation method for purchased assets, a QOF must use the QOF's unadjusted cost basis of the asset under section 1012, section 1013 (with regards to inventory), or its fair market value. See part V.B of this Summary of Comments and Explanation of Revisions (providing additional discussion regarding the valuation of assets for purposes of the 90-percent investment standard).

6. Clarification Regarding Entities That May Appraise Property

A commenter requested clarification regarding which entities may appraise property required to be valued for purposes of section 1400Z–2(d), including for purposes of determining compliance with the 90-percent investment standard. The Treasury Department and the IRS decline to provide additional guidance on appraisals in the final regulations. However, the Treasury Department and the IRS note that entities that may appraise property for valuation purposes under section 1400Z–2 and the section 1400Z–2 regulations are the same entities that may appraise property for AFS purposes.

B. Valuation of Assets for Purposes of the 90-Percent Investment Standard

1. Comments Regarding Determination Dates, Includable Assets, and Safe Harbors

Section 1400Z–2(d)(1) provides that a QOF must maintain an average of 90 percent of its assets in qualified opportunity zone property, measured on both the last day of the first six-month period and on the last day of the taxable year (that is, the 90-percent investment standard). Section 1400Z–2(f)(1) provides that, if a QOF fails to maintain the 90-percent investment standard, the QOF must pay a penalty for each month that the QOF fails to meet that standard. Proposed § 1.1400Z2(d)–1(b) provided that, to meet the requirements of the 90-percent investment standard, a QOF may value its assets on a semiannual basis using (i) the AFS valuation method, if the QOF has an AFS, or (ii) the alternative valuation method.

The Treasury Department and the IRS received several comments regarding the application of the 90-percent investment standard. For example, a commenter requested confirmation that the 90-percent investment standard is determined for each year of the QOF's existence. Another commenter suggested that the final regulations make explicit that the 90-percent investment standard will be considered to have been fully satisfied for any year if the QOF meets the 90-percent investment standard on at least two semiannual testing dates. The Treasury Department and the IRS agree with the commenters that the proposed rules should be clarified. As a result, the final regulations make clear that a QOF may determine whether the 90-percent investment standard is satisfied by valuing its assets on the semiannual testing dates as provided by section 1400Z–2(d)(1).

Several commenters also suggested that the final regulations provide greater clarity regarding the assets of a QOF taken into account for determining whether the 90-percent investment standard is satisfied. Commenters inquired as to whether selling commissions, offering expenses, deferred gain, investments in intangible property, and financial accounting depreciation are included or excluded in that valuation calculation. The Treasury Department and the IRS confirm that all of a QOF's assets cognizable for Federal income tax purposes are required to be valued on each semiannual testing date in determining whether the 90-percent investment standard is satisfied. However, mere expenses arising from organizing a QOF or day-to-day operations with regard thereto (such as selling commissions, organization expenses, offering expenses, and similar expenses) do not result in any QOF asset cognizable for Federal income tax purposes and therefore are not taken into account to any extent in determining satisfaction of the 90-percent investment standard.

Two commenters suggested that the Treasury Department and the IRS should include in the final regulations a grace period for the QOF's first year to meet the 90-percent investment standard. The Treasury Department and the IRS have determined that the statutory text of section 1400Z–2 does not permit adoption of the commenters' suggestion, but rather requires that the 90-percent investment standard be met for each taxable year of the QOF's existence. As a result, the final regulations do not incorporate this suggestion.

In addition, a commenter recommended that, if a qualified opportunity zone business qualifies on each relevant testing date, then that entity should be treated also as qualifying during the periods between each relevant testing date. The Treasury Department and the IRS agree that if an entity satisfies all of the requirements of a qualified opportunity zone business determined as of the end of the entity's taxable year, the entity qualifies as a qualified opportunity zone business for the entire taxable year of the entity. However, a QOF and an entity whose equity the QOF owns may have different taxable years, making it difficult to determine whether the entity qualifies as a qualified opportunity zone business of the QOF on a semiannual basis based

on the QOF's taxable year pursuant to section 1400Z–2(d)(1). Accordingly, the Treasury Department and the IRS have provided a safe harbor rule for determining on the two semiannual testing dates of a QOF whether an entity is a qualified opportunity zone business for at least 90 percent of the cumulative holding period beginning on the first date the QOF's self-certification is effective and the end of the entity's most recent taxable year ending on or before a semiannual testing date of the QOF for purposes of the 90-percent investment standard.

Finally, the Treasury Department and the IRS note that, if a QOF operates a business through an entity that is transparent for Federal income tax purposes, the transparent entity is not treated as a qualified opportunity zone business in which the QOF has invested. Such transparent entities include a qualified subchapter S subsidiary (as defined in section 1361(b)(3)(B)), a grantor trust, or an entity disregarded as separate from the QOF under § 301.7701–3. For Federal income tax purposes, the assets of the transparent entity are treated as assets of the QOF, and therefore are taken into account for determining whether the QOF satisfies the 90-percent investment standard. The 70-percent tangible property standard for qualified opportunity zone businesses set forth in § 1.1400Z2(d)–1(d)(1)(i) (70-percent tangible property standard) is not relevant with respect to the assets directly held by a transparent entity owned by a QOF.

2. Ability of a QOF With an AFS To Use the Alternative Valuation Method

Proposed § 1.1400Z2(d)–1(b)(2) provided that a QOF may utilize the AFS valuation method to value each asset owned or leased by the QOF for purposes of determining compliance with the 90-percent investment standard. Under the AFS valuation method, the value of each asset owned or leased by the QOF equals the value of that asset as reported on the QOF's AFS for the relevant reporting period. Proposed § 1.1400Z2(d)–1(b)(2)(ii) clarified that a QOF may select the AFS valuation to value an asset leased by the QOF only if the AFS of the QOF (1) is prepared according to U.S. generally accepted accounting principles (GAAP) and (2) requires an assignment of value to the lease of the asset.

A commenter recommended that the final regulations allow a QOF to elect to use unadjusted cost basis to value tangible assets (that is, the alternative valuation method), regardless of whether the QOF has an AFS. The Treasury Department and the IRS note that the proposed regulations would accommodate the commenter's request without change. Specifically, under the proposed regulations and these final regulations, a QOF with an AFS may use the alternative valuation method.

3. Alternative Valuation Method

a. Valuation of Intangible Assets With a Tax Basis Not Based on Cost

Under the alternative valuation method set forth in proposed § 1.1400Z2(d)–1(b)(3), the value of each asset that is owned by a QOF is the QOF's unadjusted cost basis of the asset under section 1012 or section 1013 (with regard to inventory). One commenter considered the application of the alternative valuation method to partnership interests with a tax basis not based on cost. The commenter agreed that the alternative valuation method generally provided an appropriate valuation methodology with regard to property that has been acquired by purchase, but questioned whether that method provided an appropriate means to value a partnership interest.

The Treasury Department and the IRS agree that applying the alternative valuation method to partnership interests, as well as other intangible assets with a tax basis not based on cost, would be inconsistent with the intent and purpose of the statute. As a result, the final regulations reflect the commenter's observation and provide that the alternative valuation method may be used to value only assets owned by a QOF that are acquired by purchase or constructed for fair market value. In such instances, the QOF's unadjusted cost basis of the asset is determined under section 1012 or section 1013 (with regard to inventory). The final regulations also provide that the value of each asset owned by a QOF that is not purchased or constructed for fair market value equals the asset's fair market value. A QOF determines that fair market value on the last day of the first six-month period of the taxable year and on the last day of the taxable year.

b. Valuation of Assets Leased by a QOF

Proposed § 1.1400Z2(d)–1(b)(3)(iii)(A) provided that the value of each asset that is leased by a QOF is equal to the present value of the leased asset. The ''present value'' of such leased asset is (i) equal to the sum of the present values of each payment under the lease for the asset, and (ii) calculated at the time at which the QOF enters into the lease for the asset. See proposed § 1.1400Z2(d)–1(b)(3)(iii)(C)(*1*), (*2*). Once calculated, that present value is used as the value for the asset by the QOF for all testing dates for purposes of the 90-percent investment standard. See proposed § 1.1400Z2(d)–1(b)(3)(iii)(C)(*3*). To determine the present value of the lease payments, the proposed regulations provided that the discount rate is the applicable Federal rate (AFR) under section 1274(d)(1). See proposed § 1.1400Z2(d)–1(b)(3)(iii)(B) (present value determined under section 1274(d)(1) by substituting the term ''lease'' for ''debt instrument''). The final regulations clarify the rules to be used to determine the AFR for a particular lease, and provide that the short-term AFR must be used. The Treasury Department and the IRS have determined that use of the short-term AFR will provide a simple and objective rule for taxpayers and practitioners.

Prior to the publication of the May 2019 proposed regulations, the Treasury Department and the IRS received comments requesting that the final regulations provide flexibility regarding the valuation of leases. For example, one commenter requested that the final regulations permit QOFs to use a type of basis other than the basis used for GAAP (for example, cost basis under section 1012). This comment was particularly relevant to Indian tribal governments, which typically rely upon leases. Another commenter had suggested that QOFs and qualified opportunity zone businesses should be able to elect to use Federal income tax basis to determine the value of assets for these purposes. The commenter reasoned that the value of the operating lease, as a non-qualifying asset, would be $0 and would not affect the 90-percent investment standard.

The Treasury Department and the IRS have determined that the alternative valuation method for leased assets, as set forth in proposed § 1.1400Z2(d)–1(b)(3), addresses the concerns raised by these commenters. In addition, the Treasury Department and the IRS note that no participant of the Consultation requested additional guidance regarding these issues. Therefore, proposed § 1.1400Z2(d)–1(b)(3) has not been modified as a result of those comments.

With regard to the 90-percent investment standard, a commenter suggested that the Treasury Department and the IRS consider a valuation method for leases that are negotiated at arms-length under section 482. This valuation method would value the lease (i) as having a value of $0 regardless of whether the QOF has an AFS, or (ii) at the unadjusted cost basis of the lease, similar to purchased property. Another commenter requested that the value of leased property be excluded from the

numerator and denominator of the fraction-based test underlying the 90-percent investment standard, while the value of substantial improvements to leased property should be included. Another commenter suggested that leased property should be valued at the lease's fair market value.

The Treasury Department and the IRS have determined that the proposed regulations provided a comprehensive method to value leased property to satisfy the 90-percent investment standard. While the commenters' recommended rules would provide value in certain instances, the Treasury Department and the IRS have concluded that such rules would inject significant complexity into the final regulations that would outweigh any potential resulting benefits. As a result, the final regulations retain the method provided in the proposed regulations with some clarifications. For example, the term of a lease that is being valued for purposes of the 90-percent investment standard includes periods during which the lessee may extend the lease at a pre-defined rent. The terms of a pre-defined market rate rent must follow the criteria set forth under section 482 with a rebuttable presumption that terms of a lease between unrelated parties is market rate.

4. Option To Disregard Recently Contributed Property to a QOF for Purposes of the 90-Percent Investment Standard

Under proposed § 1.1400Z2(d)–1(b)(4), a QOF may choose to determine compliance with the 90-percent investment standard by excluding certain eligible property from both the numerator and denominator of the fraction-based test underlying that standard. Such excluded amount of property must satisfy each of the following criteria: (1) The amount of contributed property was received by the QOF partnership or the QOF corporation solely in exchange for an interest in the partnership or stock in the corporation; (2) that contribution or exchange occurred not more than six months before the date of the test from which the amount of property is excluded; and (3) between the date of that contribution or exchange and the date of the underlying asset test, the amount of property was held continuously in cash, cash equivalents, or debt instruments with a term of 18 months or less. Finally, proposed § 1.1400Z2(d)–1(b)(4) provided that a QOF need not be consistent from one semiannual test to another in whether it avails itself of this option.

While commenters largely agreed with the approach set forth in proposed § 1.1400Z2(d)–1(b)(4), many commenters suggested significant revisions. For instance, commenters suggested that the permitted six-month period (that is, the period between the date of contribution or exchange and the testing date) should be extended to a 12-month period, starting on the date of the contribution or exchange, to facilitate increased investments into beneficial qualified opportunity zone property. Another commenter recommended that the final regulations provide QOFs with a 31-month period to deploy capital into a qualified opportunity zone property, and thereby provide QOFs with a rule similar to the 31-month working capital safe harbor (as defined in part V.O of this Summary of Comments and Explanation of Revisions) for qualified opportunity zone businesses.

The Treasury Department and the IRS have considered each of these recommendations and have concluded that their adoption would achieve results inconsistent with the purposes of section 1400Z–2. In particular, the Treasury Department and the IRS have determined that the commenters' recommended rules would permit the holding of capital for extended periods of time without deployment into qualifying investments, and ultimately into QOZs. A delay of such capital investment would reduce, rather than increase, investments in QOZs and thereby delay the type of economic growth for which section 1400Z–2 was enacted to achieve.

One commenter suggested that a QOF should control, by election, the decision to disregard recently contributed property. Under the commenter's approach, a QOF could either disregard the recently contributed property, or upon an election, include the property in both the numerator and the denominator of the fraction-based test underlying the 90-percent investment standard. However, if the QOF elects to disregard the property, the commenter argued that both the numerator and the denominator of the fraction-based test would be zero, resulting in an undefined mathematical result. In the alternative, the commenter suggested that the Treasury Department and the IRS should treat recently contributed property as qualified opportunity zone property only if, and to the extent that, such property is invested in qualified opportunity zone property before the next QOF testing date following that contribution.

The Treasury Department and the IRS have determined that the option to disregard recently contributed property provides a sufficiently expansive rule set to address the concerns raised by the commenter, namely that by excluding recently contributed property from both the numerator and denominator, the resulting fraction may be undefined. The commenter's solution to allow a QOF to elect to disregard property, although potentially helpful to taxpayers in certain cases, would significantly increase the complexity of the mechanics for determining compliance with the 90-percent investment standard. Moreover, the commenter presumes that a QOF would have no other property to include in the denominator, which would allow a mathematically correct result. Further, the alternative suggested by the commenter is similar to the proposed rule and would result in the same outcome. Accordingly, the final regulations do not incorporate the commenter's suggestions. Because several commenters requested flexibility in timing of investments, the final regulations provide that a QOF has until the fifth business day after the contribution of the property to exchange such property into cash, cash equivalents, or debt instruments with a term of 18 months or less.

In addition, one commenter suggested that, with regard to periods during which the previously described contributed property is disregarded, the Treasury Department and the IRS should require that the capital be held in mission-driven institutions such as Community Development Financial Institutions (CDFIs), low-income credit unions, or minority-owned depository institutions. While the Treasury Department and the IRS appreciate the policy objectives underlying this recommendation, section 1400Z–2 does not provide sufficient authority to incorporate this recommendation into the final regulations.

5. Wind-Down Period Safe Harbor for Applying 90-Percent Investment Standard to Dissolving QOFs

For purposes of applying the 90-percent investment standard, two commenters requested that the final regulations provide a wind-down safe harbor period that would precede the start of the QOF's dissolution phase. The commenters reasoned that during a QOF wind-down period which the commenters suggested could last for up to two years, QOFs would hold larger amounts of non-qualifying property because the dissolving QOF typically would dispose of business assets (that is, qualified opportunity zone business property) in exchange for cash or other non-qualifying property. The

commenter contended that the policy rationale for a wind-down period safe harbor for QOF dissolutions would parallel the policy rationale for proposed safe harbor provisions that facilitate the development and operation by QOFs of start-up businesses.

The Treasury Department and the IRS acknowledge the policy arguments set forth by the commenter. However, the final regulations do not adopt the commenter's recommendation. In particular, the Treasury Department and the IRS note that section 1400Z–2 was enacted to encourage the development of operating businesses in QOZs and thereby increase the economic development of the communities located in those designated census tracts. Safe harbors provided by the proposed and final regulations to facilitate the success of start-up businesses in QOZs advances the achievement of those purposes. A QOF wind-down safe harbor for purposes of the 90-percent investment standard, however, potentially would encourage the opposite effect–that is, QOF dissolutions and disinvestment from QOZs.

C. Consideration of Synthetic Equity as Qualified Opportunity Zone Stock or Partnership Interest

Under proposed § 1.1400Z2(d)–1(c), qualified opportunity zone stock and a qualified opportunity zone partnership interest generally must satisfy three requirements. First, such stock or partnership interest must be stock in a corporation or an interest in a partnership that is acquired by a QOF after December 31, 2017 from the corporation or the partnership solely in exchange for cash. See proposed § 1.1400Z2(d)–1(c)(2)(i)(A) (regarding qualified opportunity zone stock), (c)(3)(i) (regarding qualified opportunity zone partnership interests). Second, at the time of acquisition, the corporation whose stock was acquired, or the partnership whose interest was acquired, must either be a qualified opportunity zone business, or in the process of becoming a qualified opportunity zone business. See proposed § 1.1400Z2(d)–1(c)(2)(i)(B) (regarding qualified opportunity zone stock), (c)(3)(ii) (regarding qualified opportunity zone partnership interests). Third, during substantially all of the QOF's holding period for the stock or partnership interest, the corporation or partnership must qualify as a qualified opportunity zone business. See proposed § 1.1400Z2(d)–1(c)(2)(i)(C) (regarding qualified opportunity zone stock), (c)(3)(iii) (regarding qualified opportunity zone partnership interests).

The Treasury Department and the IRS received comments recommending that the final regulations include in the definition of the term ''qualified opportunity zone stock'' any interest constituting synthetic equity under section 409(p)(6)(C) or an employee stock option plan. The synthetic equity definitions recommended by the commenters include an expansive range of interests, some of which would require potentially complex rules to ensure their proper application in the section 1400Z–2 regulations. The Treasury Department and the IRS continue to consider synthetic equity for purposes of the definitions of ''qualified opportunity zone stock'' and ''qualified opportunity zone partnership interest,'' but have determined that specific rules to address synthetic equity would add inappropriate complexity to the final regulations. As a result, the final regulations do not incorporate the commenters' recommendation.

D. Qualified Opportunity Zone Business Property Purchased by QOF or Qualified Opportunity Zone Business

Under proposed § 1.1400Z2(d)–1(c)(4)(i)(A) and (d)(2)(i)(A), property that is purchased (as defined in section 179(d)(2)) by a QOF or a qualified opportunity zone business from an unrelated party (as defined in section 1400Z–2(e)(2)) qualifies as ''qualified opportunity zone business property,'' provided that the property satisfies all other requirements under section 1400Z–2(d)(2)(D)(i).

1. Qualification of Property Constructed by an Eligible Entity

The Treasury Department and the IRS received several comments requesting that the final regulations expand the definition of the term ''qualified opportunity zone business property'' to include an eligible entity's self-constructed property. One commenter recommended that the final regulations treat construction costs of such self-constructed property as part of the property's purchase price. To determine the acquisition date for each testing period, one commenter suggested that the final regulations utilize the approach provided under former section 168(k)(2) and § 1.168(k)–1(b)(4)(iii). Former section 168(k)(2)E)(i) and § 1.168(k)–1(b)(4)(iii) provided that if a taxpayer manufactures, constructs or produces property for use in its trade or business (or for its production of income), the property will be treated as acquired when the taxpayer begins manufacturing, constructing or producing the property. Under § 1.168(k)–1(b)(4)(iii), manufacturing, construction or production of the property begins when physical work of a significant nature begins. Another commenter suggested that, if an eligible entity's self-constructed property is not to be included as purchased property, (i) the incorporation of non-qualifying property into new construction should not taint the new property, and (ii) that new property should be treated as a separate asset under section 1400Z–2(d)(2)(D)(i)(III).

The Treasury Department and the IRS have determined that tangible property is not disqualified from constituting qualified opportunity zone business property solely because the property is manufactured, constructed, or produced, rather than purchased, by the eligible entity. However, to qualify as qualified opportunity zone business property, such tangible property must be manufactured, constructed, or produced by the eligible entity with the intent to use the property in the trade or business of the eligible entity in a QOZ. In addition, the materials and supplies used for the construction of the qualified opportunity zone business property must be qualified opportunity zone business property. Self-constructed property must otherwise meet the requirements of section 1400Z–2(d)(2)(D)(i).

For purposes of the 90-percent investment standard and the 70-percent tangible property standard, an eligible entity must determine the date on which such self-constructed property will be treated as acquired. The Treasury Department and the IRS agree with the prior commenter that applying a standard similar to former section 168 and the regulations thereunder make logical sense. Thus, the final regulations provide that, for purposes of the 90-percent investment standard and the 70-percent tangible property standard, self-constructed property will be treated as acquired on the date physical work of a significant nature begins. Physical work of a significant nature does not include preliminary activities such as planning or designing, securing financing, exploring or researching, and will depend on a facts and circumstances analysis. The final regulations also provide a safe harbor to determine when physical work of a significant nature begins. An eligible entity may choose the date on which the eligible entity paid or incurs more than 10 percent of the total cost of the property, excluding the cost of any land and preliminary activities such as planning and designing, securing financing, exploring or researching.

2. Qualification of Property Contributed to a QOF

Several commenters suggested that property contributed to a QOF, and used in the QOF's trade or business, should be treated as qualified opportunity zone business property. Under section 1400Z–2(d)(2)(D)(i)(I), to qualify as qualified opportunity zone business property, the property must be purchased from an unrelated party. Property contributed by an entity to a QOF, while potentially used in the QOF's trade or business, will not be considered qualified opportunity zone business property because the QOF has not purchased, leased, or self-constructed the contributed property. Because the commenters' suggestion would not be consistent with the text of section 1400Z–2(d)(2)(D)(i)(I), the final regulations do not adopt it.

3. Qualification of Property Purchased Before Statutory Deadline

A commenter asserted that, by requiring the purchase of property to have occurred after December 31, 2017, the proposed regulations will irrationally exclude owners of property purchased on or before that date from the benefits of section 1400Z–2. Another commenter raised similar concerns, and requested that the final regulations treat as qualified opportunity zone business property otherwise qualifying property acquired by a QOF or qualified opportunity zone business prior to the publication date of the October 2018 proposed regulations. While the Treasury Department and the IRS are sympathetic to the concerns expressed by these commenters, the text of section 1400Z–2(d) does not provide authority to allow property purchased on or before December 31, 2017, to be treated as qualified opportunity zone business property.

One commenter requested confirmation that contractual rights to real property (including easements, land leases, timber deeds, agricultural leases, and water rights) qualify as an acquisition by purchase, and therefore could qualify as qualified opportunity zone business property. The Treasury Department and the IRS acknowledge the common usage of these types of arrangements, particularly in rural industries. While the text of section 1400Z–2 requires qualified opportunity zone business property to be purchased or leased, the Treasury Department and the IRS note that contractual rights may qualify as leases under the rules discussed in part V.E of this Summary of Comments and Explanation of Revisions. If such contractual rights do not meet the requirements of either purchased or leased property, however, the final regulations provide that the contractual rights will not qualify as qualified opportunity zone property.

4. Qualification of Property Based on Factors Not Consistent With Section 1400Z–2

For purposes of determining whether property qualifies as qualified opportunity zone business property, the text of section 1400Z–2(d)(2)(D)(i) sets forth requirements regarding the property's acquisition, location, and use. The Treasury Department and the IRS have received comments requesting that the final regulations provide exceptions to those statutory requirements. For example, a commenter requested that the final regulations provide rules that focus on the use of the subject property at the time the property is acquired, but exclude any consideration regarding the location of the property. Similarly, another commenter suggested that the final regulations should provide an exception to allow residents of a QOZ to treat previously purchased property as qualified opportunity zone business property. Commenters also have suggested that property owned by residents of a QOZ, as well as land, should be treated as completely exempt from the post–2017 acquisition requirement.

The Treasury Department and the IRS appreciate the commenters' recommendations. However, each of these suggested rules would conflict with the statutorily imposed acquisition, location, and use requirements set forth in section 1400Z–2(d)(2)(D)(i). As a result, the final regulations do not adopt the commenters' recommendations.

5. Qualification of Property Purchased From Related Persons

Section 1400Z–2(d)(2)(D)(iii) limits the purchase of qualified opportunity zone property to purchases from parties who are not related parties, as that term is defined in section 1400Z–2(e)(2). Proposed § 1.1400Z2(d)–1(c)(4)(i)(A) and (d)(2)(i)(A) provide that property must be acquired by a QOF or qualified opportunity zone business from a person that is not related under section 1400Z–2(e)(2). Under that statutory provision, persons are related to each other for purposes of section 1400Z–2 if such persons are described in section 267(b) or 707(b)(1), determined by substituting ''20 percent'' for ''50 percent'' each place the phrase ''50 percent'' occurs in those sections. See section 1400Z–2(e)(2).

The Treasury Department and the IRS received numerous comments requesting that the final regulations treat property purchased from a related person (under section 1400Z–2(e)(2)) as qualified opportunity zone business property. To prevent potential abuse that could arise from such related-party transactions, one commenter suggested that the final regulations should require purchases between related parties to be negotiated at arm's length. Other commenters recommended that the final regulations allow otherwise qualifying purchases by a QOF or qualified opportunity zone business to be carried out with (i) businesses or partnerships that owned property located in a QOZ prior to the QOZ's designation, and (ii) residents of a QOZ prior to such time. The Treasury Department and the IRS note that the text of section 1400Z–2, as described above, does not permit property purchased from a related party to qualify as qualified opportunity zone property, and therefore decline to adopt these comments.

Another commenter requested that the final regulations provide clarification as to whether any sponsorship arrangement with a sponsor, who is a QOF investor, would establish relatedness included in the definition of ''related person'' under section 1400Z–2(e)(2). The Treasury Department and the IRS have determined that (i) specific rules to address sponsorship agreements would introduce significant, additional complexity into the final regulations, and (ii) the proposed regulations provide adequate guidance to address the commenter's request. As a result, the final regulations do not incorporate specific rules to address sponsorship agreements.

The final regulations, however, have added rules to address the qualification of property purchased in certain ''sponsor-like'' arrangements as qualified opportunity zone business property. With regard to these arrangements, the final regulations provide that, in the case of real property that is purchased by a QOF or qualified opportunity zone business, if at the time of the purchase there was a plan, intent, or expectation for the real property to be repurchased by the seller of the real property for an amount of consideration other than the fair market value of the real property, the purchased real property is not qualified opportunity zone business property. Under this rule, the ''fair market value of the real property'' refers to the fair market value of that property at the time of the repurchase by the seller.

E. Qualified Opportunity Zone Business Property Leased by QOF or Qualified Opportunity Zone Business

Proposed § 1.1400Z2(d)–1(c)(4)(i)(B) and (d)(2)(i)(B) provided that a QOF or qualified opportunity zone business may treat leased tangible property as qualified opportunity zone business property for purposes of satisfying the 90-percent investment standard and the 70-percent tangible property standard. To qualify, the leased tangible property must satisfy the following two general requirements: First, analogous to owned tangible property, leased tangible property must be acquired under a lease entered into after December 31, 2017. Second, and also similar to owned tangible property, substantially all of the use of the leased tangible property must be located within a QOZ during substantially all of the period for which the business leases the property.

1. General Comments Requesting Additional Rules and Clarifications

The Treasury Department and the IRS received several comments agreeing with the rules addressing leased tangible property set forth in the May 2019 proposed regulations. However, many commenters requested that the Treasury Department and the IRS further clarify whether certain types of leased property qualify as qualified opportunity zone business property. Similarly, other commenters recommended that the final regulations provide additional detailed rules and examples, and include definitions for leases, lease-like arrangements, and licenses for purposes of determining whether such instruments qualify as qualified opportunity zone property.

As described further in this part V.E of the Summary of Comments and Explanation of Revisions, the Treasury Department and the IRS have provided additional details and examples in the final regulations to respond to the commenters' concerns and recommendations. For example, the final regulations exempt State and local governments, as well as Indian tribal governments, from the market-rate requirement for leased tangible property that otherwise must be satisfied to qualify as qualified opportunity zone business property. In addition, the final regulations provide rules that permit certain short-term leased property to lessors located outside of a QOZ to be counted as qualified opportunity zone business property for purposes of satisfying the 70-percent use test. The final regulations also contain additional examples to clarify the application of the rules regarding leased tangible property.

2. Qualification of Tangible Property Subject to an Existing Lease

Section 1400Z–2(d)(2)(D)(i)(I) requires tangible property to be purchased after December 31, 2017, which the May 2019 proposed regulations followed in requiring that leased tangible property be acquired under a lease entered into after December 31, 2017. One commenter requested that the final regulations treat an existing lease of property the same as a new lease of property for purposes of determining whether the property subject to the existing lease is qualified opportunity zone business property. The Treasury Department and the IRS note that the leased tangible property rules were included in the May 2019 proposed regulations to provide parity among diverse business models (for example, parity between business models that utilize purchased tangible property and those that utilize leased tangible property). To achieve that parity, the Treasury Department and the IRS have determined that in general acquisitions of tangible property by purchase or lease should be treated consistently. In addition, the Treasury Department and the IRS note that section 1400Z–2 requires the acquisition of such property to occur after December 31, 2017. Therefore, the final regulations confirm that property subject to an existing lease will not constitute qualified opportunity zone business property unless the lease was entered into on or after December 31, 2017.

3. Requirement That the Terms of Lease Must Be Market Rate Between Parties

Proposed § 1.1400Z2(d)–1(c)(4)(i)(B)(*2*) and (d)(2)(i)(B)(*2*) provided that, to qualify as qualified opportunity zone business property, the terms of a lease must be market rate at the time at which the lease was entered into (market-rate lease requirement). For this purpose, whether a lease is market rate (that is, whether the terms of the lease reflect common, arms-length market pricing in the locale that includes the QOZ) is determined in accordance with the regulations under section 482. This limitation operates to ensure that all of the terms of the lease are market rate. The proposed regulations applied the market-rate lease requirement to leases between unrelated parties and related parties.

The Treasury Department and the IRS received multiple comments regarding the market-rate lease requirement. For example, many commenters requested that the final regulations not apply the market-rate lease requirement to leases between unrelated parties. Rather, these commenters recommended that the final regulations provide a presumption that such unrelated-party leases are arms-length. The Treasury Department and the IRS agree with the commenters' recommendation. Accordingly, the final regulations provide that there will be a rebuttable presumption that, with regard to leases between unrelated parties, the terms of the lease were market rate (that is, the lease satisfies the market-rate lease requirement).

In addition, the Treasury Department and the IRS received several comments requesting that the final regulations exempt from the market-rate lease requirement leases between an unrelated party and a state or local government. Commenters explained that such leases are subject to numerous requirements and other special rules. The Treasury Department and the IRS agree with the commenters, and have determined that, based on the same rationale, Indian tribal governments likewise should be exempt from the market-rate lease requirement. As a result, the final regulations provide that, for purposes of satisfying the market-rate lease requirement, tangible property acquired by lease from a state or local government, or an Indian tribal government, is not considered tangible property acquired by lease from a related party.

Another commenter suggested that the final regulations replace the market-rate lease requirement with a requirement that a subject lease must have reasonable terms. This commenter, however, acknowledged that a ''reasonableness'' standard likely would inject additional uncertainty into the final regulations. The Treasury Department and the IRS appreciate the commenter's suggestion and agree that a ''reasonableness'' standard would pose additional uncertainty for taxpayers in determining whether the terms of a subject lease are reasonable. Moreover, the Treasury Department and the IRS believe that such a standard would be too complex to administer. As a result, the final regulations do not adopt the commenter's suggestion.

4. Plan, Intent, or Expectation of QOF or Qualified Opportunity Zone Business To Purchase Leased Real Property

Proposed § 1.1400Z2(d)–1(c)(4)(i)(E) and (d)(2)(i)(E) provided an anti-abuse rule to prevent the use of leases to circumvent the substantial improvement requirement for purchases by QOFs or qualified opportunity zone businesses of real property (other than unimproved land). If, at the time a QOF or qualified

opportunity zone business enters into a lease for real property (other than unimproved land), there was a plan, intent, or expectation for the QOF or qualified opportunity zone business to purchase the real property for an amount of consideration other than the fair market value of the land (as determined at the time of the purchase without regard to any prior lease payments) the leased real property does not qualify as qualified opportunity zone business property at any time.

A commenter suggested that the Treasury Department and the IRS should consider eliminating from this anti-abuse rule the reference to a plan, intent, or expectation to purchase the leased property. Rather, the commenter asserted that, even if the QOF or qualified opportunity zone business had such ''plan, intent, or expectation,'' the anti-abuse rule should not be applied if there were a fixed purchase price option, consistent with general Federal income tax principles governing the distinction between a lease and a sale, with a strike price not less than a specified amount of the fair market value at the time the option is entered into.

The Treasury Department and the IRS have considered the commenter's suggestion and have determined that such a rule might enable QOFs and qualified opportunity zone businesses to circumvent the substantial improvement requirement because leased property from an unrelated party is not required to be substantially improved. Thus, the final regulations do not reflect this suggestion.

F. Treatment of Inventory for Purposes of Determining Substantial Use in QOZ

Under section 1400Z–2(d)(2)(D)(i)(III), the term ''qualified opportunity zone business property'' refers to tangible property used in a trade or business of a QOF or qualified opportunity zone business if, during substantially all of the holding period of the QOF or qualified opportunity zone business for such property, substantially all of the use of such property was in a QOZ. Prior to the publication of the May 2019 proposed regulations, commenters inquired how inventory would be treated for purposes of determining whether substantially all of the tangible property is used in the QOZ. To address those questions, the May 2019 proposed regulations provided a safe harbor that inventory would not fail to qualify as qualified opportunity zone business property simply because the inventory is in transit outside the QOZ due to transport (i) from a vendor to a facility of the trade or business that is in a QOZ, or (ii) from a facility of the trade or business that is in a QOZ to customers outside the QOZ (inventory transit safe harbor). See proposed § 1.1400Z2(d)–1(c)(4)(iii) (setting forth the inventory transit safe harbor).

1. Inventory as Qualified Opportunity Zone Business Property and Application of 90-Percent Investment Standard and 70-Percent Tangible Property Standard

As part of the May 2019 proposed regulations, the Treasury Department and the IRS requested comments as to whether inventory, including raw materials, should be excluded from both the numerator and denominator of the fraction used to determine compliance with the 90-percent investment standard and the 70-percent tangible property standard. In response, some commenters recommended that the final regulations exclude inventory from the 90-percent investment standard and the 70-percent tangible property standard. These commenters based that recommendation upon their conclusion that inventory should never be treated as qualified opportunity zone business property because such inventory (i) is a transitory asset, (ii) does not add value to the QOZ, and (iii) does not meet the requirements for either the original use or substantial improvement requirement. Other commenters agreed that inventory should be excluded from the 70-percent tangible property standard, emphasizing that any requirement that taxpayers measure inventory would be significantly burdensome.

Several additional commenters, however, recommended that the final regulations treat inventory, in a limited manner, as qualified opportunity zone business property. These commenters suggested that taxpayers should be allowed to elect on an annual basis whether to exclude inventory from the numerator and denominator for purposes of the 90-percent investment standard and the 70-percent tangible property standard. Another commenter contended that inventory should be limited to a certain percentage of total qualified opportunity zone property, suggesting that 15 or 20 percent of such total property would provide a reasonable maximum.

The Treasury Department and the IRS also received numerous requests that the final regulations provide additional detail and clarity regarding the general application of section 1400Z–2 to inventory. Like the commenters described previously, these commenters noted that the proposed regulations did not specify whether inventory is properly includable in the numerator of the 70-percent tangible property standard or the 90-percent investment standard. These commenters also highlighted that the proposed regulations did not clarify whether inventory must be original use property or substantially improved property.

The Treasury Department and the IRS acknowledge the concerns raised by these commenters and agree that additional rules regarding the treatment of inventory would be appropriate. As a result, the final regulations provide that, for purposes of determining compliance with the 90-percent investment standard and the 70-percent tangible property standard, a QOF or qualified opportunity zone business may choose to (i) include inventory in both the numerator and the denominator, or (ii) exclude inventory entirety from both the numerator and the denominator. The final regulations also provide that, once a QOF or qualified opportunity zone business makes such choice, the QOF or qualified opportunity zone business must apply that choice consistently with respect to all semiannual tests during the holding period in which the QOF, or the qualified opportunity zone business of the QOF, holds the inventory. The Treasury Department and the IRS have determined that these rules will provide appropriate flexibility for QOFs and qualified opportunity zone businesses, as well as certainty regarding the application of the 90-percent investment standard and the 70-percent tangible property standard.

2. Comments Regarding Application of 90-Percent Investment Standard to Inventory in Transit

Commenters also expressed concern that inventory in transit on the last day of the taxable year of a QOF would be counted against the QOF when determining whether the QOF has met the 90-percent investment standard. Several commenters recommended that inventory in transit, either from the vendor or to the ultimate customer, be excluded from the numerator and denominator for purposes of the 90-percent investment standard, but should qualify for the 70-percent use test. Another commenter suggested that the location of inventory in transit should be taken into account in determining whether the inventory is qualified opportunity zone business property. One commenter generally agreed with the approach of the May 2019 proposed regulations with regard to inventory in transit, but requested clarification that (i) the distance traveled during the course of the transit, or (ii) the manner of the transit, does not affect application of the inventory transit safe harbor. The

commenter also requested clarification as to whether the inventory transit safe harbor covers instances in which the inventory is warehoused briefly (that is, for less than 30 days) in a location outside of the QOZ while in the process of transit.

The Treasury Department and the IRS appreciate the commenters' concerns regarding the manner by which transported inventory is treated for purposes of applying the 90-percent investment standard. To provide certainty for QOFs as well as qualified opportunity zone businesses on this matter, the final regulations set forth a rule that provides that (i) the distance traveled in the course of the transit, and (ii) the fact that the inventory is briefly warehoused while in transit, does not affect the application of the inventory transit safe harbor. The Treasury Department and the IRS intend for these provisions to complement the inventory transit safe harbor, which the final regulations adopt in full.

G. Definition of ''Substantially All'' for Purposes of Qualified Opportunity Zone Property and Qualified Opportunity Zone Business Determinations

The definitions of the terms ''qualified opportunity zone property'' and ''qualified opportunity zone business'' incorporate several ''substantially all'' requirements. For example, with regard to (1) qualified opportunity zone stock, (2) qualified opportunity zone partnership interests, and (3) qualified opportunity zone business property, to qualify as qualified opportunity zone property, the corporation or partnership must have qualified as a qualified opportunity zone business, and the qualified opportunity zone business property must have been used in a QOZ, during ''substantially all'' of the QOF's holding period of such stock, interest, or business, as appropriate. See section 1400Z–2(d)(2)(B)(i)(III) (regarding qualified opportunity zone stock); section 1400Z–2(d)(2)(C)(iii) (regarding qualified opportunity zone partnership interests); section 1400Z–2(d)(2)(D)(i)(III) (regarding qualified opportunity zone businesses). In this holding period context, the May 2019 proposed regulations defined ''substantially all'' of a QOF's holding period as 90 percent of the total holding period of the QOF. See proposed § 1.1400Z2(d)–1(c)(5).

In addition to QOF holding period requirements, the term ''substantially all'' appears in a ''use'' context. Specifically, tangible property used in a trade or business of a QOF or in a qualified opportunity zone business will not qualify as qualified opportunity zone business property unless ''substantially all'' of the use of such tangible property was within the geographic boundaries of a QOZ. See section 1400Z–2(d)(2)(D)(i)(III), (3)(A)(i). In this ''use'' context, the May 2019 proposed regulations defined ''substantially all'' of the use of tangible property in a QOZ by a trade or business of a QOF, or by a qualified opportunity zone business, as 70 percent of the total use of such tangible property. See proposed § 1.1400Z2(d)–1(c)(6), (d)(2)(iv).

Lastly, the term ''substantially all'' appears in the context of the portion of a business's tangible property that must be qualified opportunity zone business property in order for the business to qualify as a qualified opportunity zone business. Specifically, a trade or business qualifies as a qualified opportunity zone business only if (among the satisfaction of other requirements) ''substantially all'' of the tangible property owned or leased by the taxpayer for the trade or business is qualified opportunity zone business property. See section 1400Z–2(d)(3)(A)(i). For this determination of whether the trade or business owns or leases a sufficient amount of qualified opportunity zone business property, the October 2018 proposed regulations defined ''substantially all'' as an amount equal to 70 percent of the total amount of tangible property owned or leased by the trade or business (70-percent tangible property standard). See proposed § 1.1400Z2(d)–1(d)(3).

As discussed in the respective preambles to the October 2018 and May 2019 proposed regulations, the Treasury Department and the IRS provided a higher threshold in the holding period context to preserve the integrity of the statute and ensure that investors focus their investments within the geographic borders of QOZs. Therefore, the term ''substantially all,'' as used in the holding period context, was defined in the proposed regulations as 90 percent of the QOF's total holding period. The Treasury Department and the IRS determined that a percentage threshold higher than, for example 70 percent, was warranted because taxpayers can more easily control and determine the period for which they hold property. In addition, given the lower 70-percent thresholds for testing both the use of tangible property in the QOZ and the amount of owned and leased tangible property of a qualified opportunity zone business that must be qualified opportunity zone business property, applying a 70-percent threshold in the holding period context could result in an unacceptably low percentage of a qualified opportunity zone business's tangible property being used in a QOZ.

The Treasury Department and the IRS, however, recognized that the operations of certain types of businesses may extend beyond the census tract boundaries that define QOZs. Accordingly, the ''substantially all'' thresholds provided by the proposed regulations with regard to required amounts and use of tangible property owned or leased by a trade or business were set to a 70-percent standard. The Treasury Department and the IRS determined that a 70-percent standard would appropriately tie the ability of investors in QOFs to receive preferential capital gains treatment to a consequential amount of tangible property being used by the underlying business within a QOZ. Importantly, the Treasury Department and the IRS also determined that a 70-percent standard would provide businesses with an appropriate degree of flexibility to conduct their day-to-day operations, and therefore avoid significantly distorting or otherwise limiting the introduction of new businesses and investment in QOZs.

1. Consideration of Uniform 90-Percent ''Substantially All'' Standard

Commenters have suggested that the term ''substantially all'' should be interpreted as requiring a 90-percent standard with regard to each instance in which the term is used in section 1400Z–2. As described previously, the Treasury Department and the IRS have determined that the policy considerations underlying each use of the term ''substantially all'' are not uniform, and therefore a uniform standard would fail to effectuate such policies in all cases. For example, the Treasury Department and the IRS established the 70-percent tangible property standard and 70-percent use test to provide ''substantially all'' requirements for qualified opportunity zone businesses that, while substantial, would ensure that a diverse spectrum of businesses would be able to operate in QOZs. However, the Treasury Department and the IRS selected a higher 90-percent threshold regarding holding periods of QOFs (under the 90-percent investment standard) to encourage long-term direct or indirect investments in those qualified opportunity zone businesses. In addition, due to the compound application of the 90-percent threshold, the 70-percent tangible property standard, and the 70-percent use test, the Treasury Department and the IRS sought to ensure that each percentage

requirement, when taken together, would remain significant.

Another commenter that advocated for a uniform 90-percent standard specifically contended that the 70-percent use test presented an inappropriately low threshold to ensure that acceptable amounts of new economic activity are introduced in QOZs. The Treasury Department and the IRS appreciate the commenter's perspective, but have determined that a 70-percent standard achieves an appropriate balance between providing proper flexibility to potential investors in QOZs and limiting the potential for abuse. A 90-percent use threshold would pose a much stricter standard than the proposed 70-percent standard, and potentially would discourage investment in QOZs. As a result, the final regulations retain the 70-percent use test.

Several commenters recommended that, solely with regard to real estate businesses, the final regulations should adopt a threshold of 90 percent for the substantially all use test. The Treasury Department and the IRS have determined that such industry-specific rules would (i) not be consistent with section 1400Z–2 or its underlying policy, and (ii) present administratively burdensome tracking requirements under which taxpayers, as well as the IRS, would need to apply different rules for different types of businesses. As a result, the final regulations do not adopt this recommendation.

2. Clarification Regarding the Measurement of ''Use'' for the 70-Percent Use Test

Several commenters requested clarification regarding the scope of the term ''use'' under section 1400Z–2(d)(2)(D)(i)(III). Similarly, other commenters requested that the final regulations clarify the meaning of the term ''use'' with regard to qualified opportunity zone property located both inside, and outside the geographic borders of a QOZ. Taken together, commenters generally requested easily applicable metrics for determining compliance with the 70-percent use test that are responsive to the practical realities of businesses that utilize a range of tangible property in addition to real estate.

The Treasury Department and the IRS agree with the commenters that guidance regarding the meaning and application of the term ''use'' would be significantly helpful to taxpayers. As a result, the final regulations provide that tangible property of a trade or business is counted for purposes of satisfying the 70-percent use test (qualified tangible property) to the extent the tangible property is (1) located within the geographic borders of a QOZ, and (2) in connection with the ordinary conduct of the trade or business, utilized in the QOZ in the performance of an activity of the trade or business that contributes to the generation of gross income for the trade or business. The final regulations explicitly provide that this determination is based upon the amount of time during which the use of the subject tangible property meets those two requirements.

3. Application of 70-Percent Use Test to Mobile Tangible Property

The Treasury Department and the IRS received several comments regarding the application of the 70-percent use test to mobile tangible property that a trade or business might utilize both inside and outside a QOZ or in multiple QOZs. Commenters noted that many trades or businesses rely on delivery vehicles, construction equipment, service trucks and other types of mobile tangible property to generate gross income. Ordinarily, such trades or businesses will deploy mobile tangible property without regard to QOZ boundaries, at times utilizing the property inside a QOZ, while at other times utilizing the property outside of a QOZ. As a result, these commenters requested that the final regulations articulate standards or safe harbors for determining whether a mobile tangible property satisfies the 70-percent use test to qualify as qualified opportunity zone business property.

The Treasury Department and the IRS appreciate the concerns raised by these commenters. To provide standards that more effectively respond to the day-to-day customary operation of trades or businesses, the final regulations set forth specific rules clarifying the application of the 70-percent use test to mobile tangible property. The Treasury Department and the IRS have drafted these rules to strike an appropriate balance between allowing flexibility for business development and ensuring that such business development primarily benefits low-income communities comprising QOZs.

For example, the final regulations provide a safe harbor for tangible property utilized in rendering services both inside and outside the geographic borders of a QOZ. Under this safe harbor, a limited amount of such tangible property may be excluded from the general time of use calculation underlying the 70-percent use test. Specifically, the safe harbor permits up to 20 percent of the tangible property of a trade or business to be treated as satisfying the 70-percent tangible property standard if the tangible property is utilized in activities both inside and outside of the geographic borders of a QOZ, and if (i) the trade or business has an office or other fixed location located within a qualified opportunity zone (QOZ office), and (ii) the tangible property is operated by employees of the trade or business who regularly use a QOZ office of the trade or business in the course of carrying out their duties, and are managed directly, actively, and substantially on a day-to-day basis by one or more employees of the trade or business at a QOZ office. In addition, in order to qualify for the safe harbor, the tangible property must not be operated exclusively outside of the geographic borders of a qualified opportunity zone for a period longer than 14 consecutive days for the generation of gross income for the trade or business.

In addition, the final regulations provide a similar safe harbor for short-term leased tangible property. Under this rule, tangible property leased by a trade or business located within the geographic borders of a QOZ to a lessee that utilizes the tangible property at a location outside of a QOZ is qualified tangible property if the following two requirements are satisfied. First, consistent with the normal, usual, or customary conduct of the trade or business, the tangible property must be parked or otherwise stored at a location within a QOZ when the tangible property is not subject to a lease to a customer of the trade or business. Second, the lease duration of the tangible property (including any extensions) must not exceed 30 consecutive days. This special leased tangible property rule, however, is not subject to a limitation similar to the 20-percent limitation with regard to non-leased mobile tangible property due to the highly mobile nature of tangible property typically leased to customers by leasing businesses.

4. Use of Tangible Property in Multiple QOZs Aggregated for the 70-Percent Use Test

The Treasury Department and the IRS have received comments recommending that the final regulations clarify the manner in which use of tangible property is measured if such use occurs in multiple QOZs. To respond to these comments, the final regulations specifically provide that, if tangible property is used in one or more QOZs, satisfaction of the 70-percent use test is determined by aggregating the number of days the tangible property in each QOZ is utilized. The Treasury

Department the IRS have determined that the policy underlying the 70-percent use test would be effectuated through the introduction of new economic activity into any low-income community designated as a QOZ, regardless of specific designation.

A commenter highlighted potential confusion caused by circular language in proposed § 1.1400Z2(d)–1(c)(9)(i)(A). In general, proposed § 1.1400Z2(d)–1(c)(9) described the fraction by which the 70-percent use test is calculated. Proposed § 1.1400Z2(d)–1(c)(9)(i)(A) referred to the value of qualified opportunity zone business property that meets the requirements of § 1.1400Z2(d)–1(c)(4)(i)(A)–(C), (E), and (F). The commenter noted that this reference results in a circular analysis because qualified opportunity zone business property is the item calculated by the previously described fraction, and proposed § 1.1400Z2(d)–1(c)(4)(i)(D) sets forth the ''substantially all'' test for use in a QOZ. In other words, the 70-percent use fraction must be calculated before one can determine whether property qualifies as qualified opportunity zone business property.

The Treasury Department and the IRS appreciate the commenter's point. The final regulations set forth a significantly revised calculation for determining satisfaction of the 70-percent use test that does not implicate the issue raised by the commenter. In addition, the final regulations clarify that the use of tangible property in a QOZ is determined on an asset-by-asset basis. See part V.G. of this Summary of Comments and Explanation of Revisions.

5. Application of Holding Period Requirements Under Section 1400Z–2

The Treasury Department and the IRS received numerous requests for clarification regarding the manner by which QOFs can meet the holding period requirements under section 1400Z–2(d)(2)(B)(i)(III) and (d)(2)(C)(iii) (90-percent qualified opportunity zone property holding period) and QOFs and qualified opportunity zone businesses can meet the holding period requirement under section 1400Z–2(d)(2)(D)(i)(III) (90-percent qualified opportunity zone business property holding period). For example, several commenters suggested that QOFs and qualified opportunity zone businesses should test for satisfaction of the two 90-percent holding period requirements only at the end of their holding period for the property. One commenter recommended that the final regulations provide QOFs with an election to test for satisfaction of the 90-percent holding period requirement based on either (i) the taxpayer's actual holding period as of a testing date, or (ii) the taxpayer's projected holding period. See V.B.1. of this Summary of Comments and Explanation of Revisions.

The Treasury Department and the IRS agree that the rules for determining satisfaction of the 90-percent qualified opportunity zone property holding period requirement and 90-percent qualified opportunity zone business property holding period requirement should be clarified. Accordingly, the final regulations provide that the determination of whether the two 90-percent holding period requirements are satisfied is made on a semiannual basis, based on the cumulative amount of time the QOF or qualified opportunity zone business has held the property.

Stock or partnership interests will satisfy the 90-percent qualified opportunity zone property holding period requirement if during 90-percent of the QOF's holding period for the stock or partnership interest, beginning on the date that it's self-certification as a QOF is effective and ending on the relevant semiannual testing date, the corporation or partnership qualified as a qualified opportunity zone business. Similarly, tangible property will satisfy the 90-percent qualified opportunity zone business property holding period requirement only if the tangible property satisfied the 70-percent use test for at least 90 percent of the period during which the QOF or qualified opportunity zone business has held such property. As noted in part V.B.1. of this Summary of Comments and Explanation of Revisions, the determination of whether an eligible entity engaged in a trade or business qualified as a qualified opportunity zone business is determined at the end of the entity's taxable year but a QOF has semiannual testing dates on which it must determine if the entity was a qualified opportunity zone business for 90 percent of the QOF's holding period of the equity of the entity. Because status as a qualified opportunity zone business is defined with respect to an entity's taxable year, taxpayers may encounter difficulties when a QOF's semiannual testing date falls before the end of the entity's taxable year. The final regulations therefore provide a safe harbor for purposes of complying with the 90-percent holding period test. Under the safe harbor, the QOF may limit the period tested to the period that starts with the beginning of the QOF's status as a QOF and lasts until the last day of the entity's latest taxable year and ends on or before the relevant testing date.

To determine whether qualified opportunity zone business property meets the statutory holding period requirements, a QOF or qualified opportunity zone business must measure the use of the property on a semiannual basis, on the same testing dates as the 90-percent investment standard. (If QOFs with diverse taxable years invest in the same qualified opportunity zone business, the business may have to measure use of the property semiannually for each investing QOF). The purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified tax benefits to owners of QOFs to encourage the making of longer-term investments of new capital, through QOFs and qualified opportunity zone businesses, into one or more QOZs and to increase the economic growth therein. The Treasury Department and the IRS have determined that, if the final regulations were to permit QOFs or qualified opportunity zone businesses to use a projected holding period, or to measure the holding period only at the end of their holding period in the property, the previously described policy goals of section 1400Z–2 would be compromised. In addition, such approaches would pose administrative difficulties for the IRS in administering holding period requirements in instances in which a period of ownership extends beyond the statute of limitations for assessing the QOF.

6. Consideration of Cure Periods and Other Relief Regarding Application of 90-Percent Investment Standard

Commenters noted that, under the proposed regulations, no relief was available to a QOF that discovered that the entity in which it invested failed to qualify as a qualified opportunity zone business. Several commenters emphasized that the 90-percent investment standard posed a high threshold with severe consequences for a trade or business that failed to qualify as a qualified opportunity zone business for a testing date. As an example, one commenter described a scenario in which an entity qualified as a qualified opportunity zone business during one year, but failed to satisfy the 90-percent qualified opportunity zone property holding period during the next year, and therefore lost any potential to satisfy the 90-percent qualified opportunity zone property holding period for that stock or partnership interest in later years—regardless of whether the otherwise compliant trade or business permanently cured the defect that lead to the second-year failure. As a result, commenters recommended various ''grace periods'' during which an entity

would be treated as a qualified opportunity zone business even if the entity failed one or more requirements under section 1400Z–2.

The Treasury Department and the IRS agree that entities should be afforded appropriate relief to cure a defect that prevents qualification as a qualified opportunity zone business for purposes of the 90-percent qualified opportunity zone property holding period, without penalty to the investing QOF under section 1400Z–2(f). Accordingly, the final regulations provide a six-month period for an entity in which a QOF has invested to cure a defect that caused the entity to fail to qualify as a qualified opportunity zone business. The six-month cure period corresponds to both the testing periods for both the qualified opportunity zone business and the QOF as required in sections 1400Z–2(d)(1) and (3). The final regulations provide that during that six-month cure period, the QOF can treat the interest held in the entity as qualified opportunity zone property. Upon the conclusion of the six-month cure period, if the entity again fails to qualify as a qualified opportunity zone business, the QOF must determine if the QOF meets the 90-percent investment standard, taking into account its ownership in the non-qualifying entity. If the QOF fails to meet the 90-percent investment standard, the final regulations provide that the QOF must determine the penalty applicable to each month in which the QOF failed to meet the 90-percent investment standard, including each month during and prior to the six-month cure period. The final regulations specify that a qualified opportunity zone business can utilize a six-month cure period only once.

The Treasury Department and the IRS note that, in addition to this six-month cure period, a QOF can assert a defense of reasonable cause under section 1400Z–2(f)(3) if the QOF becomes subject to a penalty for failure to satisfy the 90-percent investment standard. Specifically, section 1400Z–2(f)(3) provides that no penalty may be imposed for failure to meet the 90-percent investment standard ''if it is shown that such failure is due to reasonable cause.'' The Treasury Department and the IRS view this relief under the statute, as well as the six-month cure period provided by the final regulations, as sufficient relief to address the commenters' concerns.

One commenter suggested that the Treasury Department and the IRS consider whether the 90-percent qualified opportunity zone property holding period should be tolled due to circumstances beyond the control of the QOF or qualified opportunity zone business. The Treasury Department and the IRS note that section 1400Z–2(f)(3) provides that a QOF can assert a defense of reasonable cause if the QOF becomes subject to the penalty for failure to maintain the 90-percent investment standard. Based on the existence of this statutory relief, the Treasury Department and the IRS have determined that a QOF possesses appropriate recourse (that is, a reasonable cause defense) with regard to circumstances beyond the QOF's control.

H. Original Use of Tangible Property Acquired by Purchase

Section 1400Z–2(d)(2)(D) requires either that the original use of qualified opportunity zone business property in the QOZ commences with the QOF or qualified opportunity zone business or that the QOF or qualified opportunity zone business substantially improve the property. Similar requirements are also found in other sections of the Code. Under the now-repealed statutory frameworks of both section 1400B (related to the DC Zone) and section 1400F (related to Renewal Communities), qualified property for purposes of those provisions was required to have its original use in a zone or to meet the requirements of substantial improvement as defined under those provisions. Following the publication of the October 2018 proposed regulations, the Treasury Department and the IRS received numerous questions and comments on the meaning of ''original use.'' Several commenters requested confirmation as to whether (i) tangible property could be previously used property, rather than solely new property; (ii) property previously placed in service in the QOZ for one use, but subsequently placed in service for a different use by an acquirer, could qualify as original use; and (iii) property previously used in the QOZ could be placed in service in the same QOZ by an acquiring, unrelated taxpayer.

After carefully considering the comments and questions received regarding the October 2018 proposed regulations, the May 2019 proposed regulations generally provided that the ''original use'' of tangible property acquired by purchase by any person commences on the date on which that person or a prior person (i) first places the property in service in the QOZ for purposes of depreciation or amortization, or (ii) first uses the property in the QOZ in a manner that would allow depreciation or amortization if that person were the property's owner. Therefore, tangible property located in the QOZ that has been depreciated or amortized by a taxpayer other than the QOF or qualified opportunity zone business would not satisfy the original use requirement of section 1400Z–2(d)(2)(D)(i)(II) under the May 2019 proposed regulations. Conversely, tangible property, other than land, located in the QOZ that has not yet been depreciated or amortized by a taxpayer other than the QOF or qualified opportunity zone business would satisfy the original use requirement of section 1400Z–2(d)(2)(D)(i)(II) under those proposed regulations. The May 2019 proposed regulations also clarified that used tangible property will satisfy the original use requirement for a QOZ so long as the property has not been previously used in the QOZ (that is, has not previously been used within that QOZ in a manner that would have allowed it to be depreciated or amortized, by any taxpayer).

1. Reliance on Certificate of Occupancy for ''Original Use'' Determination

Several commenters of the May 2019 proposed regulations recommended that the final regulations permit taxpayers to rely on certificates of occupancy for determining whether a property satisfies the original use requirement. For example, commenters suggested that, if a certificate of occupancy has not been received for property consisting of a structure, the property has not been used prior to the issuance of the certificate and therefore potentially could satisfy the original use requirement. Another commenter requested that the final regulations treat real property as meeting the original use requirement if the property receives a certificate of occupancy following a certain number of years without a certificate. Another commenter suggested that, similar to the rules under §§ 1.46–3(d)(2), 1.150–2(c), and 1.179–4(e), the final regulations permit QOFs and qualified opportunity zone businesses to elect to have ''original use'' measured from the date on which (i) the property is placed into service, or (ii) the certificate of occupancy is granted under local law.

The Treasury Department and the IRS appreciate the commenters' objective to increase certainty regarding ''original use'' determinations. However, the Treasury Department and the IRS note that standards applicable to certificates of occupancy vary by jurisdiction and therefore fail to provide a uniform standard. In addition, the processes for obtaining a certificate of occupancy vary significantly based on jurisdiction and likely would introduce additional complexity and uncertainty. As a result, the final regulations do not adopt the commenters' recommendation.

2. Consideration of Treating Acquired Non-Business Property or Newly Rezoned Property as ''Original Use'' Property

Several commenters recommended that the final regulations clarify that property previously used for non-business purposes may be treated as ''original use'' property in a QOZ upon its acquisition. For support, these commenters emphasized that such property would not have been depreciated or amortized. Similarly, one commenter requested that the final regulations provide a special rule that real property located in an area newly rezoned pursuant to a local government's master plan be treated as ''original use property'' because the local government's rezoning would fundamentally change the real property's use. Other commenters contended that no previously used property in a QOZ should qualify as satisfying the original use requirement regardless of whether, for example, the property had been depreciated or amortized.

The Treasury Department and the IRS have considered each of the arguments set forth by the commenters and have concluded that acquired property previously used in a QOZ does not satisfy the original use requirement. A rule treating historically used property in a QOZ as ''original use'' property because such property's prior use was nonbusiness in nature or classified differently under a local government's master plan would fail to sufficiently encourage the introduction of new capital investments into QOZs. Accordingly, the final regulations retain the rules set forth in the proposed regulations that a property's ''original use'' commences on the date on which the property is first (i) placed into service in the QOZ and is depreciated or amortized, or (ii) used in a manner that would allow depreciation or amortization.

3. Consideration of Safe Harbor Based on Belief That Property Was Not Placed Into Service

One commenter requested that the Treasury Department and the IRS provide a safe harbor to treat property acquired by a taxpayer as satisfying the original use requirement if the taxpayer believed that the property had not yet been placed into service. The commenter contended that, if such taxpayer held that belief, the acquired property should be treated as ''original use'' property even if the taxpayer subsequently discovers that the property actually had been placed in service shortly before its acquisition. The Treasury Department and the IRS decline to adopt this comment because the purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and qualified opportunity zone businesses, of new capital in one or more QOZs and to increase the economic growth of such QOZs. The Treasury Department and the IRS have determined that the commenter's recommended safe harbor would not help achieve those goals.

4. Consideration of Newly Constructed Buildings Acquired Prior To Being Placed Into Service

A commenter requested clarification regarding whether a building that is newly constructed and sold to a purchaser meets the original use requirement with respect to the purchaser. The commenter noted that potential QOF investors intend to invest in QOZs by acquiring newly constructed buildings for their trades or businesses that, prior to acquisition, have not been placed into service for purposes of depreciation. In such circumstances, the commenter noted that potential QOF investors have expressed uncertainty regarding the application of the original use requirement.

The Treasury Department and the IRS appreciate the commenter's concern and have determined that such newly constructed buildings satisfy the original use requirement. The construction of new buildings in economically disadvantaged communities, which are acquired for the purpose of introducing new businesses into such communities, clearly achieves the policy goals underlying section 1400Z–2 and should be encouraged. Accordingly, the final regulations provide an example that provides certainty with regard to the acquisition of such newly constructed buildings.

5. Qualification of Demolished Property, Overwhelmingly Improved Property, and Property Improvements as ''Original Use'' Property

One commenter requested that the final regulations provide that an improvement made to non-qualified property used in a QOZ satisfies the original use requirement. The commenter reasoned that such treatment would be appropriate because, under the May 2019 proposed regulations, improvements made by a lessee to leased property are treated as separate property for purposes of section 1400Z–2(d)(2)(D)(i) and therefore as satisfying the original use requirement. The Treasury Department and the IRS appreciate the argument raised by the commenter, but have determined that the administrative burdens that would arise for taxpayers and the IRS from tracking improvements made to such non-qualified property would significantly exceed those arising from the tracking of lessee improvements. As a result, the final regulations do not adopt the commenter's recommendation.

A commenter also requested that the final regulations treat tangible property that has not been purchased, but has been overwhelmingly improved, as ''original use'' property. Section 1400Z–2(d)(2)(D)(i)(I) requires that property must be acquired after December 31, 2017 to qualify as qualified opportunity zone business property. While a QOZ would benefit from the overwhelming improvement of currently owned property located within the QOZ, such improvement does not satisfy the statutory requirement set forth in section 1400Z–2(d)(2)(D)(i)(I). Therefore, the final regulations do not incorporate the commenter's recommendation.

Another commenter requested that the Treasury Department and the IRS confirm that newly constructed real property, or substantially improved property, that otherwise meets the requirements of section 1400Z–2(d)(2)(D), will not fail to qualify as qualified opportunity zone business property solely because the property is constructed upon leased land. The Treasury Department and the IRS note that land, including leased land, does not need to be substantially improved within the meaning of section 1400Z–2(d)(2)(D)(i)(II) and 1400Z–2(d)(2)(D)(ii). *Cf.* § 1400Z2(d)–1(c)(7)(iv)(B) and (d)(4)(iv)(B). Accordingly, if property otherwise qualifies as qualified opportunity zone business property, the fact that the property is constructed on leased land will not disqualify the

property from being treated as qualified opportunity zone business property.

6. Treatment of Property That Qualifies for Certain Low-Income Housing Credits

A commenter requested that the final regulations address the application of credits provided under section 42(a) of the Code for investment in certain low-income housing buildings (section 42 credits). Specifically, the commenter requested that the final regulations provide that a property that qualifies for section 42 credits be treated as satisfying the original use requirement. The Treasury Department and the IRS continue to consider the combining of other tax incentives (including credits) with the benefits provided by section 1400Z–2. As a result, the final regulations do not incorporate the commenter's request.

7. Application of Original Use Requirement to Leased Tangible Property

A commenter recommended that the final regulations require that leased tangible property located in a QOZ be (i) originally used in the QOZ, and (ii) substantially improved. The Treasury Department and the IRS note that, under the proposed regulations, improvements made by a lessee to leased property satisfy the original use requirement and are considered purchased property to the extent of the unadjusted cost basis of those improvements (as under section 1012). However, the proposed regulations do not set forth any requirement that leased property be substantially improved. After considering the commenter's analysis, the Treasury Department and the IRS have determined that a rule requiring both original use and substantial improvement with regard to leased tangible property would be inconsistent with section 1400Z–2 and unnecessary.

8. Vacancy Period for Original Use Requirement

In the May 2019 proposed regulations, the Treasury Department and the IRS proposed that, where a building or other structure has been vacant for at least five years prior to being purchased by a QOF or qualified opportunity zone business, the purchased building or structure will satisfy the original use requirement. Specifically, the May 2019 proposed regulations provided that, if property has been unused or vacant for an uninterrupted period of at least five years, original use in the QOZ commences on the date after that period when any person first so uses or places the property in service in the QOZ. See proposed § 1.1400Z2(d)–1(c)(4)(i)(B)(*6*), (c)(7)(i), (d)(2)(i)(B)(*6*). The Treasury Department and the IRS requested comments regarding that proposed approach, including the length of the vacancy period and how such a standard might be administered and enforced.

a. Duration of Vacancy Period Required To Satisfy Original Use Requirement

The Treasury Department and the IRS received several comments regarding the five-year vacancy requirement set forth in the May 2019 proposed regulations. While some commenters expressed approval, others contended that a five-year vacancy period would be inappropriately long. Commenters also recommended vacancy periods in excess of five years, contending that any shorter vacancy period would increase the number of vacant properties exempt from the substantial improvement requirement, and therefore decrease the overall magnitude of property development in QOZs. One commenter requested that the final regulations include, in addition to a five-year vacancy requirement, safeguards to reduce the incentive for taxpayers to vacate buildings for tax benefits.

In particular, several commenters suggested that the final regulations provide a vacancy period threshold similar to the threshold provided in § 1.1394–1(h), which requires a vacancy period of ''at least one-year.'' See § 1.1394–1(h) (setting forth an original use requirement for purposes of qualified zone property under section 1397D, with regard to the issuance of enterprise zone facility bonds under section 1394). However, numerous commenters disagreed with that approach, contending that the vacancy period required under § 1.1394–1(h) responds to a different policy objective than the section 1400Z–2 policy objective of increasing new economic development in QOZs. These commenters also contended that a one-year vacancy period would constitute an unacceptably weak standard that potentially would encourage owners of property in QOZs to attempt to artificially satisfy the vacancy requirement by ceasing occupation of a property for one year.

Commenters also recommended rules consisting of multiple vacancy periods to accommodate different types of situations involving vacant buildings. For example, a commenter recommended that the final regulations require (i) a vacancy period spanning not less than two years, or (ii) a five-year vacancy period, if less than 25 percent of the rentable square footage of the subject property is rented or occupied. Another commenter, while expressing general approval regarding the five-year vacancy period requirement, suggested that properties already vacant for at least one year at the time of QOZ designation should qualify as vacant.

The Treasury Department and the IRS appreciate the commenters' suggestions and recommendations, and have modified the proposed five-year vacancy requirement to better effectuate the policy of section 1400Z–2. Accordingly, the final regulations provide a special one-year vacancy requirement for property that was vacant prior to and on the date of publication of the QOZ designation notice that listed the designation of the QOZ in which the property is located, and through the date on which the property was purchased by an eligible entity. The Treasury Department and the IRS have determined that a shorter vacancy period for property vacant at the time of their QOZ designation is appropriate because (i) such buildings do not present the same potential for abuse (for example, causing a building to be vacant for one year to convert the building to ''original use'' property), and (ii) the infusion of capital investments into vacant property that contributed to the QOZ's designation would achieve a core policy objective of section 1400Z–2.

With respect to property not vacant as of the time of such QOZ designation notice but that later become vacant, the final regulations require the property to be vacant continuously for at least three years. The Treasury Department and the IRS agree that a one-year vacancy requirement similar to that imposed under § 1.1394–1(h) would spur capital investment into needed areas. However, a three-year vacancy period for property that was not vacant at the time of QOZ designation will more effectively facilitate such investment while alleviating concerns that QOFs and qualified opportunity zone businesses would intentionally cease occupying property to convert otherwise used property into ''original use'' property.

b. Buildings Located on Brownfield Sites Qualify as ''Original Use'' Property

The Department of the Treasury and the IRS have received several comments regarding the application of section 1400Z–2 and the section 1400Z–2 regulations to brownfield site redevelopment. A ''brownfield site'' comprises ''real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.'' Comprehensive

Environmental Response, Compensation and Liability Act of 1980, section 101(39) (42 U.S.C. 9601(39)). The Environmental Protection Agency has defined these sites as ''abandoned, idled or under-used industrial and commercial facilities where expansion or redevelopment is complicated by real or perceived environmental contamination.'' 60 FR 49276 (September 22, 1995). Cleaning up and reinvesting in these properties increases local tax bases, facilitates job growth, utilizes existing infrastructure, takes development pressures off of undeveloped, open land, and both improves and protects the environment.

Commenters have recommended that the final regulations contain rules to facilitate brownfield redevelopment, particularly rules to provide that the real property composing the brownfield site be treated as ''original'' use property under section 1400Z–2(d)(2)(D)(i)(II). One commenter contended that, because of the degree of contamination present in brownfield sites, remediation and construction periods for these properties generally extend beyond 30 months. The Treasury Department and the IRS agree with this observation, and have included rules in the final regulations to adopt the commenters' recommendation. Specifically, the final regulations provide that all real property composing a brownfield site, including land and structures located thereon, will be treated as satisfying the original use requirement of section 1400Z–2(d)(2)(D)(i)(II). To alleviate concerns that the property purchased will not be remediated, the final regulations also provide that the eligible entity must make investments in the brownfield site to ensure that the site meets basic safety standards for human health and the environment. The final regulations also make clear that remediation of contaminated land is taken into account for determining if the land has been more than minimally improved, and that the QOF or qualified opportunity zone business must make investments into the brownfield site to improve its safety and environmental standards.

c. Clarification of the Term ''Vacant'' for Purposes of Applying the Vacant Property Rules

The Treasury Department and the IRS received multiple suggestions to clarify the meaning of the term ''vacant''. One commenter suggested that the definition of the term should be modified to add the phrase ''substantially unused or substantially vacant.'' For this purpose, the commenter recommended that the term ''substantially vacant'' be defined to require that greater than 70 percent of the square footage of the subject building be unoccupied.

In addition, commenters suggested that the final regulations define the term ''vacant'' in a manner similar to the term under § 1.1394–1(h). Accordingly, these commenters requested that the final regulations include a provision disregarding de minimis, incidental uses of property. See § 1.1394–1(h) (providing that ''de minimis incidental uses of property, such as renting the side of a building for a billboard, are disregarded''). Another commenter suggested that the definition of ''vacant'' be revised to allow for clearly delineated portions of a larger property to be treated as vacant after five years of uninterrupted vacancy, even if the rest of the larger property had not been unoccupied.

One commenter also suggested that property that had involuntarily transferred to local government control be included in the definition of the term ''vacant.'' This commenter emphasized that local governments often acquire brownfield sites and other blighted properties through tax delinquency, abandonment, bankruptcy, and other similar events. As a result, many local governments hold large inventories of vacant properties with varying histories of use. The commenter contended that a bright-line treatment of such properties as ''vacant'' for purposes of the original use requirement will eliminate burdens regarding the determination of historical use and, importantly, expedite capital investment in properties located in distressed communities.

Several commenters suggested that the final regulations set forth a vacancy definition that relies upon vacant property determinations carried out by Federal, state, and local governmental authorities (including, for example, a local government waiver process to demonstrate vacancy). Commenters also suggested that a vacancy definition similarly could rely upon vacant property determinations by public utilities. In addition, some commenters contended that a vacancy definition should take into account a spectrum of factors, including the structure of the subject property and the length of time during which the property's structure had been significantly damaged or otherwise decrepit.

The Treasury Department and the IRS agree that the final regulations should provide a definition for the term ''vacant'' for purposes of § 1.1400Z2(d)–1. Under the final regulations, real property, including land and buildings, is considered to be in a state of vacancy if the property is ''significantly unused.'' A building or land will be considered to be ''significantly unused'' under the final regulations if more than 80 percent of the building or land, as measured by the square footage of useable space, is not being used.

In addition, the Treasury Department and the IRS appreciate that a bright-line test for ''vacancy'' would facilitate the ability for local governments to increase capital investment in underused property and increase economic activity in their respective communities. As a result, the final regulations provide that an eligible entity that purchases real property from a local government that the local government holds as the result of an involuntary transfer (including through abandonment, bankruptcy, foreclosure, or receivership) may treat all property composing the real property (including the land and structures thereon) as satisfying the original use requirement of section 1400Z–2(d)(2)(D)(i)(II).

d. Requests To Require All Vacant Buildings To Be Substantially Improved

Multiple commenters recommended that the final regulations provide that no building, regardless of occupancy, be treated as satisfying the original use requirement. One commenter also suggested that the final regulations (i) require all vacant buildings to be substantially improved, and (ii) not permit such buildings to be treated as originally used in a QOZ by a QOF or qualified opportunity zone business. The Treasury Department and the IRS appreciate the commenters' recommendations and suggestions, and agree that the improvement of all buildings acquired by a QOF or qualified opportunity zone businesses would significantly benefit the QOZs in which such buildings are located. However, the Treasury Department and the IRS have determined that, by permitting certain buildings to satisfy the original use requirement, the final regulations will encourage a larger aggregate amount of long-term investments in economically distressed communities nationwide.

I. Substantial Improvement of Qualified Opportunity Zone Business Property

1. Consideration of Asset-by-Asset Approach and Alternative Approaches

In the May 2019 proposed regulations, the Treasury Department and the IRS requested comments regarding the relative strengths and weakness of determining ''substantial improvement'' based on an asset-by-asset approach, as compared to asset aggregation and similar approaches. See 84 FR 18655

(May 1, 2019). Taxpayers and practitioners have provided numerous responses, several of which articulated examples of difficulty in applying an asset-by-asset approach—particularly within the context of building renovation.

Many of these commenters requested that the final regulations adopt an aggregate approach to determining ''substantial improvement,'' or otherwise permit taxpayers to elect such an approach. Similarly, other commenters requested that the final regulations permit asset aggregation based on (i) asset location within a QOZ, or (ii) whether the assets were acquired as part of the same transaction or business decision. In contrast, a commenter suggested that the final regulations adopt an approach similar to the ''integrated unit approach'' of § 1.1250–1(a)(2)(ii). See § 1.1250–1(a)(2)(ii) (providing for example that, ''if two or more buildings or structures on a single tract or parcel (or contiguous tracts or parcels) of land are operated as an integrated unit (as evidenced by their actual operation, management, financing, and accounting), they may be treated as a single item of section 1250 property'').

The Treasury Department and the IRS also received several recommendations to retain the asset-by-asset approach set forth in the May 2019 proposed regulations. Commenters that made these suggestions generally argued that ''substantially all'' determinations based on an asset aggregation approach would encourage businesses to target investments narrowly in rigidly defined areas, thereby preventing a broader disbursement of capital investment. Such commenters also emphasized that, by requiring the basis of each discrete asset to be doubled in value, the proposed regulations will ensure a minimum level of investment for each qualified asset. Because the asset-by-asset approach of the May 2019 proposed regulations prohibits a taxpayer from using any excess capital investment in a qualified asset to satisfy the ''doubling of basis'' requirement for a different asset, commenters noted that the total capital investments by a taxpayer often will exceed a doubling of the aggregate basis of all of the taxpayer's qualified assets.

Based on the strengths and weaknesses of each of these various approaches, the Treasury Department and the IRS have concluded that permitting asset aggregation to a limited extent is appropriate for carrying out ''substantial improvement'' determinations. Accordingly, for example, the final regulations set forth an asset aggregation approach for determining whether a non-original use asset (such as a preexisting building) has been substantially improved. Under the approach adopted by the final regulations, QOFs and qualified opportunity zone businesses can take into account purchased original use assets that otherwise would qualify as qualified opportunity zone business property if the purchased assets (i) are used in the same trade or business in the QOZ (or a contiguous QOZ) for which the non-original use asset is used, and (ii) improve the functionality of the non-original use assets in the same QOZ (or a contiguous QOZ). In the case of purchased non-original use real property, the final regulations require that the purchased property must be improved by more than an insubstantial amount. Finally, if an eligible entity chooses to use this approach, the purchased property will not be treated as original use property, and instead, the basis of that purchased property will be taken into account in determining whether the additions to the basis of the non-original use property satisfy the requirements of sections 1400Z–2(d)(2)(D)(i)(II) and 1400Z–2(d)(2)(D)(ii).

For example, if a QOF purchases and intends to substantially improve a hotel, the QOF may include ''original use'' purchased assets in the basis of the purchased hotel to meet the substantial improvement requirement if those purchased assets are integrally linked to the functionality of the hotel business. These ''original use'' purchased assets could include mattresses, linens, furniture, electronic equipment, or any other tangible property. However, for purposes of the substantial improvement requirement, the QOF may not include in the basis of that hotel an apartment building purchased by the QOF that is operated in a trade or business separate from the hotel business.

2. Aggregation of Certain Buildings To Be Treated as Single Property

The final regulations also provide that, for purposes of applying the substantial improvement requirement, certain buildings can be aggregated and treated as a single item of property, as that term is used in section 1400Z–2(d)(2)(D)(ii) (single property). Specifically, with respect to two or more buildings located within a QOZ or a single series of contiguous QOZs (eligible building group) that are treated as a single property, the amount of basis required to be added to those buildings will equal the total amount of basis calculated by adding the basis of each such building comprising the single property and additions to the basis of each building comprising the single property are aggregated to determine satisfaction of the substantial improvement requirement.

To clarify which buildings may be treated as a single property, the final regulations address eligible building groups located entirely within a parcel of land described in a single deed, as well as groups spanning contiguous parcels of land described in separate deeds. First, a QOF or QOZ business may treat all buildings that compose an eligible building group and that are located entirely within the geographic borders of a parcel of land described in a single deed as a single property. In addition, a QOF or QOZ business may treat all buildings composing an eligible building group that are located entirely within the geographic borders of contiguous parcels of land described in separate deeds as a single property to the extent each building is operated as part of one or more trades or businesses that meet the following three requirements: (1) The buildings must be operated exclusively by the QOF or by the qualified opportunity zone business; (2) the buildings must share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources; and (3) the buildings must be operated in coordination with, or reliance upon, one or more of the trades or businesses (for example, supply chain interdependencies or mixed-use facilities).

3. Inclusion of Substantial Improvement Requirement on Form 8996

A commenter recommended that the Form 8996 be revised to incorporate the substantial improvement requirement. The Treasury Department and the IRS appreciate the commenter's suggestion and will consider this recommendation during the annual review of Form 8996.

4. Items Includable in Basis of Property for Substantial Improvement Requirement

The Treasury Department and the IRS received multiple comments requesting that the final regulations clarify what items are includable in a property's basis for purposes of the substantial improvement requirement. These commenters emphasized that, while section 1400Z–2(d)(2)(D)(ii) requires a QOF or a qualified opportunity zone business to make additions to the basis of a subject property that exceed an amount equal to the initial adjusted basis of that property within a 30-month

period, the statute does not specify what items are properly includable in that basis. Several of the commenters recommended safe harbors and other simplifying rules to limit complexity and increase taxpayer certainty regarding the application of the substantial improvement requirement.

a. Consideration of Safe Harbor for ''Value Add'' Real Estate Projects

One commenter recommended that the final regulations include a safe harbor for ''value-add'' real estate projects, which ordinarily entail significant renovation or redevelopment of a real property to significantly increase the price-point of the property. The commenter asserted that a property renovated through a value-add project should be treated as automatically satisfying the substantial improvement requirement due to the significant magnitude of the project. The commenter reasoned that, because a value-add project results in a transformative modification to the QOZ property, the QOF or qualified opportunity zone business should be relieved from undertaking a granular analysis and confirmation of project costs for purposes of satisfying the substantial improvement requirement. The commenter also requested that the final regulations express a general policy that the IRS will not challenge a decision by a QOF or qualified opportunity zone business to capitalize expenses into basis.

The Treasury Department and the IRS acknowledge that the commenter's recommendation would facilitate the conduct of value-add projects in QOZs. However, the Treasury Department and the IRS have concluded that value-add projects are similar to other types of property renovation projects for which no special safe harbor is provided. As a result, the Treasury Department and the IRS have determined that no special safe harbor is warranted for value-add projects in QOZs, and the final regulations do not incorporate the commenter's recommendation.

b. Clarification Regarding Property Previously Placed in Service

A commenter requested that the final regulations confirm that additions to basis of property for purposes of the substantial improvement requirement do not include property previously placed in service. Under section 1400Z–2, and as reflected in the proposed regulations, property already placed in service can meet the substantial improvement requirement if the property was not placed in service by the QOF. Therefore, the final regulations do not adopt the commenter's request.

c. Calculation of Basis by Reference to Pre-Depreciation Adjusted Cost Basis

A commenter requested that, for purposes of the substantial improvement requirement, the final regulations permit a QOF or qualified opportunity zone business to calculate the basis of the subject property by reference to the property's pre-depreciation adjusted cost basis. Similarly, another commenter suggested that the term ''adjusted basis'' be defined as cost under section 1012. In addition, a commenter requested that the final regulations confirm that depreciation is not taken into account in determining if a property satisfies the substantial improvement requirement.

The Treasury Department and the IRS disagree with the suggestion that, for determining compliance with the substantial improvement requirement, taxpayers must use section 1012 cost basis for determining the adjusted basis of the property. Section 1400Z–2(d)(2)(D)(ii) provides that adjusted basis, not cost basis under section 1012, is the appropriate standard to determine if property has been substantially improved during the 30-month substantial improvement period. Therefore, the final regulations provide that, property has been substantially improved when the additions to basis of the property in the hands of the QOF exceed an amount equal to the adjusted basis of such property at the beginning of such 30-month substantial improvement period in the hands of the QOF. The basis, and any additions thereto, are measured on the testing dates set forth in section 1400Z–2(d)(1). See part V.O.1.d of this Summary of Comments and Explanation of Revisions.

d. Effect of Certain Improvements on Requirements for Qualified Opportunity Zone Business Property

The Treasury Department and the IRS received comments regarding the effect of certain improvements on the qualification of tangible property as qualified opportunity zone business property. For example, a commenter suggested that QOFs and qualified opportunity zone businesses should be permitted to treat tangible property purchased before December 31, 2017 as qualified opportunity zone business property if the QOF or qualified opportunity zone business substantially improves the tangible property after that date. In addition, several commenters requested that the final regulations provide that costs resulting from the creation of intangibles, as well as other research and development costs, count for purposes of satisfying the Substantial Improvement Requirement.

The Treasury Department and the IRS have determined that the text of section 1400Z–2 does not permit adoption of these suggestions. First, section 1400Z–2(d)(2)(D)(i)(I) requires that tangible property be acquired after December 31, 2017 to qualify as qualified opportunity zone business property. In addition, section 1400Z–2(d)(2)(D)(i)(II) requires that substantially improved property must be tangible property based on the reference in that provision to section 1400Z–2(d)(2)(D)(i). Accordingly, the final regulations do not incorporate the commenters' recommendations.

5. Clarification of Activities and Expenses That Count as Substantial Improvements

The Treasury Department and the IRS have received several comments requesting clarification as to whether certain activities and expenses count as substantial improvements for purposes of the substantial improvement requirement. In particular, commenters requested clarification as to whether ''substantial improvements'' to property include (i) equipment installed in a building and used in a trade or business, (ii) demolition costs, (iii) reasonable capitalized fees for development, (iv) required permits, (v) necessary infrastructure, (vi) brownfield site assessment and remediation, (vii) professional fees, and (viii) necessary site preparation costs (including remediation and utility upgrades). These commenters also requested that the final regulations provide additional rules to address the applicability of these items with regard to the substantial improvement requirement.

The Treasury Department and the IRS note that the text of section 1400Z–2(d)(2)(D)(ii) provides that any cost added to the basis of a property improved during the 30-month improvement period will be included in determining satisfaction of the substantial improvement requirement. As a result, each activity or expense described by the commenter will be included in such determination if the cost adds to the basis of the subject property. In addition, the Treasury Department and the IRS agree that certain expenses with regard to tangible property (such as ''betterment'' expenses under § 1.263(a)–3(j)(1)(i)) are included in the calculation of basis of that property for purposes of the substantial improvement requirement, even if those expenses are properly chargeable under the Code to the basis

of the land on which the property is located (which does not need to be doubled). As a result, the final regulations permit all capitalized costs with respect to the cost of residential rental property to be taken into account for determining satisfaction of the substantial improvement requirement.

6. Requests for Extensions and Safe Harbors Regarding 30-Month Substantial Improvement Period

The Treasury Department and the IRS have received several comments regarding the 30-month substantial improvement period set forth in section 1400Z–2(d)(2)(D)(ii), which provides the period during which a QOF or qualified opportunity zone business can improve acquired tangible property to satisfy the substantial improvement requirement. In particular, many commenters recommended that the final regulations extend this period to a period not exceeding 60 months in the event that (i) the QOF or qualified opportunity zone business encounters a delay not within the entity's control, (ii) the land on which the property rests requires significant preparation or remediation, or (iii) the scale of the project appropriately requires such extended period. Another commenter suggested that the final regulations provide a phase-based safe harbor, similar to that set forth in § 1.148–7(e)(1), that would allow a taxpayer to satisfy the substantial improvement requirement if the QOF or qualified opportunity zone business expended (i) at least 10 percent of the total invested funds within 8 months, (ii) at least 50 percent of the total funds within 16 months, (iii) at least 75 percent of the total funds within 24 months, and (iv) 100 percent of the total funds within 30 months.

The Treasury Department and the IRS note that the commenters' suggestions conflict with the statutory text of section 1400Z–2(d)(2)(D)(ii). That provision explicitly requires that (i) improvements be made to tangible property during the 30-month period beginning after the date of acquisition of such property, and (ii) the measurement for ''substantial improvement'' be based on additions to the basis of the subject tangible property, rather than the percentage of expended funds. As a result, the final regulations do not adopt the commenters' recommended extensions or safe harbors.

7. Safe Harbor for 90-Percent Investment Standard During 30-Month Substantial Improvement Period

One commenter suggested that a QOF or qualified opportunity zone business should be deemed to have met the 90-percent investment standard throughout the 30-month substantial improvement period. The Treasury Department and the IRS appreciate the commenter's recommendation and have revised the final regulations to address, in large part, the commenter's concern. The final regulations provide that, during the 30-month substantial improvement period, eligible tangible property in the process of being improved but not yet placed into service or used in the trade or business of the QOF or qualified opportunity zone business is treated as satisfying the original use requirement and substantial improvement requirement. For property to be eligible for this safe harbor, there must be a reasonable expectation that, not later than the conclusion of the 30-month substantial improvement period, the property will be used in a QOZ as part of the trade or business of the QOF or qualified opportunity zone business, as appropriate. The Treasury Department and the IRS, however, note that a QOF's satisfaction of the 90-percent investment standard will be measured with regard to all of the QOF's qualified opportunity zone property, not just the property being substantially improved.

8. Clarification Regarding Interaction With Substantial Rehabilitation Rules

The Treasury Department and the IRS received a request that the final regulations clarify the interaction between the substantial improvement requirement and the substantial rehabilitation rules under section 42. See section 42(e)(3) (setting forth a minimum expenditure threshold that must be satisfied for rehabilitation expenditures to be considered sufficient to constitute a rehabilitation project eligible for a section 42 credit). The commenter recommended that, with regard to projects carried out in conjunction with section 42 credits, the 30-month substantial improvement period should be subject to the rules for substantial rehabilitation under section 42(e). The Treasury Department and the IRS continue to consider the interaction of rules governing other tax incentives (including credits) with section 1400Z–2 and the regulations under section 1400Z–2. As a result, the final regulations do not incorporate the commenter's request.

9. Qualification of Land Used for Agriculture or Renewable Energy

The Treasury Department and the IRS received multiple comments regarding the qualification of land used for agriculture or renewable energy as qualified opportunity zone business property. To ease difficulties in determining qualification, one commenter suggested that the final regulations include an option to permit the use of specific metrics to calculate the increase of economic activity on unimproved land used for agriculture (for example, specific metrics to calculate increased economic activity that arises from a conversion of agricultural property from pasture to row crops). The commenter stated that such clarification would be useful for farmers. Another commenter recommended that the final regulations treat land used in agricultural activities the same as other tangible business property. Similarly, a commenter requested that the final regulations provide a safe harbor to alleviate difficulties in determining satisfaction of the substantial improvement requirement with regard to farming and biofuel businesses.

The Treasury Department and the IRS acknowledge that complex and fact-specific questions can arise when applying qualified opportunity zone business requirements to agricultural and renewable energy businesses. However, such complexities result in large part from the flexibility that the Treasury Department and the IRS intended to instill in those requirements to facilitate the inclusion of diverse ranges of businesses in QOZs. To preserve that flexibility, and reduce additional complexity that would result from business-specific rules and exceptions, the final regulations do not incorporate the commenters' suggestions.

10. Application of Substantial Improvement Requirement to Land and Buildings Located Thereon

As provided in Rev. Rul. 2018–29, 2018 I.R.B 45, and the May 2019 proposed regulations, if land that is within a QOZ is acquired by purchase in accordance with section 1400Z–2(d)(2)(D)(i)(I), the requirement under section 1400Z–2(d)(2)(D)(i)(II) that the original use of tangible property in the QOZ commence with a QOF is not applicable to the land, whether the land is improved or unimproved. See proposed § 1.1400Z2(d)–1(c)(8)(ii)(B), (d)(4)(ii)(B). Likewise, unimproved land located within a QOZ and acquired by purchase in accordance with section 1400Z–2(d)(2)(D)(i)(I) is not required to be substantially improved within the meaning of section 1400Z–2(d)(2)(D)(i)(II) and (d)(2)(D)(ii). The May 2019 proposed regulations, however, provided that a QOF or qualified opportunity zone business may not rely on these rules if the land is unimproved or minimally improved

and the QOF or the qualified opportunity zone business purchases the land with an expectation, an intention, or a view not to improve the land by more than an insubstantial amount within 30 months after the date of purchase (insubstantial improvement exception). See proposed § 1.1400Z2(d)–1(f).

a. General Applicability of Substantial Improvement Requirement to Land

The Treasury Department and the IRS received numerous comments regarding the proposed application of the substantial improvement requirement to land. While commenters expressed general approval regarding this proposed approach, several commenters disagreed or otherwise suggested revisions or clarifications. For example, multiple commenters requested that the final regulations clarify that unimproved land is treated as qualified opportunity zone business property. Another commenter requested clarification as to whether land held in conjunction with substantially improved property could be treated as qualified opportunity zone business property even if the land was not acquired through a capital contribution or substantially improved. With regard to these requests for clarification, the Treasury Department and the IRS note that land does not need to meet the original use requirement or the substantial improvement requirement to be treated as qualified opportunity zone business property. However, land must meet all other relevant requirements under section 1400Z–2(d)(2)(D) and the section 1400Z–2 regulations.

In addition, commenters recommended that the final regulations subject unimproved land to the substantial improvement requirement to ensure that the land will be used productively to encourage economic growth in the QOZ in which it is located. The Treasury Department and the IRS acknowledge the commenters' recommendations and agree that an integral policy of section 1400Z–2 is to encourage the making of longer-term investments of new capital into QOZs to enhance economic growth and development. However, the Treasury Department and the IRS continue to appreciate that ''land is a crucial business asset for numerous types of operating trades or businesses aside from real estate development, and the degree to which it is necessary or useful for taxpayers seeking to grow their businesses to improve the land that their businesses depend on will vary greatly by region, industry, and particular business.'' 84 FR 18652, 18655 (May 1, 2019). Therefore, the Treasury Department and the IRS have concluded that the imposition of a substantial improvement requirement on all types of trades or businesses for land used in such trades or businesses ''may encourage noneconomic, tax-motivated business decisions, or otherwise effectively prevent many businesses from benefitting under the opportunity zone provisions'' and ''would inject a significant degree of additional complexity'' into the final regulations. *Id.*

b. Eligibility of Naturally Occurring Structures for Substantial Improvement

A commenter requested that the final regulations clarify that naturally occurring structures are eligible for substantial improvement (including any preservation expenses incurred). The commenter contended that the substantial improvement requirement should be determined based on the aggregate expenditure made to improve such natural structures. In addition, the commenter requested that, with regard to trades or businesses in which the value of the land substantially exceeds any building thereon, the rationale of Rev. Rul. 2018–29 should apply without regard to the value of buildings constructed on the land relative to the value of the land (i) provided that the buildings were substantially improved, and (ii) taking into account improvements to natural structures on the land. The commenter also noted that ''naturally occurring structures'' should include vegetation (including trees and other plants) and water sources (including ponds and wetlands).

The Treasury Department and the IRS appreciate the commenter's request for clarity, but note that the proposed regulations did not subject land to the substantial improvement requirement. As provided in the October 2018 proposed regulations, the Treasury Department and the IRS have determined that ''an absence of a requirement to increase the basis of land itself would address many of the comments that taxpayers have made regarding the need to facilitate repurposing vacant or otherwise unutilized land.'' 83 FR 54279 (October 29, 2018). However, the Treasury Department and the IRS agree with the commenter that expenditures to improve land and any naturally occurring structures located thereon can be taken into account for purposes of the requirement that land be improved by more than an insubstantial amount under the final regulations.

c. Application of Substantial Improvement Requirement to Land Expected To Be Only Insubstantially Improved

As described previously, proposed § 1.1400Z2(d)–1(f) prohibits a QOF or qualified opportunity zone business, in certain instances, from relying on rules that except land from the substantial improvement requirement. Specifically, such exception does not apply if (i) the subject land is unimproved or minimally improved, and (ii) the QOF or qualified opportunity zone business purchased the land with an expectation not to improve the land by more than an insubstantial amount (insubstantial improvement exception). See proposed § 1.1400Z2(d)–1(f). This rule helps ensure that the QOZ in which such land is located receives an appropriate amount of capital investment from QOF investors.

The Treasury Department and the IRS received several comments and recommendations regarding the proposed insubstantial improvement exception. For example, one commenter recommended that the final regulations adopt a two-part test, which would require that (i) the subject land be used as a material income-producing factor in the section 162 trade or business conducted by the purchaser, and (ii) the use of the land be in a different trade or business than the use in the hands of the seller, or the purchaser make more than insubstantial improvements to the land. Another commenter requested clarification that the insubstantial improvement exception be revised to permit improvements to be completed after the 30-month substantial improvement period. In addition, a commenter requested that the final regulations provide that capital investments of at least 20 percent of the total cost basis of the subject land made within a 30-month period beginning on the acquisition date be deemed to have improved the land by more than an insubstantial amount.

The Treasury Department and the IRS acknowledge that the commenters' recommendations would provide additional flexibility for investors that acquire unimproved land located within a QOZ. However, the Treasury Department and the IRS have determined that the commenters' suggested rules likely would reduce overall capital investments in low-income communities by either (i) introducing significant additional complexity into the final regulations, or (ii) relaxing the timing requirements for capital investment for an inappropriate duration. As a result, the final

regulations do not adopt the commenters' recommendations.

Commenters also recommended that the final regulations limit the application of the insubstantial improvement exception solely to land the value of which is small in relation to the value of the structures on the land. One commenter argued that, with regard to a circumstance in which the value of the subject land on which a structure is located significantly exceeds the value of the structure, substantially improving only the structure should not be considered a genuine economic investment in the real property as an aggregate. Similarly, multiple commenters requested that the final regulations provide additional detail for determining the amount of capital improvement necessary to exceed an ''insubstantial amount'', including percentage thresholds that would provide a clear amount that needs to be improved. Such threshold amounts ranged from 20 percent to 33 percent.

The Treasury Department and the IRS appreciate the logic of comparing the value of the land to the value of any structures on the land when considering the proposed insubstantial improvement exception for land. However, a rule that makes a distinction between high-value land and low-value land properties would disadvantage investors who planned to make investments in QOZs with higher land value relative to the existing structures on that land. A disproportionate relationship between land value and structure value may exist for a variety of reasons, many of which do not warrant separate treatment. Moreover, a rule that includes the basis of land in the substantial improvement calculation could make development prohibitively expensive for some QOFs and qualified opportunity zone businesses. Accordingly, the final regulations do not distinguish between real property with high or low value land in relation to the structures built upon that land in the application of the exception to substantial improvement.

The Treasury Department and the IRS agree with the commenters that QOFs and qualified opportunity zone businesses should improve land by more than an insubstantial amount. The Treasury Department and the IRS, however, decline to assign a specific percentage threshold to the concept of insubstantial improvement because an appropriate amount of improvement for a particular parcel of land is a highly fact dependent inquiry. Instead, the Treasury Department and the IRS will regard improvements to the land, such as an irrigation system for a farming business or grading of the land with a sufficient nexus to a trade or business of the QOF or qualified opportunity zone business, as more than an insubstantial amount of improvement. Further, the Treasury Department and the IRS view this requirement that land be more than insubstantially improved as clarifying the overall requirement that land be qualified opportunity zone business property. Thus, the proposed rule concerning the qualification of land as qualified opportunity zone business property is moved from § 1.1400Z2(d)–1(f) to the special rules concerning land and improvements on land in § 1.1400Z2(d)–2(b)(4)(iv)(C).

d. Severability of Land From Buildings for Purposes of Applying the Substantial Improvement Requirement

A commenter requested that land on which an existing building is located, and which is not substantially improved, be severable from the existing building for purposes of applying the substantial improvement requirement. Specifically, the commenter recommended that such land should be treated as qualified opportunity zone business property, if (i) the QOF or the qualified opportunity zone business uses or improves the land as part of its trade or business, and (ii) the land otherwise meets the tests for being qualified opportunity zone business property.

However, as noted above, the proposed regulations did not subject land to the substantial improvement requirement. Instead, the land to which the commenter refers would qualify as qualified opportunity zone business property if all other requirements set forth in section 1400Z–2 and the section 1400Z–2 regulations are satisfied (including the insubstantial improvement exception). For these reasons, as well as the rationale for the insubstantial improvement exception described in part V.J.10.c of this Summary of Comments and Explanation of Revisions, the final regulations do not adopt the commenter's recommendation.

11. Speculative Land Purchasing

Several commenters requested that the final regulations provide more stringent rules to prevent the acquisition of land for speculative investment, as well as increased substantial improvement standards with regard to land. These commenters also requested that the final regulations clarify that land does not need to be improved more than an insubstantial amount if (i) the use of the land is integral to the business, and (ii) the land is reasonably expected to generate economic activity that was not reasonably expected prior to its purchase. Other commenters requested that land have a minimum level of improvement to be considered qualified opportunity zone business property. One commenter suggested that land should be improved by 33 percent of its basis. Another suggested that land that is not improved should not count as qualified opportunity zone business property if the value of the land does not exceed a certain threshold percentage of the QOF's assets.

The Treasury Department and the IRS appreciate the commenters' concerns regarding speculative land purchasing. However, the Treasury Department and the IRS have determined that a bright-line standard would be inappropriately restrictive because the determination of whether such land would qualify as qualified opportunity zone business property would require consideration of all relevant facts and circumstances. See additional discussion at VII.B of this Summary of Comments and Explanation of Revisions. Accordingly, the final regulations do not adopt additional rules for speculative land purchasing.

J. Transactions Between Qualified Opportunity Zone Businesses

Proposed § 1.1400Z2(b)–1(c)(10)(i)(A) generally provided that the acquisition of a QOF corporation's assets in a qualifying section 381 transaction is not an inclusion event if the acquiring corporation is a QOF within a prescribed period of time after the acquisition. See parts III.C and III.D of this Summary of Comments and Explanation of Revisions. In turn, proposed § 1.1400Z2(b)–1(d)(1) and (2) provided that the holding period for the target QOF stock is ''tacked'' onto the holding period of the acquiring QOF stock, and any qualified opportunity zone property transferred by the transferor QOF to the acquiring QOF in the transaction does not lose its status as qualified opportunity zone property solely as a result of the transfer. In addition, proposed § 1.1400Z2(b)–1(c)(6)(ii)(C) provided that a merger or consolidation of a partnership holding a qualifying investment, or of a partnership that holds an interest in such partnership solely through one or more partnerships, with another partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event, to the extent section 721 applies. See part III.E.1.b of this Summary of Comments and Explanation of Revisions.

As one commenter observed, however, the proposed regulations did not expressly address the merger of a qualified opportunity zone business

corporation with another qualified opportunity zone business corporation, or the merger of a qualified opportunity zone business partnership with another qualified opportunity zone business partnership. Thus, it is unclear whether the successor business would be treated as succeeding to the target business's original use of, and substantial improvements to, qualified opportunity zone business property for purposes of section 1400Z–2(d)(2)(D), and whether the QOF's stock or partnership interest in the successor business would be treated as acquired ''solely in exchange for cash'' for purposes of section 1400Z–2(d)(2)(B) and (C). The commenter recommended that, after a merger of qualified opportunity zone businesses, the original use and substantial improvement status of the target's property should continue, and the QOF's interest in the successor business should be considered to have been acquired solely in exchange for cash. Another commenter recommended more generally that, when QOFs or qualified opportunity zone businesses transact in qualified assets among themselves, those assets should retain their status as qualified assets, and the transferee QOF or qualified opportunity zone business should be afforded a new working capital safe harbor of up to 31 months to the extent the transferee intends to inject additional capital with respect to the transferred property.

The Treasury Department and the IRS agree that, if a qualified opportunity zone business that is a corporation engages in a transaction described in section 381(a)(2) with another qualified opportunity zone business, or if a qualified opportunity zone business that is a partnership engages in a transaction described in section 708(b)(2)(A) with another qualified opportunity zone business, the original use and substantial improvement status of the transferor business's property should continue, and the QOF's interest in the successor business should be considered to have been acquired solely in exchange for cash. The final regulations have been modified accordingly. See §§ 1.1502–14Z and 1.1504–3 for special rules applicable to consolidated groups.

However, the Treasury Department and the IRS do not agree that a successor qualified opportunity zone business or a successor QOF should be afforded a new 31-month working capital safe harbor because such a rule would be patently inconsistent with treating the entity as a ''successor'' for other purposes, such as original use. The Treasury Department and the IRS also do not agree that a qualified asset should retain its status as such if it is transferred from one QOF or qualified opportunity zone business to another QOF or qualified opportunity zone business in a transaction not described in section 381(a)(2) or section 708(b)(2)(A) because the transferee in such transactions is not a ''successor'' to the transferor.

K. Operation of Section 1397C Requirements Incorporated by Reference

1. 50-Percent Gross Income Requirement

Section 1397C(b) sets forth eight requirements that a corporation or partnership must satisfy to qualify as a ''qualified business entity'' and therefore an ''enterprise zone business.'' Section 1400Z–2(d)(3)(A), which describes the requirements that a trade or business must satisfy to qualify as a ''qualified opportunity zone business,'' incorporates paragraphs (2), (4), and (8) of section 1397C(b)(2). See section 1400Z–2(d)(3)(A)(ii). With regard to gross income, section 1397C(b)(2) requires that ''at least 50 percent of the total gross income of such entity is derived from the active conduct of such business.''

The Treasury Department and the IRS interpret section 1400Z–2(d)(3)(A)(ii)'s incorporation of section 1397C(b)(2) to require that a corporation or partnership, in order to qualify as a qualified opportunity zone business, must derive at least 50 percent of its total gross income from the active conduct of a trade or business within ''a'' QOZ (50-percent gross income requirement). In response to commenters' requests for clarification, the May 2019 proposed regulations provided three safe harbors and a facts-and-circumstances test for determining whether a trade or business in a QOZ has generated sufficient income to satisfy the 50-percent gross income requirement. The Treasury Department and the IRS requested comments regarding those proposed safe harbors, including suggestions for additional safe harbors and revisions to the proposed rules to prevent abuse.

a. Satisfaction of 50-Percent Gross Income Requirement Through Activities in Multiple QOZs

The Treasury Department and the IRS have received comments requesting clarification that a trade or business can satisfy the 50-percent gross income requirement by aggregating activities carried out by the trade or business in multiple QOZs. Specifically, commenters emphasized that the proposed regulations, in numerous instances, referenced a trade or business ''within the QOZ'' rather than ''within a QOZ.'' These commenters asserted that the use of the word ''the'' could be interpreted as requiring that 50 percent of the total gross income from a trade or business (as well as a startup business relying on an applicable safe harbor) be derived from activities carried out solely within a single QOZ.

The Treasury Department and the IRS did not interpret the 50-percent gross income requirement as requiring a trade or business to carry out all activities necessary to satisfy the requirement in only one QOZ. Give the purpose of section 1400Z–2 to encourage economic growth in all QOZs, the Treasury Department and the IRS intended taxpayers and practitioners to apply the 50-percent gross income requirement by aggregating all activities of a trade or business carried out among all QOZs in which the trade or business operates. As a result, the final regulations have been revised to clarify that intended interpretation.

b. Requirement That Activities of Trade or Business Be Carried Out in a QOZ

The Treasury Department and the IRS also received comments suggesting that the 50-percent gross income requirement does not require a qualified opportunity zone business to generate 50 percent of its total gross income from the active conduct of its business ''in a qualified opportunity zone.'' As stated in the preamble of the May 2019 proposed regulations, the phrase ''such business'' in section 1397C(b)(2) refers to a business mentioned in the preceding sentence, which discusses ''a qualified business within an empowerment zone.'' See 84 FR 18652, 18658 (May 1, 2019). In applying section 1397C to section 1400Z–2, references in section 1397C to ''an empowerment zone'' are treated as referring to a QOZ. See id. Therefore, the final regulations do not adopt this comment, but rather provide that the corporation or partnership must derive at least 50 percent of its total gross income from the active conduct of a business within a QOZ.

2. Services Performed in a QOZ Based on Hours and Amounts Paid for Services

The May 2019 proposed regulations provided that, if at least 50 percent of the services performed for the trade or business are performed in a QOZ, based on (i) total number of hours performed by employees and independent contractors and employees of independent contractors in a QOZ (hours performed test), or (ii) amounts paid to employees and independent

contractors and employees of independent contractors in a QOZ (amounts paid test), then the trade or business is deemed to satisfy the 50-percent gross income requirement. See proposed § 1.1400Z2(b)–1(d)(5)(i)(A) (setting forth the hours performed test), (d)(5)(i)(B) (setting forth the amounts paid test). As provided in the preamble to the May 2019 proposed regulations, the hours performed test is intended to address businesses located in a QOZ that primarily provide services. See 84 FR 18652, 18658 (May 1, 2019). In addition, the preamble explained that the amounts paid test is based upon amounts paid by the trade or business for services performed in the QOZ during the taxable year by employees and independent contractors, and employees of independent contractors. See id.

a. Calculations and Recordkeeping for Hours Performed and Amounts Paid Tests

The Treasury Department and the IRS received comments requesting clarification on how to calculate and track ''hours worked'' and ''amounts paid'' for purposes of the hours performed test and the amounts paid test. For example, some commenters highlighted difficulties in distinguishing employees from independent contractors. In particular, a commenter asked whether a trade or business is required to include hours worked by, or payments made to, third-party accountants, lawyers, or investment bankers in determining whether those safe harbors have been met. Commenters also criticized the inclusion of independent contractors and employees of independent contractors, as unreasonable for the hours performed test and amounts paid test because newer businesses, which may be unable to hire full time employees, might not be able to require independent contractors to work primarily in QOZs.

The Treasury Department and the IRS appreciate the commenters' requests and suggestions. With regard to determining satisfaction of the hours performed test and amounts paid test, a majority of the services performed (measured by hours worked or amounts paid) must be provided by employees and independent contractors, and employees of independent contractors, in a QOZ for the trade or business. These calculations do not take into account hours worked by, or amounts paid to, independent contractors and their employees for services that are not performed for the qualified opportunity zone business.

With regard to recordkeeping, the Treasury Department and the IRS have determined that taxpayers and practitioners should be afforded flexibility rather than be encumbered by rigid tracking requirements. However, the Treasury Department and the IRS expect qualified opportunity zone businesses to maintain adequate records and implement sound processes to track hours worked by and amounts paid to employees, independent contractors, and employees of independent contractors for purposes of the hours performed and amounts paid tests. Further, the classification of an employee as opposed to an independent contractor must be determined based upon all relevant facts and circumstances under the applicable common law standard and all relevant provisions of the Code and general principles of tax law.

b. Clarification Regarding Services Provided by Partners in a Partnership

Commenters requested that the final regulations clarify that hours worked by, and amounts paid to, partners in a partnership that provide services to the partnership's trade or business count towards satisfying the hours performed test and amounts paid test. In particular, these commenters emphasized that such partners constitute neither employees nor independent contractors of the subject trade or business. As a result, the commenters noted that such hours worked, and amounts paid, were not specifically covered by either safe harbor.

The Treasury Department and the IRS agree that hours worked by, and amounts paid to, partners in a partnership for services provided to the partnership's trade or business should be taken in account for the hours performed and amounts paid tests. Therefore, the final regulations adopt the commenter's suggestion. In order to ensure that amounts paid to partners are for services provided to the trade or business of the partnership, the final regulations provide that guaranteed payments for services (within the meaning of section 707(c)) to a partner are the only amounts that will be taken into account for the amounts paid test.

c. Clarification Regarding Services Provided by Partners in a Partnership

Some commenters criticized the hours performed test and amounts paid test based on the commenters' view that neither test is sufficiently stringent. These commenters encouraged the Treasury Department and the IRS to combine all three safe harbors into one conjunctive, three-prong approach to provide a better measure of overall business activity occurring within a QOZ. Commenters also requested that the operative threshold be raised from 50 percent of hours worked and amounts paid to 75 percent to ensure that the residents of the QOZ sufficiently benefit from the economic activity created by the QOF investments.

The Treasury Department and the IRS appreciate the policy concerns underlying the commenters' recommendations. However, the Treasury Department and the IRS have determined that the hours performed test and amounts paid test strike an appropriate balance between (i) ensuring economic activity is created in a QOZ (that is, by requiring that at least half of the services performed, determined by hours or amounts paid, be performed in a QOZ), and (ii) providing operating businesses with appropriate flexibility to expand and provide services outside of a QOZ. Therefore, the final regulations do not adopt these comments.

3. Clarification Regarding the Application of the Business Functions Test

In addition to the hours performed test and the amounts paid test, the May 2019 proposed regulations provided a ''business functions test.'' Under that test, a trade or business satisfies the 50-percent gross income requirement if each of (i) the tangible property of the trade or business located in a QOZ, and (ii) the management or operational functions performed in the QOZ, are necessary for the generation of at least 50 percent of the gross income of the trade or business (business functions test). See proposed § 1.1400Z2(b)–1(d)(5)(i)(C) (setting forth the business functions test). The May 2019 proposed regulations requested comments on the business functions test. See 84 FR 18652, 18659 (May 1, 2019).

In response, the Treasury Department and the IRS received several comments requesting that the final regulations clarify the application of the business functions test. Many commenters emphasized that the business functions test fails to provide clearly the manner by which to determine when an asset generates income, as well as which managerial and operational staff are necessary for the generation of income. Commenters requested that the final regulations clarify (i) the meaning of the term ''operational functions,'' and (ii) the method for tracing income generated from tangible property and managerial or operational functions in the QOZ. Also, a commenter highlighted that

administrative ''back office'' functions are necessary functions for the generation of income, although administrative tasks may not be as intrinsically related to the operation of the trade or business.

In addition, a commenter requested that the final regulations provide additional guidance regarding mobile workforces and portable assets. The commenter noted that the May 2019 proposed regulations set forth an example involving a business with a mobile workforce and portable assets that returned to the business' headquarters on a daily basis, but the example does not address a situation in which the tangible assets of the business are almost entirely located in a QOZ at all times, but the business is operated by a workforce which may be remote, mobile, or shared with other businesses. See proposed § 1.1400Z2(b)–1(d)(5)(i)(E)(*1*), 84 FR 18652, 18659 (May 1, 2019). The commenter noted that the example does not clearly indicate whether an employee's activities outside of a QOZ, even while performing key operational roles inside of a QOZ, would cause their work not to be treated as an ''operational function'' that is ''necessary'' for the generation of the business' gross income. The commenter requested that the final regulations describe what is meant by management or operational functions and whether management functions, operational functions, and the location of tangible property are similarly weighted when applying the business functions test.

Commenters also noted that the business functions test could encourage businesses to bring high-skilled, high-income workers into a QOZ, but may not encourage businesses to create jobs for lower-skilled residents of the QOZ. Commenters requested additional examples describing what may or may not meet the business functions test, particularly within the context of fixed assets that are managed or operated by service providers, some of which are physically located outside of a QOZ.

The Treasury Department and the IRS appreciate the commenters' request for clarity regarding the application of the business functions test. Based on comments received, the Treasury Department and the IRS have determined that the business functions test would present an achievable and readily applicable safe harbor for businesses that are headquartered in a QOZ and for which the bulk of business activity occurs in a QOZ. However, the Treasury Department and the IRS acknowledge that businesses with unconventional management and operational structures, as well as tangible property located both inside and outside of a QOZ, would benefit from additional guidance. For those difficult cases, the Treasury Department and the IRS continue to study the commenters' request for clarification regarding the business functions test and may consider providing additional rules and examples through guidance published in the Internal Revenue Bulletin.

L. Requirement To Use Substantial Portion of Intangible Property in a Trade or Business

Section 1400Z–2(d)(3) provides that a qualified opportunity zone trade or business must satisfy the intangible property requirement set forth in section 1397C(b)(4). Section 1400Z–2(d)(3)'s incorporation of section 1397C(b)(4) requires that, with respect to any taxable year, a substantial portion of the intangible property of a qualified opportunity zone business must be used in the active conduct of a trade or business within the QOZ (intangible property use test). However, section 1397C does not provide a definition for the term ''substantial portion.'' To provide additional certainty for determinations regarding whether a substantial portion of intangible property is used in the active conduct of a trade or business within a QOZ, the May 2019 proposed regulations provided that the term ''substantial portion'' means at least 40 percent of the intangible property of the qualified opportunity zone business. See proposed § 1.1400Z2(b)–1(d)(5)(ii), 84 FR 18652, 18659 (May 1, 2019).

1. Clarification Regarding Determinations of Location and ''Use'' of Intangible Property

The Treasury Department and the IRS received comments requesting that the final regulations clarify the methods for determining the location and ''use'' of intangible property. Commenters contended that any uncertainty with regard to those determinations could discourage qualified opportunity zone businesses from developing and using intangible property. These commenters suggested that the Treasury Department and the IRS should consider a number of relevant factors for determining the location and use of intangible property, including (i) where a business provides services or has customers, (ii) where the business' tangible assets are located, (iii) how and where the business is marketed, and (iv) the geographic scope of the legal rights to use the intangible property.

One commenter suggested that, with regard to ''use,'' a determination based on both gross revenue and the location in which such revenue is earned would be appropriate. For example, the commenter contended that an active trade or business that uses intangible property both inside and outside a QOZ should undertake a comparison of gross revenues derived inside the QOZ as well as outside the QOZ. Some commenters suggested that the final regulations adopt a rule similar to the safe harbors used for the 50-percent gross income test which would be based on the location of a business' employees or tangible property located within a QOZ. A commenter noted that a rule that ties ''use'' to tangible property or employees would help prevent abusive situations and ensure that economic activity occurs within a QOZ.

Commenters also suggested methods for determining the situs of intangible property. Commenters noted that, for state property law purposes, the location of intangible property generally is treated as the location at which the owner of that property is located. These commenters asserted that such a determination might be difficult in situations in which a business owner has locations both inside and outside of a QOZ. For example, if a business has a management and operations headquarters in a QOZ, and a technology research and development facility located outside of a QOZ, commenters expressed uncertainty regarding how to determine or measure the location of the business' intangible property. Another commenter suggested that the final regulations provide a rule or rebuttable presumption that connects the situs of an intangible property to a tangible property located within a QOZ if the portion of tangible property that is used for a trade or business inside the QOZ corresponds to the portion of intangible property deemed to be used inside the QOZ. This commenter also noted that a rule providing that an intangible property's location depends upon a tangible property's location could undercut the requirement for substantial use of intangible property in the QOZ.

The Treasury Department and the IRS appreciate the commenters' concerns regarding determinations of location and ''use'' of intangible property for purposes of applying the intangible property use test. To increase certainty in making such determinations, the final regulations provide that intangible property of a qualified opportunity zone business is used in the active conduct of a trade or business in a QOZ if the following two requirements are

satisfied. First, the use of the intangible property must be normal, usual, or customary in the conduct of the trade or business. In addition, the intangible property must be used in the QOZ in the performance of an activity of the trade or business that contributes to the generation of gross income for the trade or business.

2. Consideration of 40-Percent Threshold for Use of Intangible Property

Commenters generally agreed with the 40-percent threshold for defining the minimum level of use necessary to satisfy the section 1397C(b)(4) requirement that a substantial portion of intangible property be used in a QOZ. However, some commenters asserted that the threshold percentage should be increased to more effectively prevent abuse. Commenters highlighted the potential for abusive transactions involving intangible property, noting that intangible property is highly mobile, may appreciate significantly in value, and is not subject to the same restrictions that apply to tangible property under section 1400Z–2(d)(2)(D) (regarding qualified opportunity zone business property). These commenters suggested that the final regulations apply anti-abuse rules similar to those set forth in section 1400Z–2(d)(2)(D) to the use by a trade or businesses of intangible property.

The final regulations adopt the 40-percent threshold for determining whether a ''substantial portion'' of the intangible property of a qualified opportunity zone business is used in the trade or business in a QOZ. After considering the concerns of commenters regarding potential abuses involving intangible property, the Treasury Department and the IRS have determined that the 40-percent threshold requires an appropriately substantial amount of intangible property to be used in a QOZ. In addition, the Treasury Department and the IRS have determined that a 40-percent threshold will provide appropriate flexibility for trades and businesses to expand and operate outside of a QOZ.

3. Clarification Regarding Reference to ''Such Business'' in Section 1397C(b)(4)

A commenter requested clarification regarding whether an intellectual property holding company can be a qualified opportunity zone business in light of section 1397C(d)(4), which excludes any trade or business the activities of which consist predominantly of developing or holding intangibles for sale or license. This commenter noted that section 1397C(b)(4) provides the following condition: ''a substantial portion of the intangible property of such entity is used in the active conduct of any such business.'' The commenter requested that the final regulations confirm whether the use of ''such business'' in section 1397(b)(4) incorporates the qualified business definition set forth in section 1397C(d).

As provided in the preamble to the May 2019 proposed regulations, the Treasury Department and the IRS addressed a similar question with regard to section 1397C(b)(2), which provides that, in order to be a ''qualified business entity'' (in addition to other requirements found in section 1397C(b)) with respect to any taxable year, a corporation or partnership must derive at least 50 percent of its total gross income ''from the active conduct of such business.'' See 84 FR 18652, 18658 (May 1, 2019). As noted in that preamble, the phrase ''such business'' refers to a business mentioned in the preceding sentence, referring to section 1397C(b)(1), which discusses ''a qualified business within an empowerment zone.'' See id. The preamble goes on to state that for purposes of applying section 1400Z–2, references in section 1397C to ''an empowerment zone'' are treated as meaning a qualified opportunity zone. Therefore, section 1400Z–2 does not incorporate the concept of ''qualified business'' within an empowerment zone under section 1397C(d), but instead reads ''such business'' in section 1397C(b)(2) and (4) to refer to ''a business within a qualified opportunity zone.'' As a result, the Treasury Department and the IRS have concluded that the exception set forth in section 1397C(d)(4) has no application with respect to the qualification of an intellectual property holding company as a qualified opportunity zone business.

M. Limitation on Nonqualified Financial Property of Qualified Opportunity Zone Business

Section 1400Z–2(d)(3) incorporates section 1397C(b)(8), which limits the portion of the qualified opportunity zone business' assets that may be held in nonqualified financial property (NQFP) to less than five percent of the average of the aggregate unadjusted bases of the property of the entity in a taxable year (five-percent NQFP limitation). Section 1397C(e) defines the term ''nonqualified financial property'' as debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, annuities, and other similar properties. However, section 1397C(e) excludes from that definition reasonable amounts of working capital held in cash, cash equivalents, or debt instruments with a term of 18 months or less.

1. Consideration of Industry-Specific Revisions to Five-Percent NQFP Limitation

The Treasury Department and the IRS received several recommendations that the final regulations tailor the five-percent NQFP limitation to provide flexibility for certain industries. For example, several commenters expressed a general concern that ordinary-course transactions in the real estate sector may be prohibited by the definition of NQFP. One commenter noted that the definition of NQFP may cover commonplace items such as leases with prepaid or front-loaded rent that are treated in part as loans, prepaid expenses, prepaid development fees, and options to acquire property. The commenter requested that (i) the definition of NQFP provide exceptions for the aforementioned items, and (ii) the five-percent NQFP limitation be revised to exclude commonplace real estate transactions. For support, the commenter asserted that the definition of NQFP creates a trap for the unwary and that the five-percent NQFP limitation was not intended to prevent qualified opportunity zone businesses from engaging in the ordinary-course real estate transactions that develop QOZs.

The Treasury Department and the IRS also received comments requesting similar revisions to the five-percent NQFP limitation to accommodate other industries. For example, a commenter requested that insurance company general account assets be excluded from the definition of NQFP. The commenter emphasized that insurance companies are required to invest a significant portion of their assets in financial property to satisfy obligations to policy holders. By not excluding insurance companies from the five-percent NQFP limitation, the commenter reasoned that the section 1400Z–2 regulations would prevent insurance companies from being qualified opportunity zone businesses.

The Treasury Department and the IRS acknowledge the concerns raised by the commenters. However, sections 1400Z–2(d)(3)(A)(ii) and 1397C(b)(8) provide a clear statutory definition of NQFP and an equally clear limitation on the percentage of NQFP that a qualified opportunity zone business may own. As a result, the final regulations do not adopt the commenters' recommended

revisions to the five-percent NQFP limitation.

2. Consideration of Special Rules To Facilitate the Use of Tax-Exempt Municipal Bonds

Several commenters stressed the importance of adequate infrastructure for the economic development of a QOZ, and the critical role of tax-exempt municipal bonds in the financing of infrastructure projects. These commenters recommended that the final regulations provide favorable treatment for municipal bonds used to finance new or improve existing infrastructure projects located within a QOZ. In particular, these commenters recommended that the final regulations treat municipal bonds essentially as qualified opportunity zone property in which a QOF would be eligible to invest. Further, these commenters recommended that the final regulations treat municipal bonds as property that would not be treated as NQFP in the hands of an entity seeking to qualify as a qualified opportunity zone business. In support of these recommendations, a commenter highlighted that two-thirds of all domestic infrastructure projects are financed by municipal bonds. This commenter reasoned that, if the final regulations were not to remove municipal bonds from the definition of NQFP, infrastructure developments that might otherwise occur would not be financed.

The Treasury Department and the IRS recognize the significant need for additional investment in public infrastructure in QOZs, and that expanded debt and equity tax incentives could facilitate such increased investment. In addition, the Treasury Department and the IRS acknowledge that municipal bonds provide an important source of financing for infrastructure projects. However, section 1400Z–2(d) does not contemplate direct investments in municipal bonds as qualifying property for QOFs. Municipal bonds, which are intangible debt instruments, cannot qualify under the statutory categories of qualified opportunity zone property because municipal bonds are neither (i) equity in a qualified opportunity zone business nor (ii) a tangible asset that is qualified opportunity zone business property. A QOF could make a direct equity investment in tangible property that meets the definition of qualified opportunity zone business property, and the property also may have municipal bond financing (for example, a private water facility financed with tax-exempt private activity bonds under section 142 of the Code). Further, if held by a qualified opportunity zone business, municipal bonds generally constitute NQFP and can qualify for the reasonable working capital safe harbor only in limited circumstances in which the bonds have a term of 18 months or less. For the foregoing reasons, the Treasury Department and the IRS decline to adopt the recommendations of these commenters regarding municipal bond investments.

3. Consideration of Special Rules To Facilitate Tiered Entity Structures

The Treasury Department and the IRS have received several comments regarding the application of sections 1400Z–2(d)(3)(A)(ii) and 1397C(b)(4) to groups of related corporations and partnerships structured to conduct integrated qualified opportunity zone businesses. In particular, several commenters expressed concern that the text of section 1397C(e) prohibits qualified opportunity zone businesses from owning operating subsidiaries due to the inclusion of stock and partnership interests in the statutory definition of NQFP. However, one commenter contended that Congress clearly intended the statute only to prevent qualified opportunity zone businesses from owning publicly traded securities that are passive investments, rather than prevent the ownership of operating subsidiaries. Accordingly, the commenter recommended that the definition of NQFP be clarified to prohibit actively traded personal property for purposes of § 1.1092(d)–1, but not equity interests in operating subsidiaries.

Similarly, other commenters requested that all requirements for a qualified opportunity zone business under section 1400Z–2(d)(3) (including the five-percent NQFP limitation) be applied to an entire group that conducts an integrated business. These commenters asserted that an entity-by-entity test would not be appropriate because such integrated businesses often are organized by entity-specific functions that, in the view of the commenters, would distort the intended application of the five-percent NQFP limitation. For example, an integrated business carried out by a holding corporation that owns all of the equity interests in an operating subsidiary and a treasury subsidiary might comply with the five-percent NQFP limitation if tested in the aggregate, even though the treasury subsidiary, tested on its own, would exceed that limitation.

The Treasury Department and the IRS agree that section 1400Z–2(d)(3) should be applied in a manner that permits flexibility to taxpayers in structuring and conducting qualified opportunity zone businesses. However, with regard to the five-percent NQFP limitation, sections 1397C(b)(8) and 1397C(e) clearly provide that (i) less than five percent of the average of the aggregate unadjusted bases of the property of the subject entity, rather than any group of related entities, must be attributable to NQFP, and (ii) the definition of the term ''nonqualified financial property'' includes stock and partnership interests. As a result, the final regulations do not adopt a group-based test for purposes of the five-percent NQFP limitation.

In addition, the final regulations do not adopt a group-based approach for testing the remaining requirements for a qualified opportunity zone business under section 1400Z–2(d)(3). The Treasury Department and the IRS have determined that an inconsistent application of the requirements for qualified opportunity zone business qualification would significantly increase the complexity of the final regulations and create potential traps for unwary taxpayers. In addition, the Treasury Department and the IRS note that these section 1400Z–2(d)(3) requirements (including the five-percent NQFP limitation) can be applied on a group basis with regard to a qualified opportunity zone business that owns interests in function-specific entities disregarded as separate from their owner for Federal income tax purposes.

N. Trade or Business of a Qualified Opportunity Zone Business

1. Significance of Trade or Business Concept in Section 1400Z–2

Section 1400Z–2(d)(2)(D)(i) and (d)(3)(A)(i) require that qualified opportunity zone business property be tangible property used in the trade or business of a QOF or qualified opportunity zone business. Under section 1400Z–2(d), both QOFs and qualified opportunity zone businesses must meet ''substantially all'' property requirements. For QOFs, at least 90 percent of the qualified entity's property must be qualified opportunity zone property, which includes qualified opportunity zone stock and qualified opportunity zone partnership interests (that is, the 90-percent investment standard). For qualified opportunity zone businesses, at least 70 percent of the qualified entity's property must be qualified opportunity zone business property (that is, the 70-percent tangible property standard). In addition, section 1400Z–2(d)(3)(A)(ii) imposes an additional requirement on qualified opportunity zone businesses but not on QOFs. Under this requirement, at least

50 percent of the total gross income of a qualified entity must be derived from the active conduct of a trade or business within a QOZ (that is, the 50-percent gross income requirement).

2. Proposed Definition Based on a ''Trade or Business'' Under Section 162

The October 2018 proposed regulations contained the term ''active conduct of a trade or business'' in several provisions. See proposed § 1.1400Z2(d)–1(d)(5). Following the publication of that proposal, the Treasury Department and the IRS received comments asking whether future guidance would define the phrase ''active conduct of a trade or business'' for purposes of section 1400Z–2. Commenters also expressed concern that the leasing of real property by a qualified opportunity zone business may not amount to the active conduct of a trade or business if the business has limited leasing activity.

With regard to the term ''trade or business,'' the May 2019 proposed regulations set forth a definition for QOFs and qualified opportunity zone businesses that referenced section 162 of the Code. See 84 FR 18652, 18659 (May 1, 2019). See also § 1.1400Z2(d)–1(c)(4)(ii) (regarding QOFs); § 1.1400Z2(d)–1(d)(2)(ii) (regarding qualified opportunity zone businesses). Section 162(a) permits a deduction for ordinary and necessary expenses paid or incurred in carrying on a trade or business. Because neither the Code nor the regulations define the meaning of a ''trade or business'' under section 162, courts have established requirements to determine the existence of a trade or business. The Supreme Court has set forth a two-pronged test, providing that, ''to be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and that the taxpayer's primary purpose for engaging in the activity must be for income or profit.'' *Commissioner* v. *Groetzinger,* 480 U.S. 23, 25 (1987). With respect to the requirement that the activity must be engaged for income or profit, the Court has expressly provided that section 162 qualification ''requires only an intent to earn an economic profit.'' *Portland Golf Club* v. *Commissioner,* 497 U.S. 154, 164, 169 (1990) (citing *Commissioner* v. *Groetzinger* for the Court's observation that it ''has ruled that a taxpayer's activities fall within the scope of [section] 162 only if an intent to profit has been shown'').

3. Application of Section 162 Trade or Business Standard to Start-Up Businesses

While commenters agreed that section 162 provides an appropriate standard for trade or business qualification under section 1400Z–2(d)(2)(D)(i) and (d)(3)(A)(i), many noted significant uncertainties in applying the section 162 standard to a trade or business of a QOF or qualified opportunity zone business that does not expect to generate profits immediately. In general, these commenters have noted that QOF property used in a start-up business cannot qualify as qualified opportunity zone property unless the start-up business that utilizes such property qualifies as a section 162 trade or business. With regard to QOFs that hold an equity interest in a newly formed partnership or corporation organized for the purpose of being a qualified opportunity zone business, commenters have questioned how section 162 would apply if the partnership or corporation experiences a start-up phase of significant duration. See section 1400Z–2(d)(2)(B)(i)(II) and (d)(2)(C)(ii). With regard to qualified opportunity zone businesses, commenters similarly have expressed uncertainty regarding the qualification of a start-up business as a qualified opportunity zone business if the start-up business has not yet matured to a trade or business under section 162.

a. Comments Suggesting Safe Harbors for Start-Up Businesses

To provide certainty to current and potential investors of start-up businesses in QOZs, commenters suggested a variety of safe harbors. These suggestions included (1) a grace period for a QOF to use tangible property in a trade or business to satisfy the 90-percent investment standard, as well as (2) a provision similar to that under § 1.45D–1(d)(4)(iv) in the New Markets Tax Credit regulations that treats an entity as engaged in the active conduct of a trade or business if, at the time an investment is made, there is a reasonable belief that the entity will generate revenues during the subsequent three-year period. To support the addition of a safe harbor for start-ups, commenters correctly noted that section 1400Z–2 contemplates the start-up phase of a trade or business. Sections 1400Z–2(d)(2)(B)(i)(II) and (d)(2)(C)(ii), as discussed previously, reference newly formed partnerships and corporations organized for the purpose of being a qualified opportunity zone business. In addition, commenters highlighted section 1400Z–2(d)(2)(D)(ii), which provides QOFs 30 months to improve tangible property acquired for use in a QOF's trade or business to meet the substantial improvement requirement.

b. Comments Requesting Clarifications and Simplifying Rules for Start-Up Businesses

Commenters also requested that the final regulations provide a number of clarifications or simplifying rules. For example, commenters requested clarification on whether the conduct of a section 162 trade or business must have begun by the conclusion of a working capital safe harbor period in situations in which the plan underlying the development of the trade or business contemplates the utilization of multiple contributions to which a working capital safe harbor would otherwise apply. Another commenter requested that the final regulations include an example to clarify that the conduct of a trade or business would be required only upon the conclusion of all working capital safe harbors carried out as components of a single integrated plan. Consistent with that request, commenters contended that many types of business ventures, to achieve qualification as a section 162 trade or business, require start-up periods in excess of a single 31-month working capital safe harbor period.

With regard to simplifying rules, a commenter suggested that the final regulations treat the development of a section 162 trade or business as a qualifying section 162 trade or business, regardless of whether the operations that constitute the trade or business have actually begun. Other commenters requested clarification that the ongoing development of real estate constitutes the active conduct of a trade or business even if rent or other revenues are not yet being collected. Similarly a commenter suggested that the final regulations treat a QOF as engaged in a trade or business under section 162 even if the subject business activity had generated no income. Another commenter suggested that the ''active conduct'' requirements set forth in paragraphs (2) and (4) of section 1397C(b) should not be treated as applying to section 1400Z–2(d)(3)(A)(ii).

c. Creation of New 62-Month Working Capital Safe Harbor for Start-Up Businesses

The Treasury Department and the IRS appreciate the commenters' concerns and recommendations regarding the application of the section 162 trade or business standard to start-up businesses. To provide taxpayers with

straightforward and responsive rules, the Treasury Department and the IRS have created an additional 62-month safe harbor for start-up businesses (62-month working capital safe harbor). Unlike the 31-month working capital safe harbor, this start-up-focused safe harbor addresses each qualified opportunity zone business requirement, other than the ''sin business'' prohibition under section 1400Z–2(d)(3)(A)(iii).

As set forth in the final regulations, the 62-month working capital safe harbor provides that, during the maximum 62-month covered period, (1) NQFP in excess of the five-percent NQFP limitation will not cause a trade or business to fail to qualify as a qualified opportunity zone business, and (2) gross income earned from the trade or business will be counted towards satisfying the 50-percent gross income requirement (each of clauses (1) and (2) function in a manner similar to the 31-month working capital safe harbor). In addition, the 62-month working capital safe harbor provides that, during the maximum 62-month covered period, (i) tangible property purchased, leased, or improved by a business with cash covered by a working capital safe harbor, pursuant to the plan submitted with respect to that safe harbor, will count towards satisfaction of the 70-percent tangible property standard, and (ii) intangible property purchased or licensed with that cash, and pursuant to that plan, likewise will count towards the satisfaction of the 40-percent intangible property use test.

To qualify for a maximum 62-month safe harbor period, a start-up business must receive multiple cash infusions during its start-up phase. Specifically, under the 62-month working capital safe harbor, a start-up business can qualify for a 31-month safe harbor period with respect to the business' first cash infusion. Upon receipt of a subsequent contribution of cash (subsequent cash infusion), the business can both (i) extend the original 31-month safe harbor period that covered the initial cash infusion, and (ii) receive safe-harbor coverage for the subsequent cash contribution for a maximum 31-month period, if the business satisfies the following two conditions. First, the subsequent cash infusion must be independently covered by an additional working capital safe harbor. Second, the working capital safe harbor plan for the subsequent cash infusion must form an integral part of the working capital safe harbor plan that covered the initial cash infusion.

To ensure the proper application of the 62-month working capital safe harbor, the final regulations also provide additional operating rules. For example, the final regulations make clear that, regardless of the number of subsequent cash infusions, the 62-month working capital safe harbor cannot extend past the 62 month-period beginning on the date of the first cash infusion covered by the safe harbor (for example, a subsequent cash infusion received 60 months after the date of the first cash infusion will be covered by the 62-month working capital safe harbor for only two months). In addition, the 62-month working capital safe harbor features a minimum investment threshold for each subsequent cash infusion to ensure that a de minimis subsequent infusion does not unlock a subsequent 31-month period for previously covered tangible and intangible property. The final regulations also provide that tangible property covered by the 62-month working capital safe harbor plan is not considered qualified opportunity zone business property for purposes of the special rule in section 1400Z–2(d)(3)(B).

4. Expansion of 30-Month Substantial Improvement Period

The October 2018 proposed regulations provided a 30-month substantial improvement period of tangible property for purposes of applying the substantial improvement requirement. Under that proposal, tangible property is treated as substantially improved by a QOF or qualified opportunity zone business only if, during any 30-month period beginning after the date of acquisition of the property, additions to the basis of the property in the hands of the QOF or qualified opportunity zone business exceed an amount equal to the adjusted basis of the property at the beginning of the 30-month period in the hands of the QOF or qualified opportunity zone business. See proposed § 1.1400Z2(d)–1(c)(8) (setting forth the requirement with regard to QOFs); proposed § 1.1400Z2(d)–1(d)(4) (setting forth the requirement with regard to qualified opportunity zone businesses). The May 2019 proposed regulations provided that the term trade or business means a trade or business within the meaning of section 162, for both QOFs and qualified opportunity zone businesses, and requested comments on whether additional clarification or guidance was needed.

Several commenters pointed out that the proposed regulations are unclear regarding the treatment of tangible property during the 30-month substantial improvement period for a QOF and a qualified opportunity zone business that is not utilizing 31-month working capital safe harbor. Commenters noted that the proposed regulations do not clarify whether non-original use tangible property undergoing a substantial improvement process will be treated as qualified opportunity zone business property during the 30-month substantial improvement period. A commenter noted that just as startup businesses have difficulty satisfying the ''used in a trade or business requirement'' found in section 1400Z–2(d)(2)(D)(i), a QOF or qualified opportunity zone business generally will not be able to use tangible property in a section 162 trade or business during a 30-month substantial improvement period.

Another commenter requested a new safe harbor for work in progress, applicable to both QOFs and qualified opportunity zone businesses, unrelated to the working capital safe harbor. The commenter noted that some projects do not need working capital and that, without an additional safe harbor, projects not utilizing the working capital safe harbor would fail to qualify as qualified opportunity zone business property during the 30-month substantial improvement period. The commenter requested that assets held for work in progress be treated as qualified opportunity zone business property for the 90-percent investment standard found in section 1400Z–2(d)(1) (and the property be treated as used in a trade or business) during the substantial improvement period, if certain criteria are met.

The Treasury Department and the IRS recognize that QOFs are ineligible to utilize the benefits of the working capital safe harbor since the requirements found in paragraphs (2), (4), and (8) of section 1397C(b) are not applicable to QOFs, and that not all qualified opportunity zone businesses will be able to utilize the working capital safe harbor for a variety of reasons. Therefore, the final regulations provide that for QOFs and qualified opportunity zone businesses, tangible property purchased, leased, or improved by a trade or business that is undergoing the substantial improvement process but has not been placed in service or used in a trade or business by the QOF or qualified opportunity zone business is treated as used in a trade or business and satisfies the requirements of section 1400Z–2(d)(2)(D)(i) for the 30-month substantial improvement period with respect to that property. In order to receive such treatment, the QOF or qualified opportunity zone business

must reasonably expect that the property will be substantially improved, as defined in section 1400Z–2(d)(2)(D)(ii), and used in a trade or business in the QOZ by the end of the 30-month substantial improvement period.

5. Consideration of Excluding Real Estate Speculation From the Definition of ''Trade or Business''

A commenter suggested that the final regulations modify the definition of the term ''trade or business'' to specifically exclude real estate speculation. The commenter asserted that real estate speculation on projects carried out within QOZs presents a significant potential for abuse, and reasoned that a specific exclusion of real estate speculation from the definition of ''trade or business'' would eliminate such potential. The Treasury Department and the IRS appreciate the concern raised by the commenter, but note that the final regulations address real estate speculation abuse by requiring that land (1) be more than insubstantially improved and (2) be used in the trade or business of a QOF or qualified opportunity zone business. Accordingly, the final regulations do not adopt the commenter's recommendation.

6. Consideration of Triple-Net-Leases for Active Conduct a Trade or Business Requirement

Proposed § 1.1400Z2(d)–1(d)(5)(ii)(B)(*2*) provided that, solely for the purposes of determining whether a trade or business qualified as a qualified opportunity zone business, the ownership and operation, including leasing, of real property qualifies as an active conduct of a trade or business. The proposed rule, however, provided that merely entering into a triple-net-lease with respect to real property owned by a taxpayer does not constitute an active conduct of a trade or business by such taxpayer. See proposed § 1.1400Z2(d)–1(d)(5)(ii)(B)(*2*) (second sentence). The Treasury Department and the IRS determined that, solely for purposes of determining qualified opportunity zone business qualification, triple-net-leases constitute inappropriately passive activities similar to holding publicly traded stock or securities.

a. Comments Suggesting Special Definitions for ''Triple-Net-Lease''

In general, commenters requested additional guidance regarding the meaning of the term ''triple net lease'' for purposes of applying proposed § 1.1400Z2(d)–1(d)(5)(ii)(B)(*2*). Several commenters suggested that the final regulations define the term ''triple-net-lease'' as a lease in which the tenant, in addition to rent and utilities, pays the tenant's proportionate share of the taxes, insurance, maintenance, and other fees for the property leased. Multiple commenters recommended that a triple-net-lease of a taxpayer be defined to constitute an active conduct of a trade or business if the taxpayer meaningfully participates in the management or operations of the trade or business of the lessee. Similarly, another commenter requested that the final regulations define a triple-net-lease to exclude arrangements pursuant to which a taxpayer retains contractual responsibility for meaningful capital obligations or meaningful operating obligations. The commenter indicated that an obligation to maintain certain structural or operating systems of a building would qualify as a meaningful capital obligation, while obligations to provide cleaning or grounds-keeping services would qualify as meaningful operating obligations.

b. Comments Suggesting Active Trade or Business Qualification Based on Section 162 Case Law

Another commenter recommended that the final regulations adopt a rule based on case law under section 162 to determine whether a triple-net-lease qualifies as the active conduct of a trade or business. According to the commenter, the case law under section 162 allows a deduction for ordinary and necessary expenses paid or incurred in carrying on any trade or business related to a triple-net-lease if the landlord, or an employee, agent, or contractor of the landlord, performs the services related to the taxes, maintenance, insurance, and similar fees even though the landlord receives payment for these services from the tenant. Therefore, the commenter suggested that a triple-net-lease in which the landlord, or an employee, agent, or contractor of the landlord, performs these services should qualify as the active conduct of a trade or business, regardless of which party ultimately bears the cost for these services.

c. Comments Suggesting Special Rules for Active Trade or Business Qualification

Commenters also recommended that the final regulations provide special rules for determining whether a taxpayer entering into a triple-net-lease with respect to real property owned by a taxpayer constitutes an active conduct of a trade or business by such taxpayer. For example, a commenter contended that a triple-net-lease qualify as the active conduct of a trade or business if (1) the underlying property meets the test under the original use requirement or the substantial improvement requirement, and (2) assuming all other requirements are met, qualifies as qualified opportunity zone business property. For support, the commenter highlighted the May 2019 proposed regulations, which provided that leased property can qualify as qualified opportunity zone business property to a tenant that is a QOF or a qualified opportunity zone business. This commenter reasoned that, because leased property would be qualified opportunity zone business property to a tenant notwithstanding the fact that the property was subject to a triple-net-lease, it could also be qualified opportunity zone business property to the landlord. Therefore, under the commenter's reasoning, a lessor's participation in a triple-net-lease could constitute the active conduct of a trade or business.

Commenters also recommended that lessor participation in certain arrangements that utilize the rehabilitation tax credit under section 47 of the Code should qualify as an active conduct of a trade or business. In such arrangements, a landlord owns a building that is the subject of a rehabilitation project. The landlord acquires the property, obtains permits and approvals, assembles the development team, raises the funds necessary to develop the property, and places the rehabilitated structure into service. After that initial phase, the landlord leases the building to a tenant, who may further lease the property to a subtenant. The landlord transfers the rehabilitation tax credits to the original tenant pursuant to section 50(d)(5). The commenter noted that this arrangement between the landlord and the original tenant may constitute a triple-net-lease. As a result, the commenter recommended that the final regulations adopt a rule to provide specifically that such arrangements constitute the active conduct of a trade or business.

d. Comments Suggesting Triple-Net-Leases Qualify as an Active Trade or Business

However, other commenters disagreed with the premise of proposed § 1.1400Z2(d)–1(d)(5)(ii)(B) that merely entering into a triple-net-lease for property owned by a taxpayer does not constitute the active conduct of a trade or business. Several commenters noted that triple-net-leases cause capital to enter a QOZ and provide property for use in trades or businesses within the QOZ. These commenters also

emphasized that landlords and tenants often prefer triple-net-lease arrangements, as opposed to employing a separate property manager or agent of the landlord, because tenants often are better positioned to control and maintain the leased property. Accordingly, the commercial real estate industry widely employs triple-net-leasing.

e. Revisions to Proposed Triple-Net-Lease Rule for Active Trade or Business Qualification

The Treasury Department and the IRS appreciate the comments and recommendations received with respect to triple-net-leases. In general, the final regulations confirm that merely entering into a triple-net-lease with respect to real property owned by a taxpayer does not constitute the active conduct of a trade or business by such taxpayer. To illustrate the application of this rule, the final regulations set forth examples describing a triple-net-lease as a lease arrangement pursuant to which the tenant is responsible for all of the costs relating to the leased property (for example, paying all taxes, insurance, and maintenance expenses) in addition to paying rent. In an instance in which the taxpayer's sole business consists of a single triple-net-lease of a property, the final regulations confirm that the taxpayer does not carry out an active trade or business with respect to that property solely for purposes of section 1400Z–2(d)(3)(A).

The Treasury Department and the IRS agree with commenters that, in certain cases, a taxpayer that utilizes a triple-net-lease as part of the taxpayer's leasing business could be treated as conducting an active trade or business solely for purposes of section 1400Z–2(d)(3)(A). Accordingly, the final regulations provide an example in which a lessor leases a three-story mixed-use building to three tenants, each of which rents a single floor. In that example, (i) the lessor leases one floor of the building under a triple-net-lease, but leases the remaining two floors under leases that do not constitute triple-net-leases, and (ii) the employees of the lessor meaningfully participate in the management and operations of those two floors. As a result, the example provides that the lessor is treated as carrying out an active trade or business with respect to the entire leased building solely for purposes of section 1400Z–2(d)(3)(A).

O. Safe Harbor for Reasonable Amounts of Working Capital

The October 2018 proposed regulations provided a 31-month working capital safe harbor for QOF investments in qualified opportunity zone businesses that acquire, construct, or rehabilitate tangible business property, which includes both real property and other tangible property used in a business operating in a QOZ (31-month working capital safe harbor). See proposed § 1.1400Z2(d)–1(d)(5)(iv); 83 FR 54279, 54284 (October 29, 2018). Solely for purposes of applying section 1397C(e)(1) to the definition of a qualified opportunity zone business under section 1400Z–2(d)(3), working capital assets held by the business are treated as reasonable in amount under sections 1397C(b)(2) and 1400Z–2(d)(3)(A)(ii) for a period of up to 31 months. See id. To qualify, the qualified opportunity zone business (1) must have a written plan that identifies the financial property as property held for the acquisition, construction, or substantial improvement of tangible property in the QOZ, (2) must have a written schedule consistent with the ordinary business operations of the business that the property will be used within 31 months, and (3) must substantially comply with the schedule. See id.

The May 2019 proposed regulations provided revisions to the 31-month working capital safe harbor in response to comments. First, the May 2019 proposal modified the rule requiring a written designation for planned use of working capital to include the development of a trade or business in the QOZ as well as acquisition, construction, and/or substantial improvement of tangible property. See proposed § 1.1400Z2(d)–1(d)(5)(iv)(A); 84 FR 18652, 18659 (May 1, 2019). Second, the May 2019 proposal provided that exceeding the 31-month period does not violate the 31-month working capital safe harbor if the delay is attributable to waiting for government action the application for which is completed during the 31-month period. See proposed § 1.1400Z2(d)–1(d)(5)(iv)(C); 84 FR 18652, 18659 (May 1, 2019). The May 2019 proposed regulations also clarified that a business may benefit from multiple overlapping or sequential applications of the working capital safe harbor, provided that each application independently satisfies all of the requirements in proposed § 1.1400Z2(d)–1(d)(5)(iv)(A) through (C) (multiple safe harbor rule). See proposed § 1.1400Z2(d)–1(d)(5)(iv)(D).

1. Additional Guidance Regarding Reasonable Delays to Toll the 31-Month Working Capital Safe Harbor

The Treasury Department and the IRS have received several comments and requests for additional guidance regarding delays relating to governmental action, as well as delays arising from a variety of other events. With regard to applying proposed § 1.1400Z2(d)–1(d)(5)(iv)(C), one commenter requested confirmation as to whether a delay attributable to governmental action, the application for which is completed during the 31-month period, means that (i) the governmental action must be pending at the end of the 31-month period or (ii) a waiting period for governmental action at any time ''stops the clock'' on the 31-month period (and therefore the waiting period is added at the end of the 31-month period). The commenter noted that, in certain instances, a governmental action might be completed predictably within a relatively short period of time, and therefore automatic tolling might provide an overly generous result. Another commenter, however, emphasized that the governmental permitting guidelines regarding natural resource projects lack predictable completion timeframes because such projects often require the receipt of several state and local permits that are subject to various timelines. As a result, this commenter requested that the 31-month period be tolled to accommodate successive permits in a circumstance in which the business has received the first serious of permits that initially tolled the 31-month period.

Commenters also recommended that the final regulations provide that, in additional to delays resulting from governmental action, certain events outside of a business' control will toll the 31-month working capital safe harbor. For example, several commenters requested that events delaying the 31-month period include, among other occurrences, severe weather conditions, natural disasters, labor stoppages, financing delays, and supply shortages. Another commenter requested that trades or businesses receive an extension of the 31-month period to account for delays arising from the cleanup of a brownfield site due because the cleanup of such a site ordinarily will require other lengthy regulatory approval from states and local governments.

The Treasury Department and the IRS acknowledge the concerns raised by the commenters. In many ordinary-course instances, however, applicants can

obtain governmental permits through a routine process of predictable duration. The Treasury Department and the IRS continue to expect a qualified opportunity zone business, to the maximum extent practicable, to take any actions during the governmental permitting period that are necessary for the improvement of tangible property subject to the 31-month working capital safe harbor. Therefore, with regard to instances in which governmental delay does not pose a substantial obstacle for improving such tangible property, a tolling of the 31-month period would not be appropriate.

The Treasury Department and the IRS have determined that the 31-month working capital safe harbor should be tolled in certain instances, however, and have clarified and expanded the scope of proposed § 1.1400Z2(d)–1(d)(5)(iv)(C). In general, the final regulations make clear that, if a governmental permitting delay has caused the delay of a project covered by the 31-month working capital safe harbor, and no other action could be taken to improve the tangible property or complete the project during the permitting process, then the 31-month working capital safe harbor will be tolled for a duration equal to the permitting delay. In such case, the final regulations require that the permit for the governmental action was completed during the 31-month period. The final regulations also provide that, if a project that otherwise meets the requirements of the 31-month working capital safe harbor is located within a QOZ designated as a part of a Federally declared disaster area (as defined in section 165(i)(5)(A)), the qualified opportunity zone business may receive up to an additional 24 months to consume its working capital assets, provided the project is delayed due to that disaster.

2. Clarification Regarding Overlapping or Sequential Applications of the 31-Month Working Capital Safe Harbor

The Treasury Department and the IRS received several comments and requests for clarification regarding the multiple safe harbor rule. In particular, commenters questioned whether a successive application of the 31-month working capital safe harbor can occur for the same piece of tangible property, given that multiple 31-month harbor periods can be utilized for that same piece of tangible property. These commenters contended that a successive application of the 31-month working capital safe harbor would appropriately accommodate practical realities of improving tangible property in a trade or business (such as ordinary course-improvement projects that typically require durations in excess of 31 months).

The Treasury Department and the IRS confirm that a qualified opportunity zone business may string together subsequent or overlapping working capital safe harbors with respect to the same tangible property. Accordingly, the final regulations specifically provide that a qualified opportunity zone business may choose to apply subsequent 31-month working capital safe harbors for a maximum 62-month period (that is, a duration equal to two working capital safe harbor periods), provided that each 31-month period satisfies the requirements for applying a 31-month working capital safe harbor. To qualify for a subsequent 31-month working capital safe harbor period, (i) working capital subject to an expiring 31-month period must be expended in accordance with each requirement set forth in the section 1400Z–2 regulations, and (ii) the subsequent infusions of working capital must form an integral part of the plan covered by the initial 31-month working capital safe harbor.

3. Treatment of Tangible Property Not Used Upon Conclusion of a 31-Month Working Capital Safe Harbor

Commenters also noted that, although the May 2019 proposed regulations expanded the 31-month working capital safe harbor to include the development of a trade or business, the proposal failed to clarify the application of the safe harbor regarding situations in which the qualified opportunity zone business does not use the tangible property in the QOZ by the end of the 31-month period. For example, commenters requested that the final regulations describe circumstances in which a business that uses a contribution of working capital during a 31-month period, but does not use the tangible property in a trade or business in the QOZ by the end of the 31-month period, may continue to be covered by the 31-month working capital safe harbor. These commenters asserted that such a business should continue to receive coverage by the safe harbor if, based on a consideration of the relevant facts and circumstances, the business diligently and reasonably continues to develop the trade or business and uses the tangible property in a trade or business in the QOZ within a reasonable period of time.

Another commenter suggested that the final regulations provide a rebuttable assumption that all working capital that will be expended by the business has been expended before each testing date, including future tranches of working capital that, as part of the working capital plan, will be used to substantially improve or construct new property in a QOZ. Similarly, a commenter suggested that the final regulations provide that, if a trade or business receives serial capital contributions under a common written plan, the trade or business must use cash equal to the first capital contribution within 31 months, but is not required to use 70 percent of its tangible property in the QOZ by the end of the 31-month period associated with the first capital contribution. In addition, a commenter suggested that the 31-month working capital safe harbor be revised to provide that the 70-percent tangible property standard would not be applied until all working capital has been expended and the substantially improved (or new) property is placed in service by the business in the QOZ.

The Treasury Department and the IRS appreciate the commenters' suggestions and requests for clarification, and have included additional guidance in the final regulations. In general, the final regulations permit a qualified opportunity zone business to treat tangible property for which working capital covered by the 31-month working capital safe harbor is expended as (i) used in the trade or business of the qualified opportunity zone business, and (ii) qualified opportunity zone business property throughout the period during which such working capital is covered by the safe harbor. The final regulations make clear that such improvements must be made pursuant to the written plan governing the expenditure of the working capital assets. In addition, the tangible property subject to such improvements must be used in a trade or business, within the meaning of section 162, of the qualified opportunity zone business by the end of the 31-month working capital safe harbor. The final regulations also clarify that unexpended amounts of working capital covered by the 31-month working capital safe harbor are not, following the conclusion of the final safe harbor period, treated as tangible property for purposes of applying the 70-percent tangible property standard.

4. Consideration of Special Debt-Financed Safe Harbor for QOFs and Qualified Opportunity Zone Businesses

A commenter requested that the final regulations provide a new safe harbor to cover debt-financed work-in-progress projects that (i) would operate in addition to the 31-month working capital safe harbor, and (ii) could be

applied by QOFs and qualified opportunity zone businesses. For support, the commenter emphasized that many construction projects are debt financed and would not be covered by the 31-month working capital safe harbor during the construction period. Accordingly, the absence of a debt-financed safe harbor would complicate the ability to carry out construction projects within QOZs.

The commenter suggested that, if certain requirements were met, the final regulations should provide that (i) assets held for work-in-progress construction projects be treated as qualified opportunity zone business property during the construction period, and (ii) the QOF or qualified opportunity zone business be treated as engaged in a section 162 trade or business. Requirements suggested by the commenter for this safe harbor included (1) mandatory increases to the basis of the trade or business in the qualified opportunity zone business property by a prescribed multiple during the 31-month period, (2) periodic certification requirements during the construction period, and (3) continuous and diligent construction by the trade or business until the completion of project and the placed-in-service date of the subject building. Upon such date, the commenter suggested that the final regulations retroactively treat (i) the work-in-progress property as qualified opportunity zone business property, and (ii) the trade or business as engaged in a section 162 trade or business beginning on the first day of the investment by the QOF in the trade or business and throughout the project's construction period.

The Treasury Department and the IRS appreciate the commenter's recommendation and are sympathetic to the commenter's concern regarding the existing business practice of using debt to finance construction. However, section 1397C(e) clearly treats as NQFP any debt with a term greater than 18 months. Based on the text of section 1397C(e), the final regulations do not adopt the commenter's request to provide a special safe harbor for debt-financed construction projects.

5. Consequence of Failure To Qualify for a 31-Month Working Capital Safe Harbor

The Treasury Department and the IRS received comments requesting clarification with regard to the consequences that would result if a trade or business fails to satisfy the requirements for a 31-month working capital safe harbor, including the imposition of penalties. In general, if a qualified opportunity zone business fails to satisfy the conditions for applying a 31-month working capital safe harbor, then the qualified opportunity zone business must satisfy the requirements of section 1400Z–2 and the 1400Z–2 regulations for qualifying as a qualified opportunity zone business in the absence of the safe harbor. Such failure could cause a QOF to fail to satisfy the 90-percent investment standard, which would result in penalties to the QOF as provided under section 1400Z–2 and the section 1400Z–2 regulations.

P. *Real Property Straddling QOZ and Non-QOZ Census Tracts*

To determine whether a QOZ is the location of services, tangible property, or business functions for purposes of satisfying the requirements of section 1400Z–2(d)(3)(A)(ii), proposed § 1.1400Z2(d)–1(d)(5)(viii) provided that section 1397C(f) applies, substituting the term ''QOZ'' for the term ''empowerment zone'' in each instance in which the term ''empowerment zone'' appears. In addressing the circumstance in which a business owns real property that is located in more than one census tract, only one of which is a QOZ, proposed § 1.1400Z2(d)–1(d)(5)(viii) provided that if (1) the amount of real property based on square footage located within the QOZ is substantial as compared to the amount of real property based on square footage outside of the QOZ (square footage test); and (2) the real property outside of the QOZ is contiguous to part or all of the real property located inside the QOZ, then all of the property is deemed to be located within a QOZ.

1. Consideration for Eliminating Proposed Square Footage Test

Several commenters praised the Treasury Department and the IRS for allowing real property that straddles census tracts to be treated as located within a QOZ for purposes of determining whether the QOZ should be treated as the location of services, tangible property, or business functions. However, one commenter suggested that the proposed square footage test be eliminated. The commenter reasoned that only property located entirely within the geographic borders of a QOZ should be treated as within a QOZ because section 1400Z–2 was enacted to increase investment and business activity in QOZ, rather than non-QOZ census tracts. That commenter further contended that, if the proposed square footage test were to be finalized, at least 75 percent of the square footage or value of the property should be located in the QOZ, with an allocation of capital gains and profits to the property located within the QOZ.

The Treasury Department and the IRS decline to adopt the commenter's recommendations. With regard to the commenter's suggestion to eliminate the proposed square footage test, the Treasury Department and the IRS note that parcels of real property commonly extend across census tract lines, particularly in highly populated areas. As a result, the Treasury Department and the IRS have determined that guidance addressing such situations would provide flexibility for potential investors in QOZs, and therefore is consistent with the underlying policy of section 1400Z–2. Based on the same rationale for providing appropriate flexibility to QOF investors and encourage additional investment within QOZs, the Treasury Department and the IRS decline to adopt the commenter's suggestion to require that at least 75 percent of the square footage or value of the real property be located in the QOZ in order for real property to be treated as wholly located within the QOZ.

2. Clarification Regarding Applicability of the Unadjusted Cost Test

A number of commenters noted that the preamble to the May 2019 proposed regulations set forth an unadjusted cost test, rather than the square footage test, to determine whether property that straddles QOZ and non-QOZ census tracts would be treated as located within a QOZ (unadjusted cost test). See 84 FR 18652, 18658 (May 1, 2019) (setting forth the unadjusted cost test); proposed § 1.1400Z2(d)–1(d)(5)(viii) (setting forth the square footage test). These commenters highlighted the relative strengths of each of these tests, and the flexibility afforded by multiple approaches for taxpayers with land that straddles QOZ and non-QOZ census tracts. The Treasury Department and the IRS acknowledge that both tests would provide helpful guidance such taxpayers and accordingly have revised the final regulations to include both the square footage test and the unadjusted cost test.

3. Consideration of Revisions to the Square Footage Test and the Unadjusted Cost Test and Additional Safe Harbors

The Treasury Department and the IRS received numerous comments and recommendations regarding the square footage test and the unadjusted cost basis test, including rules that would govern the application of such tests in certain circumstances. For example, one commenter suggested that, with regard to real property acquired as a single

parcel, the final regulations should apply the unadjusted cost test and set forth a presumption that unadjusted cost is allocated based on the area of the real property located inside, as compared to outside, the QOZ. In applying this presumption to buildings, however, the commenter suggested that the final regulations should apply the square footage test.

The Treasury Department and the IRS also received several recommendations regarding appropriate thresholds for the safe harbor tests. For instance, one commenter requested that the final regulations provide a rule to treat real property located in a QOZ as substantial, as compared to real property located outside of a QOZ, if more than 50 percent of the total square footage of real property is located inside of the QOZ. Another commenter suggested that the percentage of property located in a QOZ should be increased to at least 75 percent of the total square footage of the property. A third commenter suggested that the final regulations provide a safe harbor to treat real property located within a QOZ as substantial if more than 50 percent of the real property is located in the QOZ, as measured by square footage, unadjusted cost, fair market value, or other types of quantitative measures. The commenter indicated that such quantitative measures might reference the occurrence of business activities conducted on the portion of the real property located inside of the QOZ that are integral to the business activities conducted on the portion of real property located outside of the QOZ.

The Treasury Department and the IRS have determined that the square footage test and the unadjusted cost test provide appropriate levels of flexibility for owners of property that straddles QOZ and non-QOZ census tracts. While adoption of the commenters' recommendations would increase the degree of guidance available to owners of such parcels, the Treasury Department and the IRS have concluded that the complexity resulting from adoption of these recommendations would outweigh their intended benefits. As a result, the final regulations do not adopt the commenters' recommendations.

4. Requested Clarification for Applying the Unadjusted Cost Test to Leased Property

One commenter requested clarification in applying the unadjusted cost test to leased property. Under proposed § 1.1400Z2(d)–1(d)(3)(ii)(B)(*3*), to determine the value of tangible property owned by a qualified opportunity zone business for purposes of the 70-percent tangible property standard, the unadjusted cost basis of the property under section 1012 may be used. For tangible property leased by a qualified opportunity zone business to meet the requirements of section 1400Z–2(d)(3)(A)(i), a taxpayer may use the methodology in proposed § 1.1400Z2(d)–1(d)(3)(ii)(B)(*4*). Because the unadjusted cost of real property may be used to determine whether property located inside of a QOZ is substantial relative to property located outside of a QOZ, the commenter requested clarification on which method to use.

The Treasury Department and the IRS acknowledge that such guidance could benefit taxpayers and practitioners in applying these rules. However, because the valuation methodology in proposed § 1.1400Z2(d)–1(d)(3)(ii)(B)(*4*) is used to value property to meet the statutory requirements for the 70-percent tangible property standard, the Treasury Department and the IRS decline to apply these methodologies for all purposes. Accordingly, qualified opportunity zone businesses may use only the square footage test or the unadjusted cost test, to determine if the subject property is located substantially within a QOZ when property straddles QOZ and non-QOZ tracts. The method chosen must be applied consistently throughout the holding period under section 1400Z–2(d)(2)(D)(iii) for such property.

5. Requested Clarification Regarding Contiguous Requirement for Straddle Property

A number of commenters requested clarification regarding the requirement that real property located outside of a QOZ be contiguous to all or part of the real property located inside the QOZ. Some commenters requested that the contiguity requirement be relaxed in the following circumstances: (1) Two or more parcels of real property that are not contiguous because they are separated by public property, such as a road or a sidewalk; and (2) two or more parcels of real property that are not contiguous because a third-party owns a right that burdens the bordering area between the two tracts, such as an easement or other right-of-way. Similarly, commenters have recommended that the contiguity requirement be treated as satisfied in cases in which a development project that is located outside of a QOZ, but in a location either adjacent to or within a short distance from a QOZ.

The Treasury Department and the IRS appreciate the commenters' request, and agree that the final regulations should clarify and define contiguous property. As a result, the final regulations provide that parcels or tracts of land will be considered contiguous if they possess common boundaries, and would be contiguous but for the interposition of a road, street, railroad, stream or similar property. In addition, the final regulations exclude from the definition of the term ''common boundaries'' boundaries of parcels of land that touch only at a common corner.

6. Extension of Straddle Safe Harbor Principles for Purposes of the 70-Percent Use Test

The Treasury Department and the IRS received multiple recommendations that the final regulations extend the principles of proposed § 1.1400Z2(d)–1(d)(5)(viii) to determine whether real property is used in a QOZ for the 70-percent use test. A portion of these commenters requested that the extension of these principles apply to QOFs as well as qualified opportunity zone businesses. These commenters contended that QOFs and qualified opportunity zone businesses should be treated similarly in this context to further the policy of introducing new capital investment into QOZs.

For purposes of determining whether real property qualifies as qualified opportunity zone business property, the Treasury Department and the IRS have determined that it would be appropriate to extend the treatment of real property that straddles QOZ and non-QOZ tracts to the 70-percent use test. The final regulations also confirm that this extension of treatment applies to both qualified opportunity zone businesses and QOFs. The extension of this concept provides flexibility for trades or businesses within QOZs, and the Treasury Department and the IRS note that the requirements for substantiality (that is, the square footage and unadjusted cost tests) and contiguity will minimize the occurrence of abusive arrangements.

7. Requested Expansion of QOZ Definition Under Section 1400Z–2

The Treasury Department and the IRS received a comment requesting that the final regulations expand the definition of a QOZ. Specifically, the commenter suggested that the definition of a QOZ be revised to include any census tract in which a development or project is located if (1) the relevant statistics of the census tract meet the criteria that were originally used to identify eligible QOZ tracts; (2) the development or project is located within one-quarter mile of an existing or proposed high-quality transit stop; or (3) the census tract is located

directly adjacent to, or within a short distance from, an existing QOZ. For support, the commenter contended that the process to nominate census tracts as QOZs may have omitted other tracts with similar statistical profiles that might have qualified as QOZs if the selection process were to have had a longer duration.

Another commenter recommended that the final regulations expand the QOZ concept by treating certain projects located completely outside a QOZ as though such projects are located within a QOZ. Specifically, the commenter suggested that project components located outside of a QOZ that are connected or necessary to the project components located inside of the QOZ should be treated as if located in a QOZ. For support, the commenter provided examples of industries that rely on natural resources that might be located outside of a QOZ, and may be of limited portability due to their connection to certain geological or topographic land features.

The Treasury Department and the IRS appreciate the commenters' recommendations but decline to incorporate them in the final regulations. With regard to the commenter's request to expand the definition of a QOZ, the Treasury Department and the IRS have determined that such recommendation is not supported by the text of section 1400Z–1, which sets forth the process for QOZ designation. Moreover, the Treasury Department and the IRS note that Rev. Proc. 2018–16, 2018–9 I.R.B. 383, provided additional guidance to the Chief Executive Officers of each state regarding the manner by which certain population census tracts may be designated as QOZs. With regard to the commenter's request to expand the concept of QOZs to include certain projects located entirely outside of QOZs, the Treasury Department and the IRS have determined that the section 1400Z–2 regulations provide appropriate flexibility to facilitate the development of projects and economic activity that extend beyond the geographic boundaries of QOZs. The commenter's recommendation, if adopted, would exceed that degree of flexibility and in certain cases potentially conflict with locational requirements of section 1400Z–2.

Q. Application of Section 1397C Requirements and Safe Harbors to QOFs

The October 2018 and May 2019 proposed regulations provided safe harbors to address requirements described in section 1397C that trades or businesses must satisfy to qualify as qualified opportunity zone businesses. These safe harbors, including the 31-month working capital safe harbor and the active trade or business safe harbors, did not specifically apply to QOFs. Several commenters requested clarification regarding whether such requirements described in section 1397C for qualified opportunity zone businesses also apply to QOFs. Many commenters suggested that, while QOFs should not be subject to statutory requirements imposed on qualified opportunity zone businesses, QOFs should be permitted to apply safe harbors that address section 1397C requirements. In addition, two commenters suggested that the 31-month working capital safe harbor should be made available to a QOF that otherwise meets the requirements for the safe harbor.

The Treasury Department and the IRS note that the text of section 1400Z–2 does not support the application of the section 1397C requirements to QOFs, but rather limits the application of those requirements to qualified opportunity zone businesses. Consequently, the Treasury Department and the IRS have concluded that any safe harbor made available under the proposed regulations to address a section 1397C requirement imposed on a qualified opportunity zone business likewise should not be extended to QOFs. As a result, the final regulations do not incorporate the commenters' recommendations.

R. Consideration of QOF Reliance Rule Regarding Satisfaction of Qualified Opportunity Zone Business Requirements

Commenters have requested that the final regulations provide a special QOF reliance rule. Such rule would provide that an entity may be treated as a qualified opportunity zone business for the duration of a QOF's ownership of the stock or partnership interest in that entity if, at the time the QOF acquires its interest in the trade or business, (i) the QOF does not have control over the trade or business and (ii) the QOF reasonably expects the entity will satisfy each requirements described in section 1400Z–2(d)(3) to qualify as a qualified opportunity zone business.

The Treasury Department and the IRS note that, for stock or a partnership interest to be treated as qualified opportunity zone property and counted toward the 90-percent investment standard, the trade or business must meet the requirements of section 1400Z–2(d)(3). A QOF is responsible for ensuring that the requirements of section 1400Z–2(d)(3) are met when reporting the value of the QOF's assets on Form 8996. Therefore, the Treasury Department and the IRS decline to accept the commenter's suggestion.

S. Certain Businesses Described in Section 144(c)(6) Not Eligible To Be Qualified Opportunity Zone Businesses

Section 1400Z–2(d)(3)(A)(iii) provides that the term ''qualified opportunity zone business'' means a trade or business that, in addition to satisfying other requirements described in section 1400Z–2(d)(3)(A), is not a business described in section 144(c)(6)(B) (commonly referred to as a ''sin business''). Section 144(c)(6)(B) lists as a sin business any (i) private or commercial golf course, (ii) country club, (iii) massage parlor, (iv) hot tub facility, (v) suntan facility, (vi) racetrack or other facility used for gambling, or (vii) store the principal business of which is the sale of alcoholic beverages for consumption off premises. Section 1400Z–2(d)(1), which sets forth the definitional requirements for a QOF, does not prohibit QOFs from directly conducting section 144(c)(6)(B) sin businesses.

1. Consideration of General Application and Adoption of de minimis Threshold

The Treasury Department and the IRS have received several comments regarding the general application of the sin business prohibition. Many commenters have emphasized that section 1400Z–2 explicitly prohibits qualified opportunity zone businesses from being a sin business, but sets forth no such prohibition for QOFs. These commenters also have noted, however, that section 1400Z–2 does not contain any specific provision that prohibits a qualified opportunity zone business from leasing property to a sin business. In addition, commenters have contended that a de minimis use of property in any sin business should not, on its own, prevent that property from qualifying as qualified opportunity zone business property of a QOF. Similarly, commenters recommended that the final regulations provide rules prohibiting a qualified opportunity zone business from leasing more than a de minimis amount of its property to a sin business. These commenters emphasized that section 1400Z–2(d)(3)(A)(iii) clearly conveyed Congress' intent that a qualified opportunity zone business should not be a sin business, and therefore should not be permitted to circumvent the substance of the sin business prohibition simply through leasing its property to such business.

The Treasury Department and the IRS appreciate all of the comments

submitted on this issue. First, the final regulations do not extend the prohibition on sin businesses to the definition of a QOF because, as highlighted by several commenters, section 1400Z–2 explicitly prohibits qualified opportunity zone businesses from operating sin businesses, but sets forth no similar prohibition for QOFs. See section 1400Z–2(d)(3)(A)(iii) (setting forth sin business prohibition for qualified opportunity zone businesses); section 1400Z–2(d)(1) (providing QOF definition). In addition, the Treasury Department and the IRS agree that section 1400Z–2 does not explicitly prohibit a qualified opportunity zone business from leasing its property to a sin business. However, the Treasury Department and the IRS have determined that the purpose of section 1400Z–2(d)(3)(A)(iii) is to prevent qualified opportunity zone businesses from operating sin businesses, which a qualified opportunity zone business nonetheless could carry out simply by leasing such property to a sin business. To ensure that the purpose of section 1400Z–2(d)(3)(A)(iii) is effectuated, the final regulations prohibit a qualified opportunity zone business from leasing more than five percent of its property to a sin business. The Treasury Department and the IRS have determined that this de minimis threshold will reduce the risk of a qualified opportunity zone business inadvertently violating the sin business prohibition.

2. Consideration of Request for Additional Detail Regarding ''Sin Business'' Qualification

Commenters also requested that the final regulations provide additional detail regarding the spectrum of businesses covered by the descriptions set forth in section 144(c)(6)(B). One commenter requested confirmation that the ''alcoholic beverage'' restriction be limited to the clear meaning of a traditional ''liquor store'' that sells alcoholic beverages to customers for consumption off premises, but not to restaurants, wineries, breweries, or distilleries. Another commenter requested clarification that full-service spa facilities operated in hotels and other similar properties do not constitute prohibited sin businesses.

The Treasury Department and the IRS agree with the commenters that additional detail regarding the qualification of a business as a ''sin business'' would be helpful in certain cases. However, the Treasury Department and the IRS have determined that the rules suggested by the commenters, as well as similar provisions, would inject significant complexity into the final regulations and likely cause additional uncertainty regarding the scope of the term ''sin business'' due to its inherently factual nature. As a result, the final regulations do not incorporate the commenters' recommendations.

U. Tangible Property That Ceases To Be Qualified Opportunity Zone Business Property

Section 1400Z–2(d)(3)(B) provides a special rule that permits a qualified opportunity zone business to treat tangible property that ceases to be qualified opportunity zone business property as qualified opportunity zone business property for the lesser of five years after (i) the date on which such tangible property ceases to be so qualified, or (ii) the date on which such tangible property is no longer held by the qualified opportunity zone business. The phrase ''ceases to be qualified opportunity zone business property'' indicates that the tangible property must have been used in a trade or business for a period of time. The Treasury Department and the IRS have determined that tangible property must have been qualified opportunity zone business property used in a trade or business for at least two years.

Therefore, the final regulations provide that a qualified opportunity zone business may apply section 1400Z–2(d)(3)(B) only if the qualified opportunity zone business property was qualified opportunity zone business property used by a qualified opportunity zone business in a QOZ for at least two years. Further, to ensure that only qualified opportunity zone business property used in a qualified opportunity zone business is eligible for the benefits of section 1400Z–2(d)(3)(B), the final regulations provide that the 31-month working capital safe harbor period and the 30-month substantial improvement period pursuant to which tangible property may be treated as qualified opportunity zone business property for purposes of the 70-percent tangible property standard, are not taken into consideration in determining whether property meets the requirements for eligibility under section 1400Z–2(d)(3)(B).

V. Exceptions Based on Location in Which an Entity Is Created, Formed or Organized

The proposed regulations clarified that a QOF must be an entity classified as a corporation or partnership for Federal tax purposes. In addition, a QOF must be created or organized in one of the 50 states, the District of Columbia, or a U.S. territory, or organized under the laws of an Indian tribal government. If an entity is organized in a U.S. territory but not in one of the 50 states or in the District of Columbia, then the entity may be a QOF only if the entity is organized for the purpose of investing in qualified opportunity zone property that relates to a trade or business operated in the territory in which the entity is organized.

The proposed regulations further clarified that qualified opportunity zone property may include stock or a partnership interest in an entity classified as a corporation or partnership for Federal income tax purposes. In addition, that entity must be a corporation or partnership created or organized in, or under the laws of, one of the 50 states, the District of Columbia, or a U.S. territory, or organized under the laws of an Indian tribal government. If an entity is organized in a U.S. territory but not in one of the 50 states or in the District of Columbia, then an equity interest in the entity may be a qualified opportunity property only if the entity conducts a qualified opportunity zone business in the U.S. territory in which the entity is organized.

The proposed regulations defined a U.S. possession, now referred to as a U.S. territory, to mean any jurisdiction outside of the 50 states and the District of Columbia in which a designated QOZ exists under section 1400Z–1. This definition includes the following jurisdictions: (1) American Samoa, (2) Guam, (3) the Commonwealth of the Northern Mariana Islands, (4) the Commonwealth of Puerto Rico, and (5) the U.S. Virgin Islands.

Certain comments discussed the interaction between the section 1400Z–2 rules and the rules for taxation of controlled foreign corporations (as defined in section 957) (CFCs). One commenter requested the basis for the proposed rule requiring that a QOF be organized in one of the 50 states, District of Columbia, or a U.S. territory, but did not request any change. Other than for clarifying that an entity qualifying as a QOF or qualified opportunity zone business can be organized under the laws of an Indian tribal government, this rule is being finalized without change. This rule was proposed due to the difficulty of tracking whether a foreign entity continuously satisfies the requirements for QOF status. Additionally, a foreign entity may not be subject to Federal income tax; thus, imposing the penalty under section 1400Z–2(f)(1) if the entity

fails to maintain the 90-percent investment standard set forth in section 1400Z–2(d)(1) could be difficult. Finally, a foreign entity is unlikely to be a QOF given the requirement that a QOF must invest almost exclusively in QOZs, which must themselves be located only in the United States and U.S. territories.

As noted previously, although a QOF cannot be an entity organized in a foreign country, it can be an entity organized in a U.S. territory. A corporation organized in a U.S. territory is treated as a CFC on a given day if the ownership requirements in section 957 are satisfied on that day. A United States shareholder (as defined in section 951(b)) of a CFC generally includes in gross income, for its taxable year in which or with which the CFC's taxable year ends, its pro rata share of the CFC's subpart F income (as defined in section 952) under section 951(a) (subpart F regime), as well as the United States shareholder's global intangible low-taxed income under section 951A(a) (GILTI regime), which is based on the tested income (as defined in section 951A(c)(2)(A)) of the CFC and other items relevant to determining the amount of the United States shareholder's inclusion in gross income under section 951A(a).

The proposed rules relating to entities organized in U.S. territories are adopted without change.

VI. Comments on and Changes to Proposed § 1.1400Z2(e)–1

Proposed § 1.1400Z2(e)–1 provided rules regarding mixed-funds investments. This part VI of this Summary of Comments and Explanation of Revisions addresses comments regarding proposed § 1.1400Z2(e)–1 as well as comments regarding provisions of section 1400Z–2(e) that were not addressed in the proposed regulations, such as the definition of ''related persons'' in section 1400Z–2(e)(2). For a discussion of whether certain transactions between investors and QOFs or qualified opportunity zone businesses are treated as transactions between related persons, see part II.A.1.d of this Summary of Comments and Explanation of Revisions.

A. Related Persons and the Step Transaction Doctrine

Section 1400Z–2(e)(2) provides that, for purposes of section 1400Z–2, parties are ''related'' if their relationship satisfies either section 267(b) or 707(b)(1), with the threshold for relatedness lowered from 50 percent to 20 percent. This definition applies to two categories of transactions. First, eligible gain must arise from a sale or exchange with an unrelated party. See section 1400Z–2(a)(1) and proposed § 1.1400Z2(a)–1(b)(2)(i)(C). Second, in order for tangible property to qualify as qualified opportunity zone business property, a QOF or qualified opportunity zone business must acquire the subject tangible property from an unrelated party. See section 1400Z–2(d)(2)(D)(i)(I) and proposed § 1.1400Z2(d)–1(c)(4)(i)(A). The proposed regulations did not further elaborate on the statutory definition of ''relatedness.''

One commenter recommended that a sale be considered to take place between unrelated parties for purposes of section 1400Z–2 and the section 1400Z–2 regulations if, as part of an overall plan, the seller and buyer become unrelated in a series of transactions that includes the tested sale. The commenter noted that certain other income tax regulations determine ''relatedness'' after the last step in a series of related transactions and advocated a similar rule in the section 1400Z–2 regulations.

The Treasury Department and the IRS have determined that all relevant provisions of the Code and general principles of tax law, including the step transaction doctrine, govern the determination whether a transaction is between unrelated parties for purposes of section 1400Z–2 and the section 1400Z–2 regulations. Accordingly, the final regulations do not include a specific step transaction rule as requested by the commenter.

B. Non-Qualifying Investment in a QOF Corporation for Which No Stock Is Received

Commenters requested clarification regarding the treatment of mixed-funds investments in QOF corporations. More specifically, commenters asked for clarification regarding situations in which a shareholder with a qualifying investment in a QOF corporation makes a non-qualifying investment in the QOF but receives no stock in exchange (that is, a meaningless-gesture contribution). One commenter requested confirmation that the shareholder in such situations has a mixed-funds investment, and that the basis in the non-qualifying investment is determined without regard to section 1400Z–2(b)(2)(B). Another commenter questioned whether the shareholder would have two implicit blocks of stock in the QOF, with separate basis determinations and with distributions and redemptions being apportioned between the qualifying and non-qualifying blocks of stock (analogous to the result under the special rules for QOF partnerships discussed in part III.E.1 of this Summary of Comments and Explanation of Revisions), or whether each share of QOF stock would have an identical basis under general Federal income tax principles.

The final regulations confirm that a meaningless-gesture contribution results in a mixed-funds investment. However, the Treasury Department and the IRS have determined that addressing the foregoing questions regarding basis in a mixed-funds investment in a QOF corporation is beyond the scope of the final regulations. The Treasury Department and the IRS continue to study such issues. See REG–143686–07, 84 FR 11686 (March 28, 2019).

VII. Comments on and Changes to Proposed § 1.1400Z2(f)–1

Proposed § 1.1400Z2(f)–1 prescribed rules for QOFs that fail to maintain the 90-percent investment standard of section 1400Z–2(d)(1) and proposed § 1.1400Z2(d)–1. In particular, proposed § 1.1400Z2(f)–1(b) specified the time period in which proceeds must be reinvested in qualifying property, and proposed § 1.1400Z2(f)–1(c) provided a general anti-abuse rule.

A. Time Period for a QOF To Reinvest Proceeds

1. Reinvestment

Section 1400Z–2(e)(4)(B) provides that the Secretary shall prescribe such regulations as may be necessary or appropriate to ensure that a QOF has a reasonable period of time to reinvest the return of capital from investments in qualified opportunity zone property and to reinvest proceeds received from sale or disposition of qualified opportunity zone property. To this end, proposed § 1.1400Z2(f)–1(b) provided that if a QOF received proceeds from the return of capital or the sale or disposition of some or all of its qualified opportunity zone property, and if the QOF reinvested some or all of the proceeds in qualified opportunity zone property by the last day of the 12-month period beginning on the date of the distribution, sale, or disposition, then the proceeds were treated as qualified opportunity zone property in evaluating whether the QOF satisfied the 90-percent investment standard, but only to the extent the proceeds were continuously held in cash, cash equivalents or debt instruments with a term of 18-months or less. Several commenters have requested modifications to this reinvestment rule for QOFs.

In the proposed regulations, the Treasury Department and the IRS requested comments addressing

whether an analogous rule for qualified opportunity zone businesses would be beneficial. Multiple commenters have requested an extension of this QOF reinvestment rule to qualified opportunity zone businesses so that certain dispositions of qualified opportunity zone business property would not adversely affect satisfaction of the 70-percent tangible property standard in section 1400Z–2(d)(3)(A)(i). The primary argument for the extension of the QOF reinvestment rule to qualified opportunity zone businesses is that like a QOF, a qualified opportunity zone business may dispose of assets and reinvest proceeds in other qualified opportunity zone business property. These commenters assert that a qualified opportunity zone business in the course of its business operations is more likely to acquire and dispose of assets than the QOF itself.

Because section 1400Z–2(e)(4)(B) specifically directs the Secretary to prescribe regulations relating to the time period for QOFs to reinvest proceeds from the sale of qualified opportunity zone property and does not explicitly refer to qualified opportunity zone businesses, the Treasury Department and the IRS decline to extend this reinvestment concept to similar dispositions by a qualified opportunity zone business. However, qualified opportunity zone businesses may avail themselves of the working capital safe harbor to enable proceeds to qualify as qualified opportunity zone business property.

Proposed § 1.1400Z2(f)–1(b) also provides that the 12-month reinvestment period is tolled while waiting on government action if the QOF has completed the application for action and is awaiting a government response. A commenter requested that the time period for waiting on government action be expanded to 24 months if a state of emergency is declared by the federal government in the jurisdiction in which the qualified opportunity zone property is located. The Treasury Department and the IRS agree that the reinvestment period should be expanded if additional delays are caused by a Federally declared natural disaster, and have modified the rules relating to the reinvestment period to allow for such expansion. However, a QOF must invest proceeds as originally planned before the disaster. For example, if a QOF is unable to invest in a certain qualified opportunity zone business property because the property is located in a Federally declared disaster area, the QOF must invest the proceeds in similar property located in that QOZ.

2. Nonrecognition Provisions and Their Application to Section 1400Z–2

In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments identifying prior examples of tax regulations that would exclude from gross income gain from the sale or disposition of assets held by a QOF or qualified opportunity zone business without an operative statutory nonrecognition provision. Other code sections that permit nonrecognition of income or gain have operative language permitting nonrecognition. In response, one commenter recommended a rule that would exclude from gross income the gain from the disposition of assets by a QOF if the gain was reinvested in ''qualifying assets'' within a 180-day period after the disposition. In support of this recommendation, the commenter explained that such a rule would encourage reinvestment in assets located in the areas designated as QOZs. A second commenter submitted a similar recommendation with an additional suggestion that to qualify for nonrecognition treatment on the disposition of assets, a QOF or qualified opportunity zone business must satisfy a minimum holding period for the qualified opportunity zone property or qualified opportunity zone business property. Another commenter suggested that nonrecognition treatment for the disposition of QOF or qualified opportunity zone business assets should follow the principles of sections 1031 and 1033. This commenter cited § 1.1031(k)–1 with its qualified intermediary rules as an example of a regulation that expands the scope of the underlying Code section. While the Treasury Department and the IRS understand that such a rule would provide additional benefits for QOFs and qualified opportunity zone businesses, the statutory regime permits gain deferral only at the QOF owner level; section 1400Z–2 does not contemplate nonrecognition of gain arising from transactions at any other level. Consequently, in order for a QOF or qualified opportunity zone business to receive nonrecognition treatment on the disposition of assets, the disposition must qualify for nonrecognition treatment under another provision of subtitle A. Accordingly, the Treasury Department and the IRS do not adopt this recommendation.

B. Land Banking

As provided in Rev. Rul. 2018–29, 2019 I.R.B. 45, and the proposed regulations, land that is purchased and located within a qualified opportunity zone is not subject to either the original use requirement under section 1400Z–2(d)(2)(D)(i)(II) or the substantial improvement requirement under sections 1400Z–2(d)(2)(D)(i)(II) and 1400Z–2(d)(2)(D)(ii). See additional discussion at V.H, and V.I, of this Summary of Comments and Explanation of Revisions. However, in certain circumstances, unimproved land might be held in a manner that is inconsistent with the purposes of section 1400Z–2, such as if a parcel of unimproved land does not receive new capital investment or is not the subject of increased economic activity or output. As a result, the Treasury Department and the IRS have requested and received comments related to the application of the anti-abuse rule under section 1400Z–2(e)(4)(C) to so-called ''land banking'' and similar arrangements in addition to the general anti-abuse rule in proposed 1.1400Z2(f)–1(c).

Some commenters objected to the use of the term ''land banking'' to describe the practice of holding land primarily for speculative investment and without an intention to develop a trade or business on that land and similar arrangements. These commenters noted that a commonly used second definition of the term land banking involves certain arrangements whereby a local government may acquire real property and convert the property to productive use, or hold the properties for long-term strategic purposes with the objective of community development rather than to earn a profit. The Treasury Department and the IRS recognize that the use of the term ''land banking'' in the final regulations may cause confusion with this second definition. In response to this comment, these final regulations do not use the term ''land banking'' or another alternate term and instead describe the non-qualifying arrangements as holding land for speculative investment.

Several commenters requested that the final regulations explicitly identify the policy reasons that holding land for speculative investment is inconsistent with the purposes of section 1400Z–2. Commenters also requested specific examples of land use that would be abusive under the regulations. Some commenters recommended that specific types of land use be enumerated as per se abusive including long-term holding of vacant land and speculative passive holding of vacant land. Another commenter recommended an anti-abuse rule that would prohibit arrangements that only marginally improve land while providing a significant tax benefit to investors without a clear and direct economic benefit to the community.

Other commenters requested an explicit definition for the arrangements that constitute holding land for speculative investment. Several commenters requested and recommended a standard for the use of land that would be considered abusive. Multiple commenters indicated that such an anti-abuse standard should incorporate the principles of proposed § 1.1400Z2(d)–1(f), which provides that a QOF may not rely on the proposed rules for qualified opportunity zone property in proposed § 1.1400Z2(d)–1(c)(8)(ii)(B) and (d)(4)(ii)(B) if land is unimproved or minimally improved and the QOF or qualified opportunity zone business purchases the land with an expectation, an intention, or a view not to improve the land by more than an insubstantial amount within 30 months after the date of purchase. Regarding the minimal improvement or insubstantial improvement standard, commenters requested that the final regulations include either a bright-line threshold or provide examples of insubstantial improvement to land. In addition to a bright-line threshold for insubstantial improvement, one commenter suggested that the final regulations require that QOFs or qualified opportunity zone businesses provide a timeline for the improvements to be made on the unimproved land.

One commenter provided an illustration of a potentially problematic fact pattern in which a taxpayer, a QOF or a qualified opportunity zone business, constructs a small shed for use by an attendant on a parking lot and charges customers to park on the lot which is, except for the attendant's shed, vacant land. According to the commenter, this example may represent improvements that fall in the range between insubstantial and substantial improvement and would not be captured by a rule that prohibits the practice of holding unimproved land merely for passive investment due to the profit motivated trade or business activities on the lot. By contrast, referring to a similar fact pattern, another commenter provided an analysis that the proposed regulations were sufficient to thwart speculative land investment of this type. The commenter suggested that there were two existing proposed rules that would apply to such an arrangement (1) the requirement that tangible property must be used in the trade or business of a QOF or a qualified opportunity zone business to be considered qualified opportunity zone business property; and (2) the general anti-abuse rule in proposed § 1.1400Z2(f)–1(c). Under the commenter's analysis, the parking lot fact pattern would meet the trade or business standard; however, under the general anti-abuse rule, a significant purpose of the transaction would be a speculative investment purpose, therefore, the arrangement could be recast.

The Treasury Department and the IRS have provided examples to illustrate the application of the general anti-abuse rule to two fact patterns related to the acquisition of land that multiple commenters have indicated require additional guidance. The first example involves a taxpayer that establishes a parking lot business on a land parcel in a QOZ. The second example involves a taxpayer that acquires farmland, repurposes the land for a different principal business activity, and makes a significant investment of capital and labor into that new business. In the parking lot example, notwithstanding the fact that the business has built small structures on an otherwise empty lot, because a significant purpose for the acquisition of the land is to hold the land for speculative investment, the anti-abuse rule functions to recharacterize the transaction so that the taxpayer may not receive the benefits of section 1400Z–2. By contrast, in the second example, the taxpayer's post-acquisition investment tends to show that land is being used to develop an operating business in the QOZ, rather than merely being held with a minimum level of activity to reap the benefit of appreciation on what is essentially bare land. These examples serve to reiterate the guiding principle that land held for speculative purposes does not further the purposes of section 1400Z–2 and the section 1400Z–2 regulations.

C. General Anti-Abuse Rule

A number of comments addressed the anti-abuse rule of proposed § 1.1400Z2(f)–1(c), which provides that section 1400Z–2 and the 1400Z–2 regulations must be applied in a manner consistent with the purposes of section 1400Z–2. To this end, if a significant purpose of a transaction is to achieve a tax result that is inconsistent with the purposes of section 1400Z–2, then the proposed regulations provided that the Commissioner can recast a transaction to achieve consistency with the purposes of section 1400Z–2. The determination of whether a tax result is inconsistent with the purposes of section 1400Z–2 requires a facts and circumstances analysis.

Many commenters requested an articulation of the purposes of section 1400Z–2 to assist taxpayers in avoiding a recast of their transaction. The Treasury Department and the IRS have determined that the purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and qualified opportunity zone businesses, of new capital in one or more QOZs and to increase the economic growth of such QOZs. Therefore, these purposes have been included in the text of the anti-abuse rule in the final regulations.

Another commenter requested a safe harbor from the anti-abuse rule for failure to comply with the rules, where the entity's efforts are in good faith. The Treasury Department and the IRS disagree that the purposes of section 1400Z–2 are so elusive that a good faith attempt to comply with the rules would be subject to the anti-abuse rule. As stated previously, the purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and qualified opportunity zone businesses, of new capital in one or more QOZs and to increase the economic growth of such QOZs. Accordingly, the Treasury Department and the IRS decline to provide a good faith exception.

Several commenters requested enumeration of specific instances of per se abuse. Items that might be on this list include: Non-qualifying investments; a specific rule to ensure that taxpayers do not exploit the inventory safe harbor to evade the 90-percent investment standard for QOFs or the 70-percent tangible property standard; and a rule, similar to an ''anti-stuffing'' rule, that establishes that certain transactions undertaken to qualify property as qualified opportunity zone property, but with transitory effect, would be deemed abusive.

Other commenters suggested adding to the list of per se abuses activities that would be harmful to the community in which the QOF or qualified opportunity zone business operates, such as dramatically increased rents, a high number of tenant evictions, lack of direct or sustained community benefit, and activities not vetted by community or local government and that result in a dislocation of community residents. To this end, several commenters suggested that QOFs and qualified opportunity zone businesses identify, *ex ante,* one or more beneficial community outcomes that the QOF and qualified opportunity zone businesses intend to achieve. These outcomes would include creating quality jobs, developing affordable housing, and investing in community

facilities that benefit low-income residents of the community. One commenter recommended a safe harbor from the anti-abuse provision for QOFs that receive third party certification demonstrating the QOF's public benefit. The commenter cited benefit corporation legislation and standards under the Small Business Administration as precedent for this approach.

The Treasury Department and the IRS are appreciative of the comments received on the anti-abuse provision. Accordingly, several examples of the operation of the general anti-abuse rule have been included in the final regulations.

VIII. Comments on and Changes to Proposed § 1.1400Z2(g)–1

Proposed § 1.1400Z2(g)–1 prescribed rules regarding the Federal income tax treatment of QOFs owned by members of consolidated groups.

A. Section 1400Z–2 and the Consolidated Return Regulations

As discussed in part II.A.1 of this Summary of Comments and Explanation of Revisions, section 1400Z–2 and the section 1400Z–2 regulations permit the deferral of eligible gain when a taxpayer makes a qualifying investment in a QOF. The deferred gain is tracked by the taxpayer's basis in its qualifying investment and is included in gross income upon an inclusion event.

Section 1501 provides that an affiliated group of corporations, as defined in section 1504, may elect to file a consolidated income tax return. The regulations under section 1502 provide rules applicable to consolidated groups. Many of the consolidated return provisions aim to treat members of a consolidated group as a single entity. For example, the investment adjustment rules under § 1.1502–32 affect the determination of members' basis in the stock of subsidiary members. The purpose of the investment adjustment rules is to treat the consolidated group as a single entity by ensuring that members' items of income, gain, deduction, and loss are taken into account by the tax system once, and only once.

As stated in the preamble to the May 2019 proposed regulations, the respective frameworks of section 1400Z–2 and the consolidated return regulations are incompatible in many respects. The preamble emphasized that special rules would be required to harmonize the policy objectives of sections 1400Z–2 and 1502; for example, special rules would be required under §§ 1.1502–13, 1.1502–19, and 1.1502–32. For this reason, among others, the Treasury Department and the IRS proposed treating stock of a QOF C corporation as not stock for purposes of section 1504. Accordingly, under the May 2019 proposed regulations, a QOF C corporation could be the common parent of a consolidated group but could not be a subsidiary member of the consolidated group. However, the Treasury Department and the IRS requested comments on whether the burden of potentially applying two different sets of consolidated return rules would be outweighed by the benefits of permitting QOF C corporations to be subsidiary members of consolidated groups.

The Treasury Department and the IRS received numerous comments regarding the consolidated return rules in the May 2019 proposed regulations. For example, as a procedural matter, commenters recommended moving these rules to the regulations under sections 1502 and 1504. The Treasury Department and the IRS agree with this recommendation and have moved the rules regarding the Federal income tax treatment of QOFs owned by members of consolidated groups from § 1.1400Z2(g)–1 to §§ 1.1502–14Z and 1.1504–3.

Part VIII.B.1 of this Summary of Comments and Explanation of Revisions sets forth summaries of the comments received with respect to the consolidated return rules in the May 2019 proposed regulations. The remainder of part VIII of this Summary of Comments and Explanation of Revisions provides the responses of the Treasury Department and the IRS and describes the revisions adopted in the final regulations.

B. QOF C Corporation as a Subsidiary Member of a Consolidated Group

1. Comments on Consolidating Subsidiary QOF C Corporations

Commenters requested generally that QOF C corporations be permitted to join in the filing of consolidated income tax returns as subsidiary members. The commenters maintained that, if consolidation of subsidiary QOF C corporations were permitted, investors would possess greater flexibility to structure and manage qualifying investments, which would result in increased investment in QOZs. Consistent with the preamble to the May 2019 proposed regulations, commenters acknowledged that, if a QOF C corporation could be a subsidiary member of a consolidated group (QOF member), special rules might be needed under § 1.1502–13 (regarding intercompany transactions), § 1.1502–19 (regarding excess loss accounts, or ELAs), and § 1.1502–32 (regarding stock basis adjustments). In particular, commenters suggested adopting rules similar to the rules in proposed § 1.1400Z2(b)–1(e)(4) for pass-through entities to resolve complications arising from the interaction of section 1400Z–2 and § 1.1502–32.

Commenters also suggested alternatives to a blanket permission for QOF corporations to be subsidiary members of a consolidated group. For example, some commenters requested that subsidiary QOF C corporations formed as members of, or acquired by, a consolidated group prior to the publication of the May 2019 proposed regulations (pre-existing QOF subs) be permitted to continue as QOF members. Commenters argued that, even if the Treasury Department and the IRS decline to generally allow the consolidation of subsidiary QOF C corporations, grandfathering these pre-existing QOF subs would be appropriate. Those commenters stressed that many taxpayers had evaluated, structured, and completed transactions prior to the issuance of the May 2019 proposed regulations based on the assumption that subsidiary QOF C corporations could join in the filing of consolidated returns. One commenter suggested that QOF members formed within a reasonable grace period after the issuance of the May 2019 proposed regulations also be grandfathered.

As a second alternative, commenters requested that taxpayers be allowed to convert their QOF members into partnerships and treat those entities as partnerships retroactive to the date of the qualifying investment. These commenters also requested that the final regulations provide rules to ensure that such restructuring would not constitute an inclusion event. Similarly, commenters requested that taxpayers be allowed to retroactively treat a QOF C corporation either as a nonmember of a consolidated group or as a member of the consolidated group that is not a QOF.

Commenters also requested rules detailing the consequences of deconsolidating pre-existing QOF subs if the Treasury Department and the IRS decline to allow pre-existing QOF subs to remain members of the consolidated group. The commenters requested that the deconsolidation event not be treated as an inclusion event and suggested multiple approaches with regard to stock basis adjustments, ELA inclusions, application of the unified loss rule, and other issues on deconsolidation.

2. Election To Consolidate a Subsidiary QOF C Corporation

As discussed in part VIII.B.1 of this Summary of Comments and Explanation of Revisions, commenters requested that subsidiary QOF C corporations be permitted to join in the filing of consolidated returns while acknowledging that additional rules may be required to harmonize the operation of section 1400Z–2 and the consolidated return regulations. In response to these comments, the final regulations permit the consolidation of subsidiary QOF C corporations, subject to certain conditions. The final regulations also include special rules to coordinate the simultaneous application of section 1400Z–2 and the consolidated return regulations to QOF members.

a. Conditions To Consolidate a Subsidiary QOF C Corporation

These final regulations permit the consolidation of a subsidiary QOF C corporation only if certain conditions are satisfied. Specifically, except in very limited circumstances, and consistent with the general principles of section 1400Z–2, the consolidated group member that makes the qualifying investment in the QOF member (QOF investor member) must maintain a direct equity interest in the QOF member. In addition, the final regulations require all QOF investor members to be wholly owned, directly or indirectly, by the common parent of the consolidated group. The Treasury Department and the IRS have determined that these conditions will help preserve the integrity of the consolidated return regulations and ensure that taxpayers apply section 1400Z–2 and the section 1400Z–2 regulations in a manner consistent with the policies underlying section 1400Z–2 and the consolidated return regulations.

Failure to satisfy either of the foregoing conditions for consolidation will result in the deconsolidation of the QOF member. Part VIII.B.4 of this Summary of Comments and Explanation of Revisions describes the Federal income tax consequences of deconsolidation of a QOF member.

i. Direct Ownership Requirement

Section 1400Z–2 sets forth a general requirement that a QOF owner must retain its direct qualifying investment in a QOF in order to retain the benefits of that section. See § 1.1400Z2(b)–1(c) and part III.A of this Summary of Comments and Explanation of Revisions; see also the preamble to the May 2019 proposed regulations. Accordingly, to consolidate a subsidiary QOF C corporation, the investor member generally must retain direct ownership of the QOF stock of the QOF member (QOF member stock). In addition, the QOF investor member generally is subject to the same rules regarding inclusion events as an investor in a non-member QOF. However, the final regulations provide a limited exception for certain transfers of QOF member stock that are treated as intercompany transactions and are eligible for single-entity treatment. See part VIII.C.3 of this Summary of Comments and Explanation of Revisions for a discussion of this limited exception.

The direct ownership requirement is not a section 1502-specific rule, for this requirement generally applies outside of consolidation as well. The operation of the section 1400Z–2 rules requires close monitoring of a QOF owner's basis in the qualifying investment. See generally part III.G of this Summary of Comments and Explanation of Revisions. Moreover, as noted in the preamble to the May 2019 proposed regulations, application of the investment adjustment rules of § 1.1502–32 results in substantial and ongoing stock basis adjustments to QOF member stock that are unrelated to the rules and policies of section 1400Z–2 and that complicate the operation of section 1400Z–2 in the consolidated group context. In addition, the transfer of QOF member stock between consolidated group members, and across ownership chains, further increases the complexity of appropriately tracking the QOF investor member's basis in its QOF member stock. Therefore, the Treasury Department and the IRS have determined that applying the general rule in § 1.1400Z2(b)–1(c) (regarding dispositions of qualifying investments) inside the consolidated group, by imposing the direct ownership requirement on the QOF investor member, would simplify the administration of section 1400Z–2 to QOF members. But see part VIII.C.3 of this Summary of Comments and Explanation of Revisions for a discussion of an exception to the general rule for certain intercompany sales of qualifying investments.

ii. Wholly Owned QOF Investor Member

The requirement that each QOF investor member itself be wholly owned, directly or indirectly, by the common parent of the consolidated group further serves to prevent uneconomic or other inappropriate outcomes that otherwise might be achieved through the interaction of sections 1400Z–2 and 1502.

Under the general affiliation rules, to be a member of a consolidated group, an includible corporation need not be wholly owned. Instead, only 80 percent of the vote and value of the stock of an includible corporation must be owned directly by other consolidated group members. Therefore, an includible corporation that is owned 80 percent by members of a consolidated group and 20 percent by non-members can be a member of the consolidated group (80/20 member).

The final regulations impose a stricter requirement for the ownership of QOF investor members to ensure the application of the inclusion rules of section 1400Z–2(b) conforms to the policy underlying section 1400Z–2. As emphasized in part III.G of this Summary of Comments and Explanation of Revisions, the application of key provisions under section 1400Z–2 depends upon a close monitoring of the basis of the qualifying investment in the hands of the QOF owner. If QOF investor members were not required to be wholly owned, a consolidated group effectively could alienate and monetize a substantial portion of its qualifying investment by selling shares in QOF investor members or in higher-tier members in a QOF investor member's ownership chain, but the consolidated group would continue to enjoy section 1400Z–2 benefits because direct ownership of the qualifying investment would not change hands. The requirement that each QOF investor member be wholly owned, directly or indirectly, by the common parent also limits incongruities in the application of § 1.1502–32 to an ownership chain that includes a QOF member. Both of these issues are discussed later in this part VIII.B.2.a of this Summary of Comments and Explanation of Revisions.

Under § 1.1502–76(b), a consolidated group includes in its computation of taxable income all income, gain, deduction, and loss items of a consolidated group member, regardless of the percentage of the member's stock that is directly or indirectly (economically) held by the common parent. However, under § 1.1502–32, the investment adjustments that are made to the stock of that member (and up the chain through tiers of stock ownership to the common parent) reflect only the pro rata stock ownership held at each tier. For example, assume that the common parent owns 80 percent of another member (R) (an 80/20 member), which owns 80 percent of the QOF investor member (also an 80/20 member), which wholly owns the QOF member. In that case, the consolidated group's use of a $100 loss of the QOF

member would result in an $80 reduction of basis in the stock of the QOF investor member held by R, but only a $64 reduction of basis in the stock of R held by the common parent. Adding a third 80/20 member to the QOF member's ownership chain would result in a 51 percent indirect interest, and adding a fourth 80/20 member would result in a 41 percent indirect interest, thereby further reducing the extent to which the QOF member's tax items used by the consolidated group are reflected in stock basis up the chain.

The facial incongruity between the full inclusion of taxable items and the pro rata adjustment to stock basis generally does not upset the equilibrium of the consolidated return system because the rules apply to income and gain as well as deduction and loss items. In other words, even though a consolidated group may receive an overstated benefit in the case of loss and deduction items (that is, full use of a member's loss with only a pro rata decrease in the basis of the member's stock), the consolidated group also must take into account all of a member's income despite holding less than all of the member's stock (and getting only a pro rata increase in the basis of the member's stock). Over the course of years, this situation generally will remain in balance.

However, the interaction of the foregoing rules with the rules under section 1400Z–2 upsets this balance in the case of 80/20 members with outside investors. In fact, the exclusion of gain under section 1400Z–2(c) upon the sale or exchange of a qualifying investment not only ensures that there will be no balancing over the course of years, but also may offer opportunities to magnify the imbalance.

The Treasury Department and the IRS are aware that, outside of consolidation, taxpayers can monetize the value of a qualifying investment by selling an indirect interest in the QOF (that is, stock in the QOF owner). However, in that case, the QOF owner would retain all of its ownership of the qualifying investment. Because the consolidated group computes its taxable income and tax liability as a single entity (headed by the common parent), the sale of a portion of the indirect interest in the QOF member out from under the common parent is the functional equivalent of a non-consolidated QOF owner disposing of part of its qualifying investment. Therefore, these regulations require that the QOF investor member be wholly owned, directly or indirectly, by the common parent.

b. Effects of Consolidating a Subsidiary QOF C Corporation

The preamble to the May 2019 proposed regulations noted, and commenters have acknowledged, that allowing a QOF C corporation to become a subsidiary member of a consolidated group would necessitate the imposition of special rules. In addition to the requirements for consolidation of a QOF member discussed in part VIII.B.2.a of this Summary of Comments and Explanation of Revisions, these final regulations add special rules that coordinate the application of the consolidated return provisions and the rules in section 1400Z–2 by imposing restrictions on the application of the full range of consolidated return rules. The Treasury Department and the IRS have determined that this approach is preferable to the alternative—creating a complex set of parallel consolidated investment adjustment rules and intercompany transaction rules applicable to QOF member stock and transactions by QOF members.

First, as stated in the preamble to the May 2019 proposed regulations, a special rule is needed to effectuate and harmonize the ELA rules under § 1.1502–19 and the rules of section 1400Z–2. Section 1.1502–19 allows a consolidated group to use tax attributes of a member (M) in excess of the consolidated group's investment in M without recognition of gain. Instead, members owning M stock must track the negative basis (that is, the ELA) in their M shares and must include the ELA in income upon the occurrence of specified events, including the disposal of M stock. However, upon a sale or exchange of a qualifying investment, section 1400Z–2(c) permits an investor that has held its qualifying investment for at least 10 years to elect to treat its basis in the qualifying investment as equal to fair market value. Thus, an investor may eliminate the appreciation on its qualifying investment by making the election under section 1400Z–2(c). As further noted in the preamble to the May 2019 proposed regulations, the existence of negative stock basis is unique to the consolidated return regulations and is not contemplated by section 1400Z–2. Accordingly, these final regulations include a rule under which the investor member must take its ELA into account pursuant to § 1.1502–19 before its basis in the QOF member stock is adjusted to fair market value under section 1400Z–2(c).

Second, the final regulations include a special rule to determine when a distribution by a QOF member to the QOF investor member constitutes an inclusion event. Generally, as provided in § 1.1400Z2(b)–1(c)(8), a distribution by a QOF C corporation is an inclusion event to the extent section 301(c)(3) applies to the distribution. In a consolidated group, intercompany distributions are governed by the rules in § 1.1502–13(f), and distributions in excess of the distributee's basis in the distributor do not result in income to the distributee under section 301(c)(3); rather, the excess amount creates or increases the distributee's ELA in the distributor stock. Thus, to coordinate the application of section 1400Z–2 and the consolidated return rules, these final regulations provide that a distribution by a QOF member to a QOF investor member is an inclusion event to the extent the distribution otherwise would create or increase an ELA in the QOF member stock.

Third, the final regulations include a special rule for computing the amount includible by an investor member upon the occurrence of an inclusion event. Generally, the amount includible under section 1400Z–2(b)(2) is determined by reference to the investor's basis in the qualifying investment. However, when a subsidiary QOF C corporation is a member of a consolidated group, § 1.1502–32 applies to adjust the QOF investor member's basis in the stock of the QOF member to reflect the QOF member's income, gain, deduction, or loss. The preamble to the May 2019 proposed regulations raised the issue of how to properly determine the QOF investor member's amount includible when its basis in the QOF member includes basis adjustments unrelated to section 1400Z–2.

Commenters recommended that the final regulations adopt rules similar to those for pass-through entities to compute the QOF investor member's amount includible under section 1400Z–2. The investment adjustment rules under § 1.1502–32 are similar to the partnership basis provisions of section 705, and these final regulations adopt rules similar to the special rule for pass-through entities in § 1.1400Z2(b)–1(e)(4). The Treasury Department and the IRS have determined that the adoption of this rule to compute the QOF investor member's amount includible, in conjunction with the imposition of certain conditions for consolidation (as discussed in part VIII.B.2.a of this Summary of Comments and Explanation of Revisions), will avoid many complexities in the application of the inclusion rules of section 1400Z–2 within a consolidated group.

Fourth, the final regulations include a special rule applicable to transactions between the QOF's separate affiliated group (QOF SAG) and other members of the consolidated group. A QOF SAG is, with respect to a QOF member, the affiliated group that would be determined under section 1504(a) if the QOF member were the common parent. The final regulations treat a sale or exchange of property between a QOF SAG member and a member of the consolidated group that is not a member of such QOF SAG as a transaction that is not an intercompany transaction. Conversely, transactions between QOF SAG members, and transactions between a QOF SAG member and a member of the consolidated group that is not a member of such QOF SAG other than a sale or exchange of property, are intercompany transactions that are subject to the rules of § 1.1502–13.

This rule is necessary to effectuate the application of section 1400Z–2 in a consolidated group. As noted previously in this part VIII.B.2.b of this Summary of Comments and Explanation of Revisions, the election under section 1400Z–2(c) potentially allows taxpayers to permanently exclude their gain on a qualifying investment held for at least 10 years. The availability of this benefit places additional import on ensuring that the gain excluded as a result of the election under section 1400Z–2(c) is not inflated by bargain sales within the consolidated group. Treating property transactions between the QOF SAG and other members as currently taxable helps ensure that any such transactions are bona fide, arm's-length transactions. This treatment also is consistent with treating the QOF as a separate entity for purposes integral to the rules of section 1400Z–2 (for example, treating a contribution to a QOF member as a qualifying investment).

Fifth, the final regulations provide that a consolidated group is not treated as a single entity for purposes of determining whether a QOF member or a qualified opportunity zone business satisfies the investment standard rules in section 1400Z–2(d) and (f) and §§ 1.1400Z2(d)–1 and 1.1400Z2(f)–1. Instead, these rules generally apply separately to each consolidated group member that is a QOF or qualified opportunity zone business. For example, in measuring whether a QOF member meets the 90-percent investment standard, only property (including qualified opportunity zone stock or qualified opportunity zone partnership interests) owned by the QOF member itself is taken into account. To preserve the separate-entity treatment of the QOF, the QOF member cannot take into account property transferred to a member of the consolidated group that is not a member of the QOF member's QOF SAG in satisfying the requirements in section 1400Z–2(d). This issue was identified in the preamble to the May 2019 proposed regulations. See also the discussion of the inapplicability of the intercompany transaction regulations to property transactions between QOF members and certain other consolidated group members in this part VIII.B.2.b of this Summary of Comments and Explanation of Revisions.

c. Anti-Avoidance Rule

As discussed in parts VIII.A, VIII.B, and VIII.C.2 of this Summary of Comments and Explanation of Revisions, the interactions between the consolidated return regulations and section 1400Z–2 are novel and complex, particularly for QOF members whose consolidation is allowed under these final regulations in response to comments received on the May 2019 proposed regulations. In response to comments, these final regulations also make single-entity treatment available for purposes of section 1400Z–2 following certain transfers of qualifying investments, including deemed transactions, between members of a consolidated group. To prevent inappropriate interactions between the two sets of rules, certain consolidated return regulations have been made inapplicable in relation to QOF members and qualifying investments transferred between consolidated group members, and the application of other consolidated return rules has been modified. However, due to the novelty of the interactions between the rules, the Treasury Department and the IRS are concerned that additional, unanticipated issues may arise from those interactions, which might be exploited to produce results that violate the purposes underlying section 1400Z–2 or the consolidated return regulations.

To be responsive to comments received but still provide the flexibility necessary to obtain an appropriate balancing of the purposes underlying section 1400Z–2 and the consolidated return rules, these final regulations include an anti-avoidance rule. This rule provides that, if a transaction is structured with a view to avoiding the application of the rules of section 1400Z–2 and the section 1400Z–2 regulations or the consolidated return regulations (including section 1.1502–14Z), appropriate adjustments will be made to carry out the purposes of section 1400Z–2 and the section 1400Z–2 regulations. For example, if a consolidated group engages in a restructuring (such as a distribution described in section 355) with a purpose to make use of stock basis adjustments under § 1.1502–32 resulting from increases in the basis of stock under section 1400Z–2(b) in a sale or exchange transaction but without disposing of any part of the consolidated group's direct ownership of the relevant qualifying interest, the transaction will be treated as an inclusion event with regard to an appropriate amount of deferred gain.

3. Transition Relief

As discussed in part VIII.B.1 of this Summary of Comments and Explanation of Revisions, commenters requested transition relief for pre-existing QOF subs. The Treasury Department and the IRS have determined that transition relief is appropriate, and these final regulations include multiple elective relief options.

Under the final regulations, a pre-existing QOF sub may elect to be reclassified as a QOF partnership, a QOF C corporation that is not a member of the consolidated group, or a member of the consolidated group that is not a QOF (reclassification election). A reclassification election is effective as of the first day the pre-existing QOF sub was acquired or formed by members of the consolidated group (day one). If a pre-existing QOF sub makes a reclassification election, appropriate adjustments (for example, with respect to basis adjustments under § 1.1502–32 and E&P under § 1.1502–33) must be made to account for the change in status of the pre-existing QOF sub. In addition, if a pre-existing QOF sub was a QOF C corporation before being acquired by a consolidated group, and if the consolidated group elects to treat the pre-existing QOF sub as a QOF partnership as of day one (that is, the date it was acquired by the consolidated group), the conversion from a QOF C corporation to a QOF partnership on day one is an inclusion event. See § 1.1400Z2(b)–1(c)(2).

In the alternative, a pre-existing QOF sub that meets certain conditions may elect to maintain its status as a QOF C corporation and remain a member of the consolidated group. See part VIII.B.2.a of this Summary of Comments and Explanation of Revisions, which describes the conditions for such an election. If a pre-existing QOF sub elects to remain a member of the consolidated group, the pre-existing QOF sub will be subject to unique rules and restrictions not typically applicable to a consolidated group member, as discussed in part VIII.B.2.b of this Summary of Comments and Explanation

of Revisions. The pre-existing QOF sub will have 90 days from the date of publication of these final regulations to satisfy the conditions for consolidating as a subsidiary QOF C corporation.

Transition relief is available only to pre-existing QOF subs. QOF C corporations formed after the publication of the May 2019 proposed regulations are not eligible for transition relief, but any such QOF C corporation may elect to be treated as a subsidiary member of a consolidated group. See part VIII.B.2 of this Summary of Comments and Explanation of Revisions for a discussion of the conditions and effects of consolidating a subsidiary QOF C corporation.

4. Deconsolidation of Subsidiary QOF C Corporation

The final regulations also provide rules regarding the deconsolidation of QOF members. Deconsolidation can occur when a QOF member fails to meet the general section 1504 affiliation requirements or fails to satisfy the conditions in these final regulations to consolidate a subsidiary QOF C corporation. In addition, deconsolidation can occur when a pre-existing QOF sub fails to elect in a timely manner one of the transition relief provisions discussed in part VIII.B.3 of this Summary of Comments and Explanation of Revisions.

If a QOF member deconsolidates, the deconsolidation is treated as a disposition for purposes of applying the rule in § 1.1502–19 that requires any ELA in the QOF member's stock to be included in income, and it is treated as a transfer of all of the QOF member stock for purposes of applying the unified loss rule in § 1.1502–36. However, the deconsolidation constitutes an inclusion event only to the extent the deconsolidation event also constitutes an inclusion event as defined in § 1.1400Z2(b)–1(c). For example, if a QOF member deconsolidates because the investor member sells 25 percent of the QOF member stock to a nonmember, the QOF deconsolidates and §§ 1.1502–19 and 1.1502–36 will apply to all QOF shares owned by members, but there will be an inclusion event only for 25 percent of the shares. In addition, if the investor member has positive basis in QOF member stock because of investment adjustments under § 1.1502–32, the investor member retains such basis in the QOF member following deconsolidation, but such basis is not taken into account in computing the investor member's amount includible under section 1400Z–2(b) post-deconsolidation.

A special E&P rule applies if the QOF member deconsolidates before December 31, 2026. The special E&P rule reverses the general rule for deconsolidations in § 1.1502–33(e) to provide that the QOF member retains its E&P, and to require elimination from the consolidated group of any QOF member's E&P taken into account by other members under § 1.1502–33. This special rule will permit the QOF C corporation to make section 301(c)(1) distributions, to the extent of its E&P, following deconsolidation without triggering inclusion of the investor member's remaining deferred gain under section 1400Z–2(b).

5. Treatment of QOF Stock Under Section 1504

The May 2019 proposed regulations treated stock in a QOF C corporation as not stock for purposes of section 1504. As discussed in part VIII.A of this Summary of Comments and Explanation of Revisions, the purpose of this rule was to prevent a subsidiary QOF C corporation from being included as a member of an affiliated group filing consolidated returns. However, commenters noted that, under this proposed rule, the dividends received deduction under section 243 would be unavailable to corporate shareholders of QOF C corporations because qualification for that deduction depends on the distributing corporation and shareholder being part of the same affiliated group. Commenters recommended that, even if the final regulations preclude a subsidiary QOF C corporation from being a member of an affiliated group for purposes of joining in the filing of a consolidated return, the final regulations should permit a QOF C corporation to be a member of an affiliated group for purposes of the dividends received deduction.

In response to the foregoing comments, these final regulations provide that QOF stock is not treated as stock only for purposes of determining eligibility to join in the filing of a consolidated return under section 1501. Therefore, this rule will not affect the availability of the dividends received deduction or any other provision that cross-references affiliation status under section 1504 other than consolidated group membership.

C. Qualifying Investments by Members of a Consolidated Group

In response to the May 2019 proposed regulations, commenters raised many questions regarding the interaction of the intercompany transaction rules of § 1.1502–13 and section 1400Z–2. For example, commenters asked about the application of § 1.1502–13 when a qualifying investment is transferred in an intercompany transaction. Many of the issues noted by commenters arise regardless of whether the QOF is a member of a consolidated group.

The stated purpose of § 1.1502–13 is to provide rules to clearly reflect the taxable income (and tax liability) of the consolidated group as a whole by preventing intercompany transactions from creating, accelerating, avoiding, or deferring consolidated taxable income or consolidated tax liability. In other words, the existence of intercompany transactions must not affect consolidated taxable income or consolidated tax liability. Therefore, § 1.1502–13 generally determines the tax treatment of items resulting from intercompany transactions by treating members of a consolidated group as divisions of a single entity (single-entity treatment).

1. Investment in QOF Member as Qualifying Investment

As discussed in part VIII.B.1 of this Summary of Comments and Explanation of Revisions, commenters requested that subsidiary QOF C corporations be permitted to join in the filing of consolidated returns. In connection with this request, commenters also sought clarification of the application of § 1.1502–13 to the gain deferred under section 1400Z–2 when an investor member makes an otherwise qualifying investment in a QOF member.

The Treasury Department and the IRS proposed to exclude a subsidiary QOF C corporation from consolidation because, among other reasons, the Treasury Department and the IRS determined that section 1400Z–2 is inconsistent with the intercompany transaction regulations under § 1.1502–13. In particular, the Treasury Department and the IRS highlighted that the stated purpose of the regulations under § 1.1502–13 is to ensure that the existence of an intercompany transaction (a transaction between two members of a consolidated group) does not result in the creation, prevention, acceleration, or deferral of consolidated taxable income or tax liability. Based on comments from taxpayers and practitioners, the Treasury Department and the IRS have considered approaches to provide additional investment structures for potential investors in QOZs while ensuring the compatibility of such structures with the consolidated return regulations. As a result, the final regulations provide that an investment of eligible gain by the investor member into a QOF member is not treated as an intercompany transaction for purposes

of § 1.1502–13 and, thus, is a qualifying investment for purposes of section 1400Z–2.

2. Treatment of S's Intercompany Gain as Eligible Gain

These final regulations also include rules that clarify whether and when capital gain from an intercompany transaction can constitute eligible gain for purposes of section 1400Z–2.

When a member (S) sells property to another member of the consolidated group (B) and recognizes gain, the gain is an intercompany gain subject to § 1.1502–13. The matching rule of § 1.1502–13(c) may apply to redetermine the attributes of S's intercompany gain and to control the timing of the reporting of S's intercompany gain. Commenters requested clarification as to whether S's intercompany gain qualifies as an eligible gain that can be deferred under section 1400Z–2 and, if so, the time at which S is treated as having an eligible gain.

The final regulations clarify that S's gain and B's gain on the property (if any) is treated as eligible gain to the extent the gain would be an eligible gain if S and B were divisions of a single entity. Moreover, the gain is treated as an eligible gain at the time the gain would be taken into account (without regard to the potential application of section 1400Z–2) if S and B were divisions of a single entity.

3. Application of § 1.1502–13 to Intercompany Transfer of a Qualifying Investment

In discussing the complications arising from the interaction of section 1400Z–2 and § 1.1502–13, the preamble to the May 2019 proposed regulations generally focused on issues that would arise if a subsidiary QOF C corporation were a member of a consolidated group. Neither the May 2019 proposed regulations nor the preamble thereto included any language on the general application of § 1.1502–13 to the transfer of qualifying investments. Whether and how § 1.1502–13 applies to an intercompany transfer of a qualifying investment is an issue regardless of whether the QOF is a QOF C corporation or a QOF partnership, and regardless of whether the QOF C corporation is a QOF member.

Commenters detailed the technical impediments under the current intercompany transaction regulations to achieving single-entity treatment when a member of the consolidated group transfers its qualifying investment in an intercompany transaction, and they requested guidance to grant single-entity treatment to a consolidated group after such an intercompany transaction. Commenters also noted that section 1400Z–2(c) does not appear to permit an election for the basis increase to be made by any party other than the taxpayer who makes the qualifying investment.

As discussed in the preamble to the May 2019 proposed regulations, the availability of benefits and the continuation of deferral under section 1400Z–2 are determined with respect to the holder's basis in the qualifying investment. For example, a shareholder's basis in its QOF stock differs from a shareholder's basis in the stock of non-QOF C corporations. Because of the difficulties in tracking basis for purposes of section 1400Z–2 following the transfer of QOF shares in certain nonrecognition transactions (for example, in exchanges to which section 351 applies or in reorganizations described in section 368(a)(1)(B)), the regulations generally applicable to investors in a QOF C corporation (whether or not the QOF C corporation is a QOF member) provide that the transfer of QOF shares in such nonrecognition transactions is an inclusion event under section 1400Z–2(b).

The same basis tracking issues exist within a consolidated group and are magnified by the application of § 1.1502–32, which adjusts an upper-tier member's basis in the stock of a lower-tier member to reflect items of income, gain, loss, and deduction produced by the lower-tier member. As discussed in part VIII.B.2.a.ii of this Summary of Comments and Explanation of Revisions, basis adjustments to lower-tier member stock ''tier up'' within a consolidated group under § 1.1502–32. In other words, economic items recognized by lower-tier members result in basis adjustments to the stock of upper-tier members, resulting in blended basis at the upper tiers. Moreover, because an upper-tier member may have economic items of its own, the basis of the upper-tier members' stock is further blended. This blended basis in the consolidated group creates additional tracking issues with regard to section 1400Z–2.

In the interest of administrability and simplicity, the Treasury Department and the IRS decline to impose complex new rules for tracing the basis in a qualifying investment through tiers of entities and across ownership chains within a consolidated group. Instead, to permit the movement of qualifying investments within consolidated groups to satisfy business needs, these final regulations allow consolidated groups to obtain single-entity treatment only on a fully taxable intercompany transfer of a qualifying investment. In a fully taxable transaction, B takes a cost basis in the qualifying investment; thus, S's basis in the qualifying investment is not replicated. As a result, in a fully taxable transaction, the gain deferred under section 1400Z–2 is not replicated in the consolidated group. All other intercompany transfers of qualifying investments are treated as not constituting intercompany transactions for purposes of § 1.1502–13.

As noted earlier in this part VIII.C.3 of this Summary of Comments and Explanation of Revisions, single-entity treatment for intercompany transfers of qualifying investments is not currently available under the consolidated return regulations. The limited application of the intercompany transaction rules in § 1.1502–13 under these final regulations provides consolidated groups with a workable option for making necessary transfers of qualifying investments within the consolidated group while preventing complications under the section 1400Z–2 rules.

To further facilitate single-entity treatment, these final regulations enable B to make an election under section 1400Z–2(c) following a transfer of a qualifying investment that is treated as an intercompany transaction. Specifically, if § 1.1502–13 applies to treat S and B as divisions of a single entity for purposes of section 1400Z–2, then B (and not S) makes the election under section 1400Z–2(c) (if eligible), as it is the member that actually owns an interest in the qualifying investment at the time of its disposition by the single entity. B is eligible to make the election under section 1400Z–2(c) only if and when, treating S and B as a single entity, the single entity would be eligible to make such an election. For example, under single-entity treatment, S and B's holding period in the qualifying investment is combined to determine whether the 10-year requirement for the election under section 1400Z–2(c) has been met.

4. Treating Investment by One Member as Qualifying Investment by Another Member

Under the May 2019 proposed regulations, the requirements in section 1400Z–2 applied separately to each member of a consolidated group. Thus, the same member of the consolidated group must both sell the capital asset giving rise to eligible gain and timely invest the proceeds in a qualifying investment. Commenters argued that this requirement is overly restrictive and may limit the ability of taxpayers to

make use of section 1400Z–2 as intended by Congress. Instead, commenters recommended that the Treasury Department and the IRS adopt a single-entity approach that permits a QOF investment by one member to be treated as a qualifying investment by another member with eligible gain. One commenter also requested that this treatment be applied to investments made prior to June 1, 2019, allowing for a one-month grace period following the publication of the May 2019 proposed regulations.

In response to these comments, and to further the purposes of section 1400Z–2, the final regulations include an election to treat the investment by one member (M2) as a qualifying investment by another member (M1). The election is available when M1 has an eligible gain and M2 makes an investment in a QOF that would be a qualifying investment if M1 (rather than M2) had made the investment. If the consolidated group makes this election, for all Federal income tax purposes M1 is treated as making an investment in the QOF and immediately selling the qualifying investment to M2 for fair market value. The sale of the qualifying investment from M1 to M2 is subject to § 1.1502–13, as discussed in part VIII.C.3 of this Summary of Comments and Explanation of Revisions.

The Treasury Department and the IRS decline to adopt the recommendation to treat M2's investment as a qualifying investment by M1 retroactively because such treatment is available only by election, subject to certain conditions. However, taxpayers generally have the option to apply these final regulations in their entirety, and in a consistent manner, to taxable years beginning after December 21, 2017, or to the portion of any taxable year after December 21, 2017. If a taxpayer chooses to adopt these final regulations in their entirety for taxable years beginning after December 21, 2017, or to the portion of any taxable year after December 21, 2017, then taxpayers may elect to treat an investment by M2 as a qualifying investment by M1 as of the earlier date.

IX. Comments Not Specifically on Regulatory Text

A. Reporting

The Treasury Department and the IRS have received hundreds of comments on whether reporting of the QOF and qualified opportunity zone investments was needed, and what type of information should be reported. On May 1, 2019, the Treasury Department published a notice and request for information to seek public input on the development of public information collection and tracking related to investment in qualified opportunity funds. See 84 FR 18648. As indicated in the proposed regulations, the Treasury Department and the IRS were considering certain changes to the Form 8996 requiring QOFs to report additional information regarding the location of their investments.

Several comments suggested that no additional reporting should be required and that the amount of reporting already required was sufficient. Several other comments requested that additional reporting be allowed, but to not be onerous or prohibitive in either cost or time. Other comments suggested that the reporting should be coordinated with other government agencies, such as the Department of Housing and Urban Development (HUD) or the Treasury Department's CDFI Fund, and local and state governments.

Many commenters requested additional reporting, on items such as location of investments, job creation in the QOZ, the impact on the local economy, number of units of affordable housing built, and any reduction in poverty. These comments requested that such information be made public, including a database which the public can use to track projects nationally and the creation of a standardized set of performance metrics. One commenter asked for reporting guidelines for entities that lend capital to QOFs.

The Treasury Department and the IRS are appreciative of the comments received focused on requiring reporting of data in addition to what is useful for tax administration purposes. Comments received in this regard are not adopted in these final regulations. However, On October 30, 2019, the IRS released an early release draft of Form 8996 for public review. The early release draft includes additional reporting requirements for QOFs. The information required to be reported focuses on data useful for tax administration purposes, data that may also be instructive in measuring the impact and effectiveness of the statute.

B. REITs

Several commenters discussed passing the benefits of a REIT's qualifying investments to the REIT's shareholders. These comments include applying the 1400Z–2(c) basis adjustment rules for E&P purposes so that distributions of gain from the disposition of a qualifying investment will not result in ordinary income to the REIT's shareholders. Additionally, the commenters asked that REITs have the ability to distribute tax-exempt capital gain dividends to the extent attributable to the REIT's gain with respect to its qualifying investments. The Treasury Department and the IRS have concluded that such special rules for REITs and their shareholders would create a vehicle in which taxpayers that do not make a qualifying investment for the required period of time pursuant to section 1400Z–2 would nevertheless receive the benefits of that section. Thus, these changes were not accepted. REITs may still qualify and elect to be QOF REITs or may distribute capital gain dividends to their shareholders who in turn may invest those capital gain dividends in a QOF pursuant to section 1400Z–2.

C. Policy

In addition to comments concerning the proposed regulations, several comments were received concerning the tax benefits of the statute. For example, some commenters requested preferred treatment for various classes of individuals and entities, including veterans, healthcare practitioners, needy individuals, and residents of QOZs. Several other commenters requested that the Treasury Department and the IRS should disallow the tax benefits provided by section 1400Z–2 if entities fail to build a sufficient number of affordable housing units. Another commenter suggested that the tax benefits provided by section 1400Z–2 in general should be disallowed if a QOF or qualified opportunity zone business fails to operate solely within a QOZ.

Many commenters requested a rule requiring managers of QOFs to certify that they had not been convicted of financial crimes within the past three years, and register with the local government that they are managing a QOF. Further, many commenters suggested requiring QOF managers to demonstrate that their actions have not encouraged any additional displacement of residents in low income areas. Some commenters were concerned with the impact that QOFs and qualified opportunity zone businesses will have on existing small businesses located within QOZs.

Several commenters requested that the Treasury Department and the IRS require that QOFs and qualified opportunity zone businesses coordinate their activities with other Federal agencies, like HUD, and CDFI Fund, and state and local government and housing agencies. Several others suggested allowing local jurisdictions to add criteria that is consistent with a locality's needs and goals. Two commenters stated that the capital invested in QOFs should be invested in

small and midsize businesses, rather than large corporations. Another commenter suggested additional guidance to permit housing finance agencies to layer their programs within QOZs with QOFs or qualified opportunity zone businesses. One commenter requested guidance on using QOF investments to satisfy requirements pertaining to certain depository institutions under the Community Reinvestment Act.

Several commenters requested coordination and integration with local government authorities including measures to coordinate projects within QOZs with other government funded projects and a formal process for local and regional authorities to review projects in QOZs. Another comment suggested that the Treasury Department and the IRS mandate cooperation by QOFs with local community banks to determine who needs the most assistance.

The Treasury Department and the IRS received several comments concerned that QOFs and qualified opportunity QOZ businesses would not benefit the existing residents and businesses in designated QOZs. These commenters suggested adding provisions to the final regulations aimed at the prevention of displacement of residents, and targeted incentives to aid the neediest of QOZs. Several others suggested that the Treasury Department and the IRS require that QOF investments target local businesses with established ties to the local communities and that serve the local community's needs. Another comment requested that preference should be shown to local and/or minority owned businesses, or sustainably focused companies. Finally, a commenter suggested that there should be a requirement that a minimum number of local residents be employed by a QOF or qualified opportunity zone business.

In addition to the comments noted earlier, the Treasury Department and the IRS received comments requesting that certain items, such as food inventory or business related property owned by the residents of QOZs, should qualify as qualified opportunity zone business property.

The Treasury Department and the IRS will continue to study the issues addressed in these comments. However, many of these comments are outside the scope of these final regulations. In addition the Treasury Department and the IRS are concerned with the potential complexity associated with creating rules that would interfere with the ultimate intent of the statute, which is to invest new capital in low-income communities.

D. QOZ Designations

The Treasury Department and the IRS received many comments regarding section 1400Z–1 and the process for designating QOZs. Several comments requested that the determination process be reopened, so new QOZs could be designated. One commenter requested that if no investment has occurred in a QOZ, that accommodation be provided to replace it with another QOZ. Another comment suggested that some designated QOZs either do not meet the statutory requirements or were mistakenly nominated.

The Treasury Department and the IRS are appreciative of the comments received on the designation of the QOZs. Section 1400Z–1 provides the statutory authority for one round of nominations and designations. Thus, there are no current or proposed plans to reopen consideration of additional census tracts to be designated as QOZs.

Several comments were received questioning how QOFs and qualified opportunity zone businesses would be treated after the QOZ designation expires. Another commenter asked for clarification for the treatment of QOFs and qualified opportunity zone businesses if the census tract boundaries change during the designation period. Under the October 2018 proposed regulations and § 1.1400Z2(c)–1(b) of the final regulations, although QOZ designations expire on December 31, 2028, a taxpayer who makes an election under section 1400Z–2(a) and whose holding period in the qualifying investment is at least 10 years, is eligible to make an election described in section 1400Z–2(c) on the sale or exchange of the qualifying investment. Accordingly, if a portion of the taxpayer's 10-year holding period under section 1400Z–2(c) accrues after the relevant census tract's QOZ designation expires on December 31, 2028, this fact alone should not disqualify a taxpayer's properly executed QOF investment from the benefit of section 1400Z–2(c).

E. Questions and Comments on the Penalty Under Section 1400Z–2(f)(1)

Under section 1400Z–2(f)(1), if a QOF fails to meet the 90-percent investment standard, the QOF shall pay a penalty for each month it fails to meet the requirements in an amount equal to the excess of the amount equal to 90-percent of its aggregate assets over the aggregate amount of qualified opportunity zone property held by the QOF, multiplied by the underpayment rate established under section 6621(a)(2) for such month.

Several commenters requested clarification on the mechanics of this penalty, including whether there is a possibility of the QOF, or its investors, of losing the benefits, if the QOF fails to meet the 90-percent investment standard for an extended period of time.

Two other commenters requested that, to calculate the penalty, only the assets that were the subject of the deferral election, should be included. They reason that the statute could be interpreted to assess a QOF based upon a shortfall related to its aggregate assets, regardless of the source of financing for those assets.

One commenter requested that the Treasury Department and the IRS eliminate the testing dates under section 1400Z–2(d)(2)(A) and instead adopt a penalty based on a per month penalty.

Finally, one commenter suggested that the Treasury Department and the IRS should use the anti-abuse provision to create penalties for failing to invest in entities that meet the policy objectives mentioned in a prior section.

The Treasury Department and the IRS appreciate the comments received on the penalty imposed on QOFs under section 1400Z–2(f)(1). All comments will be considered for future guidance.

F. Reasonable Cause

Under section 1400Z–2(f)(3), no penalty shall be imposed on a QOF with respect to any failure to meet the 90-percent investment standard if it is shown that the failure is due to reasonable cause.

Multiple commenters requested clarification on what would constitute reasonable cause. Several commenters requested that reasonable cause should be defined to include circumstances that are outside the QOF's control to deploy capital into qualifying investments. The Treasury Department and the IRS are cognizant that this is an area for which commenters requested relief. The final rules provide a 6 month period in which QOFs may choose to disregard recently contributed property from the 90-percent investment standard. That rule may be elected in circumstances in which a QOF is unable to deploy its capital into qualified opportunity zone property.

Another commenter requested that the final rule provide a non-exhaustive list of circumstances that would constitute reasonable cause. The final rule does not adopt these comments. The determination of whether there is reasonable cause for penalty relief in a particular case is inherently factual. The Treasury Department and the IRS have

determined that the appropriate standards for determining whether the reasonable cause exception to the penalty applies in a particular case are the general standards set out in the ''Penalty Handbook,'' which is included in Internal Revenue Manual (IRM) at section 20.1. The Treasury Department and the IRS will consider whether further guidance specific to the penalty under section 1400Z–2(f)(1) is necessary in the future.

G. Regulatory Flexibility Act

The Treasury Department and the IRS received comments on the Regulatory Flexibility Act (5 U.S.C. chapter 6) (RFA) urging that an RFA analysis on the potential significant economic effect of these final regulations on small entities be conducted by the Treasury Department and the Small Business Administration. The Treasury Department and the IRS do not agree that an analysis is required. There is a lack of data as to the extent to which small entities invest in QOFs, will certify as QOFs, or receive equity investments from QOFs. However, the Treasury Department and the IRS project that most of the investment flowing into QOFs will come from large corporations and wealthy individuals, though some of these funds would likely flow through an intermediary investment partnership. There may be some QOFs and qualified opportunity zone businesses that will be classified as small entities; however, the number of small entities significantly affected is not likely to be substantial.

Effective/Applicability Dates

Sections 1.1400Z2(a)–1 through 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 generally apply to taxable years beginning after March 13, 2020. However, for the portion of a taxpayer's first taxable year ending after December 22, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, taxpayers may choose either (1) to apply the rules set forth in §§ 1.1400Z2(a)–1 through 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 contained in this document, if applied in their entirety and in a consistent manner for all such taxable years, or (2) to rely on each section of the proposed regulations under §§ 1.1400Z2(a)–1 through 1.1400Z2(g)–1, except for § 1.1400Z2(c)–1, issued on October 29, 2018, and on May 1, 2019, but only if applied in their entirety and in a consistent manner for all such taxable years. See section 7805(b)(7)

Special Analyses

I. Regulatory Planning and Review—Economic Analysis

Executive Orders 13711, 13563, and 12866 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. For purposes of Executive Order 13771, this rule is deregulatory.

The final regulations have been designated as subject to review under Executive Order 12866 pursuant to the Memorandum of Agreement (April 11, 2018) between the Treasury Department and the Office of Management and Budget (OMB) regarding review of tax regulations. The Office of Information and Regulatory Affairs has designated these regulations as economically significant under section 1(c) of the Memorandum of Agreement. Accordingly, the OMB has reviewed these regulations.

A. Need for the Final Regulations

As a part of the Tax Cuts and Jobs Act (TCJA), Congress enacted section 1400Z, which provided tax incentives related to investment in qualified opportunity zones (QOZs). The Treasury Department and the IRS issued proposed regulations related to section 1400Z–2 on October 29, 2018 (October 2018 proposed regulations) and May 1, 2019 (May 2019 proposed regulations), together referred to as the proposed regulations. The numerous comments to the proposed regulations indicate substantial interest in the opportunity zone tax incentives provided in section 1400Z–2. The comments demonstrate a variety of opinions on how to interpret ambiguous parts of section 1400Z–2 and on how section 1400Z–2 interacts with other sections of the tax code and corresponding regulations. The Treasury Department and the IRS are aware of concerns raised by commenters that some investors have been reticent to make substantial investments in QOZs without first having additional clarity on which investments would qualify to receive the preferential tax treatment specified by the TCJA.

Based on these considerations, the final regulations are needed to bring clarity to instances where the meaning of the statute was unclear and to respond to comments received on the proposed regulations.

B. Background and Overview

Congress enacted section 1400Z–2, in conjunction with section 1400Z–1, as a temporary provision to encourage private sector investment in certain lower-income communities designated as QOZs (see Senate Committee on Finance, Explanation of the Bill, at 313 (November 22, 2017)). To this effect, taxpayers may elect to defer the recognition of capital gain to the extent of amounts invested in a qualified opportunity fund (QOF), provided that such amounts are invested during the 180-day period beginning on the date such capital gain would have been recognized by the taxpayer. Inclusion of the deferred capital gain in income occurs on the date the investment in the QOF is sold or exchanged or on December 31, 2026, whichever comes first. For investments in a QOF held longer than five years, taxpayers may exclude 10 percent of the deferred gain from inclusion in income, and for investments held longer than seven years, taxpayers may exclude a total of 15 percent of the deferred gain from inclusion in income. In addition, for investments held longer than 10 years, the post-acquisition gain on the qualifying investment in the QOF also may be excluded from income. In turn, a QOF is required under the statute to hold at least 90 percent of its assets in qualified opportunity zone property, as measured by the average percentage of assets held on the last day of the first six-month period of the taxable year of the fund and on the last day of the taxable year. The statute requires a QOF that fails this 90-percent investment standard to pay a penalty for each month it fails to satisfy this requirement.

C. Economic Analysis

1. Baseline

The Treasury Department and the IRS have assessed the economic effects of the final regulations relative to a no-action baseline reflecting anticipated Federal income tax-related behavior in the absence of these final regulations.

2. Summary of Economic Effects

The final regulations provide certainty and clarity to taxpayers regarding utilization of the tax preferences for capital gains provided in section 1400Z–2 by defining terms, calculations, and acceptable forms of documentation. The Treasury Department and the IRS project that this added certainty and clarity generally

will encourage taxpayers to increase the amount of investment located in QOZs relative to the no-action baseline. The certainty and clarity added by the final regulations and the specific regulatory decisions they entail will further bring the volume and diversity of investment in QOZs and in non-QOZs closer to the intent and purpose of the statute, relative to the alternative regulatory approaches that were considered, including the no-action baseline.

The Treasury Department and the IRS have not attempted to quantify the economic effects of any changes in business activity stemming from these final regulations, in part because of the uncertainty regarding the patterns of investment that will materialize as a result of QOF activity and the distribution of investments across opportunity zones. The Treasury Department and the IRS do not have readily available data or models that predict with reasonable precision the decisions that taxpayers would make under the final regulations versus alternative regulatory approaches, including the no-action baseline. Nor do they have readily available data or models that would measure with reasonable precision the loss or gain in economic surplus resulting from these investment and business decisions relative to the decisions that would be made under an alternative regulatory approach. Such estimates would be necessary to quantify the economic effects of the final regulations versus alternative approaches. Subject to these limitations, the next two sections of these Special Analyses provide a qualitative assessment of the economic effects of the final regulations relative to the alternative regulatory approaches that were considered.

The Treasury Department and the IRS welcome comments on this economic analysis as well as analysis regarding how choices made in this regulation will materially affect specific types of investments that are likely to attract capital that has been invested in QOFs.

3. Number of Affected Taxpayers

Because section 1400Z–2 is a new provision and many of the entities affected by these regulations have not yet been formed, there is considerable uncertainty regarding the number of taxpayers that will eventually be affected by the final regulations. Based in part on the preliminary number of taxpayers filing Form 8996 for tax year 2018 and the assumption that a QOF will on average have 10 investors, the Treasury Department and the IRS project that between 5,500 and 12,000 QOFs, 6,000 to 15,000 qualified opportunity zone businesses, and 55,000 to 120,000 investors in QOFs will eventually be affected by the final regulations.

4. Economic Effects of Provisions Substantially Revised From the Proposed Regulations

a. Eligible Gains From Section 1231 Property

The final regulations provide that a gain is eligible for deferral under section 1400Z–2(a) if the gain is treated as a capital gain for Federal income tax purposes. There is uncertainty, however, regarding how to treat gains arising from selling section 1231 property. Section 1231 property is certain property used in a trade or business, such as depreciable property and land, and also includes capital assets subject to an involuntary conversion, such as arising from a natural disaster or theft. Under the Code, gains from the sale or exchange of section 1231 property are characterized as capital gains if the sum of all section 1231 transactions for the taxable year is positive. If the sum of all section 1231 transactions for the year is negative, then the losses are ordinary losses.[1]

The Treasury Department and the IRS considered two main options for the treatment of gains from section 1231 property.[2] The primary issue is whether the amount of the gains eligible for deferral is based on the sum of all sales over the taxable year or on an item-by-item basis. These approaches are also referred to as the net approach and gross approach, respectively.

The statute also sets a 180-day requirement for investment in a QOF beginning on the date of the sale or exchange generating the gain, to be eligible for deferral under section 1400Z–2(a). The two options for calculating eligible section 1231 gains further determine when the 180-day requirement begins. When gains are based on the sum of sales over the taxable year, the 180-day period starts at the end of the taxable year, after it is determined whether the sum is positive or negative, and how large the net positive gain is. When gains are counted item-by-item, it is possible, although not necessary, to start the 180-day period from the date of each sale.

The proposed regulations used the net approach. Under the proposed regulations, the only gain arising from section 1231 property eligible for deferral under section 1400Z–2(a) was the amount by which the gains arising from all of a taxpayer's section 1231 property exceeded all of the taxpayer's losses from section 1231 property for a taxable year. In addition, the proposed regulations provided that the 180-day period for investment with respect to capital gain net income from section 1231 property for a taxable year began on the last day of the taxable year without regard to the date of any particular disposition of section 1231 property.

The final regulations adopt the gross approach. Under the final regulations, eligible section 1231 gains are determined on an item-by-item basis and therefore positive gains are not reduced by section 1231 losses. Furthermore, the amount of the gain is known at the time of each sale so it is not necessary for the taxpayer to wait until the end of the taxable year to determine whether any positive section 1231 sales will be offset by losses. As a consequence, the final regulations further provide that the 180-day period for investing an amount with respect to an eligible section 1231 gain for which a deferral election has been made begins on the date of the sale or exchange that gives rise to the section 1231 gain. In addition, the final regulations do not determine the character of eligible section 1231 gains, other than as gains arising from the sale or exchange of section 1231 property, until the taxable year such gains are taken into account in computing gross income pursuant to section 1231(a)(4). The treatment of section 1231 property under the gross option is essentially the same treatment provided in the final regulations for gain arising from the sale of a capital asset as defined by section 1221.

To illustrate this discussion, suppose that Corporation A sells two pieces of section 1231 property during the taxable year, one for a $100 gain early in its taxable year and the other for a $30 loss later in its taxable year. Suppose that Corporation B also sells two pieces of section 1231 property during the taxable year, one for a $20 gain, the other for a $50 loss. Neither taxpayer realizes any other capital gain during the taxable year.

Under the net approach, Corporation A's net gain is $70, which is positive. Thus, it would be able to defer up to $70 in capital gain by investing in a QOF. Corporation B has a net loss from selling section 1231 property. This net loss would be treated as ordinary and no

[1] One source of ambiguity is determining whether gain from selling an item of section 1231 property that is potentially eligible for deferral should be included in the summation of 1231 property in the year the deferral begins or the year the deferral ends.

[2] The Treasury Department and the IRS also considered the option of not issuing specific guidance on this topic but determined that this was clearly inferior to the two main options.

gains would be deferrable under section 1400Z–2(a). Furthermore, although Corporation A sells the first piece of property for a gain early in its taxable year, it would not be able to make a qualifying investment in a QOF until the last day of the taxable year, because it needs to wait until the end of the tax year to determine whether it is eligible to defer any of the gain.

Under the gross approach, only the gains need to be accounted for. Corporation A would be able to defer $100 in gain and Corporation B would be able to defer $20. In this case, the amount of gain eligible for deferral increases for both taxpayers. The total amount of gain eligible for deferral increases from $70 to $120 compared to the net approach.

Although not determinative, we note that the gross approach, as adopted under the final regulations, will generally expand the pool of gains eligible for deferral under section 1400Z–2(a) relative to the net approach specified under the proposed regulations.[3] Based on recent taxpayer records, the Treasury Department and the IRS estimate that the gross option may increase the amount of eligible gains by four to eight percent compared to the net option. The increase in potentially eligible gains overstates the likely increase in investment in QOFs resulting from using the gross approach (rather than the net approach) for two different reasons. First, for many taxpayers, the amount of section 1231 gains is not likely to be a binding constraint on the amount of investment made by the taxpayer into a QOF because of the ability of the taxpayer to defer other sources of capital gains. Second, taxpayers have considerable discretion over when to realize gains, and even under the net approach taxpayers could often plan on selling section 1231 property with sufficient net gain in a taxable year to cover the amount of desired QOF investment. The Treasury Department and the IRS have not attempted to estimate the overall effect of this provision of the final regulations (relative to the proposed regulations) on either QOZ or non-QOZ investment.

An additional effect of the gross option would be to minimize the tax considerations of determining the best time to sell section 1231 property, leading to a more efficient use of resources. Under the gross option, taxpayers would be less likely to delay or rush selling section 1231 property in order to achieve the desired amount of net gain that would be eligible for deferral within a particular year. Also, under the gross option, taxpayers would have more flexibility in realizing gains eligible to be invested in a QOF in calendar year 2019.

The Treasury Department and the IRS considered several variations to these two primary options. For example, one intermediate option would have required taxpayers to wait to determine the capital gain character of section 1231 property sales until summing at the end of the taxable year, but then allow the gross amount of gains to be eligible for deferral if the net is positive. Under this intermediate option, Corporation A would be eligible to defer $100 in gain, while Corporation B would not be able to defer any amount. The pool of eligible gains would be greater than under the net option, but less than the gross option. This intermediate option would also have the costs similar to the net option regarding the need for taxpayers to wait to until the end of the taxable year before investing in a QOF.

The number of taxpayers expected to be affected by this aspect of the final regulations ranges between 36,000 and 80,000 investors in QOFs.

b. Sales or Exchanges of Property by QOF Partnerships and QOF S Corporations

The Treasury Department and the IRS considered three options for how owners of QOF partnerships and QOF S corporations may exclude gains from tax on qualifying investments in the QOF held longer than 10 years. First, the Treasury Department and the IRS considered not providing a specialized rule for QOF partnerships and QOF S corporations. Under this option, owners of a QOF would need to sell or exchange their QOF ownership interest to another party in order to receive the exemption from tax on the gain. For certain business structures, this would not be the most efficient way to dispose of the assets of the QOF. For example, suppose QOF A has 20 partners and QOF A owns two commercial buildings that are qualified opportunity zone business property. If another investor B would like to purchase one of the buildings, it would generally be easier for QOF A to sell the building to investor B directly, rather than investor B buying out the partnership interests of several or all of the partners of QOF A. Under this first option, the owners of QOF A would only receive tax free gain from their investment if they are able to find an investor willing to buy their partnership interests in QOF A. This option would likely lead to relatively high negotiating costs and may reduce the pool of potential buyers for QOF assets.

Second, the May 2019 proposed regulations proposed that investors in a QOF partnership or a QOF S corporation could elect to exclude capital gains arising from the QOF selling qualified opportunity zone property from gross income. This option would provide a simpler way for owners of pass-through QOFs to receive tax-free gain, but it would apply only in certain cases. It would apply only to capital gains and not ordinary gains, such as the recapture of depreciation deductions. Also, this option would apply only to QOFs selling qualified opportunity zone property, and would not apply to qualified opportunity zone business property sold by a qualified opportunity zone business that is a subsidiary of the QOF.

Third, the final regulations allow QOF owners to elect to exclude from gross income all gains and losses of a QOF partnership or QOF S corporation (except those deriving from sales of inventory in the ordinary course of business). This would allow the gains from the sale of qualified opportunity zone business property by a qualified opportunity zone business to flow through to the owners of the QOF as excluded from income. This election can be made on an annual basis, but it must apply to all gains and losses of the QOF partnership or QOF S corporation for that taxable year. In addition, when the proceeds from the asset sales are reinvested, rather than distributed as cash, then the QOF owner's share of the qualifying investment is reduced as the reinvested amount is deemed to be a non-qualifying investment.

These rules generally match the tax treatment that would exist for an owner of a QOF partnership or QOF S corporation after selling a qualifying investment in the QOF after it has been held at least 10 years, but would avoid the extra costs associated with negotiating the selling price of the interest in the QOF, rather than the underlying assets owned by the QOF or qualified opportunity zone business. The Treasury Department and the IRS project that this approach will lead to a reduction in transactions costs for taxpayers relative to alternative approaches (the no-action baseline and the proposed regulations), and will continue to treat similar taxpayers similarly. The number of taxpayers

[3] For a given set of section 1231 sales, positive gains for each individual taxpayer will never be lower under the gross approach than the net approach; this result follows from mathematical principles and is not specific to this example. In practice, taxpayers might choose to recognize gains differently under the two approaches. This difference complicates any projection of actual gains that would be eligible for deferral.

expected to be affected by this rule ranges between 5,000 and 11,500 QOFs, and 50,000 to 115,000 investors in QOFs.

c. Substantial Improvement of Qualified Opportunity Zone Business Property

Section 1400Z–2(d)(2)(D) requires that if tangible property was already used in a QOZ (non-original use asset) when purchased by a QOF or qualified opportunity zone business, then it needs to be substantially improved by the QOF or qualified opportunity zone business before it can become qualified opportunity zone business property. Substantial improvement, as defined by section 1400Z–2(d)(2)(D)(ii), requires the QOF or qualified opportunity zone business to more than double the adjusted basis of the property within 30 months after acquiring the property. The Treasury Department and the IRS considered two options for how to measure substantial improvement.

First, the proposed regulations provided an asset-by-asset approach. This option would require each property to be substantially improved in order to become qualified opportunity zone business property. For example, if a QOF purchases an existing commercial building, a separate determination for each piece of tangible property associated with the building would be needed, such as the structure itself, and every item of furniture and equipment within the building that is not part of the building structure.

This approach would limit the ability of taxpayers to purchase property already used within a QOZ, place that property in service in the taxpayer's business with little improvement from the previous owner, and have the property be qualified opportunity zone business property. This option would also likely encourage the purchase and substantial improvement of existing property with low existing basis; that is, property where it is easier for improvement expenditures to double the existing basis. Such properties are more likely to be older and more in need of repair and upgrades.

Second, the final regulations allow taxpayers to use an asset-by-asset approach (as provided in the proposed regulations) or a more aggregative approach. The final regulations allow purchased original use property to count towards the determination of whether non-original use property has been substantially improved if such purchased original use property improves the functionality of the non-original use property along with other conditions. Also, certain betterment expenses, such as environmental remediation or utility upgrades, which are properly chargeable to the basis of the land, may be added to the basis of a building on the land that was non-original use property for the purpose of calculating substantial improvement of that building. These rules in effect expand the definition of what expenses could be considered improvements for a particular asset. In some cases, this option could reduce compliance costs for taxpayers, as it is not always clear under the Code and regulations when expenditures should be considered an improvement of an existing property, for example a building, or be considered separate depreciable property.

These rules will make it easier for purchased non-original use property to be substantially improved compared to the proposed regulations. This will help to smooth the cliff effect that occurs with the statutory requirement that improvements need to more than double the cost basis. For example, suppose a QOF purchases a non-original use building in a QOZ for $1 million, makes $950,000 in improvements to the building that bring that building into good condition for that local market, and purchases $50,001 of furniture or equipment for use within the building. This building would not meet the substantial improvement test under the proposed regulations but it would meet it under the final regulations.

In addition, the final regulations allow a QOF or qualified opportunity zone business to aggregate multiple buildings into a single property for purposes of the substantial improvement test. The buildings must either be entirely located within a parcel of land described in a single deed, or the buildings may be on contiguous parcels of land with separate deeds if certain conditions are met that indicate the buildings are related in management or use.

This rule would expand the number of existing buildings in a QOZ that could be purchased by a QOF or a qualified opportunity zone business and be deemed to have met the substantial improvement test relative to the first option. For example, one expensive renovation project would provide excess ''improvement expenses'' that could be applied to other buildings. This increases the likelihood that certain substantial renovation projects would be undertaken. However, the ability to aggregate improvement of non-original use property could effectively allow a QOF or qualified opportunity zone business to purchase property already fully in use in a QOZ and count it as qualified opportunity zone business property, though use by the new owner would be qualitatively similar to the previous owner.

In summary, the Treasury Department and the IRS considered two primary options for how much aggregation to allow when determining whether purchased non-original use property satisfied the substantial improvement test. The different options would likely have different effects on the amount and distribution of non-original use property purchased by QOFs and qualified opportunity zone businesses. The proposed regulations would not allow any aggregation, and instead require each of the assets purchased under this option to receive substantial improvement. This would focus improvement expenditures on properties most in need of considerable rehabilitation to remain productive.

The final regulations allow aggregation, and will likely encourage the purchase and improvement of more non-original use property compared to the proposed regulations. The final regulations will also likely lead to a broader mix of properties purchased and improved relative to the first option. However, the final regulations also increase the likelihood that some buildings will meet the substantial improvement test when the individual building receives little to moderate improvements. Overall, the rules provided in the final regulations make it easier for a non-original use property to be substantially improved relative to the proposed regulations, which will encourage more investment through QOFs.

The Treasury Department and the IRS project that the number of taxpayers expected to be affected by this rule ranges between 5,500 and 12,000 QOFs plus 6,000 to 15,000 qualified opportunity zone businesses.

d. Vacancy

Property that is eligible for opportunity zone treatment must be ''original use'' or substantially improved. This statutory language leaves open the question of the conditions under which vacant property that is developed and used by an opportunity zone business might count as original use.[4] The Treasury Department and the IRS considered options of one, three, or five years for how long existing property located in a QOZ must be vacant before the purchase

[4] The Treasury Department and the IRS also considered taking no action but determined that providing a definition of vacancy and setting a time period for when vacant property could be purchased and considered original use property would be beneficial relative to providing no specific guidance.

of such property would allow it to be considered original use property. The May 2019 proposed regulations proposed that property would need to be vacant for at least five years prior to the purchase by a QOF or qualified opportunity zone business in order to satisfy the original use requirement under section 1400Z–2(d)(2)(D)(i)(II).

In selecting among these options, the Treasury Department and the IRS recognize that vacant property is an underused resource to the owner and potential users of the property, and can lower the value and use of neighboring property. The Treasury Department and the IRS further recognize that property could become vacant due to economic reasons unrelated to section 1400Z–2, but also because the owner strategically let the property become or stay vacant in expectation that the property would have a higher resale value if it were eligible to be original use property under section 1400Z–2(d)(2)(D)(i)(II).

A shorter period of required vacancy provides a greater incentive for owners of vacant property to keep it vacant for purposes of later selling it for use as original use property. This incentive may also result in owners vacating property that is currently occupied. On the other hand, a longer period of required vacancy means that on average properties would remain vacant for a longer period before being sold and put into productive use, which would increase the likelihood that such property (and possibly surrounding property) would be inefficiently used.

The final regulations provide that the required time of vacancy is three years except for property that was vacant as of the date of publication of the QOZ designation notice in which the designation of the QOZ is listed, in which case the vacancy period is one year. This one-year period for vacant property at the time of designation provides an incentive for property that was vacant for economic reasons at the time of publication of the QOZ designation notice to be quickly placed back into service through sale to a new owner, thus reducing the social costs that would occur if those properties remained unused, relative to the longer three-year period. The three-year period for property that was not initially vacant makes it costly for owners to strategically limit the use of the property in order to gain a more favorable condition for selling the property in the future, relative to a shorter period. The Treasury Department and the IRS recognize, however, that even under this three-year specification, there may be situations where a property becomes vacant for a period of time due to economic reasons and the owner of that property decides to let the property remain vacant in order to receive an expected higher price upon selling after the three-year vacancy period is met.

The number of taxpayers expected to be affected by this rule ranges between 5,500 and 12,000 QOFs plus 6,000 to 15,000 qualified opportunity zone businesses.

e. Subsidiary of a Consolidated Group

The statute is silent regarding the treatment of corporate taxpayers that file consolidated returns and seek to invest in a QOF. The Treasury Department and the IRS considered two options to address this issue. Under the proposed regulations a consolidated group could invest in a corporate QOF only if the QOF would not be treated as part of the consolidated group for tax filing purposes. That is, a QOF could not be a subsidiary of a consolidated group, because of concerns of potential conflicts between the section 1400Z–2 rules and the consolidated group rules in § 1.1502. Under this approach, the gains and losses of a corporate QOF would not be shared with the consolidated group owning the QOF when determining aggregate tax liability of the consolidated group, but rather the QOF would file its own tax return, leading to a small increase in compliance burden.

This treatment could affect the choice of QOF entity for a consolidated corporate group that wanted to own a QOF, making a partnership QOF a more likely choice as tax attributes of the partnership QOF (income, deductions, credits, etc.) would flow to the member of the consolidated corporate group that owns the QOF. Sharing those tax attributes of a partnership QOF with other members of the group is subject to certain limitations. However, if the QOF is a corporate subsidiary member of the consolidated group, there is more flexibility with how tax attributes of the QOF are shared with the rest of the consolidated group. In addition, some corporate consolidated groups are likely to favor a using a corporate form due to familiarity with the corporate rules that would lead to lower organizational costs. These additional organizational or tax compliance costs are not likely to be large, but nevertheless may discourage investment in QOFs for some consolidated groups.

Therefore, the final regulations permit corporate taxpayers filing consolidated returns to own a QOF that is a subsidiary member of the consolidated group; and, as provided in the proposed regulations, a corporate QOF may be the parent member of a consolidated group. This option will reduce the limitations on the organizational structure of QOF investments that would have occurred under the proposed regulations. The final regulations permit the consolidation of a subsidiary QOF corporation only if certain conditions are satisfied. Specifically, except in very limited circumstances, the group member making the qualifying investment in the QOF member (investor member) must maintain direct equity interest of the QOF member stock. More importantly, all investor members must be wholly owned, directly or indirectly, by the common parent of the group. The final regulations also provide special rules to govern the treatment of an investment of eligible gain in the subsidiary QOF in order not to conflict with the consolidated return rules found in § 1.1502. However, these rules are not expected to be overly burdensome, because the choice of establishing the QOF as a subsidiary member of the consolidate group are elective; taxpayers would not choose to consolidate a corporate QOF subsidiary unless the benefits to the taxpayer were greater than the costs.

One drawback to allowing QOFs to be part of subsidiary member of a consolidated group is that there would be less information available regarding taxable income and loss of the QOF and its subsidiary qualified opportunity zone businesses, as that information will be reported as part of the aggregated income and deductions of the parent on the consolidated tax return.

The number of taxpayers expected to be affected by these rules ranges between 25 and 500.

5. Economic Effects of Provisions Not Substantially Revised From the Proposed Regulations

a. Definition of Substantially All

There are five uses of the term ''substantially all'' in section 1400Z–2 but the statute is ambiguous regarding the precise meaning of this term. The final regulations establish thresholds for all five uses of this term. The final regulations provide that ''substantially all'' means at least 90 percent with regard to the three holding period requirements in section 1400Z–2(d)(2) and at least 70 percent with regard to section 1400Z–2(d)(3)(A)(i) and in the context of ''use'' in section 1400Z–2(d)(2)(D)(i)(III). The Treasury Department and the IRS have not attempted to assess how taxpayers would have interpreted these terms in the absence of specific guidance and

therefore have not projected whether these regulations will increase or decrease investment in QOZs or non-QOZ's relative to regulatory alternatives.

In choosing what values to assign to the substantially all terms, the Treasury Department and the IRS considered the economic consequences of setting the thresholds higher or lower. Setting the threshold higher would reduce investment in QOFs but would increase the percentage of that investment that would be located within a QOZ. One reason why a higher threshold would reduce overall investment in QOFs is that it will be more difficult for businesses with diverse operations and/or multiple locations to satisfy the threshold. Setting the threshold lower would increase investment in QOFs but reduce the percentage of that investment that is located within a QOZ.

A lower threshold would further increase the likelihood that a taxpayer may receive the benefit of the preferential treatment on capital gains without placing in service more tangible property within a QOZ than would have occurred in the absence of section 1400Z–2. This effect would be magnified by the way the different requirements in section 1400Z–2 interact. For example, these final regulations imply that, in certain limited fact patterns, a QOF could satisfy the substantially all standards with as little as 40 percent of the tangible property effectively owned by the fund being used within a QOZ. This could occur if 90 percent of QOF assets are invested in a qualified opportunity zone business, in which 70 percent of the tangible assets of that business are qualified opportunity zone business property; and if, in addition, the qualified opportunity zone business property is only 70 percent in use within a QOZ, and for 90 percent of the holding period for such property. Multiplying these shares together ($0.9 \times 0.7 \times 0.7 \times 0.9 = 0.4$) generates the result that a QOF could satisfy the requirements of section 1400Z–2 under the final regulations with just 40 percent of its assets effectively in use within a QOZ.

The Treasury Department and the IRS have not undertaken quantitative estimates of the volume of investment that would be placed in QOZs under the different thresholds for ''substantially all'' because we do not have data or models that can predict spatial patterns of investment with reasonable precision. The Treasury Department and the IRS further recognize that the specified thresholds may indirectly affect investment outside of QOZs; we have likewise not undertaken quantitative estimates of this investment effect.

The Treasury Department and the IRS have determined that the substantially all thresholds provided in the final regulations represent an appropriate balance between the ability of investors in QOFs to receive preferential capital gains treatment only for placing a consequential amount of tangible property (used in the underlying business) within a QOZ, and the flexibility provided to business operations so as not to significantly distort the types of businesses that can qualify for opportunity zone funds.

b. Treatment of Leased Property

The Treasury Department and the IRS have determined that leased property that is located in a QOZ may be treated as qualified opportunity zone business property under certain conditions. This determination means, effectively, that the value of leased property should be included in both in the numerator and the denominator of the 90-percent investment standard and the substantially all tests.[5] We project that the inclusion of leased property will enhance the efficiency of business decisions compared to other available regulatory options because leasing is a common business practice and because business decisions would be distorted if otherwise similar property (owned versus leased) were treated differently.

This treatment of leased property is efficiency-enhancing (compared to alternative treatments) because of other features of the statute. For example, a start-up business that leased office space within a QOZ and owned tangible property in the form of computers and other office equipment would likely fail the substantially all test (if the office space is sufficiently valuable relative to the other tangible property) because the leased property is included in the denominator of the substantially all test; this failure to satisfy the substantially all test would occur despite all of this business's operations being located within a QOZ. This possibility may lead the business to purchase rather than lease its office property, a decision that significantly changes the nature of the business's risk and expenses.

The Treasury Department and the IRS recognize that the treatment of leased property as qualified opportunity zone business property may weaken the incentive for taxpayers to construct new real property or renovate existing real property within a QOZ, as taxpayers would be able to lease existing real property in a zone without improving it and thereby become a qualified opportunity zone business (assuming the other conditions of the statute were met). However, allowing the leasing of existing real property within a zone may encourage fuller utilization and improvement of such property and limit the abandonment or destruction of existing productive property within a QOZ when new tax-favored real property becomes available.

In summary, the Treasury Department and the IRS project that the inclusion of leased property in both the numerator and the denominator of the 90-percent investment standard and the substantially all test will increase economic activity within QOZs relative to alternative decisions including the no-action baseline. This provision will reduce potential distortions between owned and leased property that may occur under other options.

c. Valuation of Property

The final regulations provide taxpayers with a choice between two methods for determining the asset values for purposes of the 90-percent investment standard in section 1400Z–2(d)(1) for QOFs or the value of tangible property for the substantially all test in section 1400Z–2(d)(3)(A)(i) for qualified opportunity zone businesses. Under the first method (applicable financial statement valuation method), the taxpayer values owned or leased property as reported on its applicable financial statement for the reporting period. Under the alternative valuation method, the taxpayer sets the value of owned property equal to the unadjusted cost basis of the property under section 1012. The final regulations specify that the value of leased property under the alternative method equals the present value of total lease payments at the beginning of the lease. The value of the property under the alternative method for the 90-percent investment standard and substantially all test does not change over time as long as the taxpayer continues to own or lease the property.

The Treasury Department and the IRS project that the two methods will, in the majority of cases, provide similar values for leased property at the time that the lease begins because, as beginning in 2019, generally accepted accounting principles (GAAP) require public companies to calculate the present value of lease payments in order to recognize the value of leased assets on the balance sheet. However, there are situations in which the two methods may differ in the value they assign to leased property.

[5] Under the statute, the value of leased property is included in the denominator of the substantially all test. The statute is ambiguous, however, as to whether leased property should be included in the numerator.

On financial statements, the value of the leased property declines over the term of the lease. Under the alternative method, the value of the leased asset is calculated once at the beginning of the lease term and remains constant while the term of the lease is still in effect. This difference in valuation of property over time between using financial statements and the alternative method also exists for owned property. In addition, the two approaches would generally apply different discount rates, thus leading to some difference in the calculated present value under the two methods.

The Treasury Department and the IRS provide the alternative method to allow for taxpayers that either do not have applicable financial statements or do not have them available in time for the asset tests. In addition, the alternative method is simpler, thus reducing compliance costs, and provides greater certainty in projecting future compliance with the 90-percent investment standard and the substantially all test. Thus, even some taxpayers with applicable financial statements may choose to use the alternative method. One drawback to the alternative method is that it is less likely to provide accurate asset valuation over time because it does not account for depreciation or other items that may affect the value of assets after the time of purchase, and, over time, the values used for the sake of the 90-percent investment standard and the substantially all test may diverge from the actual value of the property.

Because this provision provides an election to taxpayers, the Treasury Department and the IRS project that this provision will slightly increase investment in QOFs, relative to not providing an election. The Treasury Department and the IRS have not estimated the proportion of taxpayers likely to use the alternative method nor the volume of increased investment in QOFs relative to not providing an election.

d. Gross Income Requirement of Section 1397C(b)(2)

Section 1400Z–2(d)(3)(A)(ii) incorporates the requirement of section 1397C(b)(2) that a qualified business entity must derive at least 50 percent of its total gross income during a taxable year from the active conduct of a qualified business in a zone. The final regulations provide multiple safe harbors for determining whether this standard has been satisfied.

Two of these safe harbors provide that the 50 percent of gross income standard would be satisfied if the majority of the labor input of the trade or business is located within a QOZ and provide two different methods for measuring the labor input of the trade or business. The labor input can be measured in terms of hours (hours performed test) or compensation paid (amounts paid test) of employees, independent contractors, and employees of independent contractors for the trade or business. The final regulations clarify that guaranteed payments to partners in a partnership for services provided to the trade or business are also included in the amounts paid test. The final regulations provide that if at least 50 percent of the labor input of the trade or business is located within a QOZ (as measured by one of the two provided approaches), then the section 1397C(b)(2) requirement is satisfied.

In addition, a third safe harbor (business functions test) provides that the 50-percent gross income requirement is met if the tangible property of the trade or business located in a QOZ and the management or operational functions performed in the QOZ are each necessary for the generation of at least 50 percent of the gross income of the trade or business.

The determination of the location of income for businesses that operate in multiple jurisdictions can be complex, and the rules promulgated by taxing authorities to determine the location of income are often burdensome and may distort economic activity. The provision of alternative safe harbors in the final regulations should reduce the compliance and administrative burdens associated with determining whether this statutory requirement has been met. In the absence of such safe harbors, some taxpayers may interpret the 50 percent of gross income standard to require that a majority of the sales of the entity must be located within a zone. The Treasury Department and the IRS have determined that a standard based strictly on sales would discriminate against some types of businesses (for example, manufacturing) in which the location of sales is often different from the location of the production, and thus would preclude such businesses from benefitting from the incentives provided in section 1400Z–2. Furthermore, the potential distortions introduced by the provided safe harbors would increase incentives to locate labor inputs within a QOZ. To the extent that such distortions exist, they further the statutory goal of encouraging economic activity within QOZs. Given the flexibility provided to taxpayers in choosing a safe harbor, other distortions, such as to business organizational structuring, are likely to be minimal.

e. Working Capital Safe Harbor

Section 1400Z–2 contains several rules limiting taxpayers from benefitting from the deferral and exclusion of capital gains from income offered by that section without also locating investment within a QOZ. The final regulations clarify the rules related to nonqualified financial property and what amounts can be held in cash and cash equivalents as working capital. A qualified opportunity zone business is subject to the requirements of section 1397C(b)(8), that less than 5 percent of the aggregate adjusted basis of the entity is attributable to nonqualified financial property. The final regulations establish a working capital safe harbor consistent with section 1397C(e)(1), under which a qualified opportunity zone business may hold cash or cash equivalents for a period not longer than 31 months and not violate section 1397C(b)(8). The final regulations also provide that qualified opportunity zone businesses may utilize multiple working capital safe harbors, provided that each one satisfies all of the conditions of the safe harbor provided in the final regulations. In the case where multiple working capital safe harbors applies to the same unit of tangible property, then total length of time the working capital safe harbor may last is 62 months.

The Treasury Department and the IRS expect that the establishment of the working capital safe harbors under these parameters will provide net economic benefits. Without specification of the working capital safe harbor, some taxpayers would not invest in a QOF for fear that the QOF would not be able to deploy the funds soon enough to satisfy the 90-percent asset test. Thus, this rule would generally encourage investment in QOFs by providing greater specificity to how an entity may consistently satisfy the statutory requirements for maintaining a QOF without penalty.

A longer or a shorter period could have been chosen for the working capital safe harbor. A shorter time period would minimize the ability of taxpayers to use the investment in a QOF as a way to lower taxes without actually investing in tangible assets within a QOZ, but taxpayers may also forego legitimate investments within an opportunity zone out of concern of not being able to deploy the working capital fast enough to meet the requirements. A longer period would have the opposite effects. Taxpayers could potentially invest in a QOF and receive the benefits of the tax incentive for multiple years before the money is invested into a QOZ.

f. QOF Reinvestment Rule

The final regulations provide that a QOF has 12 months from the time of the sale or disposition of qualified opportunity zone property or the return of capital from investments in qualified opportunity zone stock or qualified opportunity zone partnership interests to reinvest the proceeds in other qualified opportunity zone property before the proceeds would not be considered qualified opportunity zone property with regards to the 90-percent investment standard. This rule provides clarity and gives substantial flexibility to taxpayers in satisfying the 90-percent investment standard. The Treasury Department and the IRS have not projected the effect of this rule on the volume of investment held by QOFs compared to a no action baseline.

g. Clarity Regarding Electing Post-10-Year Gain Exclusion if Zone Designation Expires

The final regulations specify in § 1.1400Z2(c)–1 that expiration of a zone designation would not impair the ability of a taxpayer to elect the exclusion from gains for investments held for at least 10 years, provided the disposition of the investment occurs prior to January 1, 2048. The Treasury Department and the IRS considered four alternatives regarding the interaction between the expiration of the designated zones and the election to exclude gain for investments held more than 10 years. A discussion of the economic effects of the four options follows.

(i) Remaining Silent on Electing Post-10-Year Gain Exclusion

The first alternative would be for the final regulations to remain silent on this issue. Section 1400Z–2(c) permits a taxpayer to increase the basis in the property held in a QOF longer than 10 years to be equal to the fair market value of that property on the date that the investment is sold or exchanged, thus excluding post-acquisition capital gain on the investment from tax. However, the statutory expiration of the designation of QOZs on December 31, 2028, makes it unclear to what extent investments in a QOF made after 2018 would qualify for this exclusion.

In absence of the guidance provided in the final regulations, some taxpayers may have believed that only investments in a QOF made prior to January 1, 2019, would be eligible for the exclusion from gain if held greater than 10 years. Such taxpayers may have rushed to complete transactions within 2018, while others may choose to hold off indefinitely from investing in a QOF until they received clarity on the availability of the 10-year exclusion from gain for investments made later than 2018. Other taxpayers may have planned to invest in a QOF after 2018 with the expectation that future regulations would be provided or the statute would be amended to make it clear that dispositions of assets within a QOF after 2028 would be eligible for exclusion if held longer than 10 years. The ambiguity of the statute would likely lead to uneven response by different taxpayers, dependent on the taxpayer's interpretation of the statute, which may lead to an inefficient allocation of investment across QOZs.

(ii) Providing a Clear Deadline for Electing Post-10-Year Gain Exclusion

The alternative adopted by the final regulations clarifies that as long as the investment in the QOF was made with funds subject to a proper deferral election under section 1400Z–2(a), then the 10-year gain exclusion election is allowed as long as the disposition of the investment occurs before January 1, 2048. This rule would provide certainty to taxpayers regarding the timing of investments eligible for the 10-year gain exclusion. Taxpayers would have a more uniform understanding of what transactions would be eligible for the favorable treatment on capital gains. This would help taxpayers determine which investments provide a sufficient return to compensate for the extra costs and risks of investing in a QOF. This rule would likely lead to an increase in investment within QOFs compared the final regulations remaining silent on this issue.

However, setting a fixed date for the disposition of eligible QOFs investments could introduce economic inefficiencies. Some taxpayers might dispose of their investment in a QOF by the deadline in the proposed regulation primarily in order to receive the benefit of the gain exclusion, even if that selling date is not optimal for the taxpayer in terms of the portfolio of assets that the taxpayer could have chosen to invest in were there no deadline. Setting a fixed deadline may also generate an overall decline in asset values in some QOZs if many investors in QOFs seek to sell their portion of the fund within the same time period. This decline in asset values may affect the broader level of economic activity within some QOZs or affect other investors in such zones that did not invest through a QOF. In anticipation of this fixed deadline, some taxpayers may choose to dispose of QOF assets earlier than the deadline to avoid an anticipated ''rush to the exits,'' but this would seem to conflict with the purpose of the incentives in the statute to encourage ''patient'' capital investment within QOZs. While the final regulations may produce these inefficiencies, by providing a long time period for which taxpayers may dispose of their investment within a QOF and still qualify for the exclusion the final regulations will lead any such inefficiencies to be minor.

(iii) Providing No Deadline for Electing Gain Exclusion

As an alternative, the final regulations could have provided no deadline for electing the 10-year gain exclusion for investments in a QOF, while still stating that the ability to make the election is not impaired solely because the designation of one or more QOZs ceases to be in effect. While this alternative would eliminate the economic inefficiencies associated with a fixed deadline and would likely lead to greater investment in QOFs, it could introduce substantial additional administrative and compliance costs. Taxpayers would also need to maintain records and make efforts to maintain compliance with the rules of section 1400Z–2 on an indefinite basis.

(iv) Providing Fair Market Value Basis Without Disposition of Investment

Another alternative considered would allow taxpayers to elect to increase the basis in their investment in the QOF if held at least 10 years to the fair market value of the investment without disposing of the property, as long as the election was made prior to January 1, 2048. (Or, the final regulations could have provided that, at the close of business of the day on which a taxpayer first has the ability to make the 10-year gain exclusion election, the basis in the investment automatically sets to the greater of current basis or the fair market value of the investment.) This alternative would minimize the economic inefficiencies of the proposed regulations resulting from taxpayers needing to dispose of their investment in the opportunity zone at a fixed date not related to any factor other than the lapse of time. However, this approach would require a method of valuing unsold assets that could raise administrative and compliance costs. It may also require the maintenance of records and trained compliance personnel for over two decades.

(v) Summary

As discussed in section V.B of the Explanation of Provisions of the October 2018 proposed regulations, the Treasury Department and the IRS have determined the ability to exclude gains

for investment held at least 10 years in a QOF is integral to the TCJA's purpose of creating QOZs. The final regulations provide a uniform signal to all taxpayers on the availability of this tax incentive, which should encourage greater investment, and a more efficient distribution of investment, in QOFs than in the absence of the final regulations. The relative costs and benefits of the various alternatives are difficult to measure and compare. The final regulations would likely produce the lowest compliance and administrative costs among the alternatives and any associated economic inefficiencies are likely to be small.

II. Paperwork Reduction Act

The collections of information in these final regulations are in §§ 1.1400Z2(b)–1(h), 1.1502–14Z(c)(2), (f)(2)(ii), (iii), and (iv), (f)(3), and (h), and 1.1504–3(b)(2) and (c). The information in all of the collections of information provided will be used by the IRS for tax compliance purposes.

A. Partnership and S Corporation Collections of Information

The final regulations establish a new collection of information in § 1.1400Z2(b)–1(h). In § 1.1400Z2(b)–1(h)(1), the collection of information requires a partnership that takes a deferral election to notify all of its partners of the deferral election and their shares of the deferred gain. Similar requirements are set forth in § 1.1400Z2(b)–1(h)(4) regarding S corporations and S corporation shareholders.

The collection of information in § 1.1400Z2(b)–1(h)(2) requires indirect owners of a QOF partnership that sell or otherwise dispose of all or a portion of their indirect interest in the QOF partnership in a transaction that is an inclusion event to notify the QOF owner so it can recognize an appropriate amount of deferred gain. Lastly, the collection of information in § 1.1400Z2(b)–1(h)(3) requires a QOF partner to notify the QOF partnership of an election under section 1400Z–2(c) to adjust the basis of the qualifying QOF partnership interest that is disposed of in a taxable transaction. Similar requirements again are set forth in § 1.1400Z2(b)–1(h)(4) regarding QOF S corporations and QOF S corporation shareholders.

The collection of information contained in this final regulation will not be conducted using a new or existing IRS form. The notifications required by § 1.1400Z2(b)–1(h)(1) will be provided by the respective partnership to its partners n order to properly track the amount of eligible gain invested in a QOF. The notification requires a statement to be sent by the partnership electing deferral to the relevant partners.

The notifications required by § 1.1400Z2(b)–1(h)(2) will be provided by indirect owners of a QOF partnership to the QOF owner and must include information needed in order to enable the QOF owner, in a timely manner, to recognize an appropriate amount of deferred gain. The notification requires a statement to be sent from an indirect owner of a QOF partnership to the QOF owner.

The notifications required by § 1.1400Z2(b)–1(h)(3) will be provided by a QOF partner to a QOF partnership to inform the partnership that the partner made an election under section 1400Z–2(c) to adjust the basis of the qualifying QOF partnership interest disposed of in a taxable transaction. The notification requires a statement be sent by the partner electing deferral under section 1400Z–2(c) to the QOF partnership.

Similar notifications between shareholders and S Corporations are also required by § 1.1400Z2(b)–1(h)(4).

The likely respondents are partnerships and partners, and S corporations and S corporation shareholders.

Estimated total annual reporting burden: 8,500 hours.

Estimated average annual burden per respondent: 1 hour.

Estimated number of respondents: 8,500.

Estimated frequency of responses: One time notification.

B. Collections of Information Under Existing Tax Forms

The collections of information imposed on consolidated groups in these regulations are contained in §§ 1.1502–14Z(c)(2), (f)(2)(ii), (iii), (iv), and (f)(3), 1.1502–14Z(h), and 1.1504–3(b)(2) and (c). The collection of information provided by these regulations has been approved by the Office of Management and Budget (OMB) under control number 1545–0123. The information is required to inform the IRS on whether, and to what extent, a taxpayer makes any of the consolidated group elections as described in these regulations. For purposes of the Paperwork Reduction Act, 44 U.S.C. 3501 *et seq.* (PRA), the reporting burden associated with the collection of information in Form 1065, ''U.S. Return of Partnership Income,'' Form 1120, ''U.S. Corporation Income Tax Return,'' Form 851, ''Affiliations Schedule,'' and/or Form 8996 will be reflected in the Paperwork Reduction Act Submission associated with OMB control number 1545–0123.

The consolidated return rules in §§ 1.1502–14Z and 1.1504–3 provide for certain elections that are available to consolidated groups. These elections may require the consolidated group and/or the QOF to file original, amended or superseding returns and attach an election statement to such return with the required information to make the applicable election. Section 1.1504–3(b)(2) generally allows the consolidated group (subject to certain requirements and limitations) to elect to consolidate a subsidiary QOF C corporation that was formed or acquired by the consolidated group after May 1, 2019. In order to make the § 1.1504–3(b)(2) election, the consolidated group must attach an election statement as described in § 1.1504–3(c) to its Form 1120 and include the QOF C corporation as a subsidiary member on its Form 851. Section 1.1502–14Z(c)(2) allows a consolidated group to elect to treat an investment of one member as a qualifying investment by another member. This election is available to consolidated groups after March 13, 2020. The consolidated group must attach an election statement as described in § 1.1502–14Z(h)(2) with its Form 1120.

The elections provided in § 1.1502–14Z(f) are available only to consolidated groups that formed or acquired a subsidiary QOF C corporation and included the subsidiary QOF C corporation in its consolidated group prior to May 1, 2019. These elections allow the consolidated group to treat the subsidiary QOF C corporation as (i) a QOF partnership, (ii) a non-member QOF C corporation, (iii) a non-QOF C corporation, or (iv) to continue treating the pre-existing QOF subsidiary corporation as a member of the consolidated group. In general, if the consolidated group makes an election under § 1.1502–14Z(f), the consolidated group is required to amend its Form 1120 to account for the changes resulting from the election and to attach the applicable election statement as provided in § 1.1502–14Z(h)(3). If the consolidated group makes an election to treat the QOF C corporation as a QOF partnership as described in § 1.1502–14Z(f)(2)(ii), the QOF partnership is required to file its own Form 1065 as well as a new Form 8996 for the taxable year the election is effective. If the consolidated group elects to treat the subsidiary QOF C corporation as not a member of the group (as described in § 1.1502–14Z(f)(2)(iii)), the subsidiary

QOF C corporation is required to file its own Form 1120 and include its Form 8996 with the return for the taxable year the election is effective.

The following table displays the number of respondents estimated to be required to report on Form 1120, Form 851, Form 8996 and/or Form 1065, with respect to the collections of information required by the these consolidated group regulations. Due to the absence of available tax data, estimates of respondents required to attach a statement to other types of tax returns, as applicable, are not available.

	Number of respondents (estimated)
Transition Relief Elections—§ 1.1502–14Z(f):	
Form 1120	10 to 100.
Expected Number of Consolidated C Corporations formed after May 1, 2019:	
Form 1120	0 to 50.

Source: RAAS:CDW.

The numbers of respondents in the table were estimated by the Research, Applied Analytics and Statistics Division (RAAS) of the IRS from the Compliance Data Warehouse (CDW).

Data for Form 1120 represents estimates of the total number of taxpayers that may attach an election statement to their Form 1120 to make the elections in §§ 1.1.1502–14Z(c)(2), (f)(2)(ii), (iii), and (iv), and (f)(3), and 1.1504–3(b)(2). The lower bound estimate is based on the number of consolidated group taxpayers filing Form 1120 and Form 8996 through July 2019. The upper bound estimate is based on consolidated group taxpayer filing trends, the observed filings to date, and uncertainty about the number of future filers. Accordingly, the difference between the lower bound and upper bound estimates reflect an estimate of the possible number of respondents as a result of the changes made by TCJA and the regulations.

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

III. Regulatory Flexibility Act

Pursuant to the Regulatory Flexibility Act (5 U.S.C. chapter 6), it is hereby certified that the final regulations will not have a significant economic impact on a substantial number of small entities under section 601(6) of the Regulatory Flexibility Act (small entities).

As discussed elsewhere in this preamble, the final regulations provide certainty and clarity to taxpayers regarding the utilization of the tax preference for capital gains provided in section 1400Z–2 by defining terms, calculations, and acceptable forms of documentation. The Treasury Department and the IRS anticipate that this clarity generally will encourage taxpayers to invest in QOFs and will increase the amount of investment located in QOZs. Investment in QOFs is entirely voluntary, and the certainty that would be provided by these final regulations, will minimize any compliance or administrative costs, such as the estimated average annual burden (1 hour) under the Paperwork Reduction Act. For example, the final regulations provide multiple safe harbors for the purpose of determining whether the 50-percent gross income test has been met as required by section 1400Z–2(d)(3)(A)(ii) for a qualified opportunity zone business. Taxpayers affected by these final regulations include QOFs, investors in QOFs, and qualified opportunity zone businesses in which a QOF holds an ownership interest. The final regulations will not directly affect the taxable incomes and liabilities of qualified opportunity zone businesses; they will affect only the taxable incomes and tax liabilities of QOFs (and owners of QOFs) that invest in such businesses. Although there is a lack of available data regarding the extent to which small entities invest in QOFs, will certify as QOFs, or receive equity investments from QOFs, the Treasury Department and the IRS project that most of the investment flowing into QOFs will come from large corporations and wealthy individuals, though some of these funds would likely flow through an intermediary investment partnership. It is expected that some QOFs and qualified opportunity zone businesses would be classified as small entities; however, the number of small entities significantly affected is not likely to be substantial.

For the reasons explained previously, the Treasury Department and the IRS certify that the final regulations will not have a significant economic impact on a substantial number of small entities. Pursuant to section 7805(f), the notice of proposed rulemaking preceding these final regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

IV. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 (UMRA) requires that agencies assess anticipated costs and benefits and take certain other actions before issuing a final rule that includes any Federal mandate that may result in expenditures in any one year by a state, local, or tribal government, in the aggregate, or by the private sector, of $100 million in 1995 dollars, updated annually for inflation. In 2019, that threshold is approximately $154 million. This rule does not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private sector in excess of that threshold.

V. Executive Order 13132: Federalism

Executive Order 13132 (entitled Federalism) prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial, direct compliance costs on state and local governments, and is not required by statute, or preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law.

VI. Executive Order 13175: Consultation and Coordination With Indian Tribal Governments

Executive Order 13175 requires that Federal departments and agencies engage in consultation procedures in certain circumstances where regulations are issued which have substantial direct effects with respect to the Federal Government and Indian tribes. As noted in the Background, on October 21, 2019, the Treasury Department and the IRS held a government-to-government tribal consultation on Opportunity Zones (Consultation). Seven organizations representing tribal interests participated, with one tribal designee providing comments expressing support for the May 2019 proposed regulations. In addition, many tribes submitted written comments in response to the proposed regulations, and the presiding officer of one Indian tribe provided oral testimony at the February 14, 2019 public hearing.

Several commenters requested that Indian tribal governments and corporations organized under Indian tribal laws should be included in the definition of entities eligible to be a QOF. The final regulations provide that an entity ''organized in'' one of the 50 states includes an entity organized under the law of a federally recognized Indian tribe if the entity's domicile is located in one of the 50 states or the District of Columbia. Such entity satisfies the requirement in section 1400Z–2(d)(2)(B)(i) and (C) that

qualified opportunity zone stock is stock in a domestic corporation, and a qualified opportunity zone partnership interest is an interest in a domestic partnership.

The Treasury Department and the IRS, while acknowledging the sovereignty of Indian tribal governments, also note that an entity eligible to be a QOF must be subject to Federal income tax, including the penalty imposed by section 1400Z–2(f)(1) where a QOF fails to meet the 90-percent investment standard, regardless of the laws under which it is established or organized. Tribal commenters at the Consultation did not disagree with the position that if an entity organized under the law of an Indian tribal government is eligible to be a QOF, and the entity's domicile is located in one of the 50 states or the District of Columbia, that such entity would be subject to Federal income tax because the QOF would include investors from outside of the tribe. Accordingly, the Treasury Department and IRS affirm these positions and incorporate a reference to entities organized under the law of an Indian tribal government in the definition of the term ''eligible entity.''

Several tribal commenters, commenting on the October 2018 proposed regulations (83 FR 54279), requested that leased tangible property qualify as qualified opportunity zone business property for purposes of the section 1400Z–2 although the statute only addresses the qualification of tangible property acquired by purchase, as defined in section 179(d)(2), as qualified opportunity zone business property. The commenters stated that typically long-term ground leases of land held in trust by the Federal government are used for economic development purposes because such real property is generally not transferred through a sale. As provided for in the May 2019 proposed regulations (84 FR 18652), leased tangible property may qualify as qualified opportunity zone business property held by a QOF of qualified opportunity zone business, provided the regulatory requirements are met. At the Consultation, no participant requested additional guidance on this provision, or disagreed with the position taken by the Treasury Department and the IRS.

Prior to the publication of the May 2019 proposed regulations (84 FR 18652), the Treasury Department and the IRS received a comment requesting that the final regulations provide flexibility regarding the valuation of leases. The commenter requested that the final regulations permit QOFs to use a basis for valuing property other than the basis used for GAAP purposes (for example, cost basis under section 1012). Because Indian tribal governments typically rely upon leases of land held in trust by the Federal Government for economic development and recent changes to GAAP methods require the recognition of leasehold interests valued at the present value of prospective lease payments over the lifetime of the lease, the commenter was concerned that applying GAAP methods to value long-term leasehold interests would result in eligible entities not qualifying as QOFs or qualified opportunity zone businesses. In responding to this comment, as well as other comments expressing similar concerns, the Treasury Department and the IRS determined that the alternative valuation method for leased tangible property, as set forth in the final regulations, addresses the concerns raised by these commenters. In addition, the Treasury Department and the IRS note that no participant of the Consultation requested additional guidance regarding these issues. Therefore, proposed § 1.1400Z2(d)–1(b)(3) has not been modified as a result of those comments.

Following the Consultation, one tribe submitted additional comments regarding the issue of whether leased property is qualified opportunity zone business property. First, the commenter asked for clarification on whether leasehold interests of the real property subject to a sublease can be qualified opportunity zone business property for a qualified opportunity zone business where the sublease is entered into after December 31, 2017. The Treasury Department and the IRS, while declining to clarify the rule, generally do not view tangible property acquired under a sublease entered into after December 31, 2017, as necessarily different from tangible property acquired under a lease entered into after December 31, 2017, to the extent that the tangible property otherwise would qualify as qualified opportunity zone business property.

Second, the commenter inquired whether a leasehold interest that was assigned by a tribe to a qualified opportunity zone business would not qualify as qualified opportunity zone business property because the leasehold interest is not tangible property solely being leased or subleased to the qualified opportunity zone business. The Treasury Department and the IRS agree that assigning an existing lease, the parties to which are not related persons within the meaning of section 1400Z–2(e)(2), to another entity would not prevent the tangible property subject to the lease from qualifying as qualified opportunity zone business property. However, it should be noted that assigning an existing lease that was entered into by unrelated persons to an assignee that is related person with respect to the lessee may make the leased tangible property subject to the special rules for leases between related persons within the meaning of section 1400Z–2(e)(2).

In addition to these comments, one tribe requested a more robust reporting regime to measure the benefits of section 1400Z–2. As discussed in part IX.A. of this Summary of Comments and Explanation of Revision, the Treasury Department and the IRS have modified the Form 8996 to request additional reporting information from QOFs for tax administration purposes, which may also be helpful in measuring the impact and effectiveness of section 1400Z–2 on designated qualified opportunity zones.

VII. Congressional Review Act

The Administrator of the Office of Information and Regulatory Affairs of the Office of Management and Budget has determined that this is a major rule for purposes of the Congressional Review Act (CRA) (5 U.S.C. 801 *et seq.*).

Drafting Information

The principal authors of these final regulations are Alfred Bae and Kyle Griffin, Office of the Associate Chief Counsel (Income Tax & Accounting); Jeremy Aron-Dine and Sarah Hoyt, Office of the Associate Chief Counsel (Corporate); and Marla Borkson, Sonia Kothari, and Vishal Amin, Office of the Associate Chief Counsel (Passthroughs and Special Industries). Other personnel from the Treasury Department and the IRS participated in their development.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings, and Notices cited in this preamble are published in the Internal Revenue Bulletin (or Cumulative Bulletin) and are available from the Superintendent of Documents, U.S. Government Publishing Office, Washington, DC 20402, or by visiting the IRS website at *http://www.irs.gov.*

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 is amended by adding sectional authorities for §§ 1.1400Z2(a)–1 through 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 in numerical order to read in part as follows:

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

Section 1.1400Z2(a)–1 also issued under 26 U.S.C. 1400Z–2(e)(4).

Section 1.1400Z2(b)–1 also issued under 26 U.S.C. 1400Z–2(e)(4).

Section 1.1400Z2(c)–1 also issued under 26 U.S.C. 1400Z–2(e)(4).

Section 1.1400Z2(d)–1 also issued under 26 U.S.C. 1400Z–2(e)(4).

Section 1.1400Z2(d)–2 also issued under 26 U.S.C. 1400Z–2(e)(4).

Section 1.1400Z2(f)–1 also issued under 26 U.S.C. 1400Z–2(e)(4).

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Section 1.1502–14Z also issued under 26 U.S.C. 1400Z–2(e)(4) and 1502.

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Section 1.1504–3 also issued under 26 U.S.C. 1400Z–2(e)(4) and 1504(a)(5).

* * * * *

■ **Par. 2.** Section 1.1400Z2–0 is added to read as follows:

§ 1.1400Z2–0. Table of Contents.

This section lists the table of contents for §§ 1.1400Z2(a)–1 through 1.1400Z2(f)–1.

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(37) Qualifying section 355 transaction.
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(1) Attributes of gains included in income under section 1400Z–2(a)(1)(B).
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(6) Amount invested for purposes of section 1400Z–2(a)(1)(A).
(7) Eligible gains that a partnership elects to defer.
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§ 1.1400Z2 (d)–1 Qualified opportunity funds and qualified opportunity zone businesses.

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§ 1.1400Z2 (d)–2 Qualified opportunity zone business property

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§ 1.1400Z2 (e)–1 [Reserved]

§ 1.1400Z2 (f)–1 Administrative rules-penalties, anti-abuse, etc.

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(1) In general.
(2) Prior periods.

■ **Par. 3.** Section 1.1400Z2(a)–1 is added to read as follows:

§ 1.1400Z2 (a)–1 Deferring tax on capital gains by investing in opportunity zones.

(a) *Deferring tax on capital gains*—(1) *Overview.* Under section 1400Z–2(a) of the Internal Revenue Code (Code) and the section 1400Z–2 regulations (as defined in paragraph (b)(41) of this section), an eligible taxpayer may elect to defer recognition of some or all of one or more eligible gains that otherwise would be recognized by the eligible taxpayer in the taxable year to the extent that the eligible taxpayer timely acquires a qualifying investment in a qualified opportunity fund (QOF) within the meaning of section 1400Z–2(d)(1) and § 1.1400Z2(d)–1. Paragraph (a)(2) of this section describes how a taxpayer elects to defer gain. Paragraph (b) of this section defines terms used in the section 1400Z–2 regulations. Paragraph (c) of this section provides operational rules for applying section 1400Z–2 and the section 1400Z–2 regulations, including special rules regarding the election to defer gain under section 1400Z–2(a) and this section when an eligible taxpayer that is a partnership, S corporation, trust, or decedent's estate recognizes an eligible gain in a taxable year. Paragraph (d) of this section provides the manner in which a deferral election under section 1400Z–2(a) must be made. Paragraph (e) of this section provides the treatment of section 1400Z–2 for purposes of § 1.897–6T. Paragraph (f) of this section provides rules for mixed-funds investments. Paragraph (g) of this section provides dates of applicability. See §§ 1.1502–14Z and 1.1504–3 for special rules applicable to consolidated groups that invest in QOFs.

(2) *Procedure for deferring gain.* A taxpayer defers gain, in whole or in part, by making an election on its Federal income tax return for the taxable year in which the gain would be included if not deferred. The election must be made in the manner prescribed by the Internal Revenue Service in guidance published in the Internal Revenue Bulletin or in forms and instructions (see §§ 601.601(d)(2) and 601.602 of this chapter).

(b) *Definitions.* The following definitions apply for purposes of section 1400Z–2 and the section 1400Z–2 regulations:

(1) *30-month substantial improvement period.* The term *30-month substantial improvement period* means any 30-month period, beginning after the date of acquisition of tangible property, in which additions to the basis of the tangible property in the hands of the QOF or qualified opportunity zone business (see § 1.1400Z2(d)–2(b)(4)) exceed an amount equal to the adjusted basis of such property at the beginning of the 30-month period in the hands of the QOF or qualified opportunity zone business.

(2) *70-percent tangible property standard.* The term *70-percent tangible property standard* means the requirement in section 1400Z–2(d)(3)(A)(i) that a qualified opportunity zone business must satisfy with respect to qualified opportunity zone business property (see § 1.1400Z2(d)–2) that the qualified opportunity zone business holds, whether the qualified opportunity zone business property is owned by the qualified opportunity zone business or leased by the qualified opportunity zone business from another person.

(3) *70-percent use test.* The term *70-percent use test* means the test used to determine if a QOF or qualified opportunity zone business satisfies the requirement in sections 1400Z–2(d)(2)(D)(i)(III) and 1400Z–2(d)(3)(A)(i) that substantially all of the use of tangible property was in a qualified opportunity zone.

(4) *90-percent investment standard.* The term *90-percent investment standard* means the requirement provided in section 1400Z–2(d)(1) that a QOF must hold at least 90 percent of its assets in qualified opportunity zone property, as defined in section 1400Z–2(d)(2) and § 1.1400Z2(d)–1(c)(1), determined by the average of the percentage of qualified opportunity zone property held by the QOF as measured on the last day of the first six-month period and on the last day of the taxable year of the QOF.

(5) *90-percent qualified opportunity zone property holding period.* The term *90-percent qualified opportunity zone property holding period* means the minimum portion of a QOF's holding period in stock of a corporation or interests in a partnership, during which the corporation or partnership qualifies as a qualified opportunity zone business in order for the stock or the partnership interests to meet the substantially all requirement under section 1400Z–2(d)(2)(B)(i)(III) to be treated as qualified

opportunity zone stock or the substantially all requirement under section 1400Z–2(d)(2)(C)(iii) to be treated as qualified opportunity zone partnership interests, as applicable, held by the QOF.

(6) *90-percent qualified opportunity zone business property holding period.* The term *90-percent qualified opportunity zone business property holding period* means the minimum portion of a QOF's or qualified opportunity zone business's holding period in tangible property during which the 70-percent use test with respect to the tangible property must be satisfied, in order for the tangible property to meet the requirement under section 1400Z–2(d)(2)(D)(i)(III) to be treated as qualified opportunity zone business property held by the QOF or qualified opportunity zone business.

(7) *180-day period*—(i) *In general.* Except as otherwise provided elsewhere in this section, the term *180-day period* means the 180-day period referred to in section 1400Z–2(a)(1)(A) with respect to any eligible gain meeting the requirements of paragraph (b)(11) of this section that begins on the day on which the gain would be recognized for Federal income tax purposes if the eligible taxpayer did not elect under section 1400Z–2 and the section 1400Z–2 regulations to defer recognition of that gain.

(ii) *180-day period for RIC and REIT capital gain dividends*—(A) *General rule.* Unless the shareholder of a regulated investment company (RIC) or real estate investment trust (REIT) chooses to apply paragraph (b)(7)(ii)(B) of this section, the 180-day period for a RIC or REIT capital gain dividend begins on the last day of the shareholder's taxable year in which the capital gain dividend would otherwise be recognized by the shareholder.

(B) *Elective rule.* Notwithstanding the general rule in paragraph (b)(7)(ii)(A) of this section, a shareholder of a RIC or REIT may choose to treat the 180-day period with respect to a capital gain dividend that the shareholder receives from the RIC or REIT as beginning on the date of the dividend distribution; provided, however, that the aggregate amount of the shareholder's eligible gain with respect to capital gain dividends from the RIC or REIT is limited to the aggregate amount of capital gain dividends reported for that shareholder by the RIC for that shareholder's taxable year or designated for that shareholder by the REIT for that shareholder's taxable year.

(C) *Undistributed capital gains.* If section 852(b)(3)(D) or 857(b)(3)(C) (concerning undistributed capital gains) requires the holder of shares in a RIC or REIT to include an amount in the shareholder's long-term capital gains, the rule in paragraph (b)(7)(ii)(B) of this section does not apply to that amount. The 180-day period with respect to the included undistributed capital gain begins, at the shareholder's election, on either the last day of the RIC or REIT's taxable year or the last day of the shareholder's taxable year in which the amount would otherwise be recognized as long-term capital gains by the shareholder.

(iii) *180-day period for partners, S corporation shareholders, and owners of other passthrough entities.* See paragraph (c)(8) and (9) of this section for rules relating to the determination of the 180-day period for partners, S corporation shareholders, or beneficiaries of a trust or decedent's estate in cases in which a partnership, S corporation, trust, or decedent's estate is not an eligible taxpayer with respect to an eligible gain, or does not make a deferral election with respect to an eligible gain.

(iv) *Examples.* The following examples illustrate the principles of paragraph (b)(7)(i) through (iii) of this section.

(A) *Example 1. Regular-way trades of stock.* Individual A sells stock at a gain in a regular-way trade on an exchange (that is, in a transaction in which a trade order is placed on the trade date, and settlement of the transaction, including payment and delivery of the stock, occurs a standardized number of days after the trade date). The 180-day period with respect to A's gain on the stock begins on the trade date.

(B) *Example 2. Capital gain dividends received by a REIT shareholder.* REIT and Shareholder are calendar year taxpayers. REIT distributes a dividend to Shareholder on March 1, Year 1. REIT designates the March 1 dividend as a capital gain dividend before 30 days after the close of Year 1. Shareholder's 180-day period with respect to that capital gain dividend begins on December 31, Year 1. However, Shareholder may choose to begin the 180-day period on March 1, Year 1. If so, an equity interest in a QOF received by Shareholder in exchange for an investment of an amount corresponding to that capital gain dividend may be a qualifying investment to the extent that Shareholder's aggregate elected deferrals of dividends from REIT for Year 1 do not exceed Shareholder's aggregate capital gain dividends from REIT for the taxable year.

(C) *Example 3. Multiple capital gain dividends received by a RIC shareholder.* RIC is a calendar year taxpayer. RIC distributes a dividend of $100 to Shareholder, a calendar year taxpayer, on March 1, Year 1 and distributes another dividend of $50 to Shareholder on June 1, Year 1. RIC reports both the March 1 and June 1 dividends as capital gain dividends on Shareholder's Form 1099–DIV for Year 1. Shareholder's 180-day period with respect to both capital gain dividends begins on December 31, Year 1. However, Shareholder may choose to begin the 180-day period for the $100 RIC capital gain dividend on March 1, Year 1, and may choose to begin the 180-day period for the $50 RIC capital gain dividend on June 1, Year 1. Thus, if Shareholder makes a single investment of $200 in a QOF in exchange for an eligible interest (as defined in paragraph (b)(12) of this section) on July 1, Year 1, absent any other eligible gain, Shareholder may treat $150 of the eligible interest as a qualifying investment in the QOF (that is, the amount that corresponds to the aggregate amount of the RIC capital gain dividends in Year 1) and $50 of the eligible interest as a non-qualifying investment therein.

(D) *Example 4. Additional deferral of previously deferred gains*—(*1*) *Facts.* Taxpayer A invested in a QOF and properly elected to defer realized gain. On March 15, 2025, A disposes of its entire investment in the QOF in a transaction that, under sections 1400Z–2(a)(1)(B) and (b), triggers an inclusion of gain in A's gross income. Section 1400Z–2(b) determines the date and amount of the gain included in A's income. That date is March 15, 2025, the date on which A disposed of its entire interest in the QOF. A wants to make a deferral election with respect to A's gain from the disposal of the QOF investment.

(*2*) *Analysis.* Under paragraph (b)(7)(i) of this section, the 180-day period for making another investment in a QOF begins on the day on which section 1400Z–2(b) requires the prior gain to be included. As prescribed by section 1400Z–2(b)(1)(A), that is March 15, 2025, the date of the inclusion-triggering disposition. Thus, in order to make a deferral election under section 1400Z–2, A must invest the amount of the inclusion in the original QOF or in another QOF during the 180-day period beginning on March 15, 2025, the date when A disposed of its entire investment in the QOF.

(8) *Boot.* The term *boot* means money or other property that section 354 or 355 does not permit to be received without the recognition of gain.

(9) *Consolidated group.* The term *consolidated group* has the meaning provided in § 1.1502–1(h).

(10) *Deferral election.* The term *deferral election* means an election under section 1400Z–2(a) and the section 1400Z–2 regulations made before January 1, 2027, with respect to an eligible gain.

(11) *Eligible gain*—(i) *In general.* An amount of gain is an *eligible gain,* and thus is eligible for deferral under section 1400Z–2(a) and the section 1400Z–2 regulations, if the gain—

(A) Is treated as a capital gain for Federal income tax purposes or is a qualified 1231 gain within the meaning of paragraph (b)(11)(iii)(A) of this section, determined by—

(*1*) Not taking into account any losses unless otherwise specified in the section 1400Z–2 regulations; and

(*2*) Taking into account any other provision of the Code that requires the character of potential capital gain to be recharacterized or redetermined as ordinary income, as defined in section 64, for purposes of the Code;

(B) Would be recognized for Federal income tax purposes and subject to tax under subtitle A of the Code before January 1, 2027 (subject to Federal income tax), if section 1400Z–2(a)(1) did not apply to defer recognition of the gain; and

(C) Does not arise from a sale or exchange of property with a person that, within the meaning of section 1400Z–2(e)(2), is related to—

(*1*) The eligible taxpayer that would recognize the gain in the taxable year in which the sale or exchange occurs if section 1400Z–2(a)(1) and the section 1400Z–2 regulations did not apply to defer recognition of the gain; or

(*2*) Any passthrough entity or other person recognizing and allocating the gain to the eligible taxpayer described in paragraph (b)(11)(i)(C)(*1*) of this section.

(ii) *Portion of eligible gain not already subject to a deferral election.* In the case of an eligible taxpayer who has made an election under section 1400Z–2(a) and the section 1400Z–2 regulations regarding some but not all of an eligible gain, the portion of that eligible gain with respect to which no election under section 1400Z–2(a) and the section 1400Z–2 regulations has been made remains an eligible gain for which a deferral election may be made.

(iii) *Qualified 1231 gains*—(A) *Definition.* A section 1231 gain (as defined in section 1231(a)(3)(A)) recognized on the sale or exchange of property defined in section 1231(b) (1231(b) property) is a *qualified 1231 gain* to the extent that it exceeds any amount with respect to the 1231(b) property that is treated as ordinary income under section 1245 or section 1250.

(B) *180-day period.* For the applicable 180-day period with respect to a qualified 1231 gain, see paragraph (b)(7) of this section.

(C) *Attributes of included income when deferral ends.* For the Federal income tax treatment of the later inclusion of a qualified 1231 gain deferred under section 1400Z–2(a)(1) and the section 1400Z–2 regulations, see paragraph (c)(1) of this section.

(iv) *Gain arising from an inclusion event*—(A) *In general.* Gain that is otherwise required to be included in gross income under § 1.1400Z2(b)–1(e)(1), whether from the disposition of an entire interest in a QOF or a disposition of a partial interest, may be eligible for deferral under section 1400Z–2(a)(1), provided that all of the requirements to elect to defer gain under section 1400Z–2(a)(1)(A) are met. For purposes of determining whether such gain is eligible gain under section 1400Z–2(a)(1)(A) and this paragraph (b)(11)(iv)(A), the eligible taxpayer should treat such inclusion gain as if it was originally realized upon the occurrence of the inclusion event rather than on the sale or exchange that gave rise to the eligible gain to which the inclusion event relates.

(B) *180-day period.* The 180-day period for investing gain from an inclusion event begins on the date of the inclusion event.

(C) *Holding period.* The holding period for a qualifying investment attributable to eligible gain arising from an inclusion event begins on the date that the gain is reinvested in a QOF.

(v) *No deferral for gain realized upon the acquisition of an eligible interest.* Gain is not eligible for deferral under section 1400Z–2(a)(1) and the section 1400Z–2 regulations if such gain is realized upon the contribution, exchange, or other transfer of property to a QOF in exchange for an eligible interest (see paragraph (c)(6)(ii)(C) of this section) or the transfer of property to an eligible taxpayer in exchange for an eligible interest (see paragraph (c)(6)(iv) of this section).

(vi) *Gain from section 1256 contracts and from positions in a straddle*—(A) *General rule.* Except as otherwise explicitly provided in paragraph (b)(11)(vi)(B), (C), or (D) of this section, eligible gain for a taxable year does not include—

(*1*) Gain from a section 1256 contract as defined in section 1256(b);

(*2*) Gain from a position that was part of a straddle as defined in section 1092 (straddle) during the taxable year; or

(*3*) Gain from a position that was part of a straddle in a previous taxable year if, under section 1092(a)(1)(B), a loss from any position in that straddle is treated as sustained, subject to the limitations of section 1092(a)(1)(A), during the taxable year.

(B) *Exception for net gain from certain section 1256 contracts.* Paragraph (b)(11)(vi)(A)(*1*) of this section does not apply to the net gain during the taxable year from section 1256 contracts that were not part of a straddle at any time during the taxable year (qualified section 1256 contracts). For purposes of this paragraph (b)(11)(vi)(B), the net gain during the taxable year from qualified section 1256 contracts is determined by taking into account all capital gains and losses from such contracts for the taxable year that are recognized for Federal income tax purposes, determined without regard to section 1400Z–2(a)(1). The 180-day period with respect to any eligible gain described in this paragraph (b)(11)(vi)(B) begins on the last day of the taxable year, and the character of that gain when it is later included under sections 1400Z–2(a)(1)(B) and 1400Z–2(b) is determined under the general rule in paragraph (c)(1) of this section. If, under section 1256(a)(4), section 1092 does not apply to a straddle, such straddle is not treated as a straddle for purposes of this paragraph (b)(11)(vi)(B).

(C) *Exception for net gain from certain identified straddles*—(*1*) Paragraph (b)(11)(vi)(A) of this section does not apply to the net gain during the taxable year from positions in a straddle if—

(*i*) During the taxable year, the positions were part of an identified straddle under section 1092(a)(2), part of an identified mixed straddle under § 1.1092(b)–3T (and, as applicable, § 1.1092(b)–6), part of an identified straddle under section 1256(d), or included in a mixed straddle account under § 1.1092(b)–4T;

(*ii*) All gains and losses with respect to the positions that were part of such straddle or included in such mixed straddle account are recognized by the end of the taxable year (other than gain that would be recognized but for deferral under section 1400Z–2(a)(1));

(*iii*) None of the positions in such straddle or mixed straddle account were part of a straddle during the taxable year, other than a straddle described in paragraph (b)(11)(vi)(C)(*1*)(*i*) and (*ii*) of this section; and

(*iv*) None of the positions in such straddle or mixed straddle account were part of a straddle in a previous taxable year if, under section 1092(a)(1)(B), a loss from any position in such straddle is treated as sustained, subject to the limitations of section 1092(a)(1)(A), during the taxable year.

(*2*) For purposes of paragraph (b)(11)(vi)(C)(*1*) of this section, net gain during the taxable year from an identified straddle or mixed straddle account described in paragraph (b)(11)(vi)(C)(*1*)(*i*) through (*iv*) of this section is equal to the excess of the capital gains recognized in the taxable year for Federal income tax purposes, determined without regard to section 1400Z–2(a)(1), from all of the positions that were part of that straddle over the sum of the capital losses and net ordinary loss (if any) from all of the positions that were part of that straddle. For purposes of this paragraph (b)(11)(vi)(C)(*2*), capital gains and losses from an identified straddle or mixed straddle account include capital gains and losses from section 1256 contracts

and other positions marked to market either upon termination or on the last business day of the taxable year, as well as annual account net gain from positions in a mixed straddle account covered by § 1.1092(b)–4T. In addition, for purposes of this paragraph (b)(11)(vi)(C)(*2*), *net ordinary loss* means the excess of ordinary losses over ordinary gains.

(*3*) If a straddle is an identified straddle described in section 1092(a)(2), the basis adjustment provisions described in sections 1092(a)(2)(A)(ii) and (iii) must be applied in determining the net gain during the taxable year from positions that were part of that straddle.

(*4*) The 180-day period with respect to any eligible gain described in paragraph (b)(11)(vi)(C)(*2*) of this section begins on the earlier of the date when all of the positions that are, or have been, part of the straddle are disposed of (or otherwise terminated) or the last day of the taxable year.

(*5*) If net gain described in paragraph (b)(11)(vi)(C)(*2*) of this section is deferred under section 1400Z–2(a)(1), that gain is not treated as unrecognized gain for purposes of section 1092(a)(3)(A)(ii).

(D) *Additional exceptions to the general rule.* Additional exceptions to the general rule in paragraph (b)(11)(vi)(A) of this section may be prescribed in guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter).

(E) *Examples.* The following examples illustrate the rules described in paragraph (b)(11)(vi) of this section. All of the examples assume that Taxpayer holds the positions described as capital assets and that Taxpayer holds no offsetting positions other than those described in the examples.

(*1*) *Example 1.* Taxpayer owns 100 shares of publicly traded Company X common stock and acquires put options on 100 shares of Company X common stock during the taxable year. Taxpayer does not make any straddle identifications under section 1092. During the taxable year, Taxpayer sells all 100 shares of its Company X common stock and has a $40 capital gain. During the taxable year, Taxpayer also closes out all of its put options on Company X common stock and has a $30 capital loss. That $40 of capital gain is from a position that was part of a straddle during the taxable year because the position in Company X common stock and the position in put options on Company X stock are offsetting positions as defined in section 1092(c). Under paragraph (b)(11)(vi)(A) of this section, none of Taxpayer's $40 of capital gain is eligible gain.

(*2*) *Example 2.* Taxpayer's taxable year is the calendar year. Taxpayer owns 100 shares of publicly traded Company Y common stock and has a basis in each share of $10.00. Taxpayer also owns put options on 100 shares of Company Y common stock. Taxpayer makes a valid and timely identification under section 1092(a)(2) of the 100 shares of Company Y common stock and the put options on the 100 shares of Company Y common stock. On January 10, Year 1, Taxpayer closes out all of the put options and has a $30.00 capital loss. On March 10, Year 1, Taxpayer sells 40 shares of the Company Y common stock for $11.00 per share. At the end of Year 1, the fair market value of each of the 60 remaining shares of Company Y common stock held by Taxpayer is $10.50. Under section 1092(a)(2)(A)(ii), when the put options are closed out at a loss of $30.00, the basis of each of Taxpayer's shares of Company Y common stock is increased by $0.30 ($30.00/100). Thus, Taxpayer has a gain of $28.00 ((40 * $11.00) − (40 * $10.30)) on the sale of the 40 shares of Company Y common stock. Paragraph (b)(11)(vi)(A) of this section applies to all of Taxpayer's gain during the taxable year from the straddle. Because Taxpayer has unrecognized gain from the straddle at the end of the taxable year, paragraph (b)(11)(vi)(C) of this section does not shield any of Taxpayer's gain from that result. The $28 of gain is thus not eligible gain. Taxpayer must recognize and include in taxable income for the taxable year the $28.00 capital gain. Under section 1092(a)(2)(A)(iv), Taxpayer may not deduct the $30.00 loss from the put options.

(*3*) *Example 3.* The facts are the same as in paragraph (b)(11)(vi)(E)(*2*) of this section (*Example 2*), except Taxpayer sells the 100 shares of Company Y common stock on March 10, Year 1, for $11.50 per share. Under section 1092(a)(2)(A)(ii), as in paragraph (b)(11)(vi)(E)(*2*) of this section (*Example 2*), when the put options are closed out at a loss of $30.00, the basis of each of Taxpayer's shares of Company Y common stock is increased by $0.30 ($30.00/100). Taxpayer has a gain of $120.00 ((100 * $11.50) − (100 * $10.30)) on the sale of the 100 shares of Company Y common stock. Taxpayer has net gain during the taxable year from the identified straddle of $120.00. Under paragraph (b)(11)(vi)(C) of this section, paragraph (b)(11)(vi)(A) of this section does not apply to prevent the $120.00 net gain from being eligible gain. As in paragraph (b)(11)(vi)(E)(*2*) of this section (*Example 2*), under section 1092(a)(2)(A)(iv), Taxpayer may not deduct the $30.00 loss from the put options.

(*4*) *Example 4.* Taxpayer's taxable year is the calendar year. Taxpayer owns 100 shares of publicly traded Company Z common stock and has a basis in each share of $10. Taxpayer also owns put options on 100 shares of Company Z common stock. In Year 1, Taxpayer closes out the put options at a $100 loss. At the end of Year 1, the fair market value of each of the shares of Company Z common stock held by Taxpayer is $15 and, under section 1092(a)(3), Taxpayer has $500 of unrecognized gain. Because Taxpayer's unrecognized gain on the Company Z common stock at the end of Year 1 exceeds Taxpayer's loss on the put options, Taxpayer's loss is deferred under section 1092(a)(1). During Year 2, Taxpayer sells 40 shares of Company Z common stock for $14 per share. Taxpayer has a gain of $160 ((40 * $14) − (40 * $10)) on the sale of the 40 shares of Company Z common stock. Under paragraph (b)(11)(vi)(A) of this section, because Taxpayer's Company Z common stock was part of a straddle in a previous taxable year and a loss from a position in that straddle was deferred under section 1092(a) at the end of Year 1, the preceding taxable year, Taxpayer's $160 Year 2 gain on the sale of the Company Z common stock is not eligible gain. At the end of Year 2, the fair market value of each of the 60 remaining shares of Company Z common stock held by Taxpayer is $10 and Taxpayer has no unrecognized gain on its Company Z common stock. Under section 1092(a)(1)(B), Taxpayer's $100 loss from Year 1 is treated as sustained in Year 2. Because Taxpayer has no unrecognized gain on its Company Z common stock at the end of Year 2, Taxpayer may deduct the $100 loss in Year 2. In Year 3, Taxpayer sells the remaining 60 shares of Company Z common stock for $50 per share. Taxpayer has a gain of $2,400 ((60 * $50) − (60 * $10)) on the sale of the 60 shares of Company Z common stock. Because there was no loss from the straddle deferred under section 1092(a) at the end of Year 2, paragraph (b)(11)(vi)(A) of this section does not apply to prevent the $2,400 of Year 3 net gain from being eligible gain.

(*5*) *Example 5.* Taxpayer's taxable year is the calendar year. On October 5, Year 1, Taxpayer buys 100 shares of publicly traded Exchange Traded Fund A (ETF A) and acquires offsetting section 1256 contracts on the index that underlies the ETF A shares. Taxpayer makes a valid and timely identification of all 100 ETF A shares and the offsetting section 1256 contracts under § 1.1092(b)–3T. On December 31, Year 1, the fair market value of the ETF A shares has increased by $500, and the fair market value of the section 1256 contracts has decreased by $450. On December 31, Year 1, Taxpayer sells the ETF shares for a $500 gain. In addition, under section 1256(a)(1), the section 1256 contracts are treated as sold for fair market value on December 31, Year 1, for a $450 loss. Pursuant to § 1.1092(b)–3T(b)(4), Taxpayer has a net short term capital gain from the identified mixed straddle of $50 ($500–$450). Under paragraph (b)(11)(vi)(C) of this section, paragraph (b)(11)(vi)(A) of this section does not apply to prevent the $50 of net short term capital gain from being eligible gain.

(vii) [Reserved]

(viii) *Eligible installment sale gains*—(A) *In general.* The term *eligible gain* includes gains described in this paragraph (b)(11) that would be recognized by an eligible taxpayer under the installment method pursuant to section 453 and with §§ 1.453–1 through 1.453–12 for a taxable year, provided such gain otherwise meets the requirements of this paragraph (b)(11). This includes gains recognized under the installment method under section 453 from an installment sale that occurred before December 22, 2017.

(B) *180-day period for gain from installment sales.* For gains reported on

the installment method, an eligible taxpayer may treat the date the payment on the installment sale is received or the last day of the taxable year in which the eligible taxpayer would have recognized the gain under the installment method as the beginning of the 180-day period described in paragraph (b)(7) of this section. Thus, if an eligible taxpayer receives one or more payments on an installment sale and treats the date the payment on the installment sale is received as the beginning of the 180-day period, each payment will begin a new 180-day period.

(ix) *Additional rules for determining if gain is subject to Federal income tax*—(A) *Application of a treaty*—(*1*) *In general.* For purposes of paragraph (b)(11)(i)(B) of this section, whether gain would be subject to Federal income tax is determined after application of any treaty exemption provision that an eligible taxpayer elects to apply under any applicable U.S. income tax convention.

(*2*) *Treaty waiver.* An eligible taxpayer who is not a United States person within the meaning of section 7701(a)(30) (or an eligible taxpayer who is a United States person within the meaning of section 7701(a)(30) but who is treated as a resident of another country under an applicable U.S. income tax convention) may not make an election to defer gain pursuant to section 1400Z–2(a) after the applicability date of this section (see paragraph (g) of this section) unless such eligible taxpayer irrevocably waives, in accordance with forms and instructions (see § 601.602 of this chapter), any treaty benefits that would exempt such gain from being subject to Federal income tax at the time of inclusion pursuant to an applicable U.S. income tax convention. In the event that such forms and instructions that include such waiver have not yet been published when an election pursuant to paragraph (d)(1) of this section is required to be made, such an eligible taxpayer must attach a written statement, signed under penalties of perjury, to any forms on which an election is made pursuant to paragraph (d)(1) of this section, which states ''With respect to gain deferred pursuant to an election under section 1400Z–2(a), the below signed taxpayer irrevocably waives any treaty benefits that would exempt such gain from being subject to Federal income tax at the time of inclusion pursuant to an applicable U.S. income tax convention.'' If such an eligible taxpayer chooses to apply the section 1400Z–2 regulations in a consistent manner for all taxable years (see paragraph (g)(2)(i) of this section), the taxpayer must include the signed statement required under this paragraph (b)(11)(ix)(A)(*2*) with the first annual report described in paragraph (d)(2) of this section that is required to be filed on a date that is after March 13, 2020. An eligible taxpayer not described in the first sentence of this paragraph (b)(11)(ix)(A)(*2*) will only be required to make the waiver described in this paragraph (b)(11)(ix)(A)(*2*) if and to the extent required in forms and publications (see § 601.602 of this chapter).

(*3*) *Non-application to certain entities.* This paragraph (b)(11)(ix)(A) does not apply to an entity described in paragraph (b)(11)(ix)(B) of this section.

(B) *Gain of a partnership.* Subject to § 1.1400Z2(f)–1(c), with respect to a partnership, the requirement in paragraph (b)(11)(i)(B) of this section that a gain be subject to Federal income tax does not apply to an otherwise eligible gain of the partnership, provided the partnership acquires the eligible interest with respect to such gain. See § 1.1400Z2(f)–1(c)(3)(i) and (ii), *Examples 1 and 2,* for illustrations of the application of § 1.1400Z2(f)–1(c) (providing an anti-abuse rule) to a partnership.

(12) *Eligible interest*—(i) *In general.* For purposes of section 1400Z–2, an *eligible interest* in a QOF is an equity interest issued by the QOF, including preferred stock or a partnership interest with special allocations. Thus, the term *eligible interest* excludes any debt instrument including those within the meaning of section 1275(a)(1) and § 1.1275–1(d). An eligible interest includes a pre-existing interest in an entity that becomes a QOF pursuant to § 1.1400Z2(d)–1(a)(1)(iii).

(ii) *Use as collateral permitted.* Provided that the eligible taxpayer is the owner of the equity interest in the QOF for Federal income tax purposes, status as an eligible interest is not impaired by using the interest as collateral for a loan, whether as part of a purchase-money borrowing or otherwise.

(iii) *Deemed contributions not creating mixed-funds investment.* See paragraph (f)(2) of this section for rules regarding deemed contributions of money to a partnership pursuant to section 752(a).

(13) *Eligible taxpayer.* An *eligible taxpayer* is a person that is required to report the recognition of gains during the taxable year under Federal income tax accounting principles. Thus, for example, eligible taxpayers include individuals; C corporations, including RICs and REITs; organizations subject to tax under section 511; and partnerships, S corporations, trusts, and decedents' estates to the extent permitted by paragraphs (c)(7) through (9) of this section.

(14) *Inclusion event.* The term *inclusion event* has the meaning provided in § 1.1400Z2(b)–1(c).

(15) *Mixed-funds investment.* The term *mixed-funds investment* means an investment a portion of which is a qualifying investment and a portion of which is a non-qualifying investment.

(16) *Non-qualifying investment.* The term *non-qualifying investment* means an investment in a QOF described in section 1400Z–2(e)(1)(A)(ii).

(17) *Property*—(i) *In general.* The term *property* means money, securities, or any other property.

(ii) *Inclusion events regarding QOF corporation distributions.* For purposes of § 1.1400Z2(b)–1(c), in the context in which a QOF corporation makes a distribution, the term *property* does not include stock (or rights to acquire stock) in the QOF corporation that makes the distribution.

(18) *QOF.* The term *QOF* means a qualified opportunity fund, as defined in section 1400Z–2(d)(1) and § 1.1400Z2(d)–1.

(19) *QOF C corporation.* The term *QOF C corporation* means a QOF corporation other than a QOF S corporation.

(20) *QOF corporation.* The term *QOF corporation* means a QOF that is classified as a corporation for Federal income tax purposes.

(21) *QOF RIC.* The term *QOF RIC* means a QOF that elects to be taxed as a RIC for Federal income tax purposes. For purposes of section 1400Z–2 and the section 1400Z–2 regulations, a *RIC* is a regulated investment company within the meaning of section 851.

(22) *QOF REIT.* The term *QOF REIT* means a QOF that elects to be taxed as a REIT for Federal income tax purposes. For purposes of section 1400Z–2 and the section 1400Z–2 regulations, a *REIT* is a real estate investment trust within the meaning of section 856.

(23) *QOF owner.* The term *QOF owner* means a QOF shareholder or a QOF partner.

(24) *QOF partner.* The term *QOF partner* means a person that directly owns a qualifying investment in a QOF partnership or a person that owns such a qualifying investment through equity interests solely in one or more partnerships.

(25) *QOF partnership.* The term *QOF partnership* means a QOF that is classified as a partnership for Federal income tax purposes.

(26) *QOF S corporation.* The term *QOF S corporation* means a QOF

corporation that has elected under section 1362 to be an S corporation.

(27) *QOF shareholder.* The term *QOF shareholder* means a person that directly owns a qualifying investment in a QOF corporation.

(28) *QOZ designation notice.* The term *QOZ designation notice* means a notice designating population census tracts as qualified opportunity zones (QOZs) in guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter).

(29) *Qualified opportunity zone business.* The term *qualified opportunity zone business* has the meaning provided in section 1400Z–2(d)(3) and § 1.1400Z2(d)–1(d).

(30) *Qualified opportunity zone business property.* The term *qualified opportunity zone business property* has the meaning provided in section 1400Z–2(d)(2)(D) and § 1.1400Z2(d)–2.

(31) *Qualified opportunity zone partnership interest.* The term *qualified opportunity zone partnership interest* has the meaning provided in section 1400Z–2(d)(2)(C) and § 1.1400Z2(d)–1(c)(3).

(32) *Qualified opportunity zone property.* The term *qualified opportunity zone business property* has the meaning provided in section 1400Z–2(d)(2)(A) and § 1.1400Z2(d)–1(c)(1).

(33) *Qualified opportunity zone stock.* The term *qualified opportunity zone stock* has the meaning provided in section 1400Z–2(d)(2)(B) and § 1.1400Z2(d)–1(c)(2).

(34) *Qualifying investment.* The term *qualifying investment* means an eligible interest, or portion thereof, in a QOF to the extent that a deferral election is made and applies with respect to such eligible interest or portion thereof and the IRS has been timely notified of the deferral election. An eligible interest in a QOF ceases to be a qualifying investment of the owner upon, and to the extent of, the occurrence of an inclusion event with regard to that eligible interest, or portion thereof, except as is expressly provided otherwise in § 1.1400Z2(b)–1(c) or other provisions of the section 1400Z–2 regulations.

(35) *Qualifying QOF partnership interest.* The term *qualifying QOF partnership interest* means a direct or indirect interest in a QOF partnership that is a qualifying investment.

(36) *Qualifying QOF stock.* The term *qualifying QOF stock* means stock in a QOF corporation that is a qualifying investment.

(37) *Qualifying section 355 transaction.* The term *qualifying section 355 transaction* means a distribution described in § 1.1400Z2(b)–1(c)(11)(i)(B).

(38) *Qualifying section 381 transaction.* The term *qualifying section 381 transaction* means a transaction described in section 381(a)(2), except the following transactions:

(i) An acquisition of assets of a QOF by a QOF shareholder that holds a qualifying investment in the QOF;

(ii) An acquisition of assets of a QOF by a tax-exempt entity as defined in § 1.337(d)–4(c)(2);

(iii) An acquisition of assets of a QOF by an entity operating on a cooperative basis within the meaning of section 1381;

(iv) An acquisition by a QOF of assets of a QOF shareholder that holds a qualifying investment in the QOF;

(v) A reorganization of a QOF in a transaction that qualifies under section 368(a)(1)(G);

(vi) A transaction, immediately after which one QOF owns an investment in another QOF; and

(vii) A triangular reorganization of a QOF within the meaning of § 1.358–6(b)(2)(i), (ii), or (iii).

(39) *Related persons.* The term *related* when used with regard to persons and the term *related persons* means that there is a relationship described in section 267(b) or 707(b)(1), determined by substituting ''20 percent'' for ''50 percent'' each place it occurs in such sections. The term *unrelated* when used with regard to persons means that there is no relationship described in preceding sentence.

(40) *Remaining deferred gain.* With respect to a qualifying investment, the term *remaining deferred gain* means the full amount of gain that was deferred under section 1400Z–2(a)(1)(A), reduced by the amount of gain previously included under § 1.1400Z2(b)–1(b). After December 31, 2026, an eligible taxpayer's remaining deferred gain is $0.

(41) *Section 1400Z–2 regulations.* The term *section 1400Z–2 regulations* means the regulations in this chapter, which are prescribed in whole or in part under section 1400Z–2.

(c) *Operational and special rules*—(1) *Attributes of gains included in income under section 1400Z–2(a)(1)(B).* If section 1400Z–2(a)(1)(B), section 1400Z–2(b), and the section 1400Z–2 regulations require a taxpayer to include in income some or all of a previously deferred gain, the rules of paragraphs (c)(1)(i) and (ii) of this section apply with respect to such gain.

(i) *Deferral year attributes.* The gain so included per paragraph (c)(1) of this section has the same attributes in the taxable year of inclusion that the gain would have had if recognition of the gain had not been deferred under section 1400Z–2(a)(1)(A). These attributes include those taken into account by sections 1(h), 1222, 1231(b), 1256, and any other applicable provisions of the Code.

(ii) *Inclusion year treatment.* The gain so included per paragraph (c)(1) of this section is subject to the same Federal income tax provisions and rates that would apply to any other gains that are realized and recognized at the same time as the included gain and that have the same attributes as the deferred gain. For example, when a deferred qualified 1231 gain, as defined in paragraph (b)(11)(iii) of this section, is required to be included in income, the included section 1231 gain is treated as if it were a section 1231 gain (within the meaning of section 1231(a)(3)(A)) that was recognized on the date of inclusion.

(iii) *Rules for associating included gain with deferred gains*—(A) *In general.* For purposes of paragraphs (c)(1)(i) and (ii) of this section, a taxpayer determines which previously deferred gain is associated with a qualifying investment in accordance with guidance published in the Internal Revenue Bulletin or in forms and instructions (see §§ 601.601(d)(2) and 601.602 of this chapter). The rules of paragraphs (c)(1)(iii)(B) and (C) of this section only apply only to the extent a deferred gain is not clearly associated with a particular qualifying investment under this paragraph (c)(1)(iii)(A).

(B) *Only one eligible gain associated with a deferral election.* If only one eligible gain could have been deferred with respect to a qualifying investment, that deferred gain is associated with that qualifying investment. For example, if an eligible taxpayer makes a deferral election with respect to an investment in a QOF and only one eligible gain of the taxpayer satisfies the 180-day period with respect to the investment in the QOF, that eligible gain is the gain deferred with respect to the qualifying investment for purposes of paragraphs (c)(1)(i) and (ii) of this section.

(C) *Multiple eligible gains associated with a deferral election*—(*1*) *In general.* If more than one eligible gain may have been deferred with respect to an investment in a QOF for which a deferral election has been made, then for purposes of paragraphs (c)(1)(i) and (ii) of this section, the eligible taxpayer is treated as making the investment in the QOF first with respect to the earliest realized eligible gain, followed by the next earliest eligible gain and any other eligible gains in order of the date of their realization.

(*2*) *Rule for gains realized on the same day.* If in the application of paragraph

(c)(1)(iii)(C)(*1*) of this section, two eligible gains are realized on the same day, such gains are allocated to the investment in the QOF proportionately.

(2) *Identification of which interest in a QOF corporation has been disposed of*—(i) *Need for identification.* If a taxpayer holds shares of QOF stock with identical rights (*fungible interests*), and if the taxpayer disposes of less than all of the fungible interests, it is necessary to identify which interest or interests were disposed of. A taxpayer may effect this identification in accordance with the rules and principles of § 1.1012–1(c). Consistent with § 1.1012–1(c), if a taxpayer does not adequately identify which of the fungible interests are disposed of, the first-in, first-out identification method (*FIFO method*) applies.

(ii) *Consequences of identification.* The identification determines—

(A) Whether an investment disposed of is a qualifying investment or a non-qualifying investment; and

(B) In the case of qualifying investments—

(*1*) The attributes of the gain addressed in paragraph (c)(1) of this section; and

(*2*) The extent, if any, of an increase under section 1400Z–2(b)(2)(B) in the basis of an investment interest that is disposed of.

(3) *Pro-rata method.* If, after application of the FIFO method, a taxpayer is treated as having disposed of less than all of the investment interests that the taxpayer acquired on one day, and if the interests acquired on that day vary with respect to the characteristics described in paragraph (c)(2)(ii) of this section, then a proportionate allocation must be made to determine which interests were disposed of (*pro-rata method*).

(4) *Examples.* The following examples illustrate the rules of paragraph (c)(1) through (3) of this section.

(i) *Example 1. Short-term gain.* For 2018, taxpayer B properly made an election under section 1400Z–2 to defer $100 of eligible gain that, if not deferred, would have been recognized as short-term capital gain, as defined in section 1222(1). In 2022, sections 1400Z–2(a)(1)(B) and (b) require taxpayer B to include the gain in gross income. Under paragraph (c)(1) of this section, the gain included in 2022 is short-term capital gain.

(ii) *Example 2. Collectibles gain.* For 2018, taxpayer C properly made an election under section 1400Z–2 to defer a gain that, if not deferred, would have been collectibles gain as defined in section 1(h)(5). In a later taxable year, section 1400Z–2(a)(1)(B) and (b) requires some or all of that deferred gain to be included in gross income. The gain included is collectibles gain.

(iii) *Example 3. Net capital gain from section 1256 contracts.* For 2019, taxpayer D had $100 of net capital gain realized from section 1256 contracts that is eligible gain under paragraph (b)(11)(vi)(B) of this section. D timely invested $100 in a QOF and properly made an election under section 1400Z–2 to defer that $100 of gain. In 2023, section 1400Z–2(a)(1)(B) and (b) requires D to include that deferred gain in gross income. Under paragraph (c)(1) of this section, the character of the inclusion is governed by section 1256(a)(3), which requires a 40:60 split between short-term and long-term capital gain. Accordingly, $40 of the inclusion is short-term capital gain and $60 of the inclusion is long-term capital gain.

(iv) *Example 4. FIFO method.* For 2018, taxpayer E properly made an election under section 1400Z–2 to defer $300 of short-term capital gain. For 2020, E properly made a second election under section 1400Z–2 to defer $200 of long-term capital gain. In both cases, E properly invested in QOF corporation Q the amount of the gain to be deferred, resulting in a total investment in Q of $500. The two investments are fungible interests and the price of the interests was the same at the time of the two investments. E did not purchase any additional interest in Q or sell any of its interest in Q until 2024, when E sold for a gain 60 percent of its interest in Q. E did not adequately identify which investment in QOF Q E sold. Under paragraph (c)(2)(i) of this section, E must apply the FIFO method to identify which investments in Q that E disposed of. 60 percent of E's total investment in Q is $300 (60% × $500), thus under the FIFO method, E sold its entire 2018 initial investment of $300 in Q. Under section 1400Z–2(a)(1)(B) and (b), the sale triggered an inclusion of deferred gain. Because the inclusion has the same character as the gain that had been deferred, the inclusion is short-term capital gain.

(v) *Example 5. FIFO method.* In 2018, before Corporation R became a QOF, Taxpayer F invested $100 to R in exchange for 100 R common shares. Later in 2018, after R was a QOF, F invested $500 to R in exchange for 400 R common shares and properly elected under section 1400Z–2 to defer $500 of realized short-term capital gain from a separate investment. Even later in 2018, on different days, F realized $300 of short-term capital gain and $700 of long-term capital gain. On a single day that fell during the 180-day period for both of those gains, F invested $1,000 in R in exchange for 800 R common shares and properly elected under section 1400Z–2 to defer the two gains. In 2020, F sold 100 R common shares. F did not adequately identify which investment in R F sold. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R F disposed of. As determined by that identification, F sold the initially acquired 100 R common shares, which were not part of a deferral election under section 1400Z–2. R must recognize gain or loss on the sale of its R shares under the generally applicable Federal income tax rules, but the sale does not trigger an inclusion of any deferred gain.

(vi) *Example 6. FIFO method.* The facts are the same as in paragraph (c)(4)(v) of this section (*Example 5*), except that, in addition, during 2021 F sold an additional 400 R common shares, and, as with the other sale, F did not adequately identify which investment in QOF R F sold. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R were disposed of. As determined by this identification, F sold the 400 common shares which were associated with the deferral of $500 of short-term capital gain. Thus, the deferred gain that must be included upon sale of the 400 R common shares is short-term capital gain.

(vii) *Example 7. Pro-rata method.* The facts are the same as in examples 5 and 6, except that, in addition, during 2022 F sold an additional 400 R common shares. Under paragraph (c)(2)(i) of this section, F must apply the FIFO method to identify which investments in R were disposed of. In 2022, F is treated as holding only the 800 R common shares purchased on a single day, and the section 1400Z–2 deferral election associated with these shares applies to gain with different characteristics (described in paragraph (c)(2)(ii) of this section). Under paragraph (c)(3) of this section, therefore, R must use the pro-rata method to determine which of the characteristics pertain to the deferred gain required to be included as a result of the sale of the 400 R common shares. Under the pro-rata method, $150 of the inclusion is short-term capital gain ($300 × 400/800) and $350 is long-term capital gain ($700 × 400/800).

(5) *Making an investment for purposes of an election under section 1400Z–2(a)*—(i) *Transfer of cash or other property to a QOF.* A taxpayer makes an investment in a QOF by transferring cash or other property to a QOF in exchange for eligible interests in the QOF, regardless of whether the transfer is one in which the transferor would recognize gain or loss on the property transferred.

(ii) *Furnishing services.* Rendering services to a QOF is not a transfer of cash or other property to a QOF. Thus, if a taxpayer receives an eligible interest in a QOF for services rendered to the QOF or to a person in which the QOF holds any direct or indirect equity interest, then the interest in the QOF that the taxpayer receives is a non-qualifying investment.

(iii) *Acquisition of eligible interest from person other than QOF.* An eligible taxpayer may make an investment in a QOF by acquiring an eligible interest in a QOF from a person other than the QOF, provided that all of the requirements of section 1400Z–2(a)(1) and the section 1400Z–2 regulations for making a valid deferral election with respect to that investment are otherwise satisfied with respect to such acquisition. For example, an eligible taxpayer who acquires an eligible interest in a QOF other than from the QOF also must have an eligible gain within the 180-day period prior to the

eligible taxpayer's acquisition of the eligible interest in the QOF.

(6) *Amount invested for purposes of section 1400Z–2(a)(1)(A)*—(i) *In general.* In the case of any investments described in this paragraph (c)(6), the amount of a taxpayer's qualifying investment cannot exceed the amount of eligible gain to be deferred under the deferral election. If the amount of an otherwise qualifying investment exceeds the amount of eligible gain to be deferred under the deferral election, the amount of the excess is treated as a non-qualifying investment. See paragraph (c)(6)(iii) of this section for special rules applicable to transfers to QOF partnerships.

(ii) *Transfers to a QOF*—(A) *Cash.* If a taxpayer makes an investment in a QOF by transferring cash to a QOF, the amount of the taxpayer's investment is that amount of cash.

(B) *Property other than cash—Nonrecognition transactions.* This paragraph (c)(6)(ii)(B) applies if a taxpayer makes an investment in a QOF by transferring property other than cash to a QOF and if, but for the application of section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations, the taxpayer's basis in the resulting investment in the QOF would be determined, in whole or in part, by reference to the taxpayer's basis in the transferred property. This paragraph (c)(6)(ii)(B) applies separately to each item of property transferred to a QOF.

(*1*) *Amount of qualifying investment.* If paragraph (c)(6)(ii)(B) of this section applies, the amount of the taxpayer's qualifying investment is the lesser of the taxpayer's adjusted basis in the eligible interest received in the transaction, without regard to section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations, or the fair market value of the eligible interest received in the transaction, both determined immediately after the transfer.

(*2*) *Fair market value of the eligible interest received exceeds its adjusted basis.* If paragraph (c)(6)(ii)(B) of this section applies, and if the fair market value of the eligible interest received is in excess of the eligible taxpayer's adjusted basis in the eligible interest received, without regard to section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations, then the eligible taxpayer's investment in a QOF is a mixed-funds investment to which section 1400Z–2(e)(1) applies. In such a case, an amount equal to the adjusted basis of the eligible interest in the hands of the eligible taxpayer is the eligible taxpayer's qualifying investment, and the excess is the eligible taxpayer's non-qualifying investment.

(*3*) *Transfer of built-in loss property and section 362(e)(2).* If paragraph (c)(6)(ii)(B) of this section and section 362(e)(2) both apply to a transaction, the eligible taxpayer and the QOF are deemed to have made an election under section 362(e)(2)(C).

(C) *Property other than cash—Taxable transactions.* This paragraph (c)(6)(ii)(C) applies if an eligible taxpayer makes an investment in a QOF by transferring property other than cash to a QOF and if, without regard to section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations, the eligible taxpayer's basis in the eligible interest received would not be determined, in whole or in part, by reference to the eligible taxpayer's basis in the transferred property. If this paragraph (c)(6)(ii)(C) applies, the amount of the eligible taxpayer's investment in a QOF is the fair market value of the transferred property, as determined immediately before the transfer. This paragraph (c)(6)(ii)(C) applies separately to each item of property transferred to a QOF.

(D) *Basis in a mixed-funds investment.* If a taxpayer's investment in a QOF is a mixed-funds investment to which section 1400Z–2(e)(1) applies, the taxpayer's basis in the non-qualifying investment is equal to the taxpayer's basis in all of the eligible interests received, determined without regard to section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations, and reduced by the basis of the taxpayer's qualifying investment, determined without regard to section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations.

(iii) *Special rules for transfers to QOF partnerships.* In the case of an investment in a QOF partnership, the following rules apply:

(A) *Amounts not treated as a qualifying investment*—(*1*) *Non-contributions in general.* To the extent the transfer of property to a QOF partnership is characterized other than as a contribution, such as characterization as a sale under section 707 and the regulations in this part under section 707 of the Code, the transfer is not treated as being made in exchange for a qualifying investment.

(*2*) *Reductions in investments otherwise treated as contributions.* If any transfer of cash or other property to a partnership is not treated as a contribution, in whole or in part, under paragraph (c)(6)(iii)(A)(*1*) of this section, the part of the transfer to the partnership that is not disregarded is not a qualifying investment to the extent the partnership makes a distribution to the partner and the transfer to the partnership and the distribution would be recharacterized as a disguised sale under section 707 and the regulations in this part under section 707 of the Code if:

(*i*) Any cash contributed were non-cash property; and

(*ii*) In the case of a distribution by the partnership to which § 1.707–5(b) (relating to debt-financed distributions) applies, the partner's share of liabilities is zero.

(B) *Amount invested in a QOF partnership*—(*1*) *Calculation of amount of qualifying and non-qualifying investments.* To the extent paragraph (c)(6)(iii)(A) of this section does not apply, the amount of equity received by an eligible taxpayer in a QOF partnership in exchange for the lesser of the net basis or net value of the property contributed to the QOF partnership by the eligible taxpayer is a qualifying investment. The amount of equity received by an eligible taxpayer in a QOF partnership that is a non-qualifying investment is the excess, if any, of the total equity received by the eligible taxpayer over the amount treated as a qualifying investment.

(*2*) *Net basis.* For purposes of paragraph (c)(6)(iii)(B) of this section, net basis is the excess, if any, of—

(*i*) The adjusted basis of the property contributed to the partnership; over

(*ii*) The amount of any debt to which the property is subject or that is assumed by the partnership in the transaction.

(*3*) *Net value.* For purposes of paragraph (c)(6)(iii)(B) of this section, net value is the excess of—

(*i*) The gross fair market value of the property contributed to the partnership; over

(*ii*) The amount of the debt described in paragraph (c)(6)(iii)(B)(*2*)(*ii*) of this section.

(*4*) *Basis of qualifying and non-qualifying investments.* The initial basis of a qualifying investment, before application of section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations or any section 752 debt allocation, is the net basis of the property contributed. The basis of a non-qualifying investment, before any section 752 debt allocation, is the remaining net basis. The basis of the qualifying investment is adjusted as provided in section 1400Z–2(b)(2)(B) and the section 1400Z–2 regulations. The bases of qualifying and non-qualifying investments are increased by any debt allocated to those investments under the rules of § 1.1400Z2(b)–1(c)(6)(iv)(B).

(*5*) *Rules applicable to mixed-funds investments.* If one portion of an investment in a QOF partnership is a qualifying investment and another

portion is a non-qualifying investment, see § 1.1400Z2(b)–1(c)(6)(iv) for the rules that apply.

(iv) *Acquisitions from another person.* An eligible taxpayer may make an investment in a QOF by acquiring in a sale or exchange to which § 1.1001–1(a) applies an eligible interest in a QOF from a person other than the QOF. The amount of the eligible taxpayer's investment in the QOF with respect to which the eligible taxpayer may make a deferral election is the amount of the cash, or the net fair market value of the other property, as determined immediately before the exchange, that the eligible taxpayer exchanged for the eligible interest in the QOF.

(v) *Examples.* The following examples illustrate the rules of this paragraph (c)(6).

(A) *Example 1. Transfer of built-in gain property with basis less than gain to be deferred*—(*1*) *Facts.* Individual B realizes $100 of eligible gain within the meaning of paragraph (b)(11) of this section. B transfers unencumbered property with a fair market value of $100 and an adjusted basis of $60 to QOF Q, a C corporation, in a transaction that is described in section 351(a).

(*2*) *Analysis.* Paragraph (c)(6)(ii)(B) of this section applies because B transferred property other than cash to Q and, but for the application of section 1400Z–2(b)(2)(B), B's basis in the eligible interests in Q would be determined, in whole or in part, by reference to B's basis in the transferred property. The fair market value of the eligible interest B received is $100, and, without regard to section 1400Z–2(b)(2)(B), B's basis in the eligible interest received would be $60. Thus, pursuant to paragraph (c)(6)(ii)(B)(*2*) of this section, B's investment is a mixed-funds investment to which section 1400Z–2(e)(1) applies. Pursuant to paragraphs (c)(6)(ii)(B)(*1*) and (*2*) of this section, B's qualifying investment is $60 (the lesser of the taxpayer's adjusted basis in the eligible interest, without regard to section 1400Z–2(b)(2)(B), of $60 and the $100 fair market value of the eligible interest received). Pursuant to section 1400Z–2(b)(2)(B)(i), B's basis in the qualifying investment is $0. Additionally, B's non-qualifying investment is $40 (the excess of the fair market value of the eligible interest received ($100) over the taxpayer's adjusted basis in the eligible interest, without regard to section 1400Z–2(b)(2)(B) ($60)). B's basis in the non-qualifying investment is $0 (B's $60 basis in its investment determined without regard to section 1400Z–2(b)(2)(B), reduced by the $60 of adjusted basis allocated to the investment to which section 1400Z–2(e)(1)(A)(i) applies, determined without regard to section 1400Z–2(b)(2)(B)). See paragraph (c)(6)(ii)(D) of this section. Pursuant to section 362, Q's basis in the transferred property is $60.

(B) *Example 2. Transfer of built-in gain property with basis in excess of eligible gain to be deferred.* The facts are the same as in paragraph (c)(6)(v)(A)(*1*) of this section (*Example 1*), except that B realizes $50 of eligible gain within the meaning of paragraph (b)(11) of this section. Pursuant to paragraph (c)(6)(i) of this section, B's qualifying investment cannot exceed the amount of eligible gain to be deferred (that is, the $50 of eligible gain) under the section 1400Z–2(a) election. Therefore, pursuant to paragraph (c)(6)(ii)(B)(*1*) of this section, B's qualifying investment is $50 (the lesser of the taxpayer's adjusted basis in the eligible interest received, without regard to section 1400Z–2(b)(2)(B), of $60 and the $100 fair market value of the eligible interest, limited by the amount of eligible gain to be deferred under the section 1400Z–2(a) election). B's qualifying investment has an adjusted basis of $0, as provided in section 1400Z–2(b)(2)(B)(i). Additionally, B's non-qualifying investment is $50 (the excess of the fair market value of the eligible interest received ($100) over the amount ($50) of B's section 1400Z–2(a)(1)(A) investment). B's basis in the non-qualifying investment is $10 (B's $60 basis in its investment determined without regard to section 1400Z–2(b)(2)(B)), reduced by the $50 of adjusted basis allocated to B's qualifying investment, determined without regard to section 1400Z–2(b)(2)(B).

(C) *Example 3. Transfers to QOF partnerships*—(*1*) *Facts.* A and B each realized $100 of eligible gain and each transfers $100 to a QOF partnership. In a subsequent year, the partnership borrows $120 from an unrelated lender and distributes $120 equally to A and B.

(*2*) *Analysis.* If the contributions had been of property other than cash, the contributions and distributions would have been tested under the disguised sale rules of section 707 and the regulations in this part under section 707 of the Code, determining the timing of the distribution and amount of the debt allocated to each partner. Under paragraph (c)(6)(iii)(A)(*2*) of this section, the cash of $200 ($100 from A and $100 from B) is treated as property that could be sold in a disguised sale transaction and each partner's share of the debt is zero for purposes of determining the amount of the qualifying investment. To the extent there would have been a disguised sale applying the rule of paragraph (c)(6)(iii)(A)(*2*) of this section, the amount of the qualifying investment would be reduced by the amount of the contribution so recharacterized.

(D) *Example 4. Return of capital by QOF partnership*—(*1*) *Facts.* A realized $100 of eligible gain and transfers $100 of cash to a QOF partnership. Later in the partner's tax year, the partnership distributes $20 to A in a distribution that is not recharacterized under paragraph (c)(6)(iii)(A)(*2*) of this section. At the time of the distribution, no allocations of income, gain, loss, or deduction had been made to A, and A's share of the partnership's debt was zero under section 752.

(*2*) *Analysis.* Because the contribution and distribution are not recharacterized under paragraph (c)(6)(iii)(A)(*2*) of this section, the amount of A's qualifying investment is $100 despite the $20 distribution. At the time the $20 distribution is made to A, A's basis in its qualifying investment is zero, and thus the distribution is an inclusion event under § 1.1400Z2(b)–1(c)(6)(iii).

(E) *Example 5. Property contributed has built-in gain.* The facts are the same as in paragraph (c)(6)(v)(C)(*1*) of this section (*Example 3*), except that the property contributed by A had a value of $100 and basis of $20 and the partnership did not borrow money or make a distribution. Under paragraph (c)(6)(iii)(B)(*1*) of this section, the amount of A's qualifying investment is $20 (the lesser of the net value or the net basis of the property that A contributed), and the excess of the $100 contribution over the $20 qualifying investment is a non-qualifying investment. Under paragraph (c)(6)(iii)(B)(*4*) of this section, A's basis in the qualifying investment (determined without regard to section 1400Z–2(b)(2)(B) or section 752(a)) is $20. After the application of section 1400Z–2(b)(2)(B) but before the application of section 752(a), A's basis in the qualifying investment is zero. A's basis in the non-qualifying investment is zero without regard to the application of section 752(a).

(*F*) *Example 6. Property contributed has built-in gain and is subject to debt.* The facts are the same as in paragraph (c)(6)(v)(E) of this section (*Example 5*), except that the property contributed by A has a gross value of $130 and is subject to debt of $30. Under paragraph (c)(6)(iii)(B)(*1*) of this section, the amount of A's qualifying investment is zero, the lesser of the property's $100 net value ($130 minus $30) or $0 net basis ($20 minus $30, but limited to zero). The entire contribution constitutes a non-qualifying investment.

(G) *Example 7. Property contributed has built-in loss and is subject to debt.* The facts are the same as in paragraph (c)(6)(v)(F) of this section (*Example 6*), except that the property contributed by A has a basis of $150. Under paragraph (c)(6)(iii)(B)(*1*) of this section, the amount of A's qualifying investment is $100, the lesser of the property's $100 net value ($130 minus $30) or $120 net basis ($150 minus $30). The non-qualifying investment is $0, the excess of the net value ($100) over the qualifying investment ($100). A's basis in the qualifying investment (determined without regard to section 1400Z–2(b)(2)(B) and section 752(a)) is $120, the net basis. After the application of section 1400Z–2(b)(2)(B), A's basis in the qualifying investment is zero, plus its share of partnership debt under section 752(a).

(7) *Eligible gains that a partnership elects to defer.* A partnership generally is an eligible taxpayer under paragraph (b)(13) of this section and may elect to defer recognition of some or all of its eligible gains under section 1400Z–2(a)(2) and the section 1400Z–2 regulations.

(i) *Partnership deferral election.* If a partnership properly makes a deferral election, then—

(A) The partnership defers recognition of the eligible gain under the rules of section 1400Z–2 and the section 1400Z–2 regulations, that is, the partnership does not recognize gain at the time it otherwise would have in the absence of the deferral election; and

(B) The deferred eligible gain is not included in the distributive shares of the partners under section 702 and is not treated as an item described in section 705(a)(1).

(ii) *Subsequent recognition.* Absent any additional deferral under section 1400Z–2(a)(1)(A) and the section 1400Z–2 regulations, any amount of deferred gain that an electing partnership subsequently must include in income under sections 1400Z–2(a)(1)(B) and (b) and the section 1400Z–2 regulations is recognized by the electing partnership at the time of inclusion, is subject to section 702 and is treated as an item described in section 705(a)(1) in a manner consistent with recognition at that time.

(8) *Eligible gains that the partnership does not defer*—(i) *Federal income tax treatment of the partnership.* If a partnership does not elect to defer some, or all, of its eligible gains, the partnership's treatment of any such amounts is unaffected by the fact that the eligible gains could have been deferred under section 1400Z–2 and the section 1400Z–2 regulations.

(ii) *Federal income tax treatment by the partners.* If a partnership does not elect to defer some, or all, of the eligible gains—

(A) The gains for which a deferral election are not made are included in the partners' distributive shares under section 702 and are treated as items described in section 705(a)(1);

(B) If a partner's distributive share includes one or more gains that are eligible gains with respect to the partner, the partner may elect under section 1400Z–2(a)(1)(A) and the section 1400Z–2 regulations to defer some or all of such eligible gains; and

(C) A gain in a partner's distributive share is an eligible gain with respect to the partner only if it is an eligible gain with respect to the partnership and it did not arise from a sale or exchange with a person that, within the meaning of section 1400Z–2(e)(2) and the section 1400Z–2 regulations, is related to the partner.

(iii) *180-day period for a partner electing deferral*—(A) *General rule.* If a partner's distributive share includes a gain that is described in paragraph (c)(8)(ii)(C) of this section (gains that are eligible gains with respect to the partner), the 180-day period with respect to the partner's eligible gains in the partner's distributive share generally begins on the last day of the partnership taxable year in which the partner's distributive share of the partnership's eligible gain is taken into account under section 706(a).

(B) *Elective rule.* Notwithstanding the general rule in paragraph (c)(8)(iii)(A) of this section, if a partnership does not elect to defer all of its eligible gain, the partner may elect to treat the partner's own 180-day period with respect to the partner's distributive share of that gain as being—

(*1*) The same as the partnership's 180-day period; or

(*2*) The 180-day period beginning on the due date for the partnership's tax return, without extensions, for the taxable year in which the partnership realized the gain that is described in paragraph (c)(8)(ii)(C) of this section.

(C) *Example.* The following example illustrates the principles of this paragraph (c)(8)(iii).

(*1*) *Facts.* Four individuals, A, B, C, and D, have equal interests in a partnership, P. P has no other partners, and P's taxable year is the calendar year. On January 17, 2019, P realizes a capital gain of $1000*x* that P decides not to elect to defer.

(*2*) *Analysis of A's election.* A is aware of the capital gain realized by P, and decides to defer its distributive shares of P's eligible gain. A invests $250*x* in a QOF during February 2020. Under the general rule in paragraph (c)(8)(iii)(A) of this section, this investment is within the 180-day period for A, which began on December 31, 2019, the last day of P's taxable year in which A's share of P's eligible gain is taken into account under section 706(a).

(*3*) *Analysis of B's election.* B is also aware of the capital gain realized by P, and decides to defer its distributive shares of P's eligible gain. B decides to make the election provided in paragraph (c)(8)(iii)(B)(*1*) of this section, and invests $250*x* in a QOF during February 2019. Under the elective rule in paragraph (c)(8)(iii)(B)(*1*) of this section, this investment is within the 180-day period for B, which began on January 17, 2019, the same day as P's 180-day period.

(*4*) *Analysis of C's election.* On March 15, 2020, P provides all of its partners with their Schedules K–1. Upon learning that its distributive share of income from P included eligible gain, C decides to make a deferral election, and also makes the election provided in paragraph (c)(8)(iii)(B)(*2*) of this section. It then invests $250*x* in a QOF during June 2020. Under the elective rule in paragraph (c)(8)(iii)(B)(*2*) of this section, this investment is within the 180-day period for C, which began on March 15, 2020, the 180-day period beginning on the due date for P's tax return without extensions, for the taxable year in which P realized eligible gain.

(9) *Passthrough entities other than partnerships*—(i) *S corporations, nongrantor trusts, and estates.* If an S corporation, a nongrantor trust, or a decedent's estate realizes an eligible gain, then rules analogous to the rules of paragraphs (c)(7) and (8) of this section apply to that entity and to its shareholders or its beneficiaries, as the case may be, to the extent they receive or are deemed to receive an allocable share of the eligible gain.

(ii) *Grantor trusts.* If a grantor trust realizes an eligible gain, either the trust or the deemed owner of the trust may make the election to defer recognition of the gain and make the qualifying investment under rules analogous to the rules of paragraphs (c)(7) and (8) of this section (other than the rule in paragraph (c)(8)(iii) of this section regarding the 180-day period), whether or not the gain is distributed to the deemed owner of the trust.

(d) *Elections*—(1) *Taxable year of deferral election.* For a deferral election with respect to any eligible gain to be valid, an eligible taxpayer must make such election in accordance with guidance published in the Internal Revenue Bulletin or in forms and instructions (see §§ 601.601(d)(2) and 601.602 of this chapter), as to the required time, form, and manner in which an eligible taxpayer (including a partner, S corporation shareholder, or beneficiary applying the elective 180-day period provided in paragraphs (c)(8)(iii)(B) and (c)(9) of this section) may make a deferral election.

(2) *Annual reporting of qualifying investments.* An eligible taxpayer must report whether the gains that have been deferred remain deferred at the end of each taxable year, including the year of deferral, in accordance with guidance published in the Internal Revenue Bulletin or in forms and instructions (see §§ 601.601(d)(2) and 601.602 of this chapter). A failure to make this report for any given taxable year will result in a rebuttable presumption that the taxpayer has had an inclusion event described in § 1.1400Z2(b)–1(c) during that year. The presumption described in the previous sentence may be rebutted by the taxpayer making the report described in the first sentence of this paragraph (d)(2) or by the taxpayer establishing to the satisfaction of the Commissioner that an inclusion event described in § 1.1400Z2(b)–1(c) did not occur during that taxable year.

(e) *Interaction of section 1400Z–2 and § 1.897–6T.* Section 1400Z–2 is not a nonrecognition provision, as defined in § 1.897–6T(a)(2), for purposes of § 1.897–6T.

(f) *Treatment of mixed-funds investments*—(1) *Investments to which no election under section 1400Z–2(a) applies.* If a taxpayer invests in a QOF and makes a deferral election with respect to less than all of that investment, the portion of the investment to which the election does not apply is a non-qualifying investment. Similarly, an investment in a QOF with respect to which no deferral

election is made is a non-qualifying investment.

(2) *Treatment of deemed contributions of money under section 752(a).* In the case of a QOF partnership, the deemed contribution of money described in section 752(a) does not create or increase an investment in the QOF described in section 1400Z–2(e)(1)(A)(ii). Thus, any basis increase resulting from a deemed section 752(a) contribution is not taken into account in determining the portion of a partner's investment subject to section 1400Z–2(e)(1)(A)(i) or (ii). See § 1.1400Z2(b)–1(c)(6)(iv)(B) for rules relating to the application of section 752 to a mixed-funds investment.

(3) *Treatment of contributions to QOF corporation in which no stock is received.* If a taxpayer with a qualifying investment or a non-qualifying investment in a QOF corporation subsequently makes a non-qualifying investment or a qualifying investment, respectively, and if the taxpayer receives no additional QOF stock in exchange for the subsequent investment, the taxpayer has a mixed-funds investment.

(4) *Example.* The following example illustrates the rules of this paragraph (f):

(i) *Facts.* Taxpayer A realizes $1 million of eligible gain and on the next day contributes $1 million to a QOF, Partnership P, in exchange for a 50 percent interest in Partnership P. Taxpayer A makes an election under section 1400Z–2(a) with respect to $900,000 of that eligible gain. Under section 1400Z–2(e)(1), 90 percent of A's investment is described in section 1400Z–2(e)(1)(A)(i) (an investment that only includes amounts to which the election under section 1400Z–2(a) applies), and 10 percent is described in section 1400Z–2(e)(1)(A)(ii) (a separate investment consisting of other amounts). Partnership P borrows $8 million. Under § 1.752–3(a), taking into account the terms of the partnership agreement, $4 million of the $8 million liability is allocated to A.

(ii) *Analysis.* Under section 752(a), A is treated as contributing $4 million to Partnership P. Under paragraph (f) of this section, A's deemed $4 million contribution to Partnership P is ignored for purposes of determining the percentage of A's investment in Partnership P subject to the deferral election under section 1400Z–2(a) or the portion not subject to the deferral election under section 1400Z–2(a). As a result, after A's section 752(a) deemed contribution, $900,000, or 90 percent, of A's investment in Partnership P is described in section 1400Z–2(e)(1)(A)(i) and $100,000, or 10 percent, is described in section 1400Z–2(e)(1)(A)(ii).

(g) *Applicability dates*–(1) *In general.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to eligible gains that would be recognized (absent the making of a deferral election) during the portion of a taxpayer's first taxable year ending after December 21, 2017 that began on December 22, 2017, and during taxable years beginning after December 21, 2017, and on or before March 13, 2020, an eligible taxpayer may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(a)–1 contained in the notice of proposed rulemaking (REG–115420–18) published on October 29, 2018, as amplified by the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

■ **Par. 4.** Section 1.1400Z2(b)–1 is added to read as follows:

§ 1.1400Z2 (b)–1 Inclusion of gains that have been deferred under section 1400Z–2(a).

(a) *Scope.* This section provides rules under section 1400Z–2(b) of the Internal Revenue Code and the section 1400Z–2 regulations (as defined in § 1.1400Z2(a)–1(b)(41)) regarding the inclusion in income of gain deferred by a QOF owner under section 1400Z–2(a)(1)(A) and the section 1400Z–2 regulations. This section applies to a QOF owner only until all of such owner's gain deferred pursuant to a deferral election has been included in income, subject to the limitations described in paragraph (e)(5) of this section, and except as otherwise provided in paragraph (c) or (d) of this section. Paragraph (b) of this section provides general rules under section 1400Z–2(b)(1) regarding the timing of the inclusion in income of the deferred gain. Paragraph (c)(1) of this section provides the general rule regarding the determination of the extent to which an event triggers the inclusion in gross income of all, or a portion, of an eligible taxpayer's deferred gain, and paragraphs (c)(2) through (16) of this section provide specific rules for certain events that are or are not treated as inclusion events. Paragraph (d) of this section provides rules regarding holding periods for qualifying investments. Paragraph (e) of this section provides rules regarding the amount of deferred gain included in gross income under section 1400Z–2(a)(1)(B) and (b), including special rules for QOF partnerships and QOF S corporations. Paragraph (f) of this section provides examples illustrating the rules of paragraphs (c), (d), and (e) of this section. Paragraph (g) of this section provides rules regarding basis adjustments under section 1400Z–2(b)(2)(B). Paragraph (h) of this section provides special reporting rules applicable to partners, partnerships, and direct or indirect owners of QOF partnerships. Paragraph (i) is reserved. Paragraph (j) of this section provides dates of applicability.

(b) *General inclusion rule.* The gain to which a deferral election applies is included in gross income, to the extent provided in paragraph (e) of this section and in accordance with the rules of § 1.1400Z2(a)–1(c)(1), in the taxable year that includes the earlier of:

(1) The date of an inclusion event; or

(2) December 31, 2026.

(c) *Inclusion events*—(1) *In general.* Except as otherwise provided in this paragraph (c), an event is an inclusion event, if, and to the extent that—

(i) The event reduces an eligible taxpayer's direct equity interest for Federal income tax purposes in the qualifying investment;

(ii) An eligible taxpayer receives property in the event with respect to its qualifying investment and the event is treated as a distribution for Federal income tax purposes, whether or not the receipt reduces the eligible taxpayer's ownership of the QOF;

(iii) An eligible taxpayer claims a loss for worthless stock under section 165(g) or otherwise claims a worthlessness deduction with respect to its qualifying investment; or

(iv) A QOF in which an eligible taxpayer holds a qualifying investment loses its status as a QOF.

(2) *Termination or liquidation of QOF or QOF owner*—(i) *Termination or liquidation of QOF.* Except as otherwise provided in this paragraph (c), an eligible taxpayer has an inclusion event with respect to all of its qualifying investment if the QOF ceases to exist for Federal income tax purposes. For example, if a QOF partnership converts to a QOF C corporation, or if a QOF C corporation converts to a QOF partnership or to an entity disregarded as separate from its owner for Federal income tax purposes, all investors in the QOF have an inclusion event with respect to all of their qualifying investments in the QOF.

(ii) *Liquidation of QOF owner*—(A) *Portion of distribution treated as sale.* A distribution of a qualifying investment in a complete liquidation of a QOF owner is an inclusion event to the extent that section 336(a) treats the distribution as if the qualifying investment were sold to the distributee at its fair market value, without regard to section 336(d).

(B) *Distribution to 80-percent distributee.* A distribution of a qualifying investment in a complete

liquidation of a QOF owner is not an inclusion event to the extent section 337(a) applies to the distribution.

(3) *Transfer of an investment in a QOF by gift or incident to divorce*—(i) *Transfer of an investment in a QOF by gift.* Except to the extent provided in paragraph (c)(5) of this section, a taxpayer's transfer of a qualifying investment by gift, as defined for purposes of chapter 12 of subtitle B of the Code, whether outright or in trust, is an inclusion event, regardless of whether that transfer is a completed gift for Federal gift tax purposes, and regardless of the taxable or tax-exempt status of the donee of the gift.

(ii) *Transfers between spouses incident to divorce.* A transfer between spouses or incident to divorce or otherwise as provided in section 1041 of the Code is an inclusion event.

(4) *Transfer of an investment in a QOF by reason of the taxpayer's death*—(i) *In general.* Except as provided in paragraph (c)(4)(ii) of this section, a transfer of a qualifying investment by reason of the taxpayer's death is not an inclusion event. Transfers by reason of death include, for example:

(A) A transfer by reason of death to the deceased owner's estate;

(B) A distribution of a qualifying investment by the deceased owner's estate;

(C) A distribution of a qualifying investment by the deceased owner's trust that is made by reason of the deceased owner's death;

(D) The passing of a jointly owned qualifying investment to the surviving co-owner by operation of law; and

(E) Any other transfer of a qualifying investment at death by operation of law.

(ii) *Exceptions.* The following transfers are not included as a transfer by reason of the taxpayer's death, and thus are inclusion events:

(A) A sale, exchange, or other disposition by the deceased taxpayer's estate or trust, other than a distribution described in paragraph (c)(4)(i) of this section;

(B) Any disposition by the legatee, heir, or beneficiary who received the qualifying investment by reason of the taxpayer's death; and

(C) Any disposition by the surviving joint owner or other recipient who received the qualifying investment by operation of law on the taxpayer's death.

(iii) *Liability for deferred Federal income tax.* If the owner of a qualifying investment in a QOF dies before an inclusion event and the deferred gain is not includable in the decedent's gross income, the gain that the decedent elected to defer under section 1400Z–2(a) and the section 1400Z–2 regulations will be includable in the gross income, for the taxable year in which occurs an inclusion event, of the person described in section 691(a)(1).

(iv) *Qualifying investment in the hands of the person described in section 691(a)(1).* A qualifying investment received in a transfer by reason of death listed in paragraph (c)(4)(i) of this section continues to be a qualifying investment under § 1.1400Z2(a)–1(b)(34).

(5) *Grantor trusts*—(i) *Contributions to grantor trusts.* If the owner of a qualifying investment contributes it to a trust and, under subpart E of part I of subchapter J of chapter 1 of subtitle A of the Code (grantor trust rules), the contributing owner of the investment is the deemed owner of the trust (grantor trust), the contribution to the grantor trust is not an inclusion event. Similarly, a transfer of the investment by the grantor trust to the trust's deemed owner is not an inclusion event. For all purposes of the section 1400Z–2 regulations, references to the term *grantor trust* mean the portion of the trust that holds the qualifying investment in the QOF, and such a grantor trust, or portion of the trust, is a wholly grantor trust as to the deemed owner. Such contributions may include transfers by gift or any other type of transfer between the grantor and the grantor trust that is a nonrecognition event as a result of the application of the grantor trust rules (that is, subpart E of part I of subchapter J of chapter 1 of subtitle A of the Code).

(ii) *Changes in grantor trust status.* In general, a change in the income tax status of an existing trust owning a qualifying investment in a QOF, whether the termination of grantor trust status or the creation of grantor trust status, is an inclusion event. Notwithstanding the previous sentence, the termination of grantor trust status as the result of the death of the owner of a qualifying investment is not an inclusion event, but the provisions of paragraph (c)(4) of this section apply to distributions or dispositions by the trust. If a qualifying investment is held in the grantor portion of an electing small business trust (ESBT), as defined in section 1361(e)(1), and the ESBT converts into a qualified subchapter S trust (QSST), as defined in section 1361(d)(3), the beneficiary of which is the deemed owner of the grantor portion of the ESBT, there has been no change in the grantor trust status because the deemed owner continues to be taxable under subtitle A of the Code on the income and gain from the qualifying investment.

(iii) *Conversions of QSSTs and ESBTs.* With regard to conversions of QSSTs and ESBTs, see paragraphs (c)(7)(i)(B) and (C) of this section. For purposes of paragraph (c)(5)(ii) of this section, if a qualifying investment is held by a QSST that converts to an ESBT, the beneficiary of the QSST is the deemed owner of the grantor portion of the ESBT that then holds the qualifying investment, and the deemed owner is not a nonresident alien for purposes of this section (and thus notwithstanding § 1.1361–1(j)(8)), there has been no change in the grantor trust status because the deemed owner continues to be taxable under subtitle A of the Code on the income and gain from the qualifying investment.

(6) *Special rules for partners and partnerships*—(i) *Scope.* Except as otherwise provided in this paragraph (c)(6), in the case of a partnership that is a QOF or a QOF partner, the inclusion rules of this paragraph (c) apply to transactions involving any direct or indirect partner of the QOF to the extent of that partner's share of any eligible gain of the QOF.

(ii) *Transactions that are not inclusion events*—(A) *In general.* Notwithstanding paragraphs (c)(1) and (2) of this section, and except as otherwise provided in paragraph (c)(6) of this section, no transaction described in paragraph (c)(6)(ii) of this section is an inclusion event.

(B) *Section 721 contributions.* Subject to paragraph (c)(6)(v) of this section, a contribution by a QOF owner (contributing partner), of its qualifying QOF stock, qualifying QOF partnership interest, or direct or indirect partnership interest in a qualifying investment to a partnership (transferee partnership) to the extent the transaction is governed by section 721(a) is not an inclusion event, provided the interest transfer does not cause a partnership termination of a QOF partnership, or the direct or indirect owner of a QOF, under section 708(b)(1). See paragraph (c)(6)(ii)(C) of this section for transactions governed by section 708(b)(2)(A). The inclusion rules in paragraph (c) of this section apply to any part of the transaction to which section 721(a) does not apply. The transferee partnership becomes subject to section 1400Z–2 and the section 1400Z–2 regulations with respect to the eligible gain associated with the contributed qualifying investment. The transferee partnership must allocate and report the remaining deferred gain that is associated with the contributed qualifying investment to the contributing partner to the same extent that the remaining deferred gain would have been allocated and reported to the

contributing partner in the absence of the contribution. Additionally, the transferee partnership must allocate the basis increases described in section 1400Z–2(b)(2)(B)(iii) and (iv) to the contributing partner. If a transferee partnership is a direct QOF owner, only the transferee partnership may make the elections under section 1400Z–2(c) and the regulations in this part under section 1400Z–2(c) of the Code with respect to the contributed qualifying investment. See § 1400Z2(c)–1(b)(1)(ii) (election by transferee partnership).

(C) *Section 708(b)(2)(A) mergers or consolidations*—(*1*) *Merger of a partnership that is a QOF partner.* Subject to paragraphs (c)(6)(iii) and (v) of this section, a merger or consolidation of a partnership that is a QOF partner (original partnership) with another partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event to the extent section 721(a) applies to the merger. To the extent the original partnership terminates in the merger, as determined under § 1.708–1(c)(1), the partnership that is a continuation of the original partnership becomes subject to section 1400Z–2 and the section 1400Z–2 regulations to the same extent that the original partnership was so subject prior to the transaction, and must allocate and report any gain under section 1400Z–2(b) to the same extent and to the same partners that the original partnership allocated and reported such items prior to the transaction. Notwithstanding the rules in this paragraph (c)(6)(ii)(C)(*1*), the general inclusion rules of paragraph (c) of this section apply to the portion of the transaction that is otherwise treated as a sale or exchange under paragraph (c) of this section.

(*2*) *Merger of QOF partnerships.* Subject to paragraph (c)(6)(v) of this section, a merger or consolidation of a QOF partnership with another QOF partnership in a transaction to which section 708(b)(2)(A) applies is not an inclusion event under paragraph (c)(2)(i) of this section if, immediately after the merger or consolidation, the resulting partnership is a QOF. The continuing partnership, as determined under § 1.708–1(c)(1), becomes subject to section 1400Z–2 and the section 1400Z–2 regulations to the same extent that the terminated partnership was so subject prior to the transaction, and must allocate and report any gain under section 1400Z–2(b) to the same extent and to the same partners that the terminated partnership would have allocated and reported such items prior to the transaction. Notwithstanding the rules in this paragraph (c)(6)(ii)(C)(*2*), the general inclusion rules of paragraph (c) of this section apply to the portion of the transaction that is otherwise treated as a sale or exchange under paragraph (c) of this section.

(D) *Example.* The following example illustrates the rules of this paragraph (c)(6)(ii).

(*1*) *Example*—(*i*) *Facts.* In 2019, taxpayer A contributes $100 of eligible gain to a QOF partnership, X, in exchange for a qualifying QOF partnership interest in X, and taxpayer B contributes $100 of eligible gain to another QOF partnership, Y, in exchange for a qualifying QOF partnership interest in Y. In 2021, in transactions governed by section 721(a), A contributes her qualifying QOF partnership interest in X, and B contributes her qualifying QOF partnership interest in Y, to a newly formed partnership, UTP. In 2024, C receives a profits interest in UTP for services that she will provide to UTP. In 2031, X sells a non-inventory asset and allocates X's distributive share of the gain to UTP. No distributions are ever made from X, Y, or UTP.

(*ii*) *Analysis.* On December 31, 2026, UTP recognizes $170 of remaining deferred gain relating to the QOF interests. Of that gain, A is allocated the $85 of gain relating to the $100 of eligible gain that she invested in X, and B is allocated the $85 of gain relating to the $100 of eligible gain that she invested in Y. C recognizes no gain at this time. In 2031, because UTP's holding period in X includes A's holding period in X, UTP has a holding period in X that exceeds 10 years, and may make an election under § 1.1400Z2(c)–1(b)(2)(ii) to exclude the gain from X's asset sale. Even though A was the original investor in X, she may not make the election. If UTP makes the election, UTP will exclude its distributive share of gain from the sale of the X asset.

(*2*) [Reserved]

(iii) *Partnership distributions.* Subject to paragraph (c)(6)(v) of this section, an actual or deemed distribution of property, including cash, by a QOF partnership to a partner with respect to its qualifying investment is an inclusion event only to the extent that the distributed property has a fair market value in excess of the partner's basis in its qualifying investment. For purposes of this paragraph (c)(6)(iii), in the case of a merger or consolidation of a QOF partnership with another QOF partnership in a transaction to which section 708(b)(2)(A) applies, the fair market value of the distributed property is reduced by the fair market value of the QOF partnership interest received in the merger or consolidation. A distribution from a partnership that directly or indirectly owns a QOF is an inclusion event only if the distribution is a liquidating distribution. For purposes of this paragraph (c)(6)(iii), the distribution is not in complete liquidation if the partnership making the distribution is a partnership that terminates in a partnership merger or consolidation under § 1.708–1(c), the continuing partnership in the merger or consolidation continues to directly or indirectly own an interest in the QOF, and the distributee is distributed an interest in the resulting partnership as part of the merger or consolidation. See paragraph (c)(6)(iv) of this section for special rules relating to mixed-funds investments.

(iv) *Special rules for mixed-funds investments*—(A) *In general.* The rules of this paragraph (c)(6)(iv) apply solely for purposes of section 1400Z–2. A partner that holds a mixed-funds investment in a QOF partnership (a mixed-funds partner) shall be treated as holding two separate interests in the QOF partnership, one a qualifying investment and the other a non-qualifying investment (separate interests). The basis of each separate interest is determined under the rules described in paragraphs (c)(6)(iv)(B) and (g) of this section as if each interest were held by different taxpayers.

(B) *Allocations and distributions.* All section 704(b) allocations of income, gain, loss, and deduction, all section 752 allocations of debt, and all distributions made to a mixed-funds partner will be treated as made to the separate interests based on the allocation percentages of those interests as defined in paragraph (c)(6)(iv)(D) of this section. For purposes of this paragraph (c)(6)(iv)(B), in allocating income, gain, loss, or deduction between these separate interests, section 704(c) principles apply to account for any value-basis disparities attributable to the qualifying investment or non-qualifying investment. Any distribution (whether actual or deemed) to the holder of a qualifying investment is subject to the rules of paragraphs (c)(6)(iii) and (v) of this section, without regard to the presence or absence of gain under other provisions of subchapter K of chapter 1 of subtitle A of the Internal Revenue Code.

(C) *Subsequent contributions.* In the event of an increase in a partner's qualifying or non-qualifying investment, as for example, in the case of an additional contribution for a qualifying investment or for an interest that is a non-qualifying investment or a change in allocations for services rendered, the partner's interest in the separate interests must be valued immediately prior to the event and the allocation percentages adjusted to reflect the relative values of these separate interests and the additional contribution, if any.

(D) *Allocation percentages.* The allocation percentages of the separate

interests will be determined based on the relative capital contributions attributable to the qualifying investment and the non-qualifying investment. In the event a partner receives a profits interest in the QOF partnership for services provided to or for the benefit of the QOF partnership, the allocation percentage with respect to the profits interest is based on the share of residual profits the mixed-funds partner would receive with respect to that interest, disregarding any allocation of residual profits for which there is not a reasonable likelihood of application.

(E) *Examples.* The following examples illustrate the rules of this paragraph (c)(6)(iv).

(*1*) *Example 1. Allocation of residual profits for which there is no reasonable likelihood of application*—(*i*) *Facts.* A realizes $100 of eligible gain and B realizes $900 of eligible gain. A and B form Q, a QOF partnership. B contributes $900 to Q in exchange for a qualifying QOF partnership interest (B's capital interest). A contributes $100 to Q in exchange for a qualifying QOF partnership interest (A's capital interest and, with B's capital interest, the capital interests) and agrees to provide services to Q in exchange for a profits interest in Q (A's profits interest). Q's partnership agreement provides that Q's profits are first allocated to the capital interests until the capital interest holders receive a 10 percent preferred return with respect to those interests. Next, Q's profits are allocated 15 percent to A with respect to A's profits interest, 10 percent to A with respect to A's capital interest, and 75 percent to B until the capital interests receive a 1,000% preferred return. Thereafter, Q's profits are allocated 1 percent to A's profits interest and 99 percent to the capital interests. There is not a reasonable likelihood that Q's profits will be sufficient to result in an allocation in the last tranche.

(*ii*) *Analysis.* Under paragraph (c)(6)(iv)(D) of this section, the allocation percentage with respect to A's profits interest is calculated based on the share of residual profits that A would receive with respect to A's profits interest, disregarding any allocation of residual profits that has no reasonable likelihood of being achieved. Under Q's partnership agreement, A's share of Q's residual profits with respect to A's profits interest is 1 percent. However, there is no reasonable likelihood that this 1 percent allocation will apply because it is unlikely that the capital interests will receive a 1,000% preferred return. Therefore, under paragraph (c)(6)(iv)(D) of this section, A's share of Q's residual profits with respect to A's profits interest is 15 percent, the final allocation of Q's profits to A's profits interest that is reasonably likely to apply. The allocation percentage for A's capital interest in Q is 10 percent under paragraph (c)(6)(iv)(D) of this section. Thus, allocations and distributions made to A are treated as made 60 percent (15/25) to A's non-qualifying profits interest and 40 percent (10/25) to A's qualifying QOF partnership interest.

(*2*) *Example 2. Separate entity holding profits interest*—(i) *Facts.* The facts are the same as in paragraph (c)(6)(iv)(E)(*1*) of this section (*Example 1*), except that A is a partnership that has no eligible gain and P, a partnership that is owned by the same taxpayers who own A, realizes $100 of eligible gain and contributes $100 to Q for its qualifying investment.

(*ii*) *Analysis.* Under paragraph (c)(6)(iv)(D) of this section, A's profits interest is a non-qualifying investment in Q. Because P directly holds only a qualifying QOF partnership interest in Q, P is not a mixed-funds partner in Q, and 100 percent of the allocations and distributions made to P are attributable to P's qualifying QOF partnership interest.

(v) *Remaining deferred gain reduction rule.* An inclusion event occurs when and to the extent that a transaction has the effect of reducing:

(A) The amount of remaining deferred gain of one or more direct or indirect partners; or

(B) The amount of gain that would be recognized by such partner or partners under paragraph (e)(4)(ii) of this section to the extent that such amount would reduce such gain to an amount that is less than the remaining deferred gain.

(7) *Special rules for S corporations*—(i) *In general.* Except as provided in paragraphs (c)(7)(ii), (iii), and (iv) of this section, none of the following is an inclusion event:

(A) An election, revocation, or termination of a corporation's status as an S corporation under section 1362;

(B) A conversion of a QSST to an ESBT, but only if the QSST beneficiary is the deemed owner of the grantor portion of the ESBT that receives the qualifying investment and if the deemed owner is not a nonresident alien;

(C) A conversion of an ESBT to a QSST, where the qualifying investment is held in the grantor portion of the ESBT and the QSST beneficiary is the deemed owner of the grantor portion of the ESBT; and

(D) A valid modification of a trust agreement of an S-corporation shareholder whether by an amendment, a decanting, a judicial reformation, or a material modification.

(ii) *Distributions by QOF S corporation*—(A) *General rule.* An actual or constructive distribution of property by a QOF S corporation to a QOF shareholder with respect to its qualifying investment is an inclusion event to the extent that the distribution is treated as gain from the sale or exchange of property under section 1368(b)(2) and (c). For the treatment of a distribution by a QOF S corporation to which section 305(a) applies, see paragraph (c)(8)(ii). For the treatment of a distribution to which section 302(d) or section 306(a)(2) applies, see paragraph (c)(9)(ii) of this section.

(B) *Spill-over rule.* For purposes of applying paragraph (c)(7)(ii) of this section to the adjusted basis of a qualifying investment, or non-qualifying investment, as appropriate, in a QOF S corporation, the second sentence of § 1.1367–1(c)(3) applies—

(*1*) With regard to multiple qualifying investments, solely to the respective bases of such qualifying investments, and does not take into account the basis of any non-qualifying investment; and

(*2*) With regard to multiple non-qualifying investments, solely to the respective bases of such non-qualifying investments, and does not take into account the basis of any qualifying investment.

(iii) *Conversion from S corporation to partnership or disregarded entity*—(A) *General rule.* Notwithstanding paragraph (c)(7)(i) of this section, and except as provided in paragraph (c)(7)(iii)(B) of this section, a conversion of an S corporation to a partnership or an entity disregarded as separate from its owner under § 301.7701–3(b)(1)(ii) of this chapter is an inclusion event.

(B) *Exception for qualifying section 381 transaction.* A conversion described in paragraph (c)(7)(iii)(A) of this section is not an inclusion event if the conversion comprises a step in a series of related transactions that together qualify as a qualifying section 381 transaction.

(iv) *Treatment of separate blocks of stock in mixed-funds investments.* With regard to a mixed-funds investment in a QOF S corporation, if different blocks of stock are created for separate qualifying investments to track basis in such qualifying investments, the separate blocks are not treated as different classes of stock for purposes of S corporation eligibility under section 1361(b)(1).

(v) *Applicability.* Paragraph (c)(7) of this section applies regardless of whether the S corporation is a QOF or a QOF shareholder.

(8) *Distributions by a QOF corporation*—(i) *General rule for distributions by a QOF C corporation.* If a QOF C corporation distributes property to a QOF shareholder with respect to a qualifying investment, only the amount of the distribution to which section 301(c)(3) or 1059(a)(2) applies gives rise to an inclusion event. For purposes of this paragraph (c)(8)(i), a distribution of property includes a distribution of stock in the QOF C corporation making the distribution (or rights to acquire such stock) if the distribution is treated as a distribution

of property to which section 301 applies pursuant to section 305(b).

(ii) *Section 305(a) distributions.* A distribution with respect to qualifying QOF stock to which section 305(a) applies is not an inclusion event. QOF stock received in such a distribution is qualifying QOF stock. The shareholder's remaining deferred gain is allocated pro rata between the new qualifying QOF stock received and the qualifying QOF stock with respect to which the distribution was made in proportion to the fair market values of each on the date of distribution. See § 1.307–1(a).

(9) *Dividend-equivalent redemptions and redemptions of section 306 stock.*—(i) *Redemptions by QOF C corporations*—(A) *In general.* Except as provided in paragraph (c)(9)(i)(B) of this section, if a QOF C corporation redeems its stock from a QOF shareholder in a transaction described in section 302(d) or section 306(a)(2), the full amount of such redemption gives rise to an inclusion event.

(B) *Redemptions of stock of wholly owned QOF C corporation and pro rata redemptions.* Paragraph (c)(8)(i) of this section applies to a redemption described in paragraph (c)(9)(i)(A) of this section if, at the time of such redemption—

(*1*) All stock in the QOF C corporation is held directly by a single shareholder, or directly by members of a single consolidated group; or

(*2*) The QOF C corporation has outstanding only one class of stock, as defined in section 1361 and § 1.1361–1(l), and the redemption is pro rata as to all shareholders of the redeeming QOF C corporation.

(ii) *Redemptions by QOF S corporations.* If a QOF S corporation redeems its stock from a QOF shareholder in a transaction described in section 302(d) or section 306(a)(2), the amount that gives rise to an inclusion event is the amount by which the distribution exceeds basis in the QOF stock as adjusted under paragraph (c)(7)(ii) of this section.

(10) *Qualifying section 381 transactions*—(i) *Assets of a QOF are acquired*—(A) *In general.* Except to the extent provided in paragraph (c)(10)(i)(C) of this section, if the assets of a QOF corporation are acquired in a qualifying section 381 transaction, and if the acquiring corporation is a QOF immediately after the acquisition, then the transaction is not an inclusion event.

(B) *Determination of acquiring corporation's status as a QOF.* For purposes of paragraph (c)(10)(i)(A) of this section, the acquiring corporation is treated as a QOF immediately after the qualifying section 381 transaction if the acquiring corporation satisfies the certification requirements in § 1.1400Z2(d)–1 immediately after the transaction and holds at least 90 percent of its assets in qualified opportunity zone property on the first testing date after the transaction. See section 1400Z–2(d)(1) and § 1.1400Z2(d)–1.

(C) *Receipt of boot by QOF shareholder in qualifying section 381 transaction.* This paragraph (c)(10)(i)(C) applies if assets of a QOF corporation are acquired in a qualifying section 381 transaction and an eligible taxpayer that is a QOF shareholder receives boot with respect to its qualifying investment. If this paragraph (c)(10)(i)(C) applies, the QOF shareholder has an inclusion event and is treated as disposing of a portion of its qualifying investment that bears the same proportion to the QOF shareholder's total qualifying investment immediately before the inclusion event as the fair market value of the boot received by the QOF shareholder with respect to its qualifying investment in the qualifying section 381 transaction bears to the fair market value of the total consideration received by the QOF shareholder with respect to its qualifying investment in the qualifying section 381 transaction.

(ii) *Assets of a QOF shareholder are acquired*—(A) *In general.* Except to the extent provided in paragraph (c)(10)(ii)(B) of this section, a qualifying section 381 transaction in which the assets of a QOF shareholder are acquired is not an inclusion event with respect to the qualifying investment and the acquiring corporation succeeds to the target corporation's status as the QOF shareholder with respect to the qualifying investment.

(B) *Qualifying section 381 transaction in which QOF shareholder's qualifying investment is not completely acquired.* If the assets of a QOF shareholder are acquired in a qualifying section 381 transaction in which the acquiring corporation does not acquire all of the QOF shareholder's qualifying investment, the QOF shareholder has an inclusion event and is treated as disposing of the portion of its qualifying investment that is not transferred to the acquiring corporation.

(11) *Section 355 transactions*—(i) *Distribution by a QOF*—(A) *In general.* Except as provided in paragraph (c)(11)(i)(B) of this section, if a QOF corporation distributes stock or securities of a controlled corporation to a QOF shareholder with respect to a qualifying investment in the QOF corporation in a transaction to which section 355 (or so much of section 356 as relates to section 355) applies, the QOF shareholder has an inclusion event and is treated as disposing of a portion of its qualifying investment equal in value to the fair market value of the shares of the controlled corporation and the fair market value of any boot received by the QOF shareholder in the distribution with respect to its qualifying investment.

(B) *Controlled corporation becomes a QOF*—(*1*) *In general.* Except as provided in paragraph (c)(11)(i)(B)(*3*) of this section, if a QOF corporation distributes stock or securities of a controlled corporation in a transaction to which section 355, or so much of section 356 as relates to section 355, applies, and if both the distributing corporation and the controlled corporation are QOFs immediately after the final distribution (qualifying section 355 transaction), then the distribution is not an inclusion event with respect to a QOF shareholder's qualifying investment in the distributing QOF corporation or the controlled QOF corporation. This paragraph (c)(11)(i)(B) does not apply unless the distributing corporation distributes all of the stock and securities in the controlled corporation held by it immediately before the distribution within a 30-day period. For purposes of this paragraph (c)(11)(i)(B), the term *final distribution* means the last distribution that satisfies the preceding sentence.

(*2*) *Determination of distributing corporation's and controlled corporation's status as QOFs.* For purposes of paragraph (c)(11)(i)(B)(*1*) of this section, each of the distributing corporation and the controlled corporation is treated as a QOF immediately after the final distribution if the corporation satisfies the certification requirements in § 1.1400Z2(d)–1 immediately after the final distribution and holds at least 90 percent of its assets in qualified opportunity zone property on the first testing date after the final distribution. See section 1400Z–2(d)(1) and § 1.1400Z2(d)–1.

(*3*) *Receipt of boot.* If a QOF shareholder receives boot in a qualifying section 355 transaction with respect to its qualifying investment, and if section 356(a) applies to the transaction, paragraph (c)(10)(i)(C) of this section applies. If a QOF shareholder receives boot in a qualifying section 355 transaction with respect to its qualifying investment, and if section 356(b) applies to the transaction, paragraph (c)(8)(i) of this section applies.

(*4*) *Treatment of controlled corporation stock as qualified opportunity zone stock.* If stock or securities of a controlled corporation are

distributed in a qualifying section 355 transaction, and if the distributing corporation retains a portion of the controlled corporation stock after the initial distribution, the retained stock will not cease to qualify as qualified opportunity zone stock in the hands of the distributing corporation solely as a result of the qualifying section 355 transaction. This paragraph (c)(11)(i)(B)(*4*) does not apply unless the distributing corporation distributes all of the stock and securities in the controlled corporation held by it immediately before the distribution within a 30-day period.

(ii) *Distribution by a QOF shareholder.* If a QOF shareholder distributes stock or securities of a controlled QOF corporation in a transaction to which section 355 applies, then for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section, the QOF shareholder has an inclusion event and is treated as disposing of the portion of its qualifying QOF stock over which it no longer has direct Federal income tax ownership.

(12) *Recapitalizations and section 1036 transactions*—(i) *In general.* Except as otherwise provided in paragraph (c)(12)(ii) of this section, if a QOF corporation engages in a transaction that qualifies as a reorganization described in section 368(a)(1)(E) (a recapitalization), or if a QOF shareholder engages in a transaction that is described in section 1036 (a section 1036 exchange), the transaction is not an inclusion event.

(ii) *Receipt of property or boot by QOF shareholder.* If a QOF shareholder receives property or boot, or is treated as having received property or boot, with respect to its qualifying investment in a recapitalization, then the property or boot is treated as property or boot to which section 301 or section 356(a) or (c) applies, as determined under general Federal income tax principles. If, in a section 1036 exchange, a QOF shareholder receives property with respect to its qualifying investment that is not permitted to be received without the recognition of gain, then, for purposes of this section, the receipt of the property is treated in a similar manner as the receipt of such property or boot in a recapitalization. Paragraph (c)(8)(i) of this section applies to property to which section 301 applies. Paragraph (c)(10)(i)(C) of this section applies to boot to which section 356(a) or (c) applies.

(13) *Section 304 transactions.* If a QOF shareholder transfers its qualifying investment in a transaction described in section 304(a), the full amount of the consideration gives rise to an inclusion event.

(14) *Deduction for worthlessness.* If an eligible taxpayer claims a loss for worthless stock under section 165(g) or otherwise claims a worthlessness deduction with respect to all or a portion of its qualifying investment, then for purposes of section 1400Z–2 and the section 1400Z–2 regulations, the eligible taxpayer has an inclusion event and is treated as having disposed of that portion of its qualifying investment on the date it became worthless. Thus, neither section 1400Z–2(b)(2)(B)(iii) or (iv) nor section 1400Z–2(c) applies to that portion of the eligible taxpayer's qualifying investment after the date it became worthless.

(15) *Decertification of a QOF.* The decertification of a QOF, whether a self-decertification pursuant to § 1.1400Z2(d)–1(a)(3) or an involuntary decertification pursuant to § 1.1400Z2(d)–1(a)(4), is an inclusion event.

(16) *Other inclusion and non-inclusion events.* Notwithstanding any other provision of this paragraph (c), the Commissioner may determine in guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter) that a type of transaction is or is not an inclusion event.

(d) *Holding periods*—(1) *Holding period for qualifying investment*—(i) *In general.* Solely for purposes of section 1400Z–2(b)(2)(B), section 1400Z–2(c), and the section 1400Z–2 regulations, and except as otherwise provided in this paragraph (d)(1), the length of time a qualifying investment has been held is determined without regard to the period for which the eligible taxpayer had held property exchanged for such investment (even if such period would be relevant for determining the length of time for other Federal income tax purposes).

(ii) *Holding period for qualifying investment received in certain transactions with respect to QOFs.* For purposes of section 1400Z–2(b)(2)(B), section 1400Z–2(c), and the section 1400Z–2 regulations, the principles of section 1223(1) or (4) apply to determine the holding period for a qualifying investment received by a QOF owner in—

(A) A distribution described in paragraph (c)(2)(ii)(B) of this section;

(B) A distribution to which section 305(a) applies;

(C) A qualifying section 381 transaction described in paragraph (c)(10)(i) or (ii) of this section;

(D) A qualifying section 355 transaction described in paragraph (c)(11)(i)(B) of this section;

(E) A recapitalization or a section 1036 exchange described in paragraph (c)(12) of this section;

(F) A contribution of a QOF interest to a partnership to the extent section 721(a) applies to the transfer; or

(G) A distribution of a QOF interest to the extent the interest was received in a merger of two or more QOF partnerships in a transaction described in section 708(b)(2)(A).

(iii) *Tacking with deceased owner or deemed owner of a grantor trust.* For purposes of section 1400Z–2(b)(2)(B), section 1400Z–2(c), and the section 1400Z–2 regulations, the holding period of a qualifying investment held by an eligible taxpayer who received that qualifying investment by reason of the prior owner's death includes the time during which that qualifying investment was held by the deceased owner. The rule in the preceding sentence also applies to allow a grantor trust to tack the holding period of the deemed owner if the grantor trust acquires the qualifying investment from the deemed owner in a transaction that is not an inclusion event.

(2) *Status of QOF assets as qualified opportunity zone property.* For purposes of section 1400Z–2(d) and the section 1400Z–2 regulations, including for purposes of determining whether the original use of qualified opportunity zone business property commences with the acquiring corporation or partnership, qualified opportunity zone property does not lose its status as qualified opportunity zone property solely as a result of—

(i) Its transfer by the transferor corporation to the acquiring corporation in a qualifying section 381 transaction described in paragraph (c)(10)(i) of this section;

(ii) Its transfer by the distributing corporation to the controlled corporation in a qualifying section 355 transaction described in paragraph (c)(11)(i)(B) of this section; or

(iii) Its transfer by the transferor partnership to the acquiring partnership in a transaction to which section 708(b)(2)(A) applies, but only to the extent section 721(a) applies to the transaction.

(e) *Amount includible.* Except as provided in §§ 1.1400Z2(a)–1(b)(7) and 1.1400Z2(f)–1(b), the amount of gain included in gross income under section 1400Z–2(a)(1)(B) and this section on a date described in paragraph (b) of this section is determined under this paragraph (e).

(1) *In general.* Except as provided in paragraphs (e)(2) and (4) of this section, and subject to paragraph (e)(5) of this section, in the case of an inclusion

event, the amount of gain included in gross income is equal to the excess of the amount described in paragraph (e)(1)(i) of this section over the eligible taxpayer's basis in the portion of the qualifying investment that is disposed of in the inclusion event. See paragraph (c) of this section for rules regarding the amount that gave rise to the inclusion event, and see paragraph (g) of this section for applicable ordering rules.

(i) The amount described in this paragraph (e)(1)(i) is equal to the lesser of—

(A) An amount which bears the same proportion to the remaining deferred gain, as—

(*1*) The fair market value of the portion of the qualifying investment that is disposed of in the inclusion event bears to—

(*2*) The fair market value of the total qualifying investment immediately before the inclusion event; or

(B) The fair market value of the portion of the qualifying investment that is disposed of in the inclusion event.

(ii) For purposes of paragraph (e)(1)(i) of this section, the fair market value of the portion of the qualifying investment that is disposed of in the inclusion event is determined by multiplying the fair market value of the eligible taxpayer's entire qualifying investment in the QOF, determined as of the date of the inclusion event, by the percentage of the eligible taxpayer's qualifying investment that is represented by the portion that is disposed of in the inclusion event.

(2) *Property received from a QOF in certain transactions.* In the case of an inclusion event described in paragraph (c)(6)(iii) or (v), (c)(7)(ii), (c)(8)(i), or (c)(9) or (13) of this section (or in paragraph (c)(11) or (12) of this section, to the extent the rules in paragraph (c)(8)(i) of this section apply to the inclusion event), the amount of gain included in gross income is equal to the lesser of—

(i) The remaining deferred gain; or

(ii) The amount that gave rise to the inclusion event.

(3) *Gain recognized on December 31, 2026.* The amount of gain included in gross income on December 31, 2026 is equal to the excess of—

(i) The lesser of—

(A) The remaining deferred gain; and

(B) The fair market value of the qualifying investment held on December 31, 2026; over

(ii) The eligible taxpayer's basis in the qualifying investment as of December 31, 2026, taking into account only section 1400Z–2(b)(2)(B).

(4) *Special amount includible rule for partnerships and S corporations.* For purposes of paragraphs (e)(1) and (3) of this section, in the case of an inclusion event involving a qualifying investment in a QOF partnership or S corporation, or in the case of a qualifying investment in a QOF partnership or S corporation held on December 31, 2026, the amount of gain included in gross income is equal to the lesser of—

(i) The product of—

(A) The percentage of the qualifying investment that gave rise to the inclusion event; and

(B) The remaining deferred gain, less any basis adjustments pursuant to section 1400Z–2(b)(2)(B)(iii) and (iv); or

(ii) The gain that would be recognized on a fully taxable disposition at fair market value of the qualifying investment that gave rise to the inclusion event.

(5) *Limitation on amount of gain included after statutory five-year and seven-year basis increases.* The total amount of gain included in gross income under this paragraph (e) is limited to the amount deferred under section 1400Z–2(a)(1) and the section 1400Z–2 regulations, reduced by any increase in the basis of the qualifying investment made pursuant to section 1400Z–2(b)(2)(B)(iii) and (iv). See paragraph (g)(2) of this section for limitations on the amount of basis adjustments under section 1400Z–2(b)(2)(B)(iii) and (iv).

(f) *Examples.* The following examples illustrate the rules of paragraphs (c), (d) and (e) of this section. For purposes of the following examples: A, B, C, W, X, Y, and Z are C corporations that do not file a consolidated Federal income tax return; Q is a QOF corporation or a QOF partnership, as specified in each example; and each divisive corporate transaction satisfies the requirements of section 355.

(1) *Example 1. Determination of basis, holding period, and qualifying investment*—(i) *Facts.* A wholly and directly owns Q, a QOF corporation. On May 31, 2019, A sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, A transfers unencumbered asset N to Q in exchange for a qualifying investment. Asset N, which A has held for 10 years, has a basis of $500 and a fair market value of $500. A elects to defer the inclusion of $500 in gross income under section 1400Z–2(a) and § 1.1400Z2(a)–1.

(ii) *Analysis.* Under § 1.1400Z2(a)–1(c)(6)(ii)(B)(*1*), A made a qualifying investment of $500. Under section 1400Z–2(b)(2)(B)(i), A's basis in its qualifying investment in Q is $0. For purposes of sections 1400Z–2(b)(2)(B) and 1400Z–2(c), A's holding period in its new investment in Q begins on October 31, 2019. See paragraph (d)(1)(i) of this section. Other than for purposes of applying section 1400Z–2, A has a 10-year holding period in its new Q investment as of October 31, 2019.

(iii) *Transfer of built-in gain property.* The facts are the same as in paragraph (f)(1)(i) of this section (this *Example 1*), but A's basis in transferred asset N is $200. Under § 1.1400Z2(a)–1(c)(6)(ii)(B)(*1*), A made a qualifying investment of $200 and a non-qualifying investment of $300.

(2) *Example 2. Transfer of qualifying investment*—(i) *Facts.* On May 31, 2019, taxpayer A sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, A transfers $500 to newly formed Q, a QOF corporation, in exchange for a qualifying investment. On February 29, 2020, A transfers 25 percent of its qualifying investment in Q to newly formed Y in exchange for 100 percent of Y's stock in a transfer to which section 351 applies (Transfer), at a time when the fair market value of A's qualifying investment in Q is $800.

(ii) *Analysis.* Under § 1.1400Z2(a)–1(c)(6)(ii)(A), A made a qualifying investment of $500 on October 31, 2019. In the Transfer, A exchanged 25 percent of its qualifying investment for Federal income tax purposes, which reduced A's direct qualifying investment. Under paragraph (c)(1)(i) of this section, the Transfer is an inclusion event to the extent of the reduction in A's direct qualifying investment. Under paragraph (e)(1) of this section, A therefore includes in income an amount equal to the excess of the amount described in paragraph (e)(1)(i) of this section over A's basis in the portion of the qualifying investment that was disposed of, which in this case is $0. The amount described in paragraph (e)(1)(i) is the lesser of $125 ($500 × ($200/$800)) or $200. As a result, A must include $125 of its deferred capital gain in income in 2020. After the Transfer, the Q stock is not qualifying Q stock in Y's hands.

(iii) *Disregarded transfer.* The facts are the same as in paragraph (f)(2)(i) of this section (this *Example 2*), except that Y elects to be treated as an entity that is disregarded as an entity separate from its owner for Federal income tax purposes effective prior to the Transfer. Since the Transfer is disregarded for Federal income tax purposes, A's transfer of its qualifying investment in Q is not treated as a reduction in direct tax ownership for Federal income tax purposes, and the Transfer is not an inclusion event with respect to A's qualifying investment in Q for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. Thus, A is not required to include in income any portion of its deferred capital gain.

(iv) *Election to be treated as a corporation.* The facts are the same as in paragraph (f)(2)(iii) of this section (this *Example 2*), except that Y (a disregarded entity) subsequently elects to be treated as a corporation for Federal income tax purposes. A's deemed transfer of its qualifying investment in Q to Y under § 301.7701–3(g)(1)(iv) of this chapter is an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section.

(3) *Example 3. Part sale of qualifying QOF partnership interest in Year 6 when value of the QOF partnership interest has increased*—

(i) *Facts.* In October 2018, A and B each realize $200 of eligible gain, and C realizes $600 of eligible gain. On January 1, 2019, A, B, and C form Q, a QOF partnership. A contributes $200 of cash, B contributes $200 of cash, and C contributes $600 of cash to Q in exchange for qualifying QOF partnership interests in Q. A, B, and C hold 20 percent, 20 percent, and 60 percent interests in Q, respectively. On January 30, 2019, Q obtains a nonrecourse loan from a bank for $1,000. Under section 752, the loan is allocated $200 to A, $200 to B, and $600 to C. On February 1, 2019, Q purchases qualified opportunity zone business property for $2,000. On July 31, 2024, A sells 50 percent of its qualifying QOF partnership interest in Q to B for $400 cash. Prior to the sale, there were no inclusion events, distributions, partner changes, income or loss allocations, or changes in the amount or allocation of debt outstanding. At the time of the sale, the fair market value of Q's qualified opportunity zone business property is $5,000.

(ii) *Analysis.* Because A held its qualifying QOF partnership interest for at least five years, A's basis in its partnership interest at the time of the sale is $220 (the original zero basis with respect to the contribution, plus the $200 debt allocation, plus the 10% increase for interests held for five years). The sale of 50 percent of A's qualifying QOF partnership interest to B requires A to recognize $90 of gain, the lesser of $90, which is 50 percent of $180 (the $200 remaining deferred gain less the $20 five-year basis adjustment), or $390, which is the gain that would be recognized on a taxable sale of 50 percent of the interest. A also recognizes $300 of gain relating to the appreciation of its interest in Q.

(4) *Example 4. Sale of qualifying QOF partnership interest when value of the QOF partnership interest has decreased*—(i) *Facts.* The facts are the same as in paragraph (f)(3) of this section (*Example 3*), except that A sells 50 percent of its qualifying QOF partnership interest in Q to B for cash of $50, and at the time of the sale, the fair market value of Q's qualified opportunity zone business property is $1,500.

(ii) *Analysis.* Because A held its qualifying QOF partnership interest for at least five years, A's basis at the time of the sale is $220. Under section 1400Z–2(b)(2)(A), the sale of 50 percent of A's qualifying QOF partnership interest to B requires A to recognize $40 of gain, the lesser of $90 (50 percent of the excess of A's $200 remaining deferred gain over A's $20 five-year adjustment) or $40 (the gain that would be recognized by A on a sale of 50 percent of its QOF interest). A's remaining basis in its qualifying QOF partnership interest is $110.

(5) *Example 5. Amount includible on December 31, 2026*—(i) *Facts.* The facts are the same as in paragraph (f)(3) of this section (*Example 3*), except that no sale of QOF interests takes place in 2024. Prior to December 31, 2026, there were no inclusion events, distributions, partner changes, income or loss allocations, or changes in the amount or allocation of debt outstanding.

(ii) *Analysis.* For purposes of calculating the amount includible on December 31, 2026, each of A's basis and B's basis is increased by $30 to $230, and C's basis is increased by $90 to $690 because they held their qualifying QOF partnership interests for at least seven years. Each of A and B is required to recognize $170 of gain, and C is required to recognize $510 of gain.

(iii) *Sale of qualifying QOF partnership interests.* The facts are the same as in paragraph (f)(5)(i) of this section (this *Example 5*), except that, on March 2, 2030, C sells its entire qualifying QOF partnership interest in Q to an unrelated buyer for cash of $4,200. Assuming an election under section 1400Z–2(c) is made, the basis of C's Q interest is increased to its fair market value immediately before the sale by C. C is treated as purchasing the interest immediately before the sale and the bases of the partnership's assets are increased in the manner they would be if the partnership had an election under section 754 in effect.

(6) *Example 6. Mixed-funds investment*—(i) *Facts.* On January 1, 2019, A and B form Q, a QOF partnership. A contributes $200 to Q, $100 of which is in exchange for a qualifying investment, and B contributes $200 to Q in exchange for a qualifying investment. All the cash is used to purchase qualified opportunity zone property. Q has no liabilities. On March 30, 2023, when the values and bases of the qualifying investments remain unchanged, Q distributes $50 to A.

(ii) *Analysis.* Under paragraph (c)(6)(iv) of this section, A is a mixed-funds partner holding two separate interests, a qualifying investment and a non-qualifying investment. One half of the $50 distribution is treated under that provision as being made with respect to A's qualifying investment. For the $25 distribution made with respect to the qualifying investment, A is required to recognize $25 of gain.

(iii) *Basis adjustments.* Under paragraph (g)(1)(ii)(B) of this section, prior to determining the tax consequences of the distribution, A increases its basis in its qualifying QOF partnership interest by $25 under section 1400Z–2(b)(2)(B)(ii). The distribution of $25 results in no gain under section 731. After the distribution, A's basis in its qualifying QOF partnership interest is $0 ($25 − $25).

(7) *Example 7. Qualifying section 381 transaction of a QOF corporation*—(i) *Facts.* X wholly and directly owns Q, a QOF corporation. On May 31, 2019, X sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, X contributes $500 to Q in exchange for a qualifying investment. In 2020, Q merges with and into unrelated Y (with Y surviving) in a transaction that qualifies as a reorganization under section 368(a)(1)(A) (Merger). X does not receive any boot in the Merger with respect to its qualifying investment in Q. Immediately after the Merger, Y satisfies the requirements for QOF status under section 1400Z–2(d)(1) (see paragraph (c)(10)(i)(B) of this section).

(ii) *Analysis.* The Merger is not an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. See paragraph (c)(10)(i)(A) of this section. Accordingly, X is not required to include in income in 2020 its $500 of deferred capital gain as a result of the Merger. For purposes of section 1400Z–2(b)(2)(B) and (c), X's holding period for its investment in Y is treated as beginning on October 31, 2019. For purposes of section 1400Z–2(d), Y's holding period in its assets includes Q's holding period in its assets, and Q's qualified opportunity zone business property continues to qualify as such. See paragraph (d)(2) of this section.

(iii) *Merger of QOF shareholder.* The facts are the same as in paragraph (f)(7)(i) of this section (this *Example 7*), except that, in 2020, X (rather than Q) merges with and into Y in a section 381 transaction in which Y acquires all of X's qualifying investment in Q, and Y does not qualify as a QOF immediately after the merger. The merger transaction is not an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. See paragraph (c)(10)(ii) of this section.

(iv) *Receipt of boot.* The facts are the same as in paragraph (f)(7)(i) of this section (this *Example 7*), except that the value of X's qualifying investment immediately before the Merger is $1,000, X receives $100 of cash in addition to Y stock with a fair market value of $900 in the Merger in exchange for its qualifying investment, and neither Q nor Y has any earnings and profits. Under paragraph (c)(10)(i)(C) of this section, X is treated as disposing of 10 percent ($100/$1000) of its qualifying investment. Under paragraph (e)(1) of this section, X is required to include $50 ($500 × ($100/$1000)) of its deferred capital gain in income in 2020.

(8) *Example 8. Section 355 distribution by a QOF*—(i) *Facts.* A wholly and directly owns Q, a QOF corporation, which wholly and directly owns Y, a corporation that is a qualified opportunity zone business. On May 31, 2019, A sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, A contributes $500 to Q in exchange for a qualifying investment. On June 26, 2025, Q distributes all of the stock of Y to A in a transaction in which no gain or loss is recognized under section 355 (Distribution). Immediately after the Distribution, each of Q and Y satisfies the requirements for QOF status. (See paragraph (c)(11)(i)(B)(*2*) of this section.)

(ii) *Analysis.* Because each of Q, the distributing corporation, and Y, the controlled corporation, is a QOF immediately after the Distribution, the Distribution is a qualifying section 355 transaction. Thus, the Distribution is not an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. See paragraph (c)(11)(i)(B) of this section. Accordingly, A is not required to include in income in 2025 any of its $500 of deferred capital gain as a result of the Distribution. For purposes of section 1400Z–2(b)(2)(B) and (c), A's holding period for its qualifying investment in Y is treated as beginning on October 31, 2019. See paragraph (d)(1)(ii) of this section.

(iii) *Section 355 distribution by a QOF shareholder.* The facts are the same as in paragraph (f)(8)(i) of this section (this *Example 8*), except that A distributes 80 percent of the stock of Q, all of which is a qualifying investment in the hands of A, to A's shareholders in a transaction in which no

gain or loss is recognized under section 355. At the time of the distribution, the fair market value of A's Q stock exceeds $500. The distribution is an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section, and A is required to include in income $400 (80 percent of its $500 of deferred capital gain) as a result of the distribution. See paragraphs (c)(1) and (c)(11)(ii) of this section.

(iv) *Distribution of boot.* The facts are the same as in paragraph (f)(8)(i) of this section (this *Example 8*), except that A receives boot in the Distribution. Under paragraphs (c)(8)(i) and (c)(11)(i)(B)(*3*) of this section, the receipt of boot in the Distribution is an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section to the extent of gain recognized pursuant to section 301(c)(3).

(v) *Section 355 split-off.* The facts are the same as in paragraph (f)(8)(i) of this section (this *Example 8*), except that Q stock is directly owned by both A and B (each of which has made a qualifying investment in Q), and Q distributes all of the Y stock to B in exchange for B's Q stock in a transaction in which no gain or loss is recognized under section 355. The distribution is a qualifying section 355 transaction and is not an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. Neither A nor B is required to include its deferred capital gain in income in 2025 as a result of the distribution.

(vi) *Section 355 split-up.* The facts are the same as in paragraph (f)(8)(v) of this section (this *Example 8*), except that Q wholly and directly owns both Y and Z; Q distributes all of the Y stock to A in exchange for A's Q stock and distributes all of the Z stock to B in exchange for B's Q stock in a transaction in which no gain or loss is recognized under section 355; Q then liquidates; and immediately after the Distribution, each of Y and Z satisfies the requirements for QOF status. The distribution is a qualifying section 355 transaction and is not an inclusion event for purposes of section 1400Z–2(b)(1) and paragraph (b) of this section. Neither A nor B is required to include its deferred capital gain in income in 2025 as a result of the transaction.

(vii) *Section 355 split-off with boot.* The facts are the same as in paragraph (f)(8)(v) of this section (this *Example 8*), except that B also receives boot. Under paragraph (c)(11)(i)(B)(*3*) of this section, B has an inclusion event and is treated as disposing of a portion of its qualifying investment that bears the same proportion to B's total qualifying investment immediately before the inclusion event as the fair market value of the boot bears to the fair market value of the total consideration received by B.

(9) *Example 9. Recapitalization*—(i) *Facts.* On May 31, 2019, each of A and B sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, A contributes $500 to newly formed Q in exchange for 50 shares of class A stock of Q (A's qualifying investment) and B contributes $500 to Q in exchange for 60 shares of class B stock of Q (B's qualifying investment). A and B are the sole shareholders of Q. In 2020, B exchanges all of its class B stock of Q for 40 shares of class A stock of Q as well as other property in a transaction that qualifies as a reorganization under section 368(a)(1)(E).

(ii) *Analysis.* Because A did not receive any boot in the transaction, A does not have an inclusion event with respect to its qualifying investment in Q. See paragraph (c)(12)(i) of this section. Therefore, A is not required to include any of its deferred gain in income as a result of this transaction. However, under paragraph (c)(12)(ii) of this section, B has an inclusion event. If section 301 applies to the boot received by B, B has an inclusion event to the extent of its section 301(c)(3) gain. If section 356(a) or (c) applies to the boot received by B, B is treated as disposing of a portion of its qualifying investment that bears the same proportion to B's total qualifying investment immediately before the inclusion event as the fair market value of the boot bears to the fair market value of the total consideration received by B.

(10) *Example 10. Debt financed distribution*—(i) *Facts.* On September 24, 2019, A and B form Q, a QOF partnership, each contributing $200 that is deferred under the section 1400Z–2(a) election to Q in exchange for a qualifying investment. On November 18, 2022, Q obtains a nonrecourse loan from a bank for $300. Under section 752, the loan is allocated $150 to A and $150 to B. On November 30, 2022, when the values and bases of the investments remain unchanged, Q distributes $50 to A.

(ii) *Analysis.* A is not required to recognize gain under paragraph (c) of this section because A's basis in its qualifying investment is $150 (the original zero basis with respect to the contribution, plus the $150 debt allocation). The distribution reduces A's basis to $100.

(11) *Example 11. Debt financed distribution in excess of basis*—(i) *Facts.* The facts are the same as in paragraph (f)(10) of this section (*Example 10*), except that the loan is entirely allocated to B under section 752. On November 30, 2024, when the values of the investments remain unchanged, Q distributes $50 to A.

(ii) *Analysis.* Under paragraph (c)(6)(iii) of this section, A is required to recognize $30 of eligible gain under paragraph (c) of this section because the $50 distributed to A exceeds A's $20 basis in its qualifying investment (the original zero basis with respect to its contribution, plus $20 with regard to section 1400Z–2(b)(2)(B)(iii)).

(g) *Basis adjustments*—(1) *Basis adjustments under section 1400Z–2(b)(2)(B)(ii) resulting from the inclusion of deferred gain*—(i) *In general.* Except as provided in paragraph (g)(1)(ii) of this section, basis adjustments under section 1400Z–2(b)(2)(B)(ii) are made immediately after the amount of gain determined under section 1400Z–2(b)(2)(A) is included in income under section 1400Z–2(b)(1). If the basis adjustment under section 1400Z–2(b)(2)(B)(ii) is being made as a result of an inclusion event, then the basis adjustment is made before determining the other Federal income tax consequences of the inclusion event.

(ii) *Specific application to section 301(c)(3) gain, section 1059(a)(2) gain, S corporation shareholder gain, or partner gain*—(A) *Applicability.* This paragraph (g)(1)(ii) applies if a QOF makes a distribution to its owner, and if, without regard to any basis adjustment under section 1400Z–2(b)(2)(B)(ii), at least a portion of the distribution would be characterized as gain under section 301(c)(3), section 1059(a)(2), or paragraphs (c)(6)(iii) and (c)(7)(ii) of this section with respect to the owner's qualifying investment in the QOF.

(B) *Ordering rule.* If paragraph (g)(1)(ii) of this section applies, an eligible taxpayer is treated as having an inclusion event to the extent provided in paragraph (c)(6)(iii), (c)(7)(ii), or (c)(8), (9), (11), (12), or (13) of this section, as applicable. Then, the eligible taxpayer increases its basis under section 1400Z–2(b)(2)(B)(ii) before determining the Federal income tax consequences of the distribution.

(iii) *Shares in QOF C corporations to which section 1400Z–2(b)(2)(B)(ii) adjustments are made.* If a shareholder of a QOF C corporation disposes of qualifying QOF stock in an exchange subject to section 1001, basis adjustments under section 1400Z–2(b)(2)(B)(ii) are made only to the portion of the qualifying investment that is disposed of in the inclusion event.

(2) *Amount of basis adjustment under section 1400Z–2(b)(2)(B)(iii) and (iv).* The increases in basis under section 1400Z–2(b)(2)(B)(iii) and (iv) are limited to 10 percent and 5 percent, respectively, of the remaining deferred gain with respect to a qualifying investment as of the dates on which basis is increased under that section.

(3) *Examples.* The following examples illustrate the rules of paragraphs (g)(1) and (2) of this section.

(i) *Example 1*—(A) *Facts.* On May 31, 2019, A, a C corporation, sells a capital asset to an unrelated party and realizes $500 of capital gain. On October 31, 2019, A contributes $500 to Q, a newly formed QOF C corporation, in exchange for all of the outstanding Q common stock and elects to defer the recognition of $500 of capital gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. In 2020, when Q has $40 of earnings and profits, Q distributes $100 to A (Distribution).

(B) *Recognition of gain.* Under paragraph (g)(1)(ii)(B) of this section, the Distribution is first evaluated without regard to any basis adjustment under section 1400Z–2(b)(2)(B)(ii). Of the $100 distribution, $40 is treated as a dividend and $60 is treated as gain from the sale or exchange of property under section 301(c)(3), because A's basis in its Q stock is $0 under section 1400Z–2(b)(2)(B)(i). Under paragraphs (c)(8)(i) and

(e)(2) of this section, $60 of A's gain that was deferred under section 1400Z–2(a) and § 1.1400Z2(a)–1 is recognized in 2020. Pursuant to § 1.312–6(b), A's earnings and profits increase by $60.

(C) *Basis adjustments.* Under paragraph (g)(1)(ii)(B) of this section, prior to determining the further tax consequences of the Distribution, A increases its basis in its Q stock by $60 in accordance with section 1400Z–2(b)(2)(B)(ii). As a result, the Distribution is characterized as a dividend of $40 under section 301(c)(1) and a return of basis of $60 under section 301(c)(2). Therefore, after the section 301 distribution, A's basis in Q is $0 ($60 − $60).

(ii) *Example 2*—(A) *Facts.* The facts are the same as in paragraph (g)(3)(i) of this section (*Example 1*), except that, instead of receiving a distribution, A sells half of the Q stock for $250 in 2020. A continues to hold the remainder of its Q stock through 2024.

(B) *Recognition of gain and basis adjustments in 2020.* Under paragraphs (c)(1) and (e)(1) of this section, $250 of A's gain that was deferred under section 1400Z–2(a) and § 1.1400Z2(a)–1 is recognized in 2020. Under paragraphs (g)(1)(i) and (iii) of this section, A increases its basis to $250 in the sold shares in accordance with section 1400Z–2(b)(2)(B)(ii) immediately before the sale. Accordingly, A has no gain or loss on the sale ($250 − $250). Pursuant to § 1.312–6(b), A's earnings and profits increase by $250. A's basis in its remaining shares of Q stock remains $0.

(C) *Basis adjustment in 2024.* Under paragraph (g)(2) of this section, A increases its basis in its remaining shares of Q stock in accordance with section 1400Z–2(b)(2)(B)(iii). Pursuant to § 1.312–6(b), A's earnings and profits are increased by the amount of the basis adjustment.

(4) *Special partnership rules*—(i) *General rule.* The initial basis under section 1400Z–2(b)(2)(B)(i) of a qualifying investment in a QOF partnership is zero, as adjusted to take into account the contributing partner's share of partnership debt under section 752.

(ii) *Treatment of basis adjustments.* Any basis adjustment to a qualifying investment in a QOF partnership described in section 1400Z–2(b)(2)(B)(iii) and (iv) and section 1400Z–2(c) is basis for all purposes, including for purposes of suspended losses under section 704(d).

(iii) *Tiered arrangements.* Any basis adjustment described in section 1400Z–2(b)(2)(B)(iii) and (iv) and section 1400Z–2(c) (basis adjustment rules) will be treated as an item of income described in section 705(a)(1) and must be reported in accordance with the applicable forms and instructions. Any amount to which the basis adjustment rules or to which section 1400Z–2(b)(1) applies will be allocated to the owners of the QOF, and to the owners of any partnership that directly or indirectly (solely through one or more partnerships) owns the eligible interest, and will track to the owners' interests, based on their shares of the remaining deferred gain to which such amounts relate.

(5) *Basis adjustments in S corporation stock*—(i) *Treatment of basis adjustments.* Any basis adjustment to a qualifying investment in a QOF S corporation described in section 1400Z–2(b)(2)(B)(iii) and (iv) and section 1400Z–2(c) is basis for all purposes, including for purposes of suspended losses under section 1366(d).

(ii) *S corporation investor in QOF*—(A) *S corporation.* If an S corporation is an investor in a QOF, the S corporation must adjust the basis of its qualifying investment as set forth in this paragraph (g). The rule in this paragraph (g)(5)(ii)(A) does not affect adjustments to the basis of any other asset of the S corporation.

(B) *S corporation shareholder*—(*1*) *In general.* The S corporation shareholder's pro-rata share of any recognized capital gain that has been deferred at the S corporation level will be separately stated under section 1366 when recognized and will adjust the shareholders' stock bases under section 1367 at that time.

(*2*) *Basis adjustments to qualifying investments.* Any adjustment made to the basis of an S corporation's qualifying investment under section 1400Z–2(b)(2)(B)(iii) or (iv), or section 1400Z–2(c), will not:

(*i*) Be separately stated under section 1366; or

(*ii*) Until the date on which an inclusion event with respect to the S corporation's qualifying investment occurs, adjust the shareholders' stock bases under section 1367.

(*3*) *Basis adjustments resulting from inclusion events.* If the basis adjustment under section 1400Z–2(b)(2)(B)(ii) is being made as a result of an inclusion event, then the basis adjustment is made before determining the tax consequences of the inclusion event other than the computation of the tax on the deferred gain.

(iii) *QOF S corporation*—(A) *Transferred basis of assets received.* If a QOF S corporation receives an asset in exchange for a qualifying investment, the basis of the asset shall be the same as it would be in the hands of the transferor, increased by the amount of the gain recognized by the transferor on such transfer.

(B) *Basis adjustments resulting from inclusion events.* If the basis adjustment under section 1400Z–2(b)(2)(B)(ii) for the shareholder of the QOF S corporation is being made as a result of an inclusion event, then the basis adjustment is made before determining the tax consequences of the inclusion event other than the computation of the tax on the deferred gain.

(6) *Basis in the hands of a taxpayer who received a qualifying investment in a QOF by reason of the prior owner's death*—(i) *In general.* The basis of a qualifying investment in a QOF, transferred by reason of a decedent's death in a transfer that is not an inclusion event, is zero under section 1400Z–2(b)(2)(B)(i), as adjusted for increases in basis as provided under section 1400Z–2(b)(2)(B)(ii) through (iv) and (c). See paragraph (c)(4) of this section.

(ii) *Examples.* The following examples illustrate the rule of this paragraph (g)(6).

(A) *Example 1.* Taxpayer A, an individual, contributed $50X to a QOF in exchange for a qualifying investment in the QOF in January 2019. This $50X was capital gain that was excluded from A's gross income under section 1400Z–2(a)(1)(A). A's basis in the qualifying investment is zero. As of January 2024, A's basis in the QOF is increased by an amount equal to 10 percent of the amount of gain deferred by reason of section 1400Z–2(a)(1)(A), so that A's adjusted basis in 2024 is $5X. A dies in 2025 and A's heir inherits this qualifying investment in the QOF. A's death is not an inclusion event for purposes of section 1400Z–2. The heir's basis in the qualifying investment is $5X.

(B) *Example 2.* The facts are the same as in paragraph (g)(6)(ii)(A) of this section (*Example 1*), except that A dies in November 2027, when the fair market value of the qualifying investment was $75X. A was required to pay the tax on the excess of the deferred capital gain over A's basis as part of A's 2026 income. Therefore, at the time of A's death, A's basis in the qualifying investment is the sum of three basis adjustments: The adjustment made in January 2024 described in paragraph (g)(6)(ii)(A) (*Example 1*) ($5X); an additional adjustment made as of January 2026 equal to 5 percent of the amount of gain deferred by reason of section 1400Z–2(a)(1)(A) ($2.5X); and the adjustment as of December 31, 2026, by reason of section 1400Z–2(b)(1)(B) and (b)(2)(B)(ii) ($42.5X). Accordingly, the basis of the qualifying investment in the hands of A's heir is $50X.

(h) *Notifications by partners and partnerships, and shareholders and S corporations*—(1) *Notification of deferral election.* A partnership that makes a deferral election must notify all of its partners of the deferral election and state each partner's distributive share of the deferred gain in accordance with applicable forms and instructions.

(2) *Notification of deferred gain recognition by indirect QOF owner.* If an indirect owner of a QOF partnership sells or otherwise disposes of all or a portion of its indirect interest in the QOF partnership in a transaction that is an inclusion event under paragraph (c)

of this section, such indirect owner must provide to the QOF owner notification and information sufficient to enable the QOF owner, in a timely manner, to recognize an appropriate amount of deferred gain.

(3) *Notification of section 1400Z–2(c) election.* A QOF partner or QOF S corporation shareholder must notify the QOF partnership or QOF S corporation, as appropriate, of an election under section 1400Z–2(c) to adjust the basis of the qualifying QOF partnership interest or qualifying QOF stock, as appropriate, that is disposed of in a taxable transaction. Notification of the section 1400Z–2(c) election, and the adjustments to the basis of the qualifying QOF partnership interest(s) or qualifying QOF stock disposed of, or to the QOF partnership asset(s) or QOF S corporation asset(s) disposed of, as appropriate, is to be made in accordance with applicable forms and instructions.

(i) [Reserved]

(j) *Applicability dates*—(1) *In general.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a taxpayer's first taxable year ending after December 21, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, a taxpayer may choose either—

(i) To apply section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(b)–1 contained in the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

■ **Par. 5.** Section 1.1400Z2(c)–1 is added to read as follows:

§ 1.1400Z2(c)–1 Investments held for at least 10 years.

(a) *Scope.* This section provides rules under section 1400Z–2(c) of the Internal Revenue Code regarding the election to adjust the basis in a qualifying investment in a QOF or in certain eligible property held by the QOF. See § 1.1400Z2(b)–1(d) for rules for determining the holding period of a qualifying investment for purposes of this section.

(b) *Investment for which an election can be made*—(1) *In general*—(i) *Election by taxpayer.* An eligible taxpayer who makes a deferral election with respect to, or acquires by reason of a transaction that is not an inclusion event, a qualifying investment in a QOF, recognizes gain (if any) on December 31, 2026, of an amount determined under § 1.1400Z2(b)–1(e)(3) (and so much of § 1.1400Z2(b)–1(e)(4) as relates to § 1.1400Z2(b)–1(e)(3)) with respect to that qualifying investment, and whose holding period in that qualifying investment is at least ten years, is eligible to make an election described in section 1400Z–2(c) on the sale or exchange of that qualifying investment. Except as otherwise provided in this paragraph (b)(1), to the extent a taxpayer described in the preceding sentence has an inclusion event described in § 1.1400Z2(b)–1(c) with respect to any portion of a qualifying investment, that portion is no longer a qualifying investment and the taxpayer is not eligible to make an election pursuant to section 1400Z–2(c) and this section with respect to that portion. See § 1.1400Z2(c)–1(b)(2) for special election rules for QOF partnerships and QOF S corporations.

(ii) *Transferee partnership to make an election under section 1400Z–2(c)*—(A) *In general.* This paragraph (b)(1)(ii)(A) applies if an eligible taxpayer (transferor) transfers its qualifying investment to a transferee in a transaction described in § 1.1400Z2(b)–1(c)(6)(ii) to the extent governed by section 721(a). If this paragraph (b)(1)(ii)(A) applies, and if the transferee sells or exchanges a qualifying investment that has a holding period of at least 10 years under § 1.1400Z2(b)–1(d)(1)(ii)(F), then the transferee can make an election described in section 1400Z–2(c) on the sale or exchange of the qualifying investment. See § 1.1400Z2(b)–1(c)(6)(ii)(B) (transferee partnership makes section 1400Z–2(c) election regarding contributed qualifying investment).

(B) *Conditions for transferee partnership or merged partnership to make an election described in section 1400Z–2(c).* A transferee referred to in paragraph (b)(1)(ii)(A) of this section is eligible to make an election described in section 1400Z–2(c) with respect to a qualifying investment only if the transferee:

(*1*) Files a statement, at the time and in the manner that the Commissioner of Internal Revenue may prescribe by Internal Revenue Service forms and instructions or by publication in the Internal Revenue Bulletin (see § 601.601(d)(ii)(b) of this chapter), providing the name of the transferor, the date of the transfer, and the transferor's holding period in the transferred qualifying investment immediately before the transfer; and

(*2*) Files form 8997, *Initial and Annual Statement of Qualified Opportunity Fund (QOF) Investments,* with the transferee's timely filed Federal Tax Return.

(iii) *Limitation on the 10-year rule.* As required by section 1400Z–2(e)(1) (treatment of investments with mixed funds), section 1400Z–2(c) applies only to the portion of an investment in a QOF that is a qualifying investment. For rules governing the application of section 1400Z–2(c) to the portion of an investment in a QOF for which a loss has been claimed under section 165(g) or otherwise, see § 1.1400Z2(b)–1(c)(14).

(iv) *Transactions to which section 301(c)(3), section 1059(a)(2), or section 1368(b)(2) or (c)(3) applies.* The receipt of amounts treated as gain from the sale or exchange of property under section 301(c)(3), section 1059(a)(2), or section 1368(b)(2) or (c)(3) with respect to qualifying QOF stock in a transaction treated as an inclusion event under § 1.1400Z2(b)–1(c) does not prevent the QOF shareholder from making a subsequent election described in section 1400Z–2(c) with respect to that qualifying QOF stock.

(v) *Partnership distributions in excess of basis.* The occurrence of an inclusion event described in § 1.1400Z2(b)–1(c)(6)(iii), which addresses a distribution of property by a QOF partnership to a QOF partner where the distributed property has a fair market value in excess of the QOF partner's basis in its qualifying investment, does not prevent the QOF partner from making a subsequent election described in section 1400Z–2(c) with respect to the QOF partner's qualifying QOF partnership interest.

(2) *Special election rules for QOF partnerships and QOF S corporations*—(i) *Dispositions of qualifying QOF partnership interests.* If a QOF partner's basis in a qualifying QOF partnership interest is adjusted under section 1400Z–2(c) upon the disposition of a qualifying investment, then the basis of the QOF partnership interest is adjusted to an amount equal to the net fair market value of the interest, plus the QOF partner's share of QOF partnership indebtedness under section 752 with respect to that interest, and immediately prior to the sale or exchange, the bases of the assets of the QOF partnership and of any partnership owned directly or indirectly by the QOF partnership solely through one or more partnerships are also adjusted with respect to the disposed-of qualifying investment. For purposes of this paragraph (b)(2)(i), section 7701(g) will apply in determining the value of a qualifying investment in a QOF partnership. The adjustments in this paragraph (b)(2)(i) are calculated in a manner similar to the section 743(b) adjustments that would

have been made if the transferor QOF partner had purchased its interest in the QOF partnership for cash equal to the fair market value of the interest immediately prior to the sale or exchange, assuming that valid section 754 elections had been in place with respect to the QOF partnership and any partnerships directly or indirectly owned by the QOF partnership, whether or not an actual section 754 election is in place for any of the partnerships. This paragraph (b)(2)(i) applies without regard to the amount of deferred gain that was included under section 1400Z–2(b)(1) or the timing of that inclusion.

(ii) *Sales or exchanges of QOF property by QOF partnerships or QOF S corporations*—(A) *Election to exclude gains and losses.* If a taxpayer has held a qualifying investment in a QOF partnership or QOF S corporation for at least 10 years, as determined under § 1.1400Z2(b)–1(d), and the QOF partnership or QOF S corporation or any partnership that is owned directly, or indirectly solely through one of more partnerships, by the QOF partnership or QOF S corporation sells or exchanges property, the taxpayer may make an election under this paragraph (b)(2)(ii)(A) to exclude from the taxpayer's income all gains and losses allocable to the qualifying investment that arise from all such sales or exchanges for the QOF partnership's or QOF S corporation's taxable year. In order for the election to be valid, the requirements set forth in paragraph (b)(2)(ii)(B) of this section must be satisfied. For purposes of paragraph (b)(2)(ii) of this section, gains and losses include all gains and losses other than gains or losses from the sale or exchange of any item of inventory, as defined in section 1221(a)(1), in the ordinary course of business.

(B) *Deemed distribution and recontribution*—(*1*) *In general.* If any partner of a QOF partnership, or shareholder of a QOF S corporation, makes an election under paragraph (b)(2)(ii)(A) of this section, the taxpayer is treated as receiving a distribution of cash as calculated under paragraph (b)(2)(ii)(B)(*2*) of this section, from the QOF partnership or QOF S corporation at the end of the QOF partnership's or QOF S corporation's taxable year and immediately recontributing the cash to the QOF partnership or QOF S corporation in exchange for a non-qualifying investment in the QOF partnership or QOF S corporation. In determining the post-contribution qualifying investment and non-qualifying investment, the QOF will value each interest based on the underlying values of the QOF's assets determined at the end of its taxable year in accordance with the principles of § 1.704–1(b)(2)(iv) (in the case of a QOF partnership) or fair market value (in the case of a QOF S corporation). If the QOF partner or QOF S corporation shareholder is a mixed-funds partner or shareholder prior to the sale or exchange, the deemed distribution will be treated as made proportionately with respect to the partner's or shareholder's qualifying investment and non-qualifying investment in the QOF partnership in accordance with § 1400Z2(b)–1(c)(6)(iv)(B), or the QOF S corporation. The distribution and recontribution rule of paragraph (b)(2)(ii)(B) of this section is solely for purposes of determining the taxpayer's interests in the QOF partnership or QOF S corporation that constitute a qualifying investment and a non-qualifying investment, and has no other Federal income tax consequence (for example, the rule does not affect the accumulated adjustments account of an S corporation and cannot be treated as a disproportionate distribution by an S corporation).

(*2*) *Amount of deemed distribution and re-contribution.* The amount of cash referred to in paragraph (b)(2)(ii)(B)(*1*) of this section that is deemed distributed by and recontributed to the QOF partnership or QOF S corporation is equal to—

(*i*) The partner's or shareholder's share of net proceeds from all sales and exchanges of property described in paragraph (b)(2)(ii)(A) of this section (other than sales of inventory in the ordinary course of business) for the taxable year for which the election under paragraph (b)(2)(ii)(A) is made (calculated without regard to whether any gain or loss is recognized with regard to such property); less

(*ii*) All actual distributions of cash by the QOF partnership or QOF S corporation with respect to any such sale or exchange that is made within 90 days of the sale or exchange.

(*3*) *Meaning of net proceeds*—(*i*) *QOF partnerships.* For purposes of paragraph (b)(2)(ii)(B)(*2*)(*i*) of this section, with respect to QOF partnerships, the term ''net proceeds'' means the amount realized from the sale of property described in paragraph (b)(2)(ii)(A) of this section less any indebtedness included in the amount realized that would constitute a qualified liability under § 1.707–5(a)(6) if the sold or exchanged property had been contributed to a lower-tier partnership subject to the debt.

(*ii*) *QOF S corporations.* For purposes of paragraph (b)(2)(ii)(B)(*2*)(*i*) of this section, with respect to QOF S corporations, the term ''net proceeds'' means the amount realized from the sale of property described in paragraph (b)(2)(ii)(A) of this section less any indebtedness included in the amount realized that would constitute a qualified liability under the principles of § 1.707–5(a)(6).

(C) *Treatment as exempt income*—(*1*) *General rule.* With respect to the taxpayer making an election under paragraph (b)(2)(ii) of this section, the excess of any gains over losses excluded from income under paragraph (b)(2)(ii) of this section is treated as income of the partnership or S corporation that is exempt from tax under the Internal Revenue Code for purposes of section 705(a)(1)(B) or section 1367(a)(1)(A). Section 265 or any similar provisions do not apply to disallow any deductions otherwise allowable under subtitle A for amounts paid or incurred by a taxpayer that are allocable to any gain excluded from income under paragraph (b)(2)(ii) of this section.

(*2*) *Special rule regarding accumulated adjustments account.* Solely for purposes of determining whether an adjustment must be made to the accumulated adjustments account of an S corporation, the excess amount described in paragraph (b)(2)(ii)(C)(*1*) of this section is not treated as tax exempt income.

(D) *Time and manner of making the election to exclude gain.* An election under paragraph (b)(2)(ii)(A) of this section is made by filing the applicable form with the taxpayer's timely filed income tax return, without extensions, for its taxable year that includes the taxable year end of the QOF partnership or QOF S corporation. A taxpayer must make the election under paragraph (b)(2)(ii)(A) of this section for each taxable year in which it wishes to exclude gains and losses of a QOF partnership or QOF S corporation.

(3) *Basis adjustments upon sale or exchange of qualifying QOF stock*—(i) *In general.* Except as provided in paragraph (b)(3)(ii) of this section, if a QOF shareholder's basis in qualifying QOF stock is adjusted under section 1400Z–2(c), then the basis of the qualifying QOF stock is adjusted to an amount equal to the fair market value of the qualifying QOF stock immediately prior to the sale or exchange. This paragraph (b)(3)(i) applies without regard to the amount of deferred gain that was included under section 1400Z–2(b)(1) or the timing of that inclusion.

(ii) *Specific application to transactions to which section 301(c)(3), section 1059(a)(2), or section 1368(b)(2) or (c)(3) applies*—(A) *Applicability.* This paragraph (b)(3)(ii) applies if a QOF

corporation makes a distribution to a QOF shareholder, at least a portion of the distribution would be characterized as gain from a sale or exchange under section 301(c)(3), section 1059(a)(2), or section 1368(b)(2) or (c)(3) with respect to the QOF shareholder's qualifying QOF stock without regard to any basis adjustment under section 1400Z–2(c), and the QOF shareholder elects to adjust the basis of its qualifying QOF stock under section 1400Z–2(c).

(B) *Ordering rule.* If paragraph (b)(3)(ii) of this section applies with respect to a QOF corporation, the QOF shareholder increases its basis by the lesser of the amount of the distribution characterized as gain from a sale or exchange or the fair market value of the QOF shareholder's qualifying QOF stock before determining the Federal income tax consequences of the distribution.

(c) *Extension of availability of the election described in section 1400Z–2(c).* The ability to make an election under section 1400Z–2(c) for investments held for at least 10 years is not impaired solely because, under section 1400Z–1(f), the designation of one or more qualified opportunity zones ceases to be in effect. The preceding sentence does not apply to elections under section 1400Z–2(c) that are related to dispositions occurring after December 31, 2047.

(d) *Examples.* The following examples illustrate the principles of paragraphs (a) through (c) of this section.

(1) *Example 1*—(i) *Facts.* In 2020, taxpayer A invests $100 in QOF S, a QOF S corporation, in exchange for a qualifying investment and defers $100 of gain. At the end of 2028, the qualified opportunity zone designation expires for the population census tract in which QOF S primarily conducts its trade or business. In 2031, A sells all of its QOF S shares, realizes gain, and makes an election to increase the qualifying basis in its QOF S shares to fair market value. But for the expiration of the designated zones in section 1400Z–1(f), QOF S and A's conduct is consistent with continued eligibility to make the election under section 1400Z–2(c).

(ii) *Analysis.* Under paragraph (c) of this section, although the designation expired on December 31, 2028, the expiration of the zone's designation does not, without more, invalidate A's ability to make an election under section 1400Z–2(c). Accordingly, pursuant to that election, A's basis in the QOF stock is increased to its fair market value and A recognizes no gain or loss on the sale.

(2) *Example 2*—(i) *Facts.* In 2019, taxpayer A realizes $100 of eligible gain and contributes $100 to a QOF partnership, X, in exchange for a qualifying QOF partnership interest in X, and taxpayer B contributes $100 of eligible gain to another QOF partnership, Y, in exchange for a qualifying QOF partnership interest in Y. In 2021, in transactions governed by section 721(a), A contributes her qualifying QOF partnership interest in X, and B contributes her qualifying QOF partnership interest in Y, to a newly formed partnership, UTP. In 2024, C receives a profits interest in UTP for services that she will provide to UTP. In 2031, X sells a non-inventory asset and allocates X's distributive share of the gain to UTP. No distributions are ever made from X, Y, or UTP.

(ii) *Analysis.* On December 31, 2026, UTP recognizes $170 of remaining deferred gain relating to the QOF interests. Of that gain, A is allocated the $85 of gain relating to the $100 of eligible gain that she invested in X, and B is allocated the $85 of gain relating to the $100 of eligible gain that she invested in Y. C recognizes no gain at this time. In 2031, because UTP's holding period in X includes A's holding period in X, UTP has a holding period in X that exceeds 10 years, and may make an election under § 1.1400Z2(c)–1(b)(2)(ii)(A) to exclude the gain from X's asset sale. Even though A was the original investor in X, she may not make the election. If UTP makes the election, UTP will exclude its distributive share of gain from the sale of the X asset.

(3) *Example 3*—(i) *Facts.* In 2019, taxpayer B invests $100 in P, a QOF partnership, in exchange for a qualifying investment and properly makes an election under section 1400Z–2(a) to defer $100 of eligible gain. B's interest in the partnership is 50 percent. In 2030, when B's interest in P has a value of $130 and a basis of $100, B sells the interest, recognizing $30 of gain, $15 of which is attributable to inventory assets of P. B makes an election under section 1400Z–2(c) with respect to the sale.

(ii) *Analysis.* Because B's election under section 1400Z–2(c) is in effect with respect to the sale, the bases of B's interest in P and of P's assets with respect to the interest sold are adjusted to fair market value immediately before B's sale under paragraph (b)(2)(i) of this section, and B recognizes no gain or loss on the sale.

(4) *Example 4*—(i) *Facts.* The facts are the same as in paragraph (d)(3) of this section (*Example 3*), except that P sells qualified opportunity zone property that is not inventory sold in the ordinary course of business and distributes all of the proceeds from the sale to partners within 90 days of the sale (the qualified opportunity zone property was the only property sold by P in the taxable year). The sold property has a value of $60 and a basis of $40. P recognizes $20 of gain, $10 of which is allocable to B, and B makes an election under paragraph (b)(2)(ii)(A) of this section for the year in which B's allocable share of the partnership's recognized gain would be included in B's gross income.

(ii) *Analysis.* Because B's election under paragraph (b)(2)(ii)(A) of this section is in effect, B will exclude its entire $10 allocable share of the partnership's $20 of recognized gain. Because $10 of the sale proceeds were actually distributed to B within 90 days of the sale, P is not treated as making a deemed distribution and receiving a recontribution under paragraph (b)(2)(ii)(B) of this section with respect to B.

(5) *Example 5*—(i) *Facts.* In 2019, taxpayer C invests $100 in Q, a QOF partnership, in exchange for a qualifying investment and properly makes an election under section 1400Z–2(a) to defer $100 of eligible gain. C's interest in Q is 50%. Q's taxable year ends on December 31. In 2025, Q purchases three qualified opportunity zone properties, X, Y, and Z. On January 22, 2031, Q sells property X for $200, recognizing $140 of gain. On July 31, 2031, Q sells property Y for $80, recognizing $20 of loss. Q makes no distributions to its partners in 2031, has no indebtedness, and has no other gain or loss other than from the sales of properties X and Y. Property Z has a value of $280 at all times throughout 2031. C's share of Q's gain and loss is $70 and $10, respectively, for a net gain of $60, and C makes an election under paragraph (b)(2)(ii)(A) of this section to exclude the gains and losses from its income.

(ii) *Analysis.* Because C has made an election under paragraph (b)(2)(ii)(A) of this section, under paragraph (b)(2)(ii)(B) of this section, C is treated as receiving a cash distribution of $140 from Q, C's share of the net proceeds from the sales of properties X and Y, on December 31, 2031, and immediately recontributing $140 to Q in exchange for a non-qualifying investment in Q. Beginning on January 1, 2032, 50 percent of A's interest in Q is a qualifying investment, and 50 percent of A's investment in Q is a non-qualifying investment. This amount is calculated as a fraction, the numerator of which is $140, the amount deemed distributed and recontributed, and the denominator of which is $280, the value of C's interest prior to the deemed distribution.

(6) *Example 6*—(i) *Facts.* The facts are the same as in paragraph (d)(5) of this section (*Example 5*), except that Q distributes all of the proceeds from the sale of property X to its partners on March 30, 2031. Q does not make any distribution of proceeds from the sale of property Y.

(ii) *Analysis.* Under paragraph (b)(2)(iii)(B)(*2*)(*ii*) of this section, the actual distribution of cash to C on March 30, 2031, reduces the amount of the deemed distribution and recontribution with respect to C on December 31, 2031. Accordingly, the amount of C's deemed distribution and recontribution is $40, which increases C's non-qualifying investment to 22 percent. This amount is calculated as a fraction, the numerator of which is $40, the amount deemed distributed and recontributed, and the denominator of which is $180, the value of C's interest.

(7) *Example 7. Section 301(c)(3) gain*—(i) *Facts.* In 2020, taxpayer X makes an investment in Q, a QOF corporation, in exchange for a qualifying investment. In 2031, when X's qualifying Q stock is worth $1000x, Q makes a distribution to X with respect to X's qualifying QOF stock, $500x of which is treated as gain from a sale or exchange under section 301(c)(3). In 2032, X disposes of all of its qualifying QOF stock in Q.

(ii) *Analysis*—(A) *Section 301(c)(3) distribution.* X is eligible to make an election described in section 1400Z–2(c) in 2031 with respect to its $500x gain. Under paragraph (b)(3)(ii) of this section, the basis adjustment is $500x, the lesser of $500x, the amount of

the distribution treated as gain from the sale or exchange of property, and $1000x, the fair market value of the qualifying QOF stock before the distribution. As a result of the election, X increases its basis in its qualifying QOF stock in Q by $500x immediately before the distribution; consequently, the $500x is treated as a return of basis under section 301(c)(2).

(B) *Disposition of qualifying QOF stock.* X is eligible to make an election described in section 1400Z–2(c) in 2032 with respect to all of its qualifying QOF stock in Q, notwithstanding X's receipt of a section 301(c)(3) distribution in 2031. See paragraph (b)(1)(iv) of this section.

(e) *Capital gain dividends paid by a QOF RIC or QOF REIT that some shareholders may be able to elect to receive tax free under section 1400Z–2(c)*—(1) *Eligibility.* For purposes of paragraph (b) of this section, if a shareholder of a QOF RIC or QOF REIT receives a capital gain dividend identified with a date, as defined in paragraph (e)(2) of this section, then, to the extent that the shareholder's shares in the QOF RIC or QOF REIT paying the capital gain dividend are a qualifying investment in the QOF RIC or QOF REIT—

(i) The shareholder may treat the capital gain dividend, or part thereof, as gain from the sale or exchange of a qualifying investment on the date that the QOF RIC or QOF REIT identified with the dividend; and

(ii) If, on the date identified, the shareholder had held that qualifying investment in the QOF RIC or QOF REIT for at least 10 years, then the shareholder may exclude that capital gain dividend, or part thereof, from its taxable income for the taxable year.

(2) *Definition of capital gain dividend identified with a date.* A *capital gain dividend identified with a date* means an amount of a capital gain dividend, as defined in section 852(b)(3)(C) or 857(b)(3)(B), or part thereof, and a date that the QOF RIC reports or QOF REIT designates in a notice provided to the shareholder not later than one week after the QOF RIC reports or QOF REIT designates the capital gain dividend pursuant to section 852(b)(3)(C) or 857(b)(3)(B). The notice must be mailed to the shareholder unless the shareholder has provided the QOF RIC or QOF REIT with an email address to be used for this purpose. In the manner and at the time determined by the Commissioner, the QOF RIC or QOF REIT must provide the Commissioner all data that the Commissioner specifies with respect to the amounts of capital gain dividends and the dates reported or designated by the QOF RIC or QOF REIT for each shareholder.

(3) *General limitations on the amounts of capital gain with which a date may be identified*—(i) *No identification in the absence of any capital gains with respect to qualified opportunity zone property.* If, during its taxable year, the QOF RIC or QOF REIT did not recognize long-term capital gain on any sale or exchange of qualified opportunity zone property, then no date may be identified with any capital gain dividends, or parts thereof, with respect to that year.

(ii) *Proportionality.* Reportings and designations of capital gain dividends identified with a date must be proportional for all capital gain dividends paid with respect to the taxable year. See section 857(g)(2). Greater than *de minimis* violation of proportionality invalidates all of the purported identifications for a taxable year.

(iii) *Undistributed capital gains.* If section 852(b)(3)(D)(i) or 857(b)(3)(C)(i) requires a shareholder of a QOF RIC or QOF REIT to include a reported or designated amount in the shareholder's long-term capital gain for a taxable year, then inclusion of this amount in this manner is treated as receipt of a capital gain for purposes of this paragraph (e) and may be identified with a date.

(iv) *Gross gains.* The amount determined under paragraph (e)(4) of this section is determined without regard to any losses that may have been recognized on other sales or exchanges of qualified opportunity zone property. The losses do, however, limit the total amount of capital gain dividends that may be reported or designated under section 852(b)(3) or section 857(b)(3).

(4) *Determination of the amount of capital gain with which a date may be identified.* A QOF RIC or QOF REIT may choose to identify the date for an amount of capital gain in one of the following manners:

(i) *Simplified determination.* If, during its taxable year, the QOF RIC or QOF REIT recognizes long-term capital gain on one or more sales or exchanges of qualified opportunity zone property, then the QOF RIC or QOF REIT may identify the first day of that taxable year as the date identified with each reported or designated amount with respect to the capital gain dividends for that taxable year. A reported or designated identification is invalid in its entirety if the amount of gains that the QOF RIC or QOF REIT identifies with that date exceeds the aggregate long-term capital gains recognized on those sales or exchanges for that taxable year.

(ii) *Sale date determination*—(A) *In general.* If, during its taxable year, the QOF RIC or QOF REIT recognizes long-term capital gain on one or more sales or exchanges of qualified opportunity zone property, then the QOF RIC or QOF REIT may identify capital gain dividends, or a part thereof, with the latest date on which there was such a recognition. The amount of capital gain dividends so identified must not exceed the aggregate long-term capital gains recognized on that date from sales or exchanges of qualified opportunity zone property. A reported or designated identification is invalid in its entirety if the amount of gains that the QOF RIC or QOF REIT identifies with that date violates the preceding sentence.

(B) *Iterative application.* The process described in paragraph (e)(4)(ii)(A) of this section is applied iteratively to increasingly earlier transaction dates (from latest to earliest) until all capital gain dividends are identified with dates or there are no earlier dates in the taxable year on which the QOF RIC or QOF REIT recognized long-term capital gains with respect to a sale or exchange of qualified opportunity zone property, whichever comes first.

(f) *Applicability dates.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

■ **Par. 6.** Section 1.1400Z2(d)–1 is added to read as follows:

§ 1.1400Z2 (d)–1 Qualified opportunity funds and qualified opportunity zone businesses.

(a) *Overview.* This section provides rules that an eligible entity (as defined in paragraph (a)(1) of this section) must satisfy to be a qualified opportunity fund (QOF) or a qualified opportunity zone business. Paragraphs (a)(2) through (4) of this section provide rules that eligible entities must follow to be certified as QOFs, as well as rules for the de-certification of QOFs. Paragraph (b) of this section provides rules for determining whether the property held by a QOF satisfies the *90-percent investment standard* of section 1400Z–2(d)(1) or the property held by a qualified opportunity zone business satisfies the *70-percent tangible property standard* of section 1400Z–2(d)(3)(A)(i). Paragraph (c) of this section provides rules regarding qualified opportunity zone property that a QOF must hold to satisfy the 90-percent investment standard. Paragraph (d) of this section provides rules that an eligible entity must satisfy to be a qualified opportunity zone business that is owned, in whole or in part, by one or more QOFs. Paragraph (e) of this section provides applicability dates for this section. See § 1.1400Z2(d)–2 for rules that must be satisfied for tangible property of an eligible entity to be

treated as qualified opportunity zone business property.

(1) *Eligible entity*—(i) *In general.* Except as provided in paragraph (a)(1)(ii) of this section, the term *eligible entity* means an entity that is classified as a corporation or partnership for Federal income tax purposes. In order to be treated as a QOF, an eligible entity must self-certify on an annual basis that it satisfies the requirements of paragraphs (b) and (c) of this section, as appropriate. An eligible entity is a qualified opportunity zone business if it satisfies the requirements of paragraph (d) of this section.

(ii) *Exceptions based on where an entity is created, formed, or organized*—(A) *QOFs.* An entity classified as a corporation or partnership for Federal income tax purposes (an entity) but that is not organized under the law of the United States or the law of one of the 50 states, a government of a federally recognized tribe (Indian tribal government), the District of Columbia, or a U.S. territory, is not an eligible entity and is ineligible to be a QOF. An entity described in the preceding sentence is also ineligible to be a qualified opportunity zone business, and therefore an equity interest in the entity is neither qualified opportunity zone stock nor a qualified opportunity zone partnership interest for purposes of section 1400Z–2(d)(2).

(B) *Entities organized in a U.S. territory*—(*1*) *In general.* If an entity is organized in a U.S. territory but not in one of the 50 States or the District of Columbia, the entity may be a QOF only if the entity is organized for investing in qualified opportunity zone property that relates to a trade or business operated in the U.S. territory in which the entity is organized. If an entity is organized in a U.S. territory but not in one of the 50 States or the District of Columbia, an equity interest in the entity may be qualified opportunity zone stock or a qualified opportunity zone partnership interest, as the case may be, only if the entity conducts a qualified opportunity zone business in the U.S. territory in which the entity is organized. An entity described in the preceding sentence is treated as satisfying the requirement, as applicable, of being a domestic corporation for purposes of section 1400Z–2(d)(2)(B)(i) or of being a domestic partnership for purposes of section 1400Z–2(d)(2)(C).

(*2*) *U.S. territory defined.* For purposes of this paragraph (a)(1), the term *U.S. territory* means American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, the Commonwealth of Puerto Rico, the U.S. Virgin Islands, and any other territory not under the jurisdiction of one of the 50 States, an Indian tribal government, or the District of Columbia where a qualified opportunity zone has been designated under section 1400Z–1.

(iii) *Pre-existing entities.* There is no legal barrier to a pre-existing eligible entity qualifying as a QOF or a qualified opportunity zone business, but the pre-existing eligible entity must satisfy all of the applicable requirements of section 1400Z–2, this section, and § 1.1400Z2(d)–2.

(2) *Self-certification as a QOF.* The following rules apply to the required self-certification of an eligible entity as a QOF:

(i) *Time, form, and manner.* The self-certification must be timely-filed and effected annually in such form and manner as may be prescribed by the Commissioner of Internal Revenue (Commissioner) in the Internal Revenue Service (IRS) forms or instructions, or in publications or guidance published in the Internal Revenue Bulletin (see §§ 601.601(d)(2) and 601.602 of this chapter).

(ii) *First taxable year.* The self-certification must identify the first taxable year for which the self-certification takes effect.

(iii) *First month.* The self-certification may identify the first month (in that initial taxable year) in which the self-certification takes effect.

(A) *Failure to specify first month.* If the self-certification fails to specify the month in the initial taxable year that the self-certification takes effect, then the self-certification is treated as taking effect in the first month of that taxable year.

(B) *Investments before entity's first month as QOF not eligible for deferral.* If an investment in eligible interests of an eligible entity occurs prior to the eligible entity's first month as a QOF, any election under section 1400Z–2(a)(1) made for that investment is invalid and the investment is a non-qualifying investment.

(iv) *Becoming a QOF in a month that is not the first month of the taxable year.* This paragraph (a)(2)(iv) applies to an eligible entity if its self-certification as a QOF is first effective for a month that is not the first month of that entity's taxable year.

(A) For purposes of applying section 1400Z–2(d)(1)(A) and (B) in the first year of the QOF's existence, the phrase *first six-month period of the taxable year of the fund* means the first six months each of which is in the taxable year and in each of which the entity is a QOF. Thus, if an eligible entity becomes a QOF in the seventh or later month of a 12-month taxable year, the 90-percent investment standard in section 1400Z–2(d)(1) takes into account only the QOF's assets on the last day of the QOF's taxable year.

(B) The computation of any penalty under section 1400Z–2(f)(1) does not take into account any months before the first month in which an eligible entity is a QOF.

(3) *Self-decertification of a QOF.* If a QOF chooses to self-decertify as a QOF, the following rules apply:

(i) *Form and manner.* The self-decertification must be effected in such form and manner as may be prescribed by the Commissioner in IRS forms or instructions or in publications or guidance published in the Internal Revenue Bulletin (see §§ 601.601(d)(2) and 601.602 of this chapter).

(ii) *Time.* The self-decertification becomes effective at the beginning of the month following the month specified by the taxpayer, which month must not be earlier than the month in which the taxpayer files its self-decertification as provided in paragraph (a)(3)(i) of this section.

(4) [Reserved]

(b) *Valuation of property for purposes of the 90-percent investment standard and the 70-percent tangible property standard*—(1) *In general.* An eligible entity may value its owned or leased property using the valuation methods provided in paragraphs (b)(3) and (4) of this section to determine whether—

(i) In the case of an eligible entity that has self-certified as a QOF, the assets owned or leased by the QOF satisfy the 90-percent investment standard in section 1400Z–2(d)(1); and

(ii) In the case of an eligible entity that has issued qualified opportunity zone partnership interests or qualified opportunity zone stock to a QOF, the tangible property owned or leased by the eligible entity satisfies the *70-percent tangible property standard* in section 1400Z–2(d)(3)(A)(i).

(2) *Special rules*—(i) *QOFs*—(A) *In general.* To meet the *90-percent investment standard* in section 1400Z–2(d)(1), on a semiannual basis, a QOF may value its assets using the applicable financial statement valuation method set forth in paragraph (b)(3) of this section, if the QOF has an applicable financial statement within the meaning of § 1.475(a)–4(h), or the alternative valuation method set forth in paragraph (b)(4) of this section. During each taxable year, a QOF must apply consistently the valuation method that it selects under paragraph (b) of this section to all assets valued with respect to the taxable year.

(B) *Option for QOFs to disregard recently contributed property.* A QOF

may choose to determine compliance with the *90-percent investment standard* by excluding from both the numerator and denominator of the test any property that satisfies all the criteria in paragraphs (b)(2)(i)(B)(*1*) through (*3*) of this section. A QOF need not be consistent from one semiannual test to another in whether it avails itself of the option in this paragraph (b)(2)(i)(B).

(*1*) The amount of the property was received by the QOF partnership as a contribution or by the QOF corporation solely in exchange for stock of the corporation;

(*2*) The contribution or exchange occurred not more than 6 months before the test from which it is being excluded; and

(*3*) Between the date of the fifth business day after the contribution or exchange and the date of the semiannual test, the amount was held continuously in cash, cash equivalents, or debt instruments with a term of 18 months or less.

(C) *Safe harbor for QOFs to determine whether equity in an entity is qualified opportunity zone property.* A QOF may choose to determine compliance with the *90-percent investment standard* for each semiannual testing date of the QOF by including in both the numerator and denominator of the test the equity of each entity the QOF holds on that testing date that satisfies all the criteria in paragraph (b)(2)(i)(C)(*1*) or (*2*) of this section.

(*1*) The entity was a qualified opportunity zone business for at least 90 percent of the QOF's cumulative holding period for that equity of the entity—

(*i*) Beginning on the date the QOF's self-certification as a QOF is first effective; and

(*ii*) Ending on the last day of the entity's most recent taxable year ending on or before the semiannual testing date of the QOF.

(*2*) An entity that would not be a qualified opportunity zone business as of the end of its last taxable year ending on or before a semiannual testing date of the QOF is a qualified opportunity zone business with respect to the QOF for that taxable year of the entity if—

(*i*) A cure is achieved for the entity under paragraph (d)(6) of this section; and

(*ii*) The QOF files its Federal income tax return for the taxable year of the QOF containing the testing date on a date that is timely (taking extensions into account) and that is not later than when that cure is achieved.

(ii) *Qualified opportunity zone businesses*—(A) *In general.* For purposes of the fraction set forth in paragraph (d)(2)(ii)(A) of this section, the owned or leased tangible property of a qualified opportunity zone business may be valued using the applicable financial statement valuation method set forth in paragraph (b)(3) of this section, if the qualified opportunity zone business has an applicable financial statement within the meaning of § 1.475(a)–4(h), or the alternative valuation method set forth in paragraph (b)(4) of this section. During each taxable year, the valuation method selected under this paragraph (b) must be applied consistently to all tangible property valued with respect to the taxable year.

(B) *Five-percent zone taxpayer.* If a taxpayer both has self-certified as a QOF and holds an equity interest in an eligible entity that is tested as a qualified opportunity zone business, then that taxpayer may value the eligible entity's tangible property for purposes of satisfying the *70-percent tangible property standard* using the same valuation methodology under this paragraph (b) that the taxpayer uses for determining its own compliance with the 90-percent investment standard (compliance methodology), provided that no other equity holder in the eligible entity is a five-percent zone taxpayer. If two or more taxpayers that have self-certified as QOFs hold equity interests in the eligible entity and at least one of them is a five-percent zone taxpayer, then the values of the eligible entity's tangible property may be calculated using the compliance methodology that both is used by a five-percent zone taxpayer and that produces the highest percentage of qualified opportunity zone business property for the eligible entity for purposes of the *70-percent tangible property standard.* A *five-percent zone taxpayer* is a taxpayer that has self-certified as a QOF and that holds stock in the entity (if it is a corporation) representing at least 5 percent in voting rights and value or holds an interest of at least 5 percent in the profits and capital of the entity (if it is a partnership).

(*1*) *Example.* The example in paragraph (b)(2)(ii)(B)(*2*) of this section illustrates the principles of paragraph (b)(2)(ii)(B) of this section.

(*2*) *Example.* Entity JH is a corporation that has issued only one class of stock and that conducts a trade or business. Taxpayer X holds 94% of the JH stock, and Taxpayer Y holds the remaining 6% of that stock. (Thus, both X and Y are five percent zone taxpayers within the meaning of paragraph (b)(2)(ii)(B) of this section.) JH does not have an applicable financial statement, and, for that reason, a determination of whether JH is conducting a qualified opportunity zone business may employ the compliance methodology of X or Y. X and Y use different compliance methodologies permitted under paragraph (b)(2)(i)(A) of this section for purposes of satisfying the *90-percent investment standard* of section 1400Z–2(d)(1). Under X's compliance methodology (which is based on X's applicable financial statement), 65% of the tangible property owned or leased by JH's trade or business is qualified opportunity zone business property. Under Y's compliance methodology (which is based on Y's cost), 73% of the tangible property owned or leased by JH's trade or business is qualified opportunity zone business property. Because Y's compliance methodology would produce the higher percentage of qualified opportunity zone business property for JH (73%), both X and Y may use Y's compliance methodology to value JH's owned or leased tangible property. If JH's trade or business satisfies all additional requirements in section 1400Z–2(d)(3), the trade or business is a qualified opportunity zone business. Thus, if all of the additional requirements in section 1400Z–2(d)(2)(B) are satisfied, stock in JH is qualified opportunity zone stock in the hands of a taxpayer that has self-certified as a QOF.

(iii) *Inventory.* In determining whether the *90-percent investment standard* in section 1400Z–2(d)(1) or the *70-percent tangible property standard* in section 1400Z–2(d)(3)(A)(i) is satisfied, an eligible entity may choose to exclude from both the numerator and denominator of the applicable test the value of all inventory (including raw materials) of the trade or business, if applied consistently within a taxable year of the eligible entity.

(3) *Applicable financial statement valuation method*—(i) *In general.* Under the applicable financial statement valuation method set forth in this paragraph (b)(3), the value of each property that is owned or leased by an eligible entity is the value of that asset as reported on the eligible entity's applicable financial statement for the relevant reporting period.

(ii) *Requirement for selection of method.* An eligible entity may select the applicable financial statement valuation method set forth in this paragraph (b)(3) to value an asset leased by the eligible entity only if the applicable financial statement of the eligible entity is prepared according to U.S. generally accepted accounting principles (GAAP) and requires an assignment of value to the lease of the asset.

(4) *Alternative valuation method*—(i) *In general.* Under the alternative valuation method set forth in this paragraph (b)(4), the value of the property owned by an eligible entity is calculated under paragraph (b)(4)(ii) of this section, and the value of the property leased by an eligible entity is

calculated under paragraph (b)(4)(iii) of this section.

(ii) *Property owned by an eligible entity*—(A) *Property purchased or constructed.* The value of each property owned by an eligible entity that is acquired by purchase for fair market value or constructed for fair market value is the eligible entity's unadjusted cost basis of the asset under section 1012 or section 1013.

(B) *Other property.* The value of each item of property owned by an eligible entity that is not purchased or constructed for fair market value is the item of property's fair market value, determined on the last day of the first 6 month period of the taxable year and on the last day of the taxable year.

(iii) *Property leased by an eligible entity*—(A) *In general.* The value of each property that is leased by an eligible entity is equal to the present value of the leased property as defined in paragraph (b)(4)(iii)(C) of this section.

(B) *Discount rate.* For purposes of calculating present value under paragraph (b)(4)(iii) of this section, the discount rate is the short-term applicable Federal rate under section 1274(d)(1), based on semiannual compounding, for the month in which the eligible entity enters into the lease. For purposes of the preceding sentence, the three month rule in section 1274(d)(2) does not apply to determine the applicable Federal rate.

(C) *Present value.* For purposes of paragraph (b)(4)(iii) of this section, present value of a leased property—

(*1*) Is equal to the sum of the present values of each payment under the lease for the property;

(*2*) Is calculated at the time the eligible entity enters into the lease for the property; and

(*3*) Once calculated, is used as the value for the property by the eligible entity for all testing dates during the term of the lease for purposes of the *90-percent investment standard* or the *70-perecent tangible property standard.*

(D) *Term of a lease.* For purposes of paragraph (b)(4)(iii) of this section, the term of a lease includes periods during which the lessee may extend the lease at a pre-defined market rate rent. For nonresidential real property or residential real property, pre-defined rent does not include the option to renew at fair market value, determined at the time of renewal. The terms of the pre-defined rent must satisfy the following criteria:

(*1*) *General rule.* The terms of the pre-defined rent are market rate (that is, the terms of the pre-defined rent reflect common, arms-length market pricing in the locale that includes the qualified opportunity zone as determined under section 482 and all section 482 regulations in this chapter) at the time the lease is entered into.

(*2*) *Rebuttable presumption regarding leases not between related persons.* There will be a rebuttable presumption that the terms of the extension of the lease are market rate for leases not between related persons (within the meaning of section 1400Z–2(e)(2)), and thus, the parties to the lease are not required to perform a section 482 analysis.

(*3*) *Exception for state, local, and Indian tribal governments.* For purposes of this paragraph (b)(4)(iii)(D), tangible property acquired by lease from a state or local government, or an Indian tribal government, is not considered tangible property acquired by lease from a related person.

(c) *Qualified opportunity zone property*—(1) *In general.* Pursuant to section 1400Z–2(d)(2)(A), the following property is *qualified opportunity zone property:*

(i) Qualified opportunity zone stock as defined in paragraph (c)(2) of this section;

(ii) Qualified opportunity zone partnership interest as defined in paragraph (c)(3) of this section; and

(iii) Qualified opportunity zone business property as defined in § 1.1400Z2(d)–2.

(2) *Qualified opportunity zone stock*—(i) *In general.* Except as provided in paragraph (c)(2)(ii) of this section, if an eligible entity is classified as a corporation for Federal income tax purposes (corporation), then an equity interest (stock) in the eligible entity is *qualified opportunity zone stock* if the requirements described in this paragraph (c)(2)(i) are satisfied:

(A) *Date of acquisition.* The stock is acquired by a QOF after December 31, 2017, at its original issue (directly or through an underwriter) from the corporation solely in exchange for cash;

(B) *Qualified opportunity zone business.* As of the time the stock was issued, the corporation was a qualified opportunity zone business as defined in section 1400Z–2(d)(3) and paragraph (d) of this section (or, in the case of a new corporation, the corporation was being organized for purposes of being such a qualified opportunity zone business); and

(C) *90-percent qualified opportunity zone property holding period*—(*1*) *Cumulative holding period test.* During at least 90 percent of the QOF's holding period for the corporation's stock, determined on a cumulative basis in accordance with paragraph (c)(2)(i)(C)(*2*) of this section, the corporation qualified as a qualified opportunity zone business.

(*2*) *Semiannual qualified opportunity zone business test.* For purposes of determining satisfaction of the cumulative 90-percent qualified opportunity zone property holding period test described in paragraph (c)(2)(i)(C)(*1*) of this section, the determination of whether a corporation engaged in a trade or business qualifies as a qualified opportunity zone business is made by the QOF on a semiannual basis pursuant to section 1400Z–2(d)(1). However, a QOF may choose to apply the safe harbor rule in paragraph (b)(2)(i)(C) of this section to make this determination.

(ii) *Redemptions of stock.* Pursuant to section 1400Z–2(d)(2)(B)(ii), the following rules apply for purposes of determining whether stock in a corporation qualifies as qualified opportunity zone stock:

(A) *Redemptions from taxpayer or related person.* Stock acquired by a QOF is not treated as qualified opportunity zone stock if, at any time during the 4-year period beginning on the date 2 years before the issuance of the stock, the corporation issuing the stock purchased either directly or indirectly any of its stock from the QOF or from a person related (within the meaning of section 1400Z–2(e)(2)) to the QOF. Even if the purchase occurs after the issuance, the stock was never qualified opportunity zone stock.

(B) *Significant redemptions*—(*1*) *In general.* Stock issued by a corporation is not treated as qualified opportunity zone stock if, at any time during the 2-year period beginning on the date one year before the issuance of the stock, the corporation made one or more purchases of more than a de minimis amount of its stock and the purchased stock has an aggregate value (as of the time of the respective purchases) exceeding 5 percent of the aggregate value of all of its stock as of the beginning of the 2-year period. The aggregate value is determined as of the time of the stock purchases. Even if one or more of the disqualifying purchases occurs after the issuance, the stock was never qualified opportunity zone stock.

(*2*) *De minimis amount.* For purposes of this paragraph (c)(2)(ii)(B), stock acquired from the taxpayer or a related person exceeds a de minimis amount only if the aggregate amount paid for the stock exceeds $10,000 and more than 2 percent of the stock held by the taxpayer and related persons (within the meaning of section 1400Z–2(e)(2)) is acquired. The rules in the following sentences of this paragraph (c)(2)(ii)(B)(*2*) apply for purposes of determining whether the 2-

percent limit is exceeded. The percentage of stock acquired in any single purchase is determined by dividing the stock's value (as of the time of purchase) by the value (as of the time of purchase) of all stock held (directly or indirectly) by the taxpayer and related persons immediately before the purchase. The percentage of stock acquired in multiple purchases is the sum of the percentages determined for each separate purchase.

(C) *Treatment of certain transactions.* If any transaction is treated under section 304(a) as a distribution in redemption of the stock of any corporation, for purposes of paragraphs (c)(2)(ii)(A) and (B) of this section, that corporation is treated as purchasing an amount of its stock equal to the amount that is treated as such a distribution under section 304(a).

(D) *Principles of § 1.1202–2(c) and (d).* The principles of § 1.1202–2(c) and (d) apply in determining whether stock is redeemed or purchased for purposes of paragraph (c)(2)(ii) of this section.

(iii) *Reorganizations of corporations otherwise qualifying as qualified opportunity zone businesses*—(A) *Qualification as qualified opportunity zone stock.* Stock that meets all of the requirements of paragraph (c)(2)(i) of this section except for the requirement in paragraph (c)(2)(i)(A) of this section is qualified opportunity zone stock if it is received solely in exchange for qualified opportunity zone stock in a transaction described in section 381(a)(2). The requirements in paragraphs (c)(2)(i)(B) and (C) of this section must be met with respect to both the stock held before such transaction and the stock for which it is exchanged in such transaction.

(B) *Satisfaction of original use and substantial improvement tests.* The requirements of § 1.1400Z2(d)–2 apply to property of a qualified opportunity zone business acquired from a qualified opportunity zone business in a transaction described in section 381(a)(2) as if the acquiring corporation had held the property during the period in which the target corporation held the property. For example, an item of property must be substantially improved by the same date by which the target corporation was required to satisfy the substantial improvement test for such property.

(C) *Reorganizations of qualified opportunity zone businesses within a consolidated group.* See §§ 1.1502–14Z and 1.1504–3 for special rules applicable to consolidated groups.

(3) *Qualified opportunity zone partnership interest*—(i) *In general.* If an *eligible* entity is classified as a partnership for Federal tax purposes (partnership), any capital or profits interest (partnership interest) in the eligible entity is a *qualified opportunity zone partnership interest* if—

(A) *Date of acquisition.* The partnership interest is acquired by a QOF after December 31, 2017, from the partnership solely in exchange for cash;

(B) *Qualified opportunity zone business.* As of the time the partnership interest was acquired, the partnership was a qualified opportunity zone business as defined in section 1400Z–2(d)(3) and paragraph (d) of this section (or, in the case of a new partnership, the partnership was being organized for purposes of being a qualified opportunity zone business); and

(C) *90-percent qualified opportunity zone property holding period*—(*1*) *Cumulative holding period test.* During at least 90-percent of the QOF's holding period for the partnership interest, determined on a cumulative basis in accordance with paragraph (c)(3)(i)(C)(*2*) of this section, the partnership qualified as a qualified opportunity zone business.

(*2*) *Semiannual qualified opportunity zone business test.* For purposes of determining satisfaction of the cumulative 90-percent qualified opportunity zone property holding period test described in paragraph (c)(3)(i)(C)(*1*) of this section, the determination of whether a partnership engaged in a trade or business qualifies as a qualified opportunity zone business is made by the QOF on a semiannual basis pursuant to section 1400Z–2(d)(1). However, a QOF may choose to apply the safe harbor rule in paragraph (b)(2)(i)(C) of this section to make this determination.

(ii) *Reorganizations of partnerships otherwise qualifying as qualified opportunity zone businesses*—(A) *Qualification as a qualified opportunity zone partnership interest.* A partnership interest that meets all of the requirements of paragraph (c)(3)(i) of this section except for the requirement in paragraph (c)(3)(i)(A) of this section is a qualified opportunity zone partnership interest if it is received solely in exchange for a qualified opportunity zone partnership interest in a merger or consolidation transaction described in section 708(b)(2)(A). The requirements in paragraphs (c)(3)(i)(B) and (C) of this section must be met with respect to both the partnership interest held before the transaction and the partnership interest for which it is exchanged in the transaction.

(B) *Satisfaction of original use and substantial improvement tests.* The requirements of § 1.1400Z2(d)–2 apply to property of a qualified opportunity zone business acquired from a qualified opportunity zone business in a transaction described in section 708(b)(2)(A) as if the resulting partnership had held the property during the period in which the merging or consolidating partnership held the property. For example, an item of property must be substantially improved by the same date by which the merging or consolidating partnership was required to satisfy the substantial improvement test for such property.

(d) *Qualified opportunity zone business*—(1) *In general.* An eligible entity engaged in a trade or business within the meaning of section 162 is a *qualified opportunity zone business* if the entity satisfies, as determined at the end of its taxable year, all the criteria in paragraphs (d)(1)(i) through (*iii*) of this section. An eligible entity's status as a qualified opportunity zone business applies for the entire taxable year of the entity.

(i) Pursuant to section 1400Z–2(d)(3)(A)(i), the eligible entity engaged in the trade or business satisfies the *70-percent tangible property standard* with respect to its tangible property, as provided in paragraph (d)(2) of this section;

(ii) Pursuant to section 1400Z–2(d)(3)(A)(ii), the eligible entity engaged in the trade or business satisfies the requirements of section 1397C(b)(2), (4), and (8), as provided in paragraph (d)(3) of this section; and

(iii) Pursuant to section 1400Z–2(d)(3)(A)(iii), the eligible entity engaged in the trade or business is not described in section 144(c)(6)(B) as provided in paragraph (d)(4) of this section.

(2) *Satisfaction of 70-percent tangible property standard*—(i) *In general.* A trade or business of an eligible entity satisfies the *70-percent tangible property standard* if at least 70 percent of the tangible property owned or leased by the trade or business is qualified opportunity zone business property (as defined in § 1.1400Z2(d)–2).

(ii) *Calculating percent of tangible property owned or leased in a trade or business*—(A) *In general.* Whether a trade or business of the eligible entity satisfies the *70-percent tangible property standard* set forth in paragraph (d)(2)(i) of this section is determined by a fraction—

(*1*) The numerator of which is the total value of all tangible property owned or leased by the qualified opportunity zone business that is qualified opportunity zone business property; and

(*2*) The denominator of which is the total value of all tangible property owned or leased by the qualified opportunity zone business, whether located inside or outside of a qualified opportunity zone.

(B) *Valuation.* See paragraph (b)(2)(ii) of this section for rules regarding the valuation of tangible property for purposes of the *70-percent tangible property standard.*

(3) *Operation of section 1397C requirements adopted by reference*—(i) *Gross income requirement.* Section 1400Z–2(d)(3)(A)(ii) incorporates section 1397C(b)(2), requiring that for each taxable year at least 50 percent of the gross income of a qualified opportunity zone business is derived from the active conduct of a trade or business in the qualified opportunity zone (or in multiple qualified opportunity zones). A trade or business meets the 50-percent gross income requirement in the preceding sentence if the trade or business satisfies any one of the four criteria described in paragraph (d)(3)(i)(A), (B), (C), or (D) of this section, or any criteria identified in published guidance issued by the Commissioner under § 601.601(d)(2) of this chapter.

(A) *Services performed in qualified opportunity zone based on hours.* At least 50 percent of the services performed for the trade or business are performed in a qualified opportunity zone, determined by the fraction described in paragraphs (d)(3)(i)(A)(*1*) and (*2*) of this section. Amounts paid to partners that provide services to the trade or business of a partnership are taken into account in the numerator and denominator set forth in paragraphs (d)(3)(i)(A)(*1*) and (*2*) of this section only to the extent the amounts paid to the partners are guaranteed payments for services provided to the partnership within the meaning of section 707(c).

(*1*) The numerator of the fraction is the total number of hours of services performed for the trade or business in a qualified opportunity zone during the taxable year by employees, partners that provide services to a partnership, independent contractors, and employees of independent contractors; and

(*2*) The denominator of the fraction is the total number of hours of services performed for the trade or business during the taxable year by employees, partners that provide services to a partnership, independent contractors, and employees of independent contractors.

(B) *Services performed in qualified opportunity zone based on amounts paid for services.* At least 50 percent of the services performed for the trade or business are performed in a qualified opportunity zone, determined by the fraction described in paragraphs (d)(3)(i)(B)(*1*) and (*2*) of this section. Amounts paid to partners that provide services to the trade or business of a partnership are taken into account in the numerator and denominator set forth in paragraphs (d)(3)(i)(B)(*1*) and (*2*) of this section only to the extent the amounts paid to the partners are guaranteed payments for services provided to the partnership within the meaning of section 707(c).

(*1*) The numerator of the fraction is the total amount paid by the entity for services performed in a qualified opportunity zone during the taxable year, whether by employees, partners that provide services to a partnership, independent contractors, or employees of independent contractors; and

(*2*) The denominator of the fraction is the total amount paid by the entity for services performed during the taxable year, whether by employees, partners that provide services to a partnership, independent contractors, or employees of independent contractors.

(C) *Necessary tangible property and business functions.* The tangible property of the trade or business located in a qualified opportunity zone and the management or operational functions performed in a qualified opportunity zone are each necessary for the generation of at least 50 percent of the gross income of the trade or business.

(D) *Facts and circumstances.* Based on all the facts and circumstances, at least 50 percent of the gross income of a qualified opportunity zone business is derived from the active conduct of a trade or business in a qualified opportunity zone.

(E) *Examples.* The following examples illustrate the principles of paragraphs (d)(3)(i)(C) and (D) of this section.

(*1*) *Example 1.* A landscaping business has its headquarters in a qualified opportunity zone, its officers and employees manage the daily operations of the business (inside and outside the qualified opportunity zone) from its headquarters, and all its equipment and supplies are stored in the headquarters facilities. The activities occurring and the storage of equipment and supplies in the qualified opportunity zone are, taken together, necessary for the generation of the income of the business.

(*2*) *Example 2.* A trade or business is formed or organized under the laws of the jurisdiction within which a qualified opportunity zone is located, and the business has a P.O. Box located in the qualified opportunity zone. The mail received at that P.O. Box is fundamental to the income of the trade or business, but there is no other basis for concluding that the income of the trade or business is derived from activities in the qualified opportunity zone. The mere location of the P.O. Box is not necessary for the generation of gross income by the trade or business.

(*3*) *Example 3.* In 2019, Taxpayer X realized $w million of capital gains and within the 180-day period invested $w million in QOF Y, a qualified opportunity fund. QOF Y immediately acquired from partnership P a partnership interest in P, solely in exchange for $w million of cash. P is a real estate developer that has written plans to acquire land in a qualified opportunity zone on which it plans to construct a commercial building for lease to other trades or businesses. In 2023, P's commercial building is placed in service and is fully leased up to other trades or businesses. For the 2023 taxable year, at least 50 percent of P's gross income is derived from P's rental of its tangible property in the qualified opportunity zone. Thus, under P's facts and circumstances, P satisfies the gross income test under section 1397C(b)(2).

(ii) *Use of intangible property requirement*—(A) *In general.* Section 1400Z–2(d)(3)(A)(ii) incorporates section 1397C(b)(4), requiring that, with respect to any taxable year, a substantial portion of the intangible property of a qualified opportunity zone business is used in the active conduct of a trade or business in a qualified opportunity zone. For purposes of section 1400Z–2(d)(3)(A)(ii) and the preceding sentence, the term *substantial portion* means at least 40 percent.

(B) *Use of intangible property.* For purposes of section 1400Z–2(d)(3)(A)(ii) and paragraph (d)(3)(ii)(A) of this section, intangible property of a qualified opportunity zone business is used in the active conduct of a trade or business in a qualified opportunity zone if—

(*1*) The use of the intangible property is normal, usual, or customary in the conduct of the trade or business; and

(*2*) The intangible property is used in the qualified opportunity zone in the performance of an activity of the trade or business that contributes to the generation of gross income for the trade or business.

(iii) *Active conduct of a trade or business*—(A) *Operating real property.* Solely for purposes of section 1400Z–2(d)(3)(A), the ownership and operation (including leasing) of real property is the active conduct of a trade or business.

(B) *Lessee is responsible for certain costs.* Merely entering into a triple-net-lease with respect to real property owned by a taxpayer does not constitute the active conduct of a trade or business by such taxpayer.

(C) *Examples.* The following examples illustrate the rules of paragraph (d)(3)(iii) of this section.

(*1*) *Example 1. Mere triple-net-lease not active conduct of trade or business*—(*i*) *Facts.* Company N constructs and places into service a new, three-story office building in a qualified opportunity zone and leases the entire building to tenant X, an unrelated person, which uses the building as office space for its software development firm. This building is the only property owned by Company N. The lease agreement between Company N and tenant X is a triple-net-lease under which tenant X is responsible for all of the costs relating to the office building (for example, paying all taxes, insurance, and maintenance expenses) in addition to paying rent. Company N also maintains an office in the building with staff members to address any issues that may arise with respect to the triple-net-lease.

(*ii*) *Analysis.* Solely for purposes of section 1400Z–2(d)(3)(A), Company N is treated as not engaged in the active conduct of a trade or business with respect to the leased office building. Company N leases the building to tenant X under a triple-net-lease, and therefore the employees of Company N do not meaningfully participate in the management or operations of the building. The fact that Company N maintains an office in the leased building with staff members to address any issues that may arise with respect to the triple-net-lease does not alter this result. Therefore, Company N does not conduct an active trade or business in a qualified opportunity zone.

(*2*) *Example 2. Triple-net-lease and managerial and operational activities can constitute active conduct of trade or business*—(*i*) *Facts.* Company N constructs and places into service a new, three-story mixed-use building in a qualified opportunity zone and leases a floor to each of unrelated tenants X, Y, and Z, respectively. This building is the only property owned by Company N. The lease agreement between Company N and tenant X is a triple-net-lease under which tenant X is responsible for all of the costs relating to the third floor of the building (for example, paying all such taxes, insurance, and maintenance expenses) in addition to paying rent. The lease agreement between Company N and tenant Y is not a triple-net-lease and employees of Company N manage and operate the second floor of the building. Likewise, the lease agreement between Company N and tenant Z is not a triple-net-lease and employees of Company N manage and operate the first floor of the building. Company N maintains an office in the building, which the employees regularly use to carry out their managerial and operational duties with respect to the first and second floors, and address any other issues that may arise with respect to the three leases.

(*ii*) *Analysis.* Solely for purposes of section 1400Z–2(d)(3)(A), Company N is treated as engaged in the active conduct of a trade or business with respect to the leased mixed-use building. While Company N leases the third floor of the building to tenant X merely under a triple-net-lease, and therefore the employees of Company N do not meaningfully participate in the management or operations of that floor, the employees of Company N meaningfully participate in the management and operations of the first and second floors of the leased building. Therefore, in carrying out the overall leasing business of Company N with respect to the mixed-use building, employees of Company N conduct meaningful managerial and operational activities. As a result, Company N conducts an active trade or business in a qualified opportunity zone.

(iv) *Nonqualified financial property limitation.* Section 1400Z–2(d)(3)(A)(ii) incorporates section 1397C(b)(8), which requires that in each taxable year less than 5 percent of the average of the aggregate unadjusted bases of the property of a qualified opportunity zone business is attributable to nonqualified financial property. Section 1397C(e)(1), which defines the term *nonqualified financial property* for purposes of section 1397C(b)(8), excludes from that term reasonable amounts of working capital held in cash, cash equivalents, or debt instruments with a term of 18 months or less (working capital assets) and debt instruments described in section 1221(a)(4).

(v) *Safe harbor for reasonable amount of working capital.* Solely for purposes of applying section 1397C(e)(1) to the definition of a qualified opportunity zone business under section 1400Z–2(d)(3), working capital assets are treated as reasonable in amount for purposes of sections 1397C(b)(2) and 1400Z–2(d)(3)(A)(ii), if all of the requirements in paragraphs (d)(3)(v)(A) through (C) of this section are satisfied.

(A) *Designated in writing.* These amounts are designated in writing for the development of a trade or business in a qualified opportunity zone (as defined in section 1400Z–1(a)), including when appropriate the acquisition, construction, and/or substantial improvement of tangible property in such a zone.

(B) *Reasonable written schedule.* There is a written schedule consistent with the ordinary start-up of a trade or business for the expenditure of the working capital assets. Under the schedule, the working capital assets must be spent within 31 months of the receipt by the business of the assets.

(C) *Property consumption consistent.* The working capital assets are actually used in a manner that is substantially consistent with the writing and written schedule described in paragraphs (d)(3)(v)(A) and (B) of this section. If consumption of the working capital assets is delayed by waiting for governmental action the application for which is complete, that delay does not cause a failure of this paragraph (d)(3)(v)(C).

(D) *Federally declared disasters.* If the qualified opportunity zone business is located in a qualified opportunity zone within a federally declared disaster (as defined in section 165(i)(5)(A)), the qualified opportunity zone business may receive up to an additional 24 months to consume its working capital assets, as long as it otherwise meets the requirements of paragraph (d)(3)(v) of this section.

(E) *Ability of a single business to benefit from more than a single application of the safe harbor.* A business may benefit from multiple overlapping or sequential applications of the working capital safe harbor, provided that each application independently satisfies all of the requirements in paragraphs (d)(3)(v)(A) through (C) of this section.

(F) *Ability of tangible property to benefit from more than a single application of the safe harbor.* Tangible property may benefit for an additional 31-month period, for a total of 62 months, in the form of multiple overlapping or a sequential application of the working capital safe harbor, provided that each application independently satisfies all of the requirements in paragraphs (d)(3)(v)(A) through (C) of this section, the working capital assets from an expiring 31-month period were expended in accordance with the requirements in paragraphs (d)(3)(v)(A) through (C) of this section, and the subsequent infusions of working capital assets form an integral part of the plan covered by the initial working capital safe harbor period. An overlapping or sequential application of the working capital safe harbor must include a substantial amount of working capital assets (which may include debt instruments described in section 1221(a)(4)).

(G) *Examples.* The following examples illustrate the rules of paragraph (d)(3)(v) of this section.

(*1*) *Example 1. General application of working capital safe harbor*—(*i*) *Facts.* QOF F creates a domestic C corporation E to open a fast-food restaurant and acquires almost all of the equity of E in exchange for cash. E has a written plan and a 20-month schedule for the use of this cash to establish the restaurant. Among the planned uses for the cash are identification of favorable locations in the qualified opportunity zone, leasing a building suitable for such a restaurant, outfitting the building with appropriate equipment and furniture (both owned and leased), necessary security deposits, obtaining a franchise and local permits, and the hiring and training of kitchen and wait staff. Not-yet-disbursed amounts were held in assets described in section 1397C(e)(1), and these assets were eventually expended in a manner consistent with the plan and schedule.

(*ii*) *Analysis.* E's use of the cash qualifies for the working capital safe harbor described in paragraph (d)(3)(v) of this section.

(*2*) *Example 2. Multiple applications of working capital safe harbor*—(*i*) *Facts.* QOF G creates a domestic C corporation H to start a new technology company and acquires equity of H in exchange for cash on Date 1. In addition to H's rapid deployment of capital received from other equity investors, H writes a plan with a 30-month schedule for the use of the Date 1 cash. The plan describes use of the cash to research and develop a new technology (Technology), including paying salaries for engineers and other scientists to conduct the research, purchasing, and leasing equipment to be used in research and furnishing office and laboratory space. Approximately 18 months after Date 1, on Date 2, G acquires additional equity in H for cash, and H writes a second plan. This new plan has a 25-month schedule for the development of a new application of existing software (Application), to be marketed to government agencies. Among the planned uses for the cash received on Date 2 are paying development costs, including salaries for software engineers, other employees, and third-party consultants to assist in developing and marketing the new application to the anticipated customers. Not-yet-disbursed amounts that were scheduled for development of the Technology and the Application were held in assets described in section 1397C(e)(1), and these assets were eventually expended in a manner substantially consistent with the plans and schedules for both the Technology and the Application.

(*ii*) *Analysis.* H's use of both the cash received on Date 1 and the cash received on Date 2 qualifies for the working capital safe harbor described in paragraph (d)(3)(v) of this section.

(*3*) *Example 3. General application of working capital safe harbor*—(*i*) *Facts.* In 2019, Taxpayer H realized $w million of capital gains and within the 180-day period invested $w million in QOF T, a qualified opportunity fund. QOF T immediately acquired from partnership P a partnership interest in P, solely in exchange for $w million of cash. P immediately placed the $w million in working capital assets, which remained in working capital assets until used. P had written plans to acquire land in a qualified opportunity zone on which it planned to construct a commercial building. Of the $w million, $x million was dedicated to the land purchase, $y million to the construction of the building, and $z million to ancillary but necessary expenditures for the project. The written plans provided for purchase of the land within a month of receipt of the cash from QOF T and for the remaining $y and $z million to be spent within the next 30 months on construction of the building and on the ancillary expenditures. All expenditures were made on schedule, consuming the $w million. During the taxable years that overlap with the first 31-month period, P had no gross income other than that derived from the amounts held in those working capital assets. Prior to completion of the building, P's only assets were the land it purchased, the unspent amounts in the working capital assets, and P's work in process as the building was constructed.

(*ii*) *Analysis*—P met the three requirements of the safe harbor provided in paragraphs (d)(3)(v)(A) through (C) of this section. P had a written plan to spend the $w received from QOF T for the acquisition, construction, and/or substantial improvement of tangible property in a qualified opportunity zone, as defined in section 1400Z–1(a). P had a written schedule consistent with the ordinary start-up for a business for the expenditure of the working capital assets. And, finally, P's working capital assets were actually used in a manner that was substantially consistent with its written plan and the ordinary start-up of a business. First, the $x million, the $y million, and the $z million are treated as reasonable in amount for purposes of sections 1397C(b)(2) and 1400Z–2(d)(3)(A)(ii). Second, because P had no other gross income during the 31 months at issue, 100 percent of P's gross income during that time is treated as derived from an active trade or business in the qualified opportunity zone for purposes of satisfying the 50-percent test of section 1397C(b)(2). Third, for purposes of satisfying the requirement of section 1397C(b)(4), during the period of land acquisition and building construction a substantial portion of P's intangible property is treated as being used in the active conduct of a trade or business in the qualified opportunity zone. Fourth, all of the facts described are consistent with QOF T's interest in P being a qualified opportunity zone partnership interest for purposes of satisfying the 90-percent investment standard in section 1400Z–2(d)(1).

(*iii*) *Analysis if P had purchased an existing building.* The conclusions would also apply if P's plans had been to buy and substantially improve a pre-existing commercial building. In addition, the fact that P's basis in the building has not yet doubled would not cause the building to fail to satisfy section 1400Z–2(d)(2)(D)(i)(III).

(vi) *Safe harbor for gross income derived from the active conduct of business.* Solely for purposes of applying the 50-percent test in section 1397C(b)(2) to the definition of a qualified opportunity zone business in section 1400Z–2(d)(3), if any gross income is derived from property that paragraph (d)(3)(v) of this section treats as a reasonable amount of working capital, then that gross income is counted toward satisfaction of the 50-percent test.

(vii) *Safe harbor for use of intangible property.* Solely for purposes of applying the use requirement in section 1397C(b)(4) to the definition of a qualified opportunity zone business under section 1400Z–2(d)(3), intangible property purchased or licensed by the trade or business, pursuant to the reasonable written plan with a written schedule for the expenditure of the working capital, satisfies the use requirement during any period in which the business is proceeding in a manner that is substantially consistent with paragraphs (d)(3)(v)(A) through (C) of this section.

(viii) *Safe harbor for property on which working capital is being expended*—(A) *In general.* If paragraph (d)(3)(v) of this section treats property that would otherwise be nonqualified financial property as being a reasonable amount of working capital because of compliance with the three requirements of paragraphs (d)(3)(v)(A) through (C) of this section and if the tangible property referred to in paragraph (d)(3)(v)(A) is expected to satisfy the requirements of section 1400Z–2(d)(2)(D)(i) as a result of the planned expenditure of those working capital assets, then tangible property purchased, leased, or improved by the trade or business, pursuant to the written plan for the expenditure of the working capital assets, is treated as qualified opportunity zone business property satisfying the requirements of section 1400Z–2(d)(2)(D)(i), during that and subsequent working capital periods the property is subject to, for purposes of the *70-percent tangible property standard* in section 1400Z–2(d)(3).

(B) *Example. Multiple applications of working capital safe harbor to tangible property*—(i) *Facts.* B also borrows cash and forms a domestic C corporation B to develop a large mixed-use real estate development that will consist of commercial and residential real property, owning almost all of the equity of B in exchange for cash. QOF A has a master written plan for the completion of the commercial and residential real property over a 55 month period. The plan provides that the commercial real property will be completed over a 30 month schedule and subsequently, the residential real property will be completed over a 25 month schedule. The plan further provides that a portion of the commercial real property is unable to be used in a trade or business after the completion of the commercial real property since that portion of the commercial real property will be unusable during the residential construction phase. Pursuant to B's original master plan for the completion of the real estate development, QOF A acquires additional equity in B for cash after the completion of the commercial development phase, and B commences use of those working capital assets for residential development phase.

(*ii*) *Analysis.* B's use of the cash for the commercial and residential phase qualified for the working capital safe harbor described in paragraph (d)(3)(v) of this section. In addition, all of B's commercial real property developed pursuant to B's original master plan is treated as qualified opportunity zone business property under paragraph (d)(3)(viii) of this section.

(ix) *Real property straddling a qualified opportunity zone.* For purposes of satisfying the requirements in this paragraph (d)(3) in the case of

real property that straddles a qualified opportunity zone, a qualified opportunity zone is the location of services, tangible property, or business functions if—

(A) The trade or business uses the portion of the real property located within a qualified opportunity zone in carrying out its business activities;

(B) The trade or business uses the real property located outside of a qualified opportunity zone in carrying out its business activities;

(C) The amount of the real property located within a qualified opportunity zone is substantial compared to the amount of real property located outside of a qualified opportunity zone; and

(D) The real property located in the qualified opportunity zone is contiguous to part, or all, of the real property located outside of the qualified opportunity zone.

(E) In general, one of the two methods in paragraph (d)(3)(ix)(E)(*1*) and (*2*) of this section may be chosen to determine whether the amount of real property located in the qualified opportunity zone is substantial compared to the amount of real property located outside the qualified opportunity zone.

(*1*) *Square footage test.* If the amount of real property based on square footage located within the qualified opportunity zone is greater than the amount of real property based on square footage outside of the qualified opportunity zone, and the real property outside of the qualified opportunity zone is contiguous to part or all of the real property located inside the qualified opportunity zone, then all of the property is deemed to be located within a qualified opportunity zone. The test in this paragraph (d)(3)(ix)(E)(*1*) is carried out at the time at which the subject real property is acquired.

(*2*) *Unadjusted cost test.* If the unadjusted cost of the real property located inside a qualified opportunity zone is greater than the unadjusted cost of the real property outside the qualified opportunity zone, and the real property outside of the qualified opportunity zone is contiguous to all or part of the real property located inside the qualified opportunity zone, then all of the property is deemed to be located within a qualified opportunity zone. The unadjusted cost basis of property acquired as a single tract is presumed to be allocated on the basis of the square footage of the property. The test in this paragraph (d)(3)(ix)(E)(*2*) is carried out at the time at which the subject real property is acquired.

(F) For purposes of the two tests described in paragraph (d)(3)(ix)(E)(*1*) and (*2*) of this section, two or more tracts or parcels of land are contiguous if they share common boundaries or would share common boundaries but for the interposition of a road, street, railroad, stream or similar property. Tracts or parcels of land which touch only at a common corner are not contiguous.

(x) *Example.* The following example illustrates the rules of paragraph (d)(3) of this section—

(A) *Facts.* In 2019, Taxpayer H realized $w million of capital gains and within the 180-day period invested $w million in QOF T, a qualified opportunity fund. QOF T immediately acquired from partnership P a partnership interest in P, solely in exchange for $w million of cash. P immediately placed the $w million in working capital assets, which remained in working capital assets until used. P had written plans to acquire land in a qualified opportunity zone on which it planned to construct a commercial building. Of the $w million, $x million was dedicated to the land purchase, $y million to the construction of the building, and $z million to ancillary but necessary expenditures for the project. The written plans provided for purchase of the land within a month of receipt of the cash from QOF T and for the remaining $y and $z million to be spent within the next 30 months on construction of the building and on the ancillary expenditures. All expenditures were made on schedule, consuming the $w million. During the taxable years that overlap with the first 31-month period, P had no gross income other than that derived from the amounts held in those working capital assets. Prior to completion of the building, P's only assets were the land it purchased, the unspent amounts in the working capital assets, and P's work in process as the building was constructed.

(B) *Analysis*—(*1*) P met the three requirements of the safe harbor provided in paragraph (d)(3)(v) of this section. P had a written plan to spend the $w received from QOF T for the acquisition, construction, and/or substantial improvement of tangible property in a qualified opportunity zone, as defined in section 1400Z–1(a). P had a written schedule consistent with the ordinary start-up for a business for the expenditure of the working capital assets. And, finally, P's working capital assets were actually used in a manner that was substantially consistent with its written plan and the ordinary start-up of a business. Therefore, the $x million, the $y million, and the $z million are treated as reasonable in amount for purposes of sections 1397C(b)(2) and 1400Z–2(d)(3)(A)(ii).

(*2*) Because P had no other gross income during the 31 months at issue, 100 percent of P's gross income during that time is treated as derived from an active trade or business in the qualified opportunity zone for purposes of satisfying the 50-percent test of section 1397C(b)(2).

(*3*) For purposes of satisfying the requirement of section 1397C(b)(4), during the period of land acquisition and building construction a substantial portion of P's intangible property is treated as being used in the active conduct of a trade or business in the qualified opportunity zone.

(*4*) All of the facts described are consistent with QOF T's interest in P being a qualified opportunity zone partnership interest for purposes of satisfying the *90-percent investment standard* in section 1400Z–2(d)(1).

(C) *Analysis if P had purchased an existing building.* The conclusions in paragraph (d)(3)(x)(B) of this section would also apply if P's plans had been to buy and substantially improve a pre-existing commercial building. In addition, the fact that P's basis in the building has not yet doubled would not cause the building to fail to satisfy section 1400Z–2(d)(2)(D)(i)(III).

(4) *Trade or businesses described in section 144(c)(6)(B) not eligible*—(i) Pursuant to section 1400Z–2(d)(3)(A)(iii), the following trades or businesses, and businesses leasing more than a de minimis amount of property to the following trades or businesses, cannot qualify as a qualified opportunity zone business:

(A) Any private or commercial golf course;

(B) Country club;

(C) Massage parlor;

(D) Hot tub facility;

(E) Suntan facility;

(F) Racetrack or other facility used for gambling; or

(G) Any store the principal business of which is the sale of alcoholic beverages for consumption off premises.

(ii) De minimis amounts of gross income attributable to a business described in section 144(c)(6)(B) will not cause a trade or business to fail to be a qualified opportunity zone business.

(iii) The term *de minimis amount of property,* used in paragraph (d)(4)(i) of this section, means less than 5 percent of the net rentable square feet for real property and less than 5 percent of the value for all other tangible property. The term *de minimis amount of gross income,* used in paragraph (d)(4)(ii) of this section, means less than 5 percent of the gross income of the qualified opportunity zone business may be attributable to the types of business described in section 144(c)(6)(B).

(iv) The following examples illustrate the rules of paragraph (d)(4) of this section:

(A) *Example 1.* Entity A is a QOF that meets the requirements of section 1400Z–2(d)(1). Entity A owns qualified opportunity zone stock in a domestic corporation described in section 1400Z–2(d)(2)(B), which operates a hotel located in a qualified opportunity zone that qualifies as a trade or business. As part of that trade or business, the hotel operates a spa that provides massages and other therapies. Less than 5 percent of the hotel's total gross income is

attributable to the spa, and less than 5 percent of the net rentable square feet for real property and less than 5 percent of the value for all other tangible property is attributable to the spa. As a result, the operation of the spa, which is a business described in section 144(c)(6)(B), will not prevent the operation of the hotel from qualifying as a qualified opportunity zone business.

(B) *Example 2*—(*1*) *Facts.* Entity B is a qualified opportunity zone business that meets the requirements of section 1400Z–2(d)(3). Entity B plans to acquire a commercial golf course that consists of land and other related buildings and equipment in a qualified opportunity zone, that will satisfy each requirement for qualified opportunity zone business property set forth in section 1400Z–2(d)(2)(D). Instead of directly managing and operating the commercial golf course business, Entity B will lease the land and other related buildings and equipment to a third party to manage and operate the commercial golf course. The leased real property represents more than 5 percent of the net rentable square feet of Entity B's real property and the leased and other tangible property represents more than 5 percent of the value for all other tangible property of Entity B.

(*2*) *Analysis.* Because a golf course is prohibited from being a qualified trade or business under section 1400Z–2(d)(3)(A)(iii), the leasing arrangement will cause Entity B to fail to be a qualified opportunity zone business regardless of the satisfaction of each requirement set forth in section 1400Z–2(d)(2)(D).

(C) *Example 3*—(*1*) *Facts.* Entity B meets the explicit requirements of section 1400Z–2(d)(1) and has certified itself as a QOF. Entity B owns a commercial golf course that consists of land and other related buildings and equipment in a qualified opportunity zone, and the land and buildings satisfy all explicit requirements (in section 1400Z–2(d)(2)(D)) to be qualified opportunity zone business property. Entity B manages and operates the commercial golf course business, but does not manage or operate any other trade or business not described in section 144(c)(6)(B) (listing businesses not eligible to be a qualified opportunity zone business pursuant to section 1400Z–2(d)(3)(A)(iii)). Entity B chose to operate the commercial golf course through Entity B, rather than through a qualified opportunity zone business, in order to avoid the requirement in section 1400Z–2(d)(3)(A)(iii), which provides that a qualified opportunity zone business cannot operate a commercial golf course due to the inclusion of that trade or business in section 144(c)(6)(B).

(*2*) *Analysis.* The ownership and operation of the golf course at the QOF level will not disqualify the QOF because the prohibition on businesses described in section 144(c)(6)(B) is not applicable at the QOF level. In addition, if each requirement set forth in section 1400Z–2(d)(2)(D) is satisfied, the property used in the commercial golf course will qualify as qualified opportunity zone business property held by Entity B for purposes of section 1400Z–2(d)(2)(A).

(5) *Tangible property of a qualified opportunity zone business that ceases to be qualified opportunity zone business property.* For qualified opportunity zone businesses, tangible property that ceases to be qualified opportunity zone business property shall continue to be treated as qualified opportunity zone business property for the lesser of five years after the date on which such tangible property ceases to be so qualified or the date on which such tangible property is no longer held by the qualified opportunity zone business. However, tangible property is not eligible for the benefits provided in this paragraph (d)(5) unless the tangible property ceasing to qualify as qualified opportunity zone business property was qualified opportunity zone business property used by a qualified opportunity zone business in a qualified opportunity zone for two years. For purposes of this paragraph (d)(5), tangible property purchased, leased, or improved by a trade or business, that is treated as satisfying the requirements of section 1400Z–2(d)(2)(D)(i) during that working capital safe harbor period pursuant to paragraph (d)(3)(v) of this section or that 30-month substantial improvement period described in § 1.1400Z2(d)–2(b)(4), is not treated as used by a qualified opportunity zone business in a qualified opportunity zone for any portion of the two year period described in this paragraph (d)(5).

(6) *Cure period for qualified opportunity zone businesses.* (i) For purposes of the *90-percent qualified opportunity zone business holding period* requirements set forth in sections 1400Z–2(d)(2)(B)(i)(III), 1400Z–2(d)(2)(C)(iii), and 1400Z–2(d)(2)(D)(i)(III), if a trade or business causes the QOF to fail the *90-percent investment standard* on a semiannual testing date, the QOF may treat the stock or partnership interest in that business as qualified opportunity zone property for that semiannual testing date provided the business corrects the failure within 6 months of the date on which the stock or partnership interest lost its qualification.

(ii) If the failure occurs on the last testing date of the taxable year, the six-month cure period described in paragraph (d)(6)(i) of this section is available to the QOF only if the QOF files a valid application for an extension of time to file its tax return.

(iii) Each QOF is permitted only one correction pursuant to paragraph (d)(6) of this section. If the entity, at the end of the additional six-month cure period, fails to qualify as a qualified opportunity zone business, then the QOF becomes subject to the penalty under section 1400Z–2(f)(1) for each month the entity failed to qualify as a qualified opportunity zone business beginning with the first month following the last month that the QOF met the *90-percent investment standard.*

(e) *Applicability dates*—(1) *In general.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a taxpayer's first taxable year ending after December 21, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, a taxpayer may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(d)–1 contained in the notice of proposed rulemaking (REG–115420–18) published on October 29, 2018, as amplified by the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

■ **Par. 7.** Section 1.1400Z2(d)–2 is added to read as follows:

§ 1.1400Z2(d)–2 Qualified opportunity zone business property.

(a) *Qualified opportunity zone business property*—(1) *In general.* This section provides rules for determining whether owned or leased tangible property held by an eligible entity (within the meaning of § 1.1400Z2(d)–1(a)(1)) is qualified opportunity zone business property within the meaning of section 1400Z–2(d)(2)(D). Paragraph (a)(2) of this section provides general requirements that tangible property must satisfy to be qualified opportunity zone business property. Paragraph (b) of this section provides rules related to owned tangible property. Paragraph (c) of this section provides rules related to leased tangible property (that is, tangible property that the eligible entity acquires by lease from a lessor). Paragraph (d) of this section provides rules related to the 90-percent qualified opportunity zone business property holding period requirement and the 70-percent use test of section 1400Z–2(d)(2)(D)(i)(III). Paragraph (e) of this section provides the dates of applicability of this section.

(2) *Qualified opportunity zone business property requirements.* The term *qualified opportunity zone business property* means tangible property owned or leased by an eligible entity (as defined in § 1.1400Z2(d)–1(a)(1)) that—

(i) Is used by the eligible entity in a trade or business within the meaning of section 162; and

(ii) Satisfies the requirements of paragraphs (b), (c), and (d) of this section, as applicable.

(b) *Tangible property owned by an eligible entity*—(1) *Purchase requirement*—(i) *In general.* In the case of tangible property that is owned by an eligible entity, the tangible property must be acquired by the eligible entity after December 31, 2017, by purchase as defined by section 179(d)(2) from a person that is not a related person within the meaning of section 1400Z–2(e)(2) (providing that persons are related to each other if such persons are described in section 267(b) or section 707(b)(1), determined by substituting ''20 percent'' for ''50 percent'' each place it appears in such sections).

(ii) *Plan, intent, or expectation for seller to repurchase acquired property.* In the case of real property that is purchased by an eligible entity, if, at the time of the purchase, there was a plan, intent, or expectation for the acquired real property to be repurchased by the seller of the real property for an amount of consideration other than the fair market value of the real property, determined at the time of the repurchase by the seller, the purchased real property is not qualified opportunity zone business property.

(iii) *Property manufactured, constructed, or produced for use in a qualified opportunity zone*—(A) *In general.* In the case of tangible property manufactured, constructed, or produced by an eligible entity, if the property is manufactured, constructed, or produced for use by an eligible entity with the intent to use such property in a trade or business in a qualified opportunity zone, then such property satisfies the requirements of paragraph (b)(1)(i) of this section if the manufacture, construction, or production begins after December 31, 2017. The materials and supplies used to manufacture, construct, or produce qualified opportunity zone business property by the eligible entity must also be qualified opportunity zone business property.

(B) *Time when manufacture, construction or production considered to begin.* For purposes of paragraph (b)(1)(iii) of this section, the acquisition date of such property is the date on which the manufacture, construction, or production of property (as defined in paragraph (b)(1)(iii) of this section) begins. The manufacture, construction, or production of property begins when physical work of a significant nature begins. Physical work does not include preliminary activities such as planning or designing, securing financing, exploring or researching. The determination of when physical work of a significant nature begins depends on the facts and circumstances. For example, if a factory is to be constructed on-site, construction begins when physical work of a significant nature commences at the site; this could occur, for example, when work begins on the excavation of footings, or the pourings of pads for the factory. Preliminary work, such as clearing or testing of soil condition, does not constitute the beginning of construction.

(C) *Safe harbor.* For purposes of paragraph (b)(1)(iii)(B) of this section, a taxpayer may choose to determine when physical work of a significant nature begins in accordance with this paragraph (b)(1)(iii)(C). Physical work of a significant nature will not be considered to begin before the taxpayer incurs or pays more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities such as planning or designing, securing financing, exploring, or researching).

(2) *Original use or substantial improvement requirement*—(i) *In general.* In the case of tangible property owned by the eligible entity either—

(A) The original use of the owned tangible property in the qualified opportunity zone, within the meaning of paragraph (b)(3) of this section, must commence with the eligible entity; or

(B) The eligible entity must substantially improve the owned tangible property within the meaning of paragraph (b)(4) of this section (which defines substantial improvement in this context).

(ii) *Inventory.* Inventory (including raw materials) of a trade or business produced by an eligible entity after December 31, 2017, is deemed to satisfy the requirements set forth in paragraphs (b)(1) and (b)(2)(i) of this section.

(3) *Original use of tangible property acquired by purchase*—(i) *Original use*—(A) *In general.* For purposes of paragraph (b)(2) of this section, the original use of tangible property in a qualified opportunity zone commences on the date any person first places the property in service in the qualified opportunity zone for purposes of depreciation or amortization, or first uses it in a manner that would allow depreciation or amortization if that person were the property's owner.

(B) *Commencement of original use of vacant property.* For purposes of this paragraph (b)(3), if real property, including land and buildings, has been vacant for an uninterrupted period of at least one calendar year beginning on a date prior to the date on which the qualified opportunity zone in which the property is located is listed as a designated qualified opportunity zone in a QOZ designation notice and the property has remained vacant through the date on which the property was purchased by the eligible entity, or if the property has been vacant for an uninterrupted three calendar year period beginning on a date after the date of publication of the QOZ designation notice that lists as designated the qualified opportunity zone in which the property is located and the property has remained vacant through the date on which the property was purchased by the eligible entity, original use in the qualified opportunity zone commences on the date after that period when any person first so uses or places the property in service in the qualified opportunity zone. Such property must satisfy the definition of vacancy under paragraph (b)(3)(iii) of this section.

(C) *Used tangible property.* Used tangible property satisfies the original use requirement if the property has not been previously so used or placed in service in the qualified opportunity zone. If the tangible property had been so used or placed in service in the qualified opportunity zone before it is acquired by purchase, it must be substantially improved in order to satisfy the requirements of section 1400Z–2(d)(2)(D)(i)(II).

(D) *Example.* The following example illustrates the principles of paragraph (b)(3)(i)(A) of this section.

(*1*) *Facts.* On January 1, 2019, QOF A purchases from a developer a newly constructed hotel building located in a qualified opportunity zone for $10 million. The developer purchased a parcel of land in that qualified opportunity zone, and constructed the hotel building thereon, with the intent and expectation to sell the building to a QOF. As of the time of the purchase, the developer had not placed the hotel building in service in the qualified opportunity zone for purposes of depreciation. Other than the original use requirement, assume that the hotel building satisfies all requirements under section 1400Z–2(d)(2)(D). In addition, assume that, at the time of the purchase, the developer had no plan, intent, or expectation to repurchase the hotel building.

(*2*) *Analysis.* At the time of QOF A's purchase of the hotel building, the original use of the hotel building had not commenced because the developer had not yet placed the hotel building into service for purposes of depreciation in a qualified opportunity zone. See paragraph (b)(3)(i)(A) of this section. Therefore, the original use of the hotel building in the qualified opportunity zone in which the building is located is treated as commencing with QOF A. See paragraph (b)(3)(i)(A) of this section. As a result, the hotel building purchased by QOF A is treated as satisfying the original use requirement of section 1400Z–2(d)(2)(D)(i)(II).

(ii) *Lessee improvements to leased property.* Improvements made by a lessee to leased property satisfy the original use requirement in section 1400Z–2(d)(2)(D)(i)(II) as purchased property for the amount of the unadjusted cost basis under section 1012 of such improvements.

(iii) *Vacancy.* Solely for purposes of meeting the requirements of section 1400Z–2, real property, including land and buildings, is considered to be in a state of vacancy if the property is significantly unused. A building or land will be considered significantly unused if more than 80 percent of the building or land, as measured by the square footage of useable space, is not currently being used.

(iv) *Brownfield sites.* An eligible entity that purchases a parcel of land that is a brownfield site, as defined by section 101 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. 9601) (brownfield site), may treat all property composing the brownfield site (including the land and structures thereon) as satisfying the original use requirement of section 1400Z–2(d)(2)(D)(i)(II), if, within a reasonable period, the eligible entity makes investments in the brownfield site to ensure that all property composing the brownfield site meets basic safety standards for both human health and the environment.

(v) *Property involuntarily transferred to local government.* An eligible entity that purchases real property from a local government that the local government holds as the result of an involuntary transfer (including through abandonment, bankruptcy, foreclosure, or receivership) may treat all property composing the real property (including the land and structures thereon) as satisfying the original use requirement of section 1400Z–2(d)(2)(D)(i)(II).

(4) *Substantial improvement of tangible property acquired by purchase*—(i) *In general.* Except as provided in paragraph (b)(4)(iv) of this section, for purposes of paragraph (b)(2) of this section, tangible property is treated as substantially improved by an eligible entity only if it meets the requirements of section 1400Z–2(d)(2)(D)(ii) during the *30-month substantial improvement period.* The property has been substantially improved when the additions to basis of the property in the hands of the QOF exceed an amount equal to the adjusted basis of such property at the beginning of such 30-month period in the hands of the QOF (substantial improvement requirement).

(ii) *Treatment of property in the 30-month substantial improvement period.* For purposes of the *90-percent investment standard* under section 1400Z–2(d)(1), tangible property purchased, leased, or improved by a trade or business that is undergoing the substantial improvement process but has not yet been placed in service by the eligible entity or used in the eligible entity's trade or business is treated as satisfying the requirements of section 1400Z–2(d)(2)(D)(i) and paragraph (b)(2) of this section for the *30-month substantial improvement period* with respect to that property provided the eligible entity reasonably expects that the property will be substantially improved as defined in paragraph (b)(4)(i) of this section and used in the eligible entity's trade or business in a qualified opportunity zone by the end of such 30-month period. Tangible property described in the preceding sentence is not considered qualified opportunity zone business property for purposes of the special rule in section 1400Z–2(d)(3)(B) unless the tangible property is qualified opportunity zone business property for at least two years without regard to this paragraph (b)(4)(ii).

(iii) *Aggregation of original use property that improves the functionality of non-original use property*—(A) *General rule.* The cost of purchased property that would otherwise qualify as qualified opportunity zone business property may be taken into account in determining whether additions to the basis of non-original use property acquired by purchase satisfy the substantial improvement requirement under section 1400Z–2(d)(2)(D)(ii), so long as the purchased property is located in the same qualified opportunity zone (or a contiguous qualified opportunity zone) as the non-original use property, is used in the same trade or business as the non-original use property, and improves the functionality of the non-original use property.

(B) *Improvement of non-original use real property.* If an eligible entity chooses to apply this paragraph (b)(4)(iii) to non-original use real property, the eligible entity must improve the non-original use real property by more than an insubstantial amount within the meaning of paragraph (b)(4)(iv)(C) of this section.

(C) *Effect on purchased property.* If an eligible entity chooses to apply this paragraph (b)(4)(iii), the purchased property that would otherwise qualify as qualified opportunity zone business property will not be treated as original use property, and instead the basis of that purchased property will be taken into account in determining whether additions to the basis of the non-original use property satisfy the requirements under section 1400Z–2(d)(2)(D)(i)(II) and (d)(2)(D)(ii).

(D) *Examples.* The following examples illustrate the principles of paragraph (b)(4)(iii) of this section.

(*1*) *Example 1*—(*i*) *Facts.* On January 1, 2019, QOF A purchases the assets of a hotel business located in a qualified opportunity zone for $5 million. The purchased assets include land, a building, linens, furniture and other fixtures attached to the building. $1 million of the purchase price is allocated to land and the remaining $4 million is allocated to the building, furniture and fixtures. During the course of renovations over the 30-month substantial improvement period, the QOF spent $1 million replacing linens, mattresses and furniture, $500,000 on the purchase of new exercise equipment for a gym located in the hotel building, $1 million on renovations for a restaurant (including restaurant equipment) attached to the hotel, and $1.5 million on structural renovations to the hotel. The QOF chooses to apply paragraph (b)(4)(iii) of this section to determine whether the substantial improvement requirement in section 1400Z–2(d)(2)(D)(ii) is met.

(*ii*) *Analysis.* In order for the hotel to be considered qualified opportunity zone business property, QOF A must substantially improve the hotel as the hotel had previously been placed in service in the qualified opportunity zone. (QOF A was not required to substantially improve the land on which the hotel was located pursuant to paragraph (b)(4)(iv) of this section.) Because the amount of basis allocated to the hotel was $4 million, QOF A must expend $4 million to improve the hotel within the 30-month substantial improvement period provided in section 1400Z–2(d)(2)(D)(ii). The new linens, mattresses and furniture, new exercise equipment, and new restaurant equipment all qualify as original use assets under section 1400Z–2(d)(2)(D)(i)(II). QOF A also substantially improved the hotel, which was the asset that needed to be improved under section 1400Z–2(d)(2)(D)(i)(II). QOF A chose, at the start of the 30-month period, to include the costs of the newly purchased assets that improve the functionality of the hotel to the basis of the hotel. Thus, the cost of these items is eligible to be added to the hotel's basis pursuant to paragraph (b)(4)(iii) of this section. Therefore, QOF A has met the substantial improvement requirement under section 1400Z–2(d)(2)(D)(i)(II) by doubling its basis in the hotel and its fixtures within the 30-month substantial improvement period. The amounts spent replacing linens, mattresses, furniture, exercise equipment, and new restaurant equipment that were counted toward the substantial improvement requirement for the hotel are not considered original use assets for purposes of the *90-percent investment standard.*

(*2*) *Example 2*—(*i*) *Purchase of unrelated property.* The facts are the same as in paragraph (b)(4)(iii)(D)(*1*)(*i*) of this section, except that in addition to purchasing the

hotel and the related land, QOF A also purchases an apartment building one block away from the hotel for $10 million. The apartment building is located in the same qualified opportunity zone as the hotel.

(*ii*) *Analysis.* QOF A may not include any improvements made to the apartment building, including purchased property that improves the functionality of the apartment building, to the basis of the hotel. QOF A may choose, under paragraph (b)(4)(iii) of this section, to include the purchased property that improves the functionality of the apartment building in the basis of the apartment building for purposes of the substantial improvement requirement under section 1400Z–2(d)(2)(D)(i)(II).

(iv) *Special rules for land and improvements on land*—(A) *Buildings located in a qualified opportunity zone.* In accordance with the rules set forth in this paragraph (b)(4)(iv)(A), if an eligible entity purchases a building located on a parcel of land within the geographic borders of a qualified opportunity zone, for purposes of section 1400Z–2(d)(2)(D)(ii), a substantial improvement to the building is measured by the eligible entity's additions to the basis of the building, as determined under section 1012.

(B) *Unimproved land.* Unimproved land that is within a qualified opportunity zone and acquired by purchase in accordance with section 1400Z–2(d)(2)(D)(i)(I) is not required to be substantially improved within the meaning of section 1400Z–2(d)(2)(D)(i)(II) and (d)(2)(D)(ii).

(C) *Exception for insubstantially improved land.* Notwithstanding paragraph (b)(4)(iv)(B) of this section, if the land is unimproved or minimally improved and the eligible entity purchases the land with an expectation or an intention to not improve the land by more than an insubstantial amount within 30 months after the date of purchase, paragraph (b)(4)(iv)(B) of this section does not apply with respect to such land and such land is not considered qualified opportunity zone business property unless it is substantially improved within the meaning of sections 1400Z–2(d)(2)(D)(i)(II) and (d)(2)(D)(ii). In determining whether an eligible entity had an expectation or an intention to improve the land by more than an insubstantial amount, improvements to the land by the eligible entity (including grading, clearing of the land, remediation of the contaminated land, or acquisition of related qualified opportunity zone business property that facilitates the use of the land in a trade or business of the eligible entity) will be taken into account.

(D) *Remediation of contaminated land.* Betterments to land within the meaning of § 1.263(a)–3(j)(1)(i) may be added to the basis of the purchased land and included for purposes of section 1400Z–2(d)(2)(D)(ii) if the betterments are paid for by the eligible entity.

(E) *Separate improvement to underlying land not required.* In determining whether the substantial improvement test under section 1400Z–2(d)(2)(D) has been met with respect to a building, there is no requirement that the eligible entity separately substantially improve the land upon which the building is located.

(v) *Aggregation of purchased buildings*—(A) *Substantial improvement requirement for eligible building group.* For purposes of applying the substantial improvement requirement under sections 1400Z–2(d)(2)(D)(i)(II) and 1400Z–2(d)(2)(D)(ii), an eligible entity may apply paragraph (b)(4)(v)(D) of this section with respect to two or more buildings located within a qualified opportunity zone or a single series of contiguous qualified opportunity zones, as described in paragraph (b)(4)(v)(B) or (C) of this section (eligible building group), respectively.

(B) *Eligible building group located entirely within parcel of land described in single deed.* All buildings comprising an eligible building group may be treated as a single property as that term is used in section 1400Z–2(d)(2)(D)(ii) (single property), if each building comprising the eligible building group is located entirely within the geographic borders of a parcel of land described in a single deed.

(C) *Eligible building group spanning contiguous parcels of land described in separate deeds.* An eligible entity may treat all buildings comprising an eligible building group located entirely within the geographic borders of contiguous parcels of land described in separate deeds as a single property to the extent each building is operated as part of one or more trades or businesses that—

(*1*) Are operated exclusively by the eligible entity;

(*2*) Share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources; and

(*3*) Are operated in coordination with, or reliance upon, one or more of the trades or businesses (for example, supply chain interdependencies or mixed-use facilities).

(D) *Calculation of aggregate building basis and additions to basis of single property*—(*1*) *In general.* For purposes of the substantial improvement requirement under section 1400Z–2(d)(2)(D)(ii), the amount of basis required to be added to the portion of an eligible building group treated as a single property equals the total amount of basis calculated by adding the basis of each building comprising the single property at the beginning of the 30-month period and additions to the basis of each building comprising the single property are aggregated to determine satisfaction of the substantial improvement requirement.

(*2*) *Aggregation of original use property that improves the functionality of single property.* In applying paragraph (b)(4)(v)(D)(*1*) of this section, purchased property that would otherwise qualify as qualified opportunity zone business property may be taken into account in determining whether additions to the basis of a single property described in paragraph (b)(4)(v)(B) or (C) of this section satisfy the substantial improvement requirement under section 1400Z–2(d)(2)(D)(ii).

(c) *Tangible property leased by an eligible entity.* In the case of tangible property with respect to which an eligible entity is a lessee—

(1) *Qualifying acquisition of possession.* The tangible property must be acquired by the eligible entity under a lease entered into after December 31, 2017.

(2) *Arms-length terms*—(i) *General rule.* The terms of the lease must be market rate (that is, the terms of the lease reflect common, arms-length market pricing in the locale that includes the qualified opportunity zone as determined under section 482 and all section 482 regulations in this chapter) at the time that the lease was entered into.

(ii) *Rebuttable presumption regarding unrelated persons.* There will be a rebuttable presumption that the terms of the lease were market rate for leases between persons not related within the meaning of section 1400Z–2(e)(2) (unrelated persons), and thus, the parties to the lease are not required to perform a section 482 analysis.

(iii) *Exception for state, local, and Indian tribal governments.* For purposes of this paragraph (c)(2), tangible property acquired by lease from a state or local government, or an Indian tribal government, is not considered tangible property acquired by lease from a related person within the meaning of section 1400Z–2(e)(2) (related person).

(3) *Additional requirements for tangible property leased from a related person.* If the lessor is a related person with respect to an eligible entity that is the lessee of tangible property, the requirements of paragraphs (c)(3)(i) and (ii) of this section, as applicable, must

be satisfied in order for the tangible property to be treated as qualified opportunity zone business property.

(i) *Prepayments of not more than one year.* The lessee at no time makes any prepayment in connection with the lease relating to a period of use of the tangible property that exceeds 12 months.

(ii) *Purchase of other qualified opportunity zone business property.* In the case of leased tangible property that is personal property, if the original use of the leased tangible personal property in a qualified opportunity zone (within the meaning of paragraph (c)(3)(iii) of this section) does not commence with the lessee, the property is not qualified opportunity zone business property unless, during the relevant testing period (as defined in paragraph (c)(3)(iv) of this section), the lessee becomes the owner of tangible property that is qualified opportunity zone business property having a value not less than the value of that leased tangible personal property. There must be substantial overlap of the qualified opportunity zone(s) in which the owner of the tangible property so acquired uses it and the qualified opportunity zone(s) in which that person uses the leased tangible personal property.

(iii) *Original use of leased tangible property*—(A) *In general.* For purposes of paragraph (c)(3)(ii) of this section, the original use of leased tangible property in a qualified opportunity zone commences on the date any person first places the property in service in the qualified opportunity zone for purposes of depreciation (or first uses the property in the qualified opportunity zone in a manner that would allow depreciation or amortization if that person were the property's owner).

(B) *Used leased tangible property.* Used leased tangible personal property can satisfy the original use requirement if the property has not been previously so used or placed in service in the qualified opportunity zone.

(iv) *Relevant testing period.* For purposes of paragraph (c)(3)(ii) of this section, the *relevant testing period* is the period that begins on the date that the lessee receives possession under the lease of the leased tangible personal property and ends on the earlier of—

(A) The date 30-months after the date the lessee receives possession of the leased tangible personal property under the lease; or

(B) The last day of the term of the lease (within the meaning of § 1.1400Z2(d)–1(b)(4)(iii)(D)).

(4) *Plan, intent, or expectation for purchases not for fair market value.* In the case of real property that is leased by an eligible entity, if, at the time the lease is entered into, there was a plan, intent, or expectation for the real property to be purchased by the eligible entity for an amount of consideration other than the fair market value of the real property determined at the time of the purchase without regard to any prior lease payments, the leased real property is not qualified opportunity zone business property.

(d) *Holding period and use within a qualified opportunity zone of owned or leased tangible property*—(1) *In general.* In the case of tangible property that is owned or leased by an eligible entity, during substantially all of the eligible entity's holding period for the tangible property, substantially all of the use of the tangible property must be in a qualified opportunity zone.

(2) *Valuation of owned and leased property.* For purposes of the 70-percent use test in paragraph (d)(4) of this section, the value of owned and leased property is required to be determined in accordance with the valuation methodologies provided in § 1.1400Z2(d)–1(b), and such value in the case of leased tangible personal property is to be determined on the date the lessee receives possession of the tangible personal property under the lease.

(3) *Substantially all of an eligible entity's holding period for owned or leased tangible property*—(i) *In general.* For purposes of determining whether the holding period requirement in paragraph (d)(1) of this section is satisfied, the term *substantially all* means at least 90 percent. The holding period requirement is applied on a semiannual basis, based on the entire amount of time the eligible entity has owned or leased such property. Thus, on each semiannual testing date of the eligible entity, the tangible property satisfies the 90-percent qualified opportunity zone business property holding period requirement of section 1400Z–2(d)(2)(D)(i)(III) only if, during at least 90 percent of the period during which the QOF has owned or leased the property, the property has satisfied the 70-percent use test in paragraph (d)(4) of this section.

(ii) *Semiannual qualified opportunity zone business test.* For purposes of determining satisfaction of the 90-percent qualified opportunity zone business property holding period test described in paragraph (d)(3)(i) of this section in the case of a QOF, the determination of whether property satisfies the 70-percent use test is made on a semiannual basis pursuant to section 1400Z–2(d)(1) and paragraph (d)(4) of this section.

(4) *Substantially all of the use of owned or leased tangible property in a qualified opportunity zone*—(i) *70-percent use test.* Tangible property used in a trade or business of an eligible entity satisfies the *substantially all* requirement of paragraph (d)(2)(i) of this section (that is, the 70-percent use test) if and only if the tangible property is qualified tangible property. Qualified tangible property is tangible property that satisfies the requirements of paragraph (d)(4)(ii), (iii) (subject to the limitation in paragraph (d)(4)(iv) of this section), or (v) of this section.

(ii) *Qualified tangible property.* Tangible property held by a trade or business is qualified tangible property to the extent, based on the number of days between two consecutive semiannual testing dates, not less than 70 percent of the total utilization of the tangible property by the trade or business occurs at a location within the geographic borders of a qualified opportunity zone.

(iii) *Safe harbor for tangible property utilized in rendering services inside and outside of a qualified opportunity zone.* Subject to the limitation described in paragraph (d)(4)(iv) of this section, tangible property utilized by a trade or business in rendering services both inside and outside of the geographic borders of a qualified opportunity zone may be treated as qualified tangible property if—

(A) The tangible property utilized in rendering the service directly generates gross income for the trade or business both inside and outside of the geographic borders of a qualified opportunity zone;

(B) The trade or business has an office or other facility located within the geographic borders of a qualified opportunity zone (QOZ office);

(C) The tangible property is operated by employees of the trade or business who—

(*1*) Regularly use a QOZ office of the trade or business in the course of carrying out their duties; and

(*2*) Are managed directly, actively, and substantially on a day-to-day basis by one or more employees of the trade or business who carry out their duties at a QOZ office; and

(D) The tangible property is not operated exclusively outside of the geographic borders of a qualified opportunity zone for a period longer than 14 consecutive days for the generation of gross income for the trade or business.

(iv) *Limitation.* For purposes of the *70-percent tangible property standard,* the safe harbor provided in paragraph (d)(4)(iii) of this section may not be used

to treat more than 20 percent of the tangible property of the trade or business as qualified tangible property.

(v) *Safe harbor for tangible property owned by leasing businesses with QOZ offices.* Tangible property of a trade or business, the employees of which use a QOZ office of the trade or business to regularly lease such tangible property to customers of the trade or business, may be treated as qualified tangible property if—

(A) Consistent with the normal, usual, or customary conduct of the trade or business, when not subject to a lease to a customer of the trade or business, the tangible property is parked or otherwise stored at a QOZ office; and

(B) No lease under which a customer of the trade or business acquires possession of the tangible property is for a duration (including extensions) longer than 30 consecutive days.

(vi) *Use of tangible property in one or more qualified opportunity zones.* In accordance with paragraphs (d)(4)(ii) through (v) of this section, if qualified tangible property is utilized by the trade or business in one or more qualified opportunity zones, satisfaction of the 70-percent use test is determined by aggregating the number of days the tangible property is utilized by the trade or business in each qualified opportunity zone.

(vii) *Real property straddling a qualified opportunity zone.* For purposes of satisfying the requirements in this paragraph (d), the rules of § 1.1400Z2(d)–1(d)(3)(ix) apply to a QOF or qualified opportunity zone business for determining whether real property is situated in a qualified opportunity zone.

(viii) *Safe harbor for inventory in transit*—(A) *In general.* In determining whether tangible property is used in a qualified opportunity zone for purposes of applying the 70-percent use test under paragraph (d)(4) of this section, inventory (including raw materials) of a trade or business does not fail to be used in a qualified opportunity zone solely because the inventory is in transit—

(*1*) From a vendor to a facility of the trade or business that is in a qualified opportunity zone; or

(*2*) From a facility of the trade or business that is in a qualified opportunity zone to customers of the trade or business that are not located in a qualified opportunity zone.

(B) *No effect from certain events in transit.* The distance traveled by the inventory while it is in transit, or the fact that the inventory is briefly warehoused while in transit, does not affect the application of the safe harbor described in paragraph (d)(4)(viii) of this section.

(e) *Applicability dates*—(1) *In general.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a taxpayer's first taxable year ending after December 21, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, a taxpayer may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(d)–1 contained in the notice of proposed rulemaking (REG–115420–18) published on October 29, 2018, as amplified by the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

§ 1.1400Z2(e)–1 [Added and Reserved]

■ **Par. 8.** Reserved § 1.1400Z2(e)–1 is added.

■ **Par. 9.** Section 1.1400Z2(f)–1 is added to read as follows:

§ 1.1400Z2(f)–1 Administrative rules-penalties, anti-abuse, etc.

(a) *In general.* Except as provided by § 1.1400Z2(d)–1(a)(2)(iv)(B) with respect to a taxpayer's first taxable year as a QOF, if a QOF fails to satisfy the 90-percent investment standard in section 1400Z–2(d)(1), then the QOF must pay the statutory penalty set forth in section 1400Z–2(f) for each month it fails to meet the 90-percent investment standard.

(b) *Time period for a QOF to reinvest certain proceeds*—(1) *In general.* If a QOF receives proceeds from the return of capital or the sale or disposition of some or all of its qualified opportunity zone property within the meaning of section 1400Z–2(d)(2)(A), and if the QOF reinvests some or all of the proceeds in qualified opportunity zone property by the last day of the 12-month period beginning on the date of the distribution, sale, or disposition, then the proceeds, to the extent that they are so reinvested, are treated as qualified opportunity zone property for purposes of the 90-percent investment standard in section 1400Z–2(d)(1), but only to the extent that prior to the reinvestment in qualified opportunity zone property the proceeds are continuously held in cash, cash equivalents, or debt instruments with a term of 18 months or less. If reinvestment of the proceeds is delayed by waiting for governmental action the application for which is complete, that delay does not cause a failure of the 12-month requirement in this paragraph (b).

(2) *Federally declared disasters.* If the QOF's plan to reinvest some or all of the proceeds described in paragraph (b)(1) of this section in qualified opportunity zone property is delayed due to a federally declared disaster (as defined in section 165(i)(5)(A)), the QOF may receive up to an additional 12 months to reinvest such proceeds, provided that the QOF invests such proceeds in the manner originally intended before the disaster.

(c) *Anti-abuse rules*—(1) *General anti-abuse rule.* Pursuant to section 1400Z–2(e)(4)(C), the rules of section 1400Z–2 and §§ 1.1400Z2(a)–1 through 1.1400Z2(d)–(2), 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 must be applied in a manner consistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations (as defined in § 1.1400Z2(a)–1(b)(41)). The purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified Federal income tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and qualified opportunity zone businesses, of new capital in one or more qualified opportunity zones and to increase the economic growth of such qualified opportunity zones. Accordingly, if a significant purpose of a transaction is to achieve a Federal income tax result that is inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations, a transaction (or series of transactions) will be recast or recharacterized for Federal tax purposes as appropriate to achieve tax results that are consistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. This recasting and recharacterization may include, as appropriate, treating an investment as other than a qualifying investment. A determination of whether a Federal income tax result is inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations must be based on all facts and circumstances.

(2) *Special anti-abuse rule for partnerships*—(i) *In general.* In addition to being subject to the general anti-abuse rule of paragraph (c)(1) of this section, the application of the rules of section 1400Z–2 and §§ 1.1400Z2(a)–1 through 1.1400Z2(d)–2, 1.1400Z2(f)–1, 1.1502–14Z, and 1.1504–3 to partnerships is also subject to the special anti-abuse rule set forth in paragraph (c)(2)(ii) of this section.

(ii) *Special partnership anti-abuse rule.* If a partnership is formed or availed of with a significant purpose of

avoiding the requirements of § 1.1400Z2(a)–1(b)(11)(i)(B) that a gain be subject to Federal income tax in order to be an eligible gain, the partnership will be disregarded in whole or in part for purposes of § 1.1400Z2(a)–1(b)(11)(i)(B) and (b)(11)(ix)(B) to prevent the creation of a qualifying investment by the partnership with respect to any partner or partners that would not otherwise satisfy such requirements.

(3) *Examples.* The following examples illustrate the anti-abuse rule of paragraph (c) of this section.

(i) *Example 1*—(A) *Facts.* Two nonresident alien individuals (collectively, the individuals) plan to sell stock at a gain of $50, to invest the amount of the resulting capital gain in a QOF, and to make a deferral election under section 1400Z–2(a). They make this election with the intent of holding the QOF investment for 10 years and then making an election to increase the qualifying basis to fair market value under section 1400Z–2(c). A gain on a sale of the stock by the individuals, however, would not be subject to Federal income tax, and so the gain would not support their making a deferral election as a result of the requirement in § 1.1400Z2(a)–1(b)(11)(i)(B). Instead of selling the stock themselves, the individuals form a domestic partnership with a significant purpose of using that partnership to make a deferral election with respect to the stock under the exception in § 1.1400Z2(a)–1(b)(11)(ix)(B). The individuals contribute their stock to the partnership in exchange for partnership interests, after which the partnership sells the stock and invests the $50 gain in a QOF. Had the partnership not made a deferral election, the individuals would not be subject to tax on their allocated portion of the partnership's recognized gain on the sale of the stock.

(B) *Analysis.* Based on these facts, the partnership is formed and availed of with a significant purpose to avoid the requirements of § 1.1400Z2(a)–1(b)(11)(i)(B). Thus, under paragraph (c)(2) of this section, the partnership is disregarded for purposes of applying § 1.1400Z2(a)–1(b)(11)(ix)(B) to the $50 gain, and therefore the partnership's investment in the QOF is not a qualifying investment.

(ii) *Example 2*—(A) *Facts.* The facts are the same as in paragraph (c)(3)(i)(A) of this section (*Example 1*), except the individuals contribute their stock to an existing partnership, the sole partners of which are U.S. citizens, with a significant purpose of the individuals' use of the partnership being to make an investment in a QOF and a deferral election under the § 1.1400Z2(a)–1(b)(11)(ix)(B) exception for partnerships. During the year, the partnership sells property it owned before the individuals' contribution, resulting in capital gain of $100, all of which is eligible to be invested in a QOF. It also sells the stock contributed by the individuals, resulting in $50 of capital gain. The partnership invests $150 in a QOF and makes the requisite gain deferral election.

(B) *Analysis.* Based on these facts, the partnership is availed of by the individuals with a significant purpose to avoid the requirements of § 1.1400Z2(a)–1(b)(11)(i)(B). Thus, under paragraph (c)(2) of this section, the partnership is disregarded for purposes of applying § 1.1400Z2(a)–1(b)(11)(i)(B) and (b)(11)(ix)(B) with respect to the $50 capital gain from the sale of the individuals' contributed stock and that gain fails to be eligible gain. Under § 1.1400Z2(a)–1(b), no section 1400Z–2(a) election is available for that gain and the partnership will have a mixed-funds investment, $100 of which is a qualifying investment and $50 of which is a non-qualifying investment.

(iii) *Example 3*—(A) *Facts.* Entity C is a QOF that meets the requirements of section 1400Z–2(d)(1). Entity C owns qualified opportunity zone stock in a domestic corporation described in section 1400Z–2(d)(2)(B) (Corporation C), which operates a qualified opportunity zone business. Entity C also owns Corporation D stock, which is not qualified opportunity zone stock, which stock is less than 10% of the assets of Entity C. Under section 1400Z–2(e)(2), these stock holdings cause Entity C to be related to both Corporation C and Corporation D. On date 1, under section 1400Z–2(e)(2), Individual S is not a related person with respect to Entity C, Corporation C, or Corporation D. On that date, Individual S sells tangible property to Corporation C for use in Corporation C's qualified opportunity zone business and sells a second asset to Corporation D. Both items sold were capital assets (as defined in section 1221). As a result, Individual S realizes gain of $100 from the sale to Corporation C and $75 from the sale to Corporation D. At the time of the sale Individual S has a plan or intent to invest $175 in Entity C and to make deferral elections under section 1400Z–2(a)(1) with respect to the gain from the two sales. On date 2, for $175 Individual S acquired an eligible interest in Entity C, an acquisition that causes Individual S to become a related person with respect to Entity C within the meaning of section 1400Z–2(e)(2).

(B) *Analysis.* Under paragraph (c)(1) of this section, Individual S's $175 gain is not an eligible gain and cannot be the subject a deferral election under section 1400Z–2(a)(1). The gain fails to satisfy § 1.1400Z2a–1(b)(11)(i)(C) because of Individual S's plan to acquire sufficient equity in Entity C to become related to Corporations C and D. Moreover, for the same reason, the tangible property that Corporation C purchased from Individual S fails to satisfy the requirement that a purchase of qualified opportunity zone business property must be from an unrelated person. See sections 1400Z–2(d)(2)(D)(i)(I) and 179(d)(2)(A).

(iv) *Example 4*—(A) *Facts.* Entity D is a QOF that meets the requirements of section 1400Z–2(d)(1). Entity D owns a majority qualified opportunity zone partnership interest in a domestic partnership, Partnership D described in section 1400Z–2(d)(2)(C). Entity D organized Partnership D for the purpose of being a qualified opportunity zone business. Partnership D acquires a tract of land located in a qualified opportunity zone. At the time of the acquisition of that land, there was no plan or intent to develop or otherwise utilize the land in a trade or business that would increase substantially the economic productivity of the land. Instead, there was a plan to pave the land for use as a parking lot. Partnership D planned to install a gate to the paved parking area, a small structure that would serve as an office for a parking attendant, and two self-pay stations for use by customers. The parking lot was not reasonably expected to expand significantly, and the initial small number of employees was not reasonably expected significantly to increase. A significant purpose for the acquisition of the land was to sell the land at a profit and to exclude any gain from appreciation by making an election under section 1400Z–2(c).

(B) *Analysis.* Under paragraph (c)(1) of this section, the acquisition of the land is a transaction carried out to achieve a tax result that is inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. Consequently, the land is not qualified opportunity zone business property and gain from the sale of the land will not be eligible to be excluded from gross income under section 1400Z–2(c). This recharacterization of the qualification of the land for Federal tax purposes is appropriate to ensure that the tax results of the transaction, including the status of Partnership D as a qualified opportunity zone business, are consistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. Partnership D fails to be a qualified opportunity zone business unless other assets that it owns or leases are qualified opportunity zone business property that satisfy section 1400Z–2(d)(3)(A)(i), and the other requirements of section 1400Z–2 and the section 1400Z–2 regulations.

(v) *Example 5*—(A) *Facts.* The facts are the same as in paragraph (c)(3)(iv) of this section, except that Partnership D, in year 1, acquired a tract of land located in a qualified opportunity zone that was previously used for hog and pig farming. On its Form 1065T the previous owner, also a partnership, properly described those activities with the principal business activity code 112210. During the several-year period ending on the date of the acquisition of the land, the value of the land had significantly increased and D projected the land to continue to increase in value by ten-fold during the following 10-year period. At the time of the acquisition, Partnership D intended to conduct sheep and goat farming activities on the land and, accordingly, planned to use principal business activity code 112400 on its Form 1065. According to its plan, Partnership D conducted sheep and goat farming activities on the land during the 10-year period beginning on the date of acquisition of the land. During the 10-year period, Partnership D made significant capital improvements to the land, including improvements to existing farm structures, construction of new farm structures, and installation of a new irrigation system. As expected, the value of the land substantially increased during the following decade. The owners' entire interest in Partnership D was a qualifying investment, and, after having held it for at least 10 years

the owners sold the entire interest at a large gain. As planned the owners made an election under section 1400Z–2(c) in order to avoid tax on the gain from the sale.

(B) *Analysis.* The modification of the land to suit sheep and goat farming activity from its previous use of hog and pig farming and the significant capital improvements made to land, is a significant investment in the business activities on the land. Thus, Partnership D did not hold the land solely for speculative investment. As a result, under paragraph (c)(1) of this section, the acquisition of the land, the activities conducted on the land, the capital improvements made to the land, and the later disposition of the land for a significant profit are not inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations.

(vi) *Example 6*—(A) *Facts.* Individuals intend to sell stock at a capital gain and invest the resulting gain in a QOF pursuant to a deferral election under section 1400Z–2(a). The individuals form Entity F and file Form 8996 certifying that Entity F is a QOF organized for the purpose of investing in qualified opportunity zone property. Individuals have no intention of investing in qualified opportunity zone property. Instead individuals intend to invest in property other than qualified opportunity zone property hoping that the property will appreciate substantially in value and the individuals will be able to exclude any appreciation on their investment from gross income by making an election under section 1400Z–2(c). Each year Entity F files Form 8996 and pays the applicable penalty under section 1400Z–2(f). After holding their interests in Entity F for 10 years, individuals sell their interest in Entity F to an unrelated third party for a substantial gain and make an election to exclude the appreciation on their investment under section 1400Z–2(c).

(B) *Analysis.* A significant purpose of the transaction is to achieve a tax result that is inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations, and the transaction will be recast and recharacterized for Federal tax purposes so that Entity F is not a QOF and the individuals are not eligible for the elections under sections 1400Z–2(a) and (c).

(vii) *Example 7*—(A) *Facts.* Entity E treats itself as a QOF that meets the requirements of section 1400Z–2(d)(1). Entity E owns all of the stock in a domestic corporation, Corporation E, and Entity E treats this stock as qualified opportunity zone stock. Corporation E uses the majority of the cash invested by Entity E to purchase gold bars from unrelated parties within the meaning of section 1400Z–2(e)(2). The aggregate value of the gold bars is $1000. Corporation E rents a safe deposit box in a qualified opportunity zone and hires one employee to manage the purchase and sale of the gold bars. Each year Corporation E purchases a small number of additional gold bars and sells to customers a portion of the gold bars on hand. The aggregate value of both the purchases and sales approximates half the value of the bars held at the beginning of the year. Corporation E seeks to treat the gold bars as qualified opportunity zone business property within the meaning of section 1400Z–2(d)(3). At the time that Corporation E began the gold bar business, it did not reasonably expect the business to expand significantly, nor was the number of employees reasonably expected to increase. Gold, however, was reasonably expected to appreciate. Ten years after the formation of Entity E, the investors in Entity E sell all of their interests in the entity and seek to make an election under section 1400Z–2(c) to exclude any gain from appreciation.

(B) *Analysis.* Under paragraph (c)(1) of this section, a significant purpose of Corporation E's activities is to achieve a tax result that is inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. The gold bar business carried out by Corporation E was merely speculative in nature and was not expected to increase economic activity in the subject qualified opportunity zone in a manner consistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. As a result, Corporation E's activities are carried on to achieve tax results that are inconsistent with the purposes of section 1400Z–2 and the section 1400Z–2 regulations. Consequently, the gold bars are not qualified opportunity zone property. Corporation E fails to be a qualified opportunity zone business unless other assets that it owns or leases are qualified opportunity zone business property that satisfy section 1400Z–2(d)(3)(A)(i) (along with other requirements). If Corporation E fails to be a qualified opportunity zone business, Corporation E's stock fails to be qualified opportunity zone property in the hands of Entity E.

(d) *Applicability date*—(1) *In general.* The provisions of this section are applicable for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a taxpayer's first taxable year ending after December 21, 2017, that began on December March 13, 2020, a taxpayer may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years, or

(ii) To rely on the rules in proposed § 1.1400Z2(f)–1 contained in the notice of proposed rulemaking (REG–115420–18) published on October 29, 2018, as amplified by the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

■ **Par. 10.** Section 1.1502–14Z is added to read as follows:

§ 1.1502–14Z Application of opportunity zone rules to members of a consolidated group.

(a) *Scope and definitions*—(1) *Scope.* This section provides rules regarding the Federal income tax treatment of QOFs owned by members of a consolidated group (as defined in § 1.1502–1(b) and (h), respectively). Rules in the section 1400Z–2 regulations (as defined in § 1.1400Z2(a)–1(b)(41)) apply to consolidated groups except as modified in this section. Paragraph (b) of this section generally provides rules regarding the effects of an election under § 1.1504–3(b)(2) to treat a subsidiary QOF C corporation as a member of a consolidated group. Paragraph (c) of this section provides rules regarding qualifying investments made by members of a consolidated group (including an election to treat the investment by one member as a qualifying investment by another member) and the application of § 1.1502–13 to intercompany transfers of a qualifying investment. Paragraph (d) of this section provides coordinating rules for basis adjustments within a consolidated group. Paragraph (e) of this section provides coordinating rules for § 1.1502–36(d). Paragraph (f) of this section provides elective transition relief to taxpayers that consolidated a subsidiary QOF C corporation prior to May 1, 2019. Paragraph (g) of this section provides rules regarding the consequences of a deconsolidation of a QOF C corporation. Paragraph (h) of this section provides instructions for making the elections provided by paragraphs (c) and (f) of this section. Paragraph (i) of this section is reserved. Paragraph (j) of this section provides examples. Paragraph (k) of this section provides the applicability dates.

(2) *Definitions*—(i) *In general.* The definitions provided in §§ 1.1400Z2(a)–1(b) and 1.1400Z2(d)–1 apply for purposes of this section.

(ii) *Definitions for consolidated groups*—(A) *Day one.* The term *day one* means the date members of the consolidated group formed or acquired section 1504 control of the pre-existing QOF sub. If a pre-existing QOF sub was a member of the consolidated group prior to becoming a QOF C corporation, day one is the first day of the first month in which the member self-certified as, or is treated as, a QOF C corporation, whichever is earlier.

(B) *Election date.* The term *election date* means the date on which an election under paragraph (c) or (f) of this section is made.

(C) *Pre-existing QOF sub.* The term *pre-existing QOF sub* means a subsidiary QOF C corporation that meets the affiliation requirements in section 1504 (without regard to § 1.1504–3(b)(1)) as of May 1, 2019.

(D) *QOF investor member.* The term *QOF investor member* means any member holding a qualifying investment in the QOF member.

(E) *QOF member.* The term *QOF member* means a subsidiary QOF C

corporation that is treated as a member of a consolidated group pursuant to an election in § 1.1504–3(b)(2).

(F) *QOF member stock.* The term *QOF member stock* means the QOF stock of a QOF member.

(G) *QOF SAG.* The term *QOF SAG* means, with respect to a QOF member, the affiliated group that would be determined under section 1504(a) if the QOF member were the common parent.

(H) *Subsidiary QOF C corporation.* The term *subsidiary QOF C corporation* means a QOF C corporation that meets the requirements to be a member of an affiliated group (as defined in section 1504(a)(1), and without regard to § 1.1504–3(b)(1)) other than the common parent of such consolidated group.

(b) *Subsidiary QOF C corporation treated as member of the consolidated group*—(1) *Effects of election to treat a subsidiary QOF C corporation as a member*—(i) *Determining whether a distribution is an inclusion event.* A distribution of property with respect to qualifying QOF stock by a QOF member to a QOF investor member is an inclusion event to the extent the distribution would create or increase an excess loss account (ELA) in the qualifying QOF stock, without regard to any inclusion resulting from application of this paragraph (b)(1)(i). Solely for purposes of determining whether a distribution creates or increases an ELA during a taxable year, investment adjustments pertaining to a distribution on qualifying QOF stock by a QOF member are made after all other investment adjustments under § 1.1502–32 for that year.

(ii) *Determining the amount of deferred gain includible by the QOF investor member.* The amount of gain included in gross income of a QOF investor member under section 1400Z–2(a)(1)(B) on a date described in § 1.1400Z2(b)–1(b) (modified by paragraph (c)(3) of this section, as applicable) is determined under this paragraph (b)(1)(ii). The amount of gain included in gross income of the QOF investor member is the lesser of:

(A) The product of:

(*1*) The percentage of the qualifying investment that gave rise to the inclusion event; and

(*2*) The remaining deferred gain (see § 1.1400Z2(a)–1(b)(40)), less any basis adjustments pursuant to section 1400Z–2(b)(2)(B)(iii) and (iv); or

(B) The gain that would be recognized on a fully taxable disposition of the qualifying investment that gave rise to the inclusion event.

(iii) *Application of ELA rules on the disposition of QOF member stock.* When a QOF investor member disposes of a share of qualifying QOF member stock, any ELA in the share is taken into account as income or gain from the disposition under § 1.1502–19(b)(1) before the basis of the share is increased under section 1400Z–2(c), if applicable. See paragraph (g)(3)(i) of this section for the general rule regarding the treatment of an ELA upon the deconsolidation of a QOF member.

(iv) *Transactions between the QOF member and other members of the consolidated group*—(A) *In general.* This paragraph (b)(1)(iv) governs transactions between a member of the QOF SAG and other members of the consolidated group.

(B) *Sale or exchange of property.* A sale or exchange of property between a member of the QOF SAG and a member of the consolidated group that is not a member of such QOF SAG is not treated as an intercompany transaction (as defined in § 1.1502–13(b)(1)) and is not subject to the rules in § 1.1502–13. In contrast, a sale or exchange of property between members of the QOF SAG is an intercompany transaction that is subject to the rules in § 1.1502–13.

(C) *Other transactions.* Any transaction between a member of the QOF SAG and a member of the consolidated group that is not a member of such QOF SAG that is not a sale or exchange of property is an intercompany transaction subject to the rules in § 1.1502–13.

(v) *Separate-entity application of QOF qualifying rules to QOF member.* A consolidated group is not treated as a single entity for purposes of determining whether a QOF member or a qualified opportunity zone business that is a consolidated group member satisfies the investment standard rules in section 1400Z–2(d) and (f) and §§ 1.1400Z2(d)–1 and 1.1400Z2(f)–1; instead, the rules in this paragraph (b)(1)(v) apply on a separate-entity basis. Therefore, for example, the QOF member's satisfaction of the requirements under section 1400Z–2(d) is determined by taking into account only property (including qualified opportunity zone stock or qualified opportunity zone partnership interests) held by the QOF member, without regard to property transferred by the QOF member to other members of the consolidated group.

(2) *Anti-avoidance rule.* The purposes of section 1400Z–2 and the section 1400Z–2 regulations are to provide specified tax benefits to owners of QOFs to encourage the making of longer-term investments, through QOFs and qualified opportunity zone businesses, of new capital in one or more qualified opportunity zones and to increase the economic growth of such qualified opportunity zones. If a transaction is engaged in or structured with a view to avoid the application of the rules of section 1400Z–2, the section 1400Z–2 regulations, or the regulations in this part under section 1502 of the Code (including this section), appropriate adjustments will be made to carry out the purposes of section 1400Z–2 and the section 1400Z–2 regulations. For example, if a consolidated group engages in a restructuring (such as a distribution described in section 355) with a view to using stock basis adjustments under § 1.1502–32 resulting from increases in the basis of stock under section 1400Z–2(b) in a sale or exchange transaction without disposing of any part of the consolidated group's direct ownership of the relevant qualifying investment, the transaction will be treated as an inclusion event with regard to an appropriate amount of deferred gain.

(c) *Qualifying investments by members of a consolidated group*—(1) *In general.* Except as otherwise provided in this section or in § 1.1400Z2(b)–1 (see, for example, § 1.1400Z2(b)–1(c)(9)(i)(B)(*1*)), section 1400Z–2 applies separately to each member of a consolidated group. Therefore, for example, the same member of the consolidated group generally must both engage in the sale of a capital asset giving rise to eligible gain and timely invest an amount equal to some or all of such gain in a QOF (as provided in section 1400Z–2(a)(1)) in order to qualify for deferral of such gain under section 1400Z–2.

(2) *Election to treat investment of one member as a qualifying investment by another member*—(i) *Availability of election.* If members of a consolidated group satisfy the requirements of this paragraph (c)(2), the consolidated group may elect to treat the investment by one member as a qualifying investment by another member. The election provided by this paragraph (c)(2) is available when a member of a consolidated group (M1) has eligible gain and a second member (M2) makes an investment in a QOF that would be a qualifying investment if M1, rather than M2, had made the investment. For example, if M1 has $100x of eligible gain but M2 has none, and M2 makes a $120x investment in a QOF C corporation, only $100x of M2's investment in the QOF C corporation is eligible for the election under this paragraph (c)(2). See paragraph (h)(2) of this section for the form and manner of making this election. If M2 has its own eligible gain, M2 may make a qualifying investment on its own behalf and defer such eligible

gain under section 1400Z–2(a)(1)(A) and § 1.1400Z2(a)–1.

(ii) *Effect of election.* If a consolidated group makes an election under this paragraph (c)(2), then M1 is treated as having made the investment in the QOF that is actually made by M2. M1 is then treated as having immediately sold such investment to M2 for fair market value. The deemed sale by M1 is subject to the rules in paragraph (c)(3) of this section. The consolidated group must treat the deemed investment by M1 and the deemed sale by M1 to M2 as having occurred for all Federal income tax purposes.

(3) *Intercompany transfers of a qualifying investment*—(i) *In general.* Except as otherwise provided in this paragraph (c)(3), when one member (S) transfers its qualifying investment to another member (B), the transaction is not treated as an intercompany transaction within the meaning of § 1.1502–13(b)(1) for purposes of applying the rules of section 1400Z–2 and the section 1400Z–2 regulations. Therefore, § 1.1502–13(c) does not apply to treat S and B as divisions of a single entity for purposes of section 1400Z–2. For example, if S transfers its qualifying investment to B in a section 351 transaction, the transfer is an inclusion event for S under § 1.1400Z2(b)–1(c). In addition, because the transfer is not an intercompany transaction for purposes of section 1400Z–2, § 1.1502–13 does not apply to continue S's deferral under § 1.1400Z2(b)–1(b).

(ii) *Application of § 1.1502–13 to fully taxable intercompany transfers of a qualifying investment*—(A) *Applicable transactions.* Notwithstanding paragraph (c)(3)(i) of this section, if S transfers its qualifying investment to B in a fully taxable transaction, the transaction is treated as an intercompany transaction, and § 1.1502–13(c) applies to treat S and B as divisions of a single entity for purposes of applying section 1400Z–2.

(B) *Treatment of S's intercompany gain on its qualifying investment.* If a transaction is described in paragraph (c)(3)(ii)(A) of this section, § 1.1502–13(c)(6)(ii) is inapplicable in determining the excludability of S's gain (or the treatment of such gain as tax-exempt income) on the application of section 1400Z–2(b) and (c) to S and B as a single entity. Thus, S's gain on the qualifying investment (including the amount includible under § 1.1400Z2(b)–1(e)) may be redetermined to be excluded from gross income (or treated as tax-exempt income), as appropriate, to achieve single-entity treatment between S and B with regard to the ownership and disposal of the qualifying investment. To qualify for benefits under section 1400Z–2, S and B must otherwise satisfy the requirements of section 1400Z–2. See also § 1.1502–13(j)(4) (concerning multiple or successive intercompany transactions).

(C) *Investment adjustments and adjustments to earnings and profits.* Income of S excluded under section 1400Z–2 by application of paragraphs (c)(3)(ii)(A) and (B) of this section and § 1.1502–13 results in adjustments to S's earnings and profits and is treated as tax-exempt income to S for purposes of § 1.1502–32(b)(2)(ii).

(D) *Election under section 1400Z–2(c).* To the extent paragraph (c)(3)(ii)(A) of this section applies to S's transfer of its qualifying investment to B, B (and not S) is entitled to make the election under section 1400Z–2(c) at the time when, treating S and B as divisions of a single entity, the single entity would be entitled to make such an election. For example, pursuant to § 1.1502–13(c)(1)(ii), B takes S's holding period into account in determining whether B is treated as holding the transferred qualifying investment for 10 years. In addition, the attributes of S's intercompany item on the transfer of the qualifying investment may be redetermined based on B's election.

(4) *Intercompany transfer as qualifying investment in a QOF member.* A transfer by a consolidated group member with an eligible gain to a QOF member before January 1, 2027, is not treated as an intercompany transaction within the meaning of § 1.1502–13 and may constitute a qualifying investment. But see § 1.1504–3(b)(2) regarding conditions for consolidating a QOF C corporation.

(5) *Intercompany gain as eligible gain.* When S sells property to B, § 1.1502–13 applies to determine if, and when, S's intercompany gain and B's corresponding gain constitute eligible gain. S's gain and B's gain are treated as eligible gain only to the extent such gain would be eligible gain if S and B were divisions of a single entity. For example, if S sells a piece of property to B at a gain, B subsequently sells that property to an unrelated party at a further gain, and the gains are treated as capital gain under § 1.1502–13(c)(1) and (4), then both S's gain and B's gain are eligible gains at the time B sells the property to the unrelated party. In contrast, if S sells a piece of property to B at a loss, and B subsequently sells that property to an unrelated party at a gain, then B's corresponding gain on the property is eligible gain only to the extent that S and B, if treated as divisions of a single entity, would have eligible gain on the sale of property to the unrelated party. See § 1.1502–13(a)(1).

(d) *Tiering-up of investment adjustments provided by section 1400Z–2.* Basis increases in a qualifying investment in a QOF under sections 1400Z–2(b)(2)(B)(iii), 1400Z–2(b)(2)(B)(iv), and 1400Z–2(c) are treated as satisfying the requirements of § 1.1502–32(b)(3)(ii)(A) and thus qualify as tax-exempt income to the QOF owner. Therefore, if the QOF owner is a member of a consolidated group and is owned by other members of the same consolidated group (upper-tier members), the upper-tier members increase their bases in the shares of the QOF owner under § 1.1502–32(b)(2)(ii). However, there is no basis adjustment under § 1.1502–32(b)(2)(ii) or (iii) in shares of upper-tier members with regard to a basis adjustment under section 1400Z–2(c) and § 1.1400Z2(c)–1 unless and until the basis of the qualifying investment is adjusted to its fair market value, as provided in section 1400Z–2(c) and § 1.1400Z2(c)–1.

(e) *Application of § 1.1502–36(d).* This paragraph (e) clarifies how § 1.1502–36(d) applies if a member (M) transfers a loss share of another member (S) that is a QOF owner that owns a qualifying investment. To determine S's attribute reduction amount under § 1.1502–36(d)(3), S's basis in its qualifying investment is included in S's net inside attribute amount to compute S's aggregate inside loss under § 1.1502–36(d)(3)(iii)(A). However, S's basis in the qualifying investment is not included in S's Category D attributes available for attribute reduction under § 1.1502–36(d)(4). Thus, S's basis in the qualifying investment cannot be reduced under § 1.1502–36(d). If S's attribute reduction amount exceeds S's attributes available for reduction, then to the extent of the lesser of S's basis in the qualifying investment or the remaining attribute reduction amount, the common parent is treated as making the election under § 1.1502–36(d)(6) to reduce M's basis in the transferred loss S shares.

(f) *Transition relief*—(1) *Overview.* This paragraph (f) provides options for elective relief to pre-existing QOF subs. An election under this paragraph (f) is made in the manner provided in paragraph (h)(3) of this section. If a timely election under this paragraph (f) is not made, the pre-existing QOF sub is treated as deconsolidating on March 13, 2020.

(2) *Reclassification election*—(i) *In general.* A consolidated group may make one of the alternative, irrevocable elections provided in paragraphs (f)(2)(ii) through (iv) of this section for

its pre-existing QOF subs. All elective relief provided in this paragraph (f)(2) is effective on day one.

(ii) *Treatment as a QOF partnership*—(A) *Election.* A consolidated group may elect to treat certain pre-existing QOF subs as QOF partnerships (electing QOF partnership). To be eligible for the election in this paragraph (f)(2)(ii)(A), a pre-existing QOF sub must have converted to an entity treated as a partnership for Federal income tax purposes as of the election date.

(B) *Effect of the QOF partnership election.* As a result of making the election under this paragraph (f)(2)(ii), the pre-existing QOF sub is treated as a QOF partnership from day one. Consequently, the consolidated group must file amended or superseding returns, as applicable, to account for the electing QOF partnership's income, gain, deduction, and loss; the electing QOF partnership also must file its own partnership returns for taxable periods beginning on day one, as applicable. The electing QOF partnership must include its self-certification under § 1.1400Z2(d)–1(a) with its own returns, and the self-certification will be treated as timely so long as the consolidated group filed a timely self-certification under § 1.1400Z2(d)–1(a) for the pre-existing QOF sub. In addition, appropriate adjustments must be made to account for the change in status of the electing QOF partnership from day one, including modifications to investment adjustments to the basis in members' stock made under § 1.1502–32 and adjustments to members' earnings and profits made under § 1.1502–33.

(C) *Pre-existing QOF sub with single owner.* If a pre-existing QOF sub is wholly owned by one member of a consolidated group, then for purposes of making the election under this paragraph (f)(2)(ii), the electing QOF partnership is deemed to have had a nominal partner from day one until the date the electing QOF partnership is treated as a partnership for Federal income tax purposes without regard to this paragraph (f)(2)(ii).

(D) *Example.* The following example illustrates the election under this paragraph (f)(2)(ii).

(*1*) *Facts.* P, the common parent of a consolidated group (P group), wholly owns M1 and M2. On July 1, 2018, M1 and M2 each sell an asset to an unrelated party and realize $70x and $30x of eligible gain, respectively. On August 13, 2018, M1 and M2 form Q12 (a QOF C corporation that was formed as a corporation under state law). Also on August 13, 2018, M1 and M2 contribute $70x and $30x, respectively, to Q12 in exchange for stock of Q12 and properly elect to defer their respective eligible gains under section 1400Z–2(a) and § 1.1400Z2(a)–1. The P group also makes a timely self-certification under § 1.1400Z2(d)–(1)(a) for Q12. Following March 13, 2020, the P group intends to timely elect under this paragraph (f)(2)(ii) to treat Q12 as a QOF partnership.

(*2*) *Analysis*—(*i*) *Eligibility to elect.* For the P group to elect to treat Q12 as a QOF partnership under this paragraph (f)(2)(ii), by the date of the election, Q12 must either convert to a state law partnership or another entity treated as a partnership for Federal income tax purposes.

(*ii*) *Consequences of the election.* As a result of making the election under this paragraph (f)(2)(ii), Q12 is treated as a QOF partnership from August 13, 2018 (day one). The P group must file amended or superseding returns, as applicable and as necessary, to account for Q12's income, gain, deduction, and loss. In addition, Q12 must file its own returns for the taxable period beginning on August 13, 2018, as applicable. The returns must be filed within the time frame provided in paragraph (h)(3)(iii) of this section. Finally, because the P group filed a timely self-certification under § 1.1400Z2(d)-(1)(a) for Q12 as a QOF C corporation, Q12's self-certification as a QOF partnership would be is considered timely filed.

(*3*) *Deemed nominal partner*—(*i*) *Facts.* The facts are the same as paragraph (f)(2)(iii)(D)(*1*) of this section, except that on July 1, 2018, only M1 sells an asset to an unrelated party and realizes $70x of eligible gain. On August 13, 2018, M1 contributes cash of $70x to Q12 in exchange for stock of Q12 and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. As of the date the election is made to treat Q12 as a partnership from day one, a second party invests in Q12, and Q12 is an entity treated as a partnership for Federal income tax purposes.

(*ii*) *Analysis.* The analysis is generally the same as in paragraph (f)(2)(iii)(D)(*2*) of this section. In addition, because Q12 is wholly owned by M1, solely for purposes of treating Q12 as a QOF partnership from August 13, 2018, Q12 is deemed to have a nominal partner from August 13, 2018 until the election date or the date Q12 qualifies as a partnership, if earlier.

(iii) *Treatment as a non-member QOF C corporation*—(A) *Election.* A consolidated group may elect to treat the pre-existing QOF sub as a QOF C corporation that is not a member of the consolidated group.

(B) *Effect of the non-member QOF C corporation election.* As a result of making the election under this paragraph (f)(2)(iii), the pre-existing QOF sub is treated as not being a member of the consolidated group from day one. Consequently, the consolidated group must file amended or superseding returns, as applicable, to exclude all of the pre-existing QOF sub's income, gain, deduction, and loss from the consolidated returns; the pre-existing QOF sub also must file its own returns for taxable periods beginning on day one, as applicable. In addition, all adjustments resulting from the pre-existing QOF sub's operations must be eliminated from the consolidated group, including investment adjustments made under § 1.1502–32 to basis in members' stock (as well as stock in the pre-existing QOF sub) and adjustments made under § 1.1502–33 to members' earnings and profits.

(iv) *Treatment as a non-QOF C corporation*—(A) *Election.* A consolidated group may elect to treat a pre-existing QOF sub as if it never self-certified to be a QOF pursuant to § 1.1400Z2(d)–1.

(B) *Effect of the non-QOF C corporation election.* As a result of making the election under this paragraph (f)(2)(iv), the pre-existing QOF sub is treated from day one as a member of the consolidated group and not as a QOF. Therefore, section 1400Z–2 is not applicable, and amended returns or superseding returns must be filed, as applicable, to account for the eligible gain that was invested in the pre-existing QOF sub. In addition, appropriate adjustments must be made to account for the non-applicability of section 1400Z–2, including adjustments to members' stock basis and earnings and profits under §§ 1.1502–32 and 1.1502–33, respectively.

(3) *Election to continue treating pre-existing QOF sub as a member of the consolidated group*—(i) *Election.* A consolidated group may elect to have a pre-existing QOF sub retain its QOF status and remain a member of the consolidated group.

(ii) *Effects of electing to remain a QOF and a member of the consolidated group.* As a result of making the election under this paragraph (f)(3), the conditions and effects provided in § 1.1504–3(b)(2) and paragraph (b)(1) of this section will apply to the pre-existing QOF sub and the consolidated group as of the effective date of this election. See paragraph (h)(1) of this section for the effective date of this election, and see paragraph (h)(3)(iii) of this section regarding the timing for meeting the requirements in § 1.1504–3(b)(2)(ii).

(g) *Deconsolidation rules*—(1) *In general.* This paragraph (g) provides rules applicable on any deconsolidation of a QOF C corporation (deconsolidating QOF).

(2) *Deconsolidation and inclusion event.* A deconsolidation event is not an inclusion event unless the deconsolidation is the result of an actual transfer of the QOF member stock or a worthlessness event within the meaning of § 1.1502–80(c). For example, when a consolidated group fails to meet the

conditions in § 1.1504–3(b)(2) of this section and causes a QOF member to deconsolidate, the deconsolidation event is not an inclusion event solely as a result of the consolidated group's failure to meet the requirements in § 1.1504–3(b)(2) of this section.

(3) *Basis in the deconsolidating QOF at time of deconsolidation*—(i) *ELA in a deconsolidating QOF.* Any ELA in stock of the deconsolidating QOF at the time of the deconsolidation is taken into account under the rules of § 1.1502–19. See paragraph (b)(1)(iii) of this section for rules coordinating the application of section 1400Z–2(c) with § 1.1502–19.

(ii) *Positive basis in the deconsolidating QOF resulting from § 1.1502–32.* Consolidated group members retain any positive basis in the deconsolidating QOF resulting from investment adjustments under § 1.1502–32 following its deconsolidation. However, following the deconsolidation, for purposes of determining the amount includible under § 1.1400Z2(b)–1(e), the amount of basis referred to in section 1400Z–2(b)(2)(A)(ii) is computed by applying only those rules applicable to corporations that do not file a consolidated return (that is, the basis rules under subchapter C and section 1400Z–2). Therefore, any positive basis resulting from § 1.1502–32 adjustments is not taken into account in computing the includible amount under § 1.1400Z2(b)–1(e).

(4) *Deconsolidating QOF's earnings and profits*—(i) *Deconsolidation on or before December 31, 2026.* Notwithstanding § 1.1502–33(e)(1), if a deconsolidating QOF deconsolidates before December 31, 2026, the deconsolidating QOF retains its earnings and profits under this paragraph (g)(4)(i). Any earnings and profits of the deconsolidating QOF that were taken into account by any other members under § 1.1502–33 are eliminated from those members as of the end of the day on which the deconsolidating QOF deconsolidates.

(ii) *Deconsolidation after December 31, 2026.* If the deconsolidating QOF deconsolidates after December 31, 2026, the rules under § 1.1502–33(e) apply.

(5) *Consequences under § 1.1502–36.* See § 1.1502–36(f)(10)(i)(B) for the treatment of a deconsolidation as a transfer of all of the stock in the deconsolidating member held by other members of the consolidated group.

(h) *Form and manner of making an election under this section*—(1) *In general.* The elections provided in this section are irrevocable. The information required for each election is provided in this paragraph (h). A reclassification election under paragraph (f)(2) of this section is effective as of day one. All other elections are effective on the election date.

(2) *Election under paragraph (c)(2) of this section to treat investment by M2 as qualifying investment by M1*—(i) *Form of election.* The election under paragraph (c)(2) of this section must be made in the form of a statement titled ''THIS IS AN ELECTION UNDER § 1.1502–14Z(c)(2) TO TREAT AN INVESTMENT BY [insert name and employer identification number (E.I.N.) of M2] AS A QUALIFYING INVESTMENT BY [insert name and E.I.N. of M1].'' The statement must be included with the consolidated group's timely filed return (original, superseding, or amended return, as applicable, including extensions). In addition, the statement must include the information required under paragraph (h)(2)(ii) of this section.

(ii) *Required information.* (A) The amount of M1's eligible gain;

(B) The amount of the investment M2 has made in a QOF, including identification of the amount of the investment that is eligible for treatment as a qualifying investment under paragraph (c)(2) of this section and the amount (if any) that is not eligible for such treatment; and

(C) The date on which M1 recognized its eligible gain, and the date on which M2 made the investment in the QOF.

(3) *Elections under paragraph (f) of this section for transition relief*—(i) *Form of election.* The elections under paragraph (f) of this section must be made in the form of a statement titled ''THIS IS AN ELECTION UNDER § 1.1502–14Z(f) FOR [insert name and E.I.N. of pre-existing QOF sub].'' All actions necessary to make these elections, including the filing of an amended return (or superseding return, as applicable), or filing an original return, as applicable, must be completed within the time designated in paragraph (h)(3)(iii) of this section. The statement must be included on or with any amended prior-year consolidated return (or superseding or original return, as applicable) and on or with the consolidated group's timely filed return (original or amended if filed by the due date for the return, including extensions) for the election year. In addition, the statement must include the information required in paragraph (h)(3)(ii) of this section.

(ii) *Required information*—(A) *Reclassification election under paragraph (f)(2)(ii) of this section.* (*1*) A statement that the pre-existing QOF sub is electing to be a QOF partnership;

(*2*) The election date;

(*3*) The effective date of the election;

(*4*) Specification of the appropriate adjustments required under paragraph (f)(2)(ii) of this section made by the pre-existing QOF sub and the consolidated group; and

(*5*) Certification that the appropriate change under state law or the entity classification election under § 301.7701–3 of this chapter (as applicable) has been made, and the date of the change or entity classification election.

(B) *Reclassification election under paragraph (f)(2)(iii) or (iv) of this section.* (*1*) A statement that the pre-existing QOF sub is changing its status;

(*2*) The pre-existing QOF sub's new status (either a non-member QOF C corporation, under paragraph (f)(2)(iii) of this section, or a non-QOF C corporation, under paragraph (f)(2)(iv) of this section);

(*3*) The election date;

(*4*) The effective date of the election; and

(*5*) Specification of the appropriate adjustments made the by pre-existing QOF sub and the consolidated group pursuant to paragraph (f)(2)(iii) or (iv) of this section, as applicable.

(C) *Election to continue treating the pre-existing QOF sub as a subsidiary member of the consolidated group under paragraph (f)(3) of this section.* (*1*) A statement that the pre-existing QOF sub is electing to retain its status as a QOF C corporation and remain a member of the consolidated group;

(*2*) The election date; and

(*3*) Certification that the pre-existing QOF sub and the consolidated group are in compliance with the conditions under § 1.1504–3(b)(2)(ii) as of the date that the pre-existing QOF sub and the consolidated group are in compliance with the conditions under § 1.1504–3(b)(2)(ii).

(iii) *Time for completing the elections under paragraph (f) of this section.* (A) If the pre-existing QOF sub is making an election under paragraph (f)(2)(ii) or (f)(3) of this section, all actions necessary to make such election must be completed by April 13, 2020. Specifically, if the pre-existing QOF sub is making the election under paragraph (f)(3) of this section, the conditions in § 1.1504–3(b)(2)(ii) must be met by April 13, 2020. In addition, the consolidated group's amended return (or superseding return, as applicable), taking into account the relevant changes, if applicable, must be filed by May 12, 2020. Moreover, if the electing QOF partnership had been a QOF partnership on day one and the electing QOF partnership's return would have been

due, then such return also must be filed by May 12, 2020].

(B) If the pre-existing QOF sub is making a reclassification election under paragraph (f)(2)(iii) or (iv) of this section, all actions necessary to make such election, including the filing of the pre-existing QOF sub's own return (if the return would have been due had the pre-existing QOF sub not been included in the consolidated group on day one), and the consolidated group's amended return (or superseding return, as applicable), if applicable, must be completed by April 13, 2020.

(iv) *Extension of statute of limitations.* If, as a result of making a reclassification election in paragraph (f)(2) of this section, the consolidated group is required to file an amended return, and the electing QOF partnership is required to file a return by May 12, 2020 or the pre-existing QOF sub is required to file a return by April 13, 2020 (collectively, the related returns), then the consolidated group (and the pre-existing QOF sub, if an election under paragraph (f)(2)(iii) of this section is made) also must consent to extend the period of limitations on assessment with respect to any issues arising under section 1400Z–2 in the related returns of the consolidated group (and the pre-existing QOF sub, if applicable). This consent must be effected at such time and in such form and manner as may be prescribed by the Commissioner of Internal Revenue in Internal Revenue Service forms or instructions or in publications or guidance published in the Internal Revenue Bulletin (see §§ 601.601(d)(2) and 601.602 of this chapter).

(i) [Reserved]

(j) *Examples.* The following examples illustrate the rules of this section. For purposes of these examples, and unless otherwise stated: P is the common parent of the P consolidated group (P group); S, B, and M are members of the P group; Q is a QOF C corporation that is not a member of the P group; and X is an unrelated party.

(1) *Example 1: Distribution by a QOF member and inclusion events*—(i) *Facts.* P wholly owns S. In 2018, S sells an asset to an unrelated party and realizes $500x of eligible gain. S forms a new QOF C corporation Q2, contributes $500x to Q2 in exchange for stock of Q2, and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. The P group elects under § 1.1504–3(b)(2) to consolidate Q2. In 2024, Q2 distributes $20x to S when S's basis in Q2 is $50x, the value of Q2 exceeds $500x, and Q2 has no earnings and profits. There are no other events in 2024 that results in investment adjustments to Q2 stock.

(ii) *Analysis.* Under §§ 1.1502–13(f)(2) and 1.1502–32, the intercompany distribution from Q2 to S of $20x reduces S's basis in Q2 to $30x ($50x − $20x). Under paragraph (b)(1)(i) of this section, because the distribution does not create or increase an ELA in Q2 stock, the distribution is not an inclusion event.

(iii) *Distribution that creates an ELA.* The facts are the same as in paragraph (j)(1)(i) of this section except that in 2024 Q2 distributes $70x to S. Under §§ 1.1502–13(f)(2) and 1.1502–32, the intercompany distribution from Q2 to S of $70x reduces S's basis in Q2 to $0 and creates an ELA of $20x ($50x − $70x). Under paragraph (b)(1)(i) of this section, because an ELA is created in Q2's stock, the distribution is an inclusion event to the extent of the increase in the ELA. S therefore includes $20x of its deferred gain into income in 2024. See § 1.1400Z2(b)–1(e)(2). In addition, under § 1.1400Z2(b)–1(g)(1)(ii), the adjustment to S's basis in Q2 under section 1400Z–2(b)(2)(B)(ii) is applied before determining the other Federal income tax consequences of the distribution. Therefore, as a result of the inclusion event, S's basis in Q2 is first increased to $70x ($50x + $20x), and then S's basis in Q2 is reduced by $70x (the amount of the distribution) to $0 under § 1.1502–32.

(2) *Example 2: Basis adjustment when member owns qualifying QOF stock*—(i) *Facts.* P wholly owns S. In 2018, S sells an asset to an unrelated party and realizes $500x of eligible gain. S contributes $500x to Q in exchange for stock of Q and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. S does not otherwise own stock in Q. In 2026, the fair market value of S's qualifying investment in Q exceeds $500x. In 2029, when S still owns its qualifying investment in Q, P sells all of the stock of S to X. S retains its stock in Q.

(ii) *Analysis*—(A) *Five-year and seven-year basis increase and § 1.1502–32 tier-up.* In 2023, when S has held the stock of Q for five years, under section 1400Z–2(b)(2)(B)(iii), S increases its basis in its Q stock by $50x (10 percent of $500x, the amount of gain deferred by reason of section 1400Z–2(a)(1)(A)). The 10-percent basis increase qualifies as tax-exempt income to S under paragraph (d) of this section. Thus, P (an upper-tier member) increases its basis in S's stock by $50x under § 1.1502–32(b)(2)(ii). Similarly, in 2025, when S has held the stock of Q for seven years, under section 1400Z–2(b)(2)(B)(iv), S increases its basis in its Q stock by an additional $25x (5 percent of $500x). The 5-percent basis increase also qualifies as tax-exempt income to S under paragraph (d) of this section, and P increases its basis in S's stock by an additional $25x under § 1.1502–32(b)(2)(ii).

(B) *S's recognition of deferred capital gain in 2026.* S did not dispose of its Q stock prior to December 31, 2026. Therefore, under section 1400Z–2(b)(1)(B) and § 1.1400Z2(b)–1(b)(2), S's remaining deferred gain is included in S's income on December 31, 2026. The amount of gain included under section 1400Z–2(b)(2)(A) and § 1.1400Z2(b)–1(e)(3) is $425x ($500x of remaining deferred gain less S's $75x basis in Q). S's basis in Q is increased by $425x to $500x, and P's basis in S also is increased by $425x under § 1.1502–32(b)(2)(i).

(C) *P's disposition of S.* P's sale of S stock in 2029 results in the deconsolidation of S. S retains its Q stock, and S is not treated as selling or exchanging its Q stock for purposes of section 1400Z–2(c). Therefore, no basis adjustments under section 1400Z–2 are made as a result of P's sale of S stock.

(iii) *S sells the stock of Q after 10 years.* The facts are the same as in paragraph (j)(2)(i) of this section, except that in 2029, instead of P selling all of the stock of S, S sells all of the stock of Q to X for its fair market value of $800x. At the time of the sale, S has owned the Q stock for over 10 years, and S elects under section 1400Z–2(c) to adjust its stock basis in Q from $500x (see the analysis in paragraph (j)(2)(ii)(B) of this section) to $800x, the fair market value of Q on the date of the sale. As a result of the election, S has no gain on the sale of Q stock. Additionally, the $300x basis increase in Q is treated as tax-exempt income to S pursuant to paragraph (d) of this section. Thus, P increases its basis in P's S stock by $300x under § 1.1502–32(b)(2)(ii).

(3) *Example 3: Intercompany sale of qualifying investment*—(i) *Facts.* In 2018, S sells an asset to an unrelated party and realizes $100x of eligible gain. Also in 2018, S contributes $100x to Q in exchange for Q stock and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. S does not otherwise own stock in Q. In 2021, S sells all of its Q stock to B for $250x in a fully taxable transaction. In 2026, the fair market value of Q is $300x. In 2030, B sells the Q stock to X for $800x.

(ii) *Analysis*—(A) *Intercompany sale treated as an inclusion event.* In 2021, S's sale of its Q stock to B is an inclusion event under section 1400Z–2(b)(1) and § 1.1400Z2(b)–1(c). The amount includible pursuant to § 1.1400Z2(b)–1(e)(1) is $100x (the lesser of the remaining deferred gain of $100x and the fair market value of the qualifying investment of $250x, over S's basis in Q, $0). As a result of the inclusion, S's basis in Q increases from $0 to $100x and S also realizes a capital gain of $150x ($250x of amount realized less its $100x basis in the Q stock) from the intercompany sale of Q to B. Because S's sale of its Q stock to B is a fully taxable transaction, paragraph (c)(3)(ii) of this section applies to treat the sale as an intercompany transaction and S's intercompany gains are taken into under § 1.1502–13(c)(2)(ii). Thus, S defers the inclusion of its $100x of remaining deferred gain and its $150x of capital gain in 2021. B has a $250x basis in its Q stock.

(B) *Five-year basis increase in 2023.* Pursuant to paragraph (c)(3)(ii) of this section, S and B are treated as divisions of a single entity for purposes of applying section 1400Z–2. In 2023, the single entity would have held the QOF investment for five years and its basis in Q would be increased to $10x ($100x × 10%) under section 1400Z–2(b)(2)(B)(iii). To achieve this single entity result, $10x of S's $100x of remaining deferred gain is redetermined to be tax-exempt income. See § 1.1502–13(c)(1); see also paragraph (c)(3)(ii)(B) of this section making § 1.1502–13(c)(6)(ii) inapplicable in

determining the excludability of S's intercompany gain. Therefore, in 2023, S is treated as having $10x of tax-exempt income, S's remaining deferred gain is $90x ($100x − $10x), while B's basis in Q remains $250x.

(C) *Seven-year basis increase in 2025.* The same analysis in paragraph (j)(3)(ii)(B) of this section applies for the year 2025. Therefore, in 2025, S is treated as having $5x ($100x × 5%) of tax-exempt income, S's remaining deferred gain is $85x ($90x − $5x), and B's basis in Q remains $250x.

(D) *Inclusion of S's remaining deferred gain in 2026.* B continues to own the Q stock through 2026, and, treating S and B as divisions of a single entity for purposes of section 1400Z–2, the single entity would include its remaining deferred gain in income on December 31, 2026. See section 1400Z–2(b)(1), § 1.1400Z2(b)–1(b). On a single-entity basis, the amount includible pursuant to § 1.1400Z2(b)–1(e) is $85x (the lesser of the remaining deferred gain of $100x and the fair market value of the qualifying investment of $300x, over the single entity's basis in Q, $15x). B does not otherwise have an income event with respect to its Q stock in 2026. Therefore, under § 1.1502–13(c), all $85x of S's remaining deferred gain is taken into account in 2026. In addition, S's $150x of capital gain on its Q stock sale continues to be deferred, and B's basis in Q remains $250x.

(E) *B sells the Q stock in 2030.* In 2030, B sells all its Q stock to X for $800x. Under paragraph (c)(3)(ii)(D) of this section, B is entitled to make the election under section 1400Z–2(c) if, treating S and B as a single entity, the single entity would be eligible to make the election. Taking into account S's holding period, B has held Q for over 10 years, and B is eligible for the election when it sells Q to X in 2030. B makes the section 1400Z–2(c) election at the time of sale. Following the election, if S and B were divisions of a single entity, the single entity's basis in Q would increase from $100x to its fair market value of $800x, causing to be excluded the $700x of gain on the sale of Q stock. To achieve this single entity result, § 1.1502–13(c)(1) redetermines B's $550x ($800x − $250x) of gain and S's deferred $150x of capital gain to be tax-exempt income. See paragraph (c)(3)(ii)(B) of this section making § 1.1502–13(c)(6)(ii) inapplicable in determining the excludability of S's intercompany gain. Therefore, as a result of the sale of the Q stock and B making the section 1400Z–2(c) election, S has $150x of tax-exempt income, and B has $550x of tax-exempt income.

(4) *Example 4: Intercompany sale of qualifying investment followed by sale of QOF at a loss outside of the consolidated group*—(i) *Facts.* The facts are the same as in paragraph (j)(3)(i) of this section, except that in 2030, B sells the stock of Q for $225x to X.

(ii) *Analysis.* The analysis for tax years prior to 2030 is the same as in paragraphs (j)(3)(ii)(A) through (D) of this section. In addition, applying the analysis in paragraph (j)(3)(ii)(E) of this section, B is entitled to make the election under section 1400Z–2(c) and B makes the election. Following the election, if S and B were divisions of a single entity, the single entity's basis in Q would increase from $100x to $225x, causing to be excluded the $125x of gain on the sale of Q stock. To achieve this single entity result, § 1.1502–13(c)(1) redetermines B's $25x ($225x − $250x) of loss to be a noncapital, nondeductible expense and S's deferred $150x of capital gain to be tax-exempt income. Therefore, as a result of the sale of Q stock and B making the section 1400Z–2 election, S has $150x of tax-exempt income, and B has $25x of noncapital, nondeductible expense.

(5) *Example 5: Intercompany section 351 transfer of qualifying investment*—(i) *Facts.* In 2018, M sells an asset to an unrelated party and realizes $100x of eligible gain. Also in 2018, M contributes $100x to Q in exchange for Q stock and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. M does not otherwise own stock in Q. In 2021, when the value of Q is $200x, M contributes all of its Q stock to S in exchange for S stock in a transaction that qualifies under section 351.

(ii) *Analysis.* In 2021, M's contribution of its Q stock to S is an inclusion event under section 1400Z–2(b)(1) and § 1.1400Z2(b)–1(c). The amount includible pursuant to § 1.1400Z2(b)–1(e) is $100x (the lesser of the remaining deferred gain of $100x and the fair market value of the qualifying investment of $200x, over S's basis in Q, $0). Because M's contribution of its Q stock to S is not a fully taxable transaction, the general rule in paragraph (c)(3)(i) of this section applies to treat the contribution as not an intercompany transaction for purposes of applying section 1400Z–2, and § 1.1502–13 does not apply to treat M and S as a single entity for purposes of section 1400Z–2. Thus, as a result of the transfer, M takes its $100x of remaining deferred gain into account, M's basis in S is $100x, and S's basis in Q is $100x.

(6) *Example 6: Intercompany sale of qualifying investment followed by a tax-free transfer of the qualifying investment*—(i) *Section 351 transfer to another member of the consolidated group*—(A) *Facts.* In 2018, S sells an asset to an unrelated party and realizes $100x of eligible gain. Also in 2018, S contributes $100x to Q in exchange for Q stock and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. S does not otherwise own stock in Q. In 2021, when the fair market value of the Q stock is $250, S sells all of its Q stock to B for $250x in a fully taxable transaction. In 2024, B transfers all its Q stock to another member of the P group, B2, in a section 351 transaction. At such time, the fair market value of the Q stock is $300x.

(B) *Analysis*—(*1*) *Intercompany sale in 2021.* In 2021, S's sale of its Q stock to B is an inclusion event under section 1400Z–2(b)(1) and § 1.1400Z2(b)–1(c). The amount includible pursuant to § 1.1400Z2(b)–1(e) is $100x (the lesser of the remaining deferred gain of $100x and the fair market value of the qualifying investment of $250x, over S's basis in Q, $0). As a result of the inclusion, S's basis in its Q stock increases from $0 to $100x and S also realizes a capital gain of $150x ($250x of amount realized less its $100x basis in the Q stock) from the intercompany sale of the Q stock to B. Because S's sale of its Q stock to B is a fully taxable transaction, paragraph (c)(3)(ii) of this section applies to treat the sale as an intercompany transaction. Therefore, S's intercompany gains are taken into account under § 1.1502–13(c) and (d). Thus, S defers the inclusion of its $100x of remaining deferred gain and its $150x of capital gain in 2021. B has a $250x basis in its Q stock.

(*2*) *Five-year basis increase in 2023.* Pursuant to paragraph (c)(3)(ii) of this section, S and B are treated as divisions of a single entity for purposes of applying section 1400Z–2. In 2023, the single entity has held the QOF investment for five years and its basis in the Q stock would be increased to $10x ($100x × 10%) under section 1400Z–2(b)(2)(B)(iii). To achieve this single entity result, $10x of S's $100x of remaining deferred gain is redetermined to be tax-exempt income. See § 1.1502–13(c)(1); see also paragraph (c)(3)(ii)(B) of this section making § 1.1502–13(c)(6)(ii) inapplicable in determining the excludability of S's intercompany gain. Therefore, in 2023, S is treated as having $10x of tax-exempt income, S's remaining deferred gain is $90x ($100x − $10x), and B's basis in the Q stock remains $250x.

(*3*) *Intercompany transfer in a section 351 transaction.* In 2024, B's contribution of its Q stock to B2, a member of the P group, is an inclusion event under section 1400Z–2(b)(1) and § 1.1400Z2(b)–1(c). The amount includible pursuant to § 1.1400Z2(b)–1(e) is $90x (the remaining deferred gain as determined in paragraph (j)(6)(i)(B) of this section). Because B's contribution of its Q stock to B2 is not a fully taxable transaction, the general rule in paragraph (c)(3)(i) of this section applies to prevent the contribution from being treated as an intercompany transaction for purposes of section 1400Z–2. As a result, for purposes of section 1400Z–2, § 1.1502–13 does not apply to treat B and B2 as a single entity, and the application of § 1.1502–13(j) is adjusted accordingly. As a result of the section 351 transfer, S takes its $90x of remaining deferred gain into account. B's basis in its B2 stock is $250x, and B's basis in its Q stock is $250x. However, because S's $150x of capital gain from the intercompany sale of its Q stock to B in 2021 is not an item related to section 1400Z–2, it continues to be deferred under § 1.1502–13 because B2 is a member of the P group. See § 1.1502–13(j)(4) regarding successive intercompany transactions.

(ii) *Section 351 transfer to a non-member*—(A) *Facts.* The facts are the same as in paragraph (j)(6)(i)(A) of this section, except that B2 is not a member of the P group, and B contributes all its Q stock to B2 in a transaction that qualifies under section 351.

(B) *Analysis*—(*1*) *Intercompany sale in 2021 and five-year basis increase in 2023.* The analysis for the 2021 and 2023 tax years are the same as in paragraphs (j)(6)(i)(B)(*1*) and (*2*) of this section.

(*2*) *Transfer of Q to a non-member in a section 351 transaction.* In 2024, B's contribution of its Q stock to B2, a non-member of the P group, is an inclusion event under section 1400Z–2(b)(1) and § 1.1400Z2(b)–1(c). The amount includible

pursuant to § 1.1400Z2(b)–1(e) is $90x (the remaining deferred gain as determined in paragraph (j)(6)(ii)(B)(1) of this section). S's deferred capital gain of $150x is taken into account in 2024 under the acceleration rule of § 1.1502–13(d) because the Q stock has left the P group. B2's holding period for the qualifying investment does not include the time during which B and S held the qualifying investment.

(iii) *Section 721(a) transfer to a partnership*—(A) *Facts.* The facts are the same as in paragraph (j)(6)(i)(A) of this section, except that B2 is a partnership, and an unrelated party is the other partner in B2. B's transfer of all of its Q stock to B2 qualifies for non-recognition treatment under section 721(a). In 2026, the fair market value of Q is $330x.

(B) *Analysis*—(*1*) *Intercompany sale in 2021 and five-year basis increase in 2023.* The analysis for the 2021 and 2023 tax years are the same as in paragraphs (j)(6)(i)(B)(*1*) and (*2*) of this section.

(*2*) *Transfer of Q stock to a partnership in a section 721(a) transaction.* In 2024, B transfers its Q stock to B2, a partnership, in a section 721(a) transaction. Although a section 721(a) transaction is not an inclusion event under § 1.1400Z2(b)–1(c)(7), under the acceleration rule of § 1.1502–13(d), S must take into account its $90x of remaining deferred gain because B2 has benefited from an increased basis in the Q stock as a result of the intercompany sale between S and B such that this is the appropriate time to take the remaining deferred gain into account. S's deferred capital gain of $150x is taken into account in 2024 for the same reason.

(7) *Example 7: Computation and application of the attribute reduction amount under § 1.1502–36(d) when S owns a QOF*—(i) *Facts.* In 2018, S sells an asset to an unrelated party and realizes $5,000x of eligible gain. S contributes $5,000x to Q in exchange for stock of Q and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. In 2024, M sells all of its S stock to X for its fair market value of $100x, and M's basis in the stock of S is $300x. At the time of sale, S owns the Q stock with a basis of $500x (S's basis in its Q stock was increased under section 1400Z–2(b)(2)(B)(iii) to $500x in 2023), and S has a net operating loss carryover of $50x. M's transfer of the S shares is a transfer of loss shares under § 1.1502–36. Assume that no basis redetermination is required under § 1.1502–36(b) and no basis reduction is required under § 1.1502–36(c).

(ii) *Attribute reduction under § 1.1502–36(d).* Under § 1.1502–36(d), S's attributes are reduced by S's attribute reduction amount. Section 1.1502–36(d)(3) provides that S's attribute reduction amount is the lesser of the net stock loss and S's aggregate inside loss. The net stock loss is the excess of the $300x aggregate basis of the transferred S shares over the $100x aggregate value of those shares, or $200x. S's aggregate inside loss, which includes the basis of the stock of Q as provided by paragraph (e) of this section, is the excess of S's net inside attribute amount over the value of the S share. S's net inside attribute amount is $550x, computed as the sum of S's $50x loss carryover and its $500x basis in Q. S's aggregate inside loss is therefore $450x ($550x net inside attribute amount over the $100x value of the S share). Accordingly, S's attribute reduction amount is the lesser of the $200x net stock loss and the $450x aggregate inside loss, or $200x. Under § 1.1502–36(d)(4), S's $200x attribute reduction is first allocated and applied to reduce S's $50x loss carryover to $0. Under § 1.1502–36(d)(4)(i)(D), S generally would be able to reduce the basis of its category D assets (including stock in other corporations) by the remaining attribute reduction amount ($150x). However, paragraph (e) of this section provides that S's basis in the stock of Q is not included in S's Category D attributes that are available for reduction under § 1.1502–36(d)(4), and the remaining $150x of attribute reduction amount cannot be used to reduce the basis of Q shares under § 1.1502–36(d). Rather, under paragraph (e) of this section, P is treated as making the election under § 1.1502–36(d)(6) to reduce M's basis in the transferred loss S shares by $150x. As a result, P's basis in its M stock is also reduced by $150x.

(k) *Applicability dates*—(1) *In general.* This section applies for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a consolidated group's first taxable year ending after December 21, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, a consolidated group may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(g)–1 contained in the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

■ **Par. 11.** Section 1.1504–3 is added to read as follows:

§ 1.1504–3 Treatment of stock in a QOF C corporation for purposes of consolidation.

(a) *Scope and definitions*—(1) *Scope.* This section provides rules regarding the treatment of stock in a QOF C corporation for purposes of determining whether such corporation can join in the filing of a consolidated return. Paragraph (b) of this section generally prevents a subsidiary QOF C corporation from joining in the filing of a consolidated return, but it provides an election to consolidate a subsidiary QOF C corporation (subject to certain conditions). Paragraph (c) of this section provides instructions for making the election provided by paragraph (b) of this section. Paragraph (d) of this section provides an example. Paragraph (e) of this section provides the applicability dates.

(2) *Definitions.* The definitions provided in §§ 1.1400Z2(a)–1(b) and 1.1502–14Z(a)(2)(ii) apply for purposes of this section.

(b) *QOF stock not stock for purposes of affiliation*—(1) *In general.* Except as otherwise provided in paragraph (b)(2) of this section, stock in a QOF C corporation (whether qualifying QOF stock or otherwise) is not treated as stock under section 1504 for purposes of determining whether the issuer may join in the filing of a consolidated return under section 1501. Therefore, a QOF C corporation can be the common parent of a consolidated group, and a QOF C corporation generally can be a member of an affiliated group for purposes of section 1504, but a QOF C corporation cannot join in the filing of a consolidated return as a subsidiary member (except as provided in paragraph (b)(2) of this section).

(2) *Election to consolidate a subsidiary QOF C corporation*—(i) *In general.* Notwithstanding paragraph (b)(1) of this section, a consolidated group may elect to consolidate a subsidiary QOF C corporation that was formed, or section 1504 control of which was acquired, by the consolidated group after May 1, 2019, and that otherwise meets the affiliation requirements under section 1504. If a pre-existing corporation was a member of the consolidated group prior to becoming a QOF C corporation, a consolidated group may elect to continue to consolidate such pre-existing corporation if it self-certified to be a QOF after May 1, 2019. The consolidated group must make the election under this paragraph (b)(2) with regard to the first taxable year during which the subsidiary QOF C corporation otherwise meets the section 1504 affiliation requirements (without regard to paragraph (b)(1) of this section). See § 1.1502–14Z(f)(3) for an election available with regard to a subsidiary QOF C corporation that met the section 1504 affiliation requirements as of May 1, 2019. The election under this paragraph (b)(2) is effective on the later of May 1, 2019, or the first date on which the QOF C corporation otherwise meets the requirements of section 1504. If a consolidated group makes the election under this paragraph (b)(2), then the conditions in paragraph (b)(2)(ii) of this section apply to the consolidated group and to the QOF member. See paragraph (c) of this section for the form and manner of making this election.

(ii) *Conditions to consolidate a subsidiary QOF C corporation*—(A) *Ownership status of QOF investor member.* On and at all times after the

date of the investment, the common parent must directly or indirectly own all shares of all classes of stock (including non-qualified preferred stock) issued by any QOF investor member.

(B) *Direct investment.* Except as provided in § 1.1502–14Z(c), each QOF investor member must maintain direct ownership of its qualifying investment (see, for example, § 1.1400Z2(b)–1(c), which generally treats transfers of a qualifying investment as an inclusion event). See § 1.1502–14Z(c)(4) for rules regarding the treatment of intercompany transfers as qualifying investments in a QOF member. See also § 1.1502–14Z(c)(2) and (c)(3)(ii) for rules regarding actual and deemed intercompany transfers of qualifying investments.

(3) *Failure of continued qualification.* Consolidation of a subsidiary QOF C corporation is contingent upon continued satisfaction of all of the conditions of paragraph (b)(2)(ii) of this section. The requirements of paragraph (b)(2) of this section continue to apply (with appropriate modifications to reflect single-entity treatment) following any intercompany transfer of the QOF member stock that is subject to § 1.1502–14Z(c)(3)(ii). For example, following an intercompany transfer of the QOF member stock that is subject to § 1.1502–14Z(c)(3)(ii), the buying member must maintain a direct investment in the QOF member. On the failure to satisfy any condition of paragraph (b)(2), the QOF member will deconsolidate, and § 1.1502–14Z(g) will apply with respect to such deconsolidation.

(c) *Election under paragraph (b)(2) of this section to consolidate a subsidiary QOF C corporation*—(1) *In general.* The election under paragraph (b)(2) of this section is irrevocable and is made in the form provided in paragraph (c)(2) of this section.

(2) *Form of election.* The election under paragraph (b)(2) of this section must be made in the form of a statement titled ''THIS IS AN ELECTION UNDER § 1.1504–3(b)(2) TO CONSOLIDATE [insert name and employer identification number (E.I.N.) of subsidiary QOF C corporation] as of [insert date].'' The statement must be included with the consolidated group's timely filed return (original, superseding, or amended return, as applicable, including extensions) for the year the election under § 1.1504–3(b)(2) is made.

(d) *Example.* The following example illustrates the treatment of QOF stock as not stock for purposes of affiliation as described in paragraph (b)(1) of this section.

(1) *QOF stock as not stock for purposes of affiliation to join in the filing of a consolidated return*—(i) *Facts.* P wholly owns S, which wholly owns corporation Q1. P, S, and Q1 are members of the P group. In 2021, S sells an asset to an unrelated party and realizes $500x of eligible gain. S contributes $500x to Q1 and properly elects to defer the eligible gain under section 1400Z–2(a) and § 1.1400Z2(a)–1. At such time, Q1 qualifies and elects to be treated as a QOF, but the P group does not elect to consolidate Q1 under paragraph (b)(2) of this section.

(ii) *Analysis.* Under paragraph (b)(1) of this section, stock of a QOF C corporation (qualifying or otherwise) is not treated as stock for purposes of determining whether the QOF C corporation may join in the filing of a consolidated return. Thus, because no election has been made under paragraph (b)(2) of this section, once Q1 becomes a QOF, Q1 ceases to be affiliated with the P group members for purposes of section 1501, and it deconsolidates from the P group. See §§ 1.1502–1 through -1.1502–100 generally for the consequences of deconsolidation.

(2) [Reserved]

(e) *Applicability dates*—(1) *In general.* This section applies for taxable years beginning after March 13, 2020.

(2) *Prior periods.* With respect to the portion of a consolidated group's first taxable year ending after December 21, 2017, that began on December 22, 2017, and for taxable years beginning after December 21, 2017, and on or before March 13, 2020, a consolidated group may choose either—

(i) To apply the section 1400Z–2 regulations, if applied in a consistent manner for all such taxable years; or

(ii) To rely on the rules in proposed § 1.1400Z2(g)–1 contained in the notice of proposed rulemaking (REG–120186–18) published on May 1, 2019, but only if applied in a consistent manner for all such taxable years.

Sunita Lough,

Deputy Commissioner for Services and Enforcement.

Approved: December 18, 2019

David J. Kautter,

Assistant Secretary (Tax Policy).

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